CVB FINANCIAL CORP
Form 10-K
March 01, 2019
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 10-K

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF

1934.

For the fiscal year ended December 31, 2018

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: 000-10140

CVB FINANCIAL CORP.

(Exact name of registrant as specified in its charter)

California	**95-3629339**
(State or other jurisdiction of	(I.R.S. Employer

incorporation or organization)	Identification No.)
701 N. Haven Avenue, Suite 350	**91764**
Ontario, California	
(Address of Principal Executive Offices)	(Zip Code)

Registrant s telephone number, including area code: **(909) 980-4030**

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

Title of Class	Name of Each Exchange on Which Registered
Common Stock, no par value	NASDAQ Stock Market, LLC

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

None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes No

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted 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 such files). Yes No

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

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

Large accelerated filer	Accelerated filer
Non-accelerated filer	Smaller reporting company
Emerging growth company	

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the

Exchange Act

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). Yes No

As of June 30, 2018, the aggregate market value of the common stock held by non-affiliates of the registrant was approximately $2,304,857,385.

Number of shares of common stock of the registrant outstanding as of February 15, 2019: 139,973,017.

DOCUMENTS INCORPORATED BY REFERENCE	PART OF
Definitive Proxy Statement for the Annual Meeting of Stockholders which will be filed within 120 days of the fiscal year ended December 31, 2018	Part III of Form 10-K

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CVB FINANCIAL CORP.

2018 ANNUAL REPORT ON FORM 10-K

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INTRODUCTION

Cautionary Note Regarding Forward-Looking Statements

Certain statements in this report constitute forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, Rule 175 promulgated thereunder, Section 21E of the Securities and Exchange Act of 1934, as amended, Rule 3b-6 promulgated thereunder, or Exchange Act, and as such involve risk and uncertainties. All statements in this Form 10-K other than statements of historical fact are forward-looking statements for purposes of federal and state securities laws. Words such as will likely result, aims , anticipates , believes , could , estimates , expects , hopes , intends , may , plans , projects , seeks , should , will and variations of these expressions help to identify these forward looking statements, which involve risks and uncertainties.

These forward-looking statements relate to, among other things, anticipated future operating and financial performance, the allowance for loan losses, our financial position and liquidity, business strategies, regulatory and competitive outlook, investment and expenditure plans, capital and financing needs and availability, plans and objectives of management for future operations, expectations of the environment in which we operate, projections of future performance, perceived opportunities in the market and strategies regarding our mission and vision and statements relating to any of the foregoing. Factors that could cause actual results to differ from those discussed in the forward-looking statements include but are not limited to:

- local, regional, national and international economic and market conditions and events and the impact they may have on us, our customers and our assets and liabilities;
- our ability to attract deposits and other sources of funding or liquidity;
- supply and demand for real estate and periodic deterioration in real estate prices and/or values in California or other states where we lend, including both residential and commercial real estate;
- a prolonged slowdown or decline in real estate construction, sales or leasing activities;
- changes in the financial performance and/or condition of our borrowers, depositors, key vendors or counterparties;
- changes in our levels of delinquent loans, nonperforming assets, allowance for loan losses and charge-offs;
- the costs or effects of mergers, acquisitions or dispositions we may make, including the 2018 merger of Community Bank with and into Citizens Business Bank, whether we are able to obtain any required governmental approvals in connection with any such mergers, acquisitions or dispositions, and/or our ability to realize the contemplated financial or business benefits, including cost savings or synergies, associated with any such mergers, acquisitions or dispositions;

the effect of changes in laws, regulations and applicable judicial decisions (including laws, regulations and judicial decisions concerning financial reforms, taxes, bank capital levels, allowance for loan losses, consumer, commercial or secured lending, securities and securities trading and hedging, bank operations, compliance, fair lending, employment, executive compensation, insurance, vendor management and information security) with which we and our subsidiaries must comply or believe we should comply;

the effects of additional legal and regulatory requirements to which we have or will become subject;

changes in estimates of future reserve requirements and minimum capital requirements based upon the periodic review thereof under relevant regulatory and accounting requirements, including changes in the Basel Committee framework establishing capital standards for credit, operations and market risk;

the accuracy of the assumptions and estimates and the absence of technical error in implementation or calibration of models used to estimate the fair value of financial instruments or incurred credit losses or loan delinquencies;

inflation, interest rate, securities market and monetary fluctuations;

changes in government or bank-established interest rates or monetary policies, including the anticipated replacement of the LIBOR index on our loans which are tied to that index;

changes in the amount, cost and availability of deposit insurance;

political developments, uncertainties or instability, catastrophic events, acts of war or terrorism, or natural disasters, such as earthquakes, drought, pandemic diseases or extreme weather events, any of which may affect services we use or affect our customers, employees or third parties with which we conduct business;

disruptions in the infrastructure that supports our business and the communities where we are located, which are concentrated in California, involving or related to physical site access and /or communications facilities which we utilize,

information technology and cyber security incidents, disruptions or attacks and the possible blocking, theft or loss of Company or customer access, functionality, data, funding or money;

our timely development and acceptance of new banking products and services and the perceived overall value of these products and services by our customers and potential customers;

the Company s relationships with and reliance upon vendors with respect to certain of the Company s key internal and external systems and applications;

changes in commercial or consumer spending, borrowing and savings preferences or behaviors;

technological changes and the expanding use of technology in banking (including the adoption of mobile banking, funds transfer applications and electronic marketplaces for loans and other banking products or services);

our ability to retain and increase market share, retain and grow customers and control expenses;

changes in the competitive environment among financial and bank holding companies, banks and other financial service providers;

competition and innovation with respect to financial products and services by banks, financial institutions and non-traditional providers including retail businesses and technology companies;

volatility in the credit and equity markets and its effect on the general economy or local or regional business conditions or on the Company s customers;

fluctuations in the price of the Company s common stock or other securities, and the resulting impact on the Company s ability to raise capital or make acquisitions;

the effect of changes in accounting policies and practices, as may be adopted from time-to-time by the regulatory agencies, as well as by the Public Company Accounting Oversight Board, the Financial Accounting Standards Board and other accounting standard-setters;

changes in our organization, management, compensation and benefit plans, and our ability to retain or expand our workforce, management team and/or board of directors;

the costs and effects of legal, compliance and regulatory actions, changes and developments, including the initiation and resolution of legal proceedings (such as securities, bank operations, consumer or employee class action litigation), and any legal claims or liabilities we inherit due to an acquisition or merger;

- regulatory or other governmental inquiries or investigations, and/or the results of regulatory examinations or reviews;

- our ongoing relations with our various federal and state regulators, including the SEC, Federal Reserve Board, FDIC and California DBO; and

- our success at managing the risks involved in the foregoing items and all other risk factors set forth in the Company s public reports and releases.

For additional information concerning risks we face, see Item 1A. *Risk Factors* and any additional information we set forth in our periodic reports filed pursuant to the Exchange Act, including our Annual Report on Form 10-K. We do not undertake any obligation to update our forward-looking statements to reflect occurrences or unanticipated events or circumstances arising after the date of such statements, except as required by law.

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PART I

ITEM 1. *BUSINESS*

CVB Financial Corp.

CVB Financial Corp. (referred to herein on an unconsolidated basis as CVB and on a consolidated basis as we , our or the Company) is a bank holding company incorporated in California on April 27, 1981 and registered with the Board of Governors of the Federal Reserve System (Federal Reserve) under the Bank Holding Company Act of 1956, as amended (the Bank Holding Company Act). The Company commenced business on December 30, 1981 when, pursuant to a reorganization, it acquired all of the voting stock of Chino Valley Bank. On March 29, 1996, Chino Valley Bank changed its name to Citizens Business Bank (CBB or the Bank). The Bank is our principal asset. The Company also has one inactive subsidiary, Chino Valley Bancorp. The Company is also the common stockholder of CVB Statutory Trust III. CVB Statutory Trust III was created in January 2006 to issue trust preferred securities in order to raise capital for the Company.

CVB s principal business is to serve as a holding company for the Bank and for other banking or banking related subsidiaries, which the Company may establish or acquire. CVB has not engaged in any other material activities to date. As a legal entity separate and distinct from its subsidiaries, CVB s principal source of funds is, and will continue to be, dividends paid by and other funds advanced from the Bank and capital raised directly by CVB. Legal limitations are imposed on the amount of dividends that may be paid and loans that may be made by the Bank to CVB. See Item 1. *Business Regulation and Supervision Dividends.* As of December 31, 2018, the Company had $11.53 billion in total consolidated assets, $7.70 billion in net loans, $8.83 billion in deposits, and $1.85 billion in shareholders equity.

On August 10, 2018, we completed the acquisition of Community Bank (CB), a California banking corporation headquartered in Pasadena, California. At such time, CB merged with and into the Bank and we issued approximately 29.8 million shares of Company common stock and paid approximately $180.7 million in aggregate cash consideration to the former Community Bank shareholders. Our consolidated financial operations for 2018 include CB operations, post-merger. See Note 4 *Business Combinations* included herein.

The principal executive offices of CVB and the Bank are located at 701 North Haven Avenue, Suite 350, Ontario, California. Our phone number is (909) 980-4030.

Citizens Business Bank

The Bank commenced operations as a California state-chartered bank on August 9, 1974. The Bank s deposit accounts are insured under the Federal Deposit Insurance Act up to applicable limits. The Bank is not a member of the Federal Reserve System. At December 31, 2018, the Bank had $11.52 billion in assets, $7.70 billion in net loans, $8.85 billion in deposits, and $1.87 billion in total equity. The significant increase in our assets, loans and deposits from December 31, 2017 was primarily due to the acquisition of CB.

As of December 31, 2018, there were 68 Banking Centers (Centers) located in the Inland Empire, Los Angeles County, Orange County, San Diego County, Ventura County, Santa Barbara County, and the Central Valley area of California.

We also have three trust offices located in Ontario, Newport Beach and Pasadena. These offices serve as sales offices for the Bank s wealth management, trust and investment products.

Through our network of Centers, we emphasize personalized service combined with a wide range of banking and trust services for businesses, professionals and individuals located in the service areas of our Centers. Although we focus the marketing of our services to small-and medium-sized businesses, a wide range of banking, investment and trust services are made available to the local consumer market.

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We offer a standard range of bank deposit instruments. These include checking, savings, money market and time certificates of deposit for both business and personal accounts. We also serve as a federal tax depository for our business customers.

We also provide a full complement of lending products, including commercial, agribusiness, consumer, SBA loans, real estate loans and equipment and vehicle leasing. Commercial products include lines of credit and other working capital financing, accounts receivable lending and letters of credit. Agribusiness products are loans to finance the operating needs of wholesale dairy farm operations, cattle feeders, livestock raisers, and farmers. We provide bank qualified lease financing for municipal governments. Commercial real estate and construction loans are secured by a range of property types and include both owner-occupied and investor owned properties. Financing products for consumers include automobile leasing and financing, lines of credit, credit cards, home mortgages, and home equity loans and lines of credit.

We also offer a wide range of specialized services designed for the needs of our commercial customers. These services include cash management systems for monitoring cash flow, a credit card program for merchants, courier pick-up and delivery, payroll services, remote deposit capture, electronic funds transfers by way of domestic and international wires and automated clearinghouse, and on-line account access. We make available investment products offered by other providers to our customers, including mutual funds, a full array of fixed income vehicles and a program to diversify our customers funds in federally insured time certificates of deposit of other institutions.

In addition, we offer a wide range of financial services and trust services through our CitizensTrust division. These services include fiduciary services, mutual funds, annuities, 401(k) plans and individual investment accounts.

Business Segments

We are a community bank with one reportable operating segment. See the sections captioned Business Segments in Item 7. *Management s Discussion and Analysis of Financial Condition and Results of Operations* and Note 3 *Summary of Significant Accounting Policies Business Segments* of the notes to consolidated financial statements.

Competition

The banking and financial services business is highly competitive. The competitive environment faced by banks is a result primarily of changes in laws and regulations, changes in technology and product delivery systems, and the ongoing consolidation among insured financial institutions. We compete for loans, deposits, and customers with other commercial banks, savings and loan associations, savings banks, securities and brokerage companies, mortgage companies, insurance companies, finance companies, money market funds, credit unions, and other nonbank financial service providers, including online banks and peer-to-peer or marketplace payment processors, lenders and other small business and consumer lenders. Many competitors are much larger in total assets and capitalization, have greater access to capital markets and/or offer a broader range of financial products and services, including technology-based services. Additionally, some smaller competitors, including non-bank entities, may be more nimble and responsive to customer preferences or requirements.

Economic Conditions/Government Policies

Our profitability, like most financial institutions, is primarily dependent on interest rate spreads and noninterest income. In general, the difference between the interest rates paid by the Bank on interest-bearing liabilities, such as deposits and other borrowings, and the interest rates received by the Bank on interest-earning assets, such as loans extended to customers and securities held in the investment portfolio, will comprise the major portion of our earnings.

These rates are highly sensitive to many factors that are beyond our control, such as inflation, recession and unemployment, government monetary and other policies, and the impact which future changes in domestic and foreign economic conditions might have on us cannot be predicted.

Opportunity for banks to earn fees and other noninterest income have also been limited by restrictions imposed by the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank) and other government regulations. As the following sections indicate, the impact of current and future changes in government laws and regulations on our ability to maintain current levels of fees and other noninterest income could be material and cannot be predicted.

Our business is also influenced by the monetary and fiscal policies of the federal government and the policies of regulatory agencies, particularly the Federal Reserve. The Federal Reserve implements national monetary policies (with objectives such as curbing inflation, increasing employment and combating recession) through its open-market operations in U.S. Government securities by buying and selling treasury and mortgage-backed securities, by adjusting the required level of reserves for depository institutions subject to its reserve requirements, and by varying the target federal funds and discount rates applicable to borrowings by depository institutions. The actions of the Federal Reserve in these areas influence the growth and performance of bank loans, investments, and deposits and also affect interest earned on interest-earning assets and paid on interest-bearing liabilities. In recent years, the impact of the Federal Reserve s actions and policies have tended to assume even greater importance and impact on the lending and securities markets, and these actions and policies are continuing to evolve and change based on political and economic events and incoming data. Government fiscal and budgetary policies, including deficit spending, can also have a significant impact on the capital markets and interest rates. The nature and impact of any future changes in monetary and fiscal policies on us cannot be predicted.

Regulation and Supervision

General

The Bank is subject to significant regulation and restrictions by federal and state laws and regulatory agencies. These regulations and restrictions are intended primarily for the protection of depositors and the Federal Deposit Insurance Corporation (FDIC) Deposit Insurance Fund (DIF) and for the protection of borrowers, and secondarily for the stability of the U.S. banking system. The following discussion of statutes and regulations is a summary and does not purport to be complete nor does it address all applicable statutes and regulations. This discussion is qualified in its entirety by reference to the statutes and regulations referred to in this discussion. From time to time, federal and state legislation is enacted and implemented by regulations which may have the effect of materially increasing the cost of doing business, limiting or expanding permissible activities, or affecting the competitive balance between banks and other financial services providers.

We cannot predict whether or when other legislation or new regulations may be enacted, and if enacted, the effect that new legislation or any implemented regulations and supervisory policies would have on our financial condition and results of operations. Such developments may further alter the structure, regulation, and competitive relationship among financial institutions, may limit the types or pricing of the products and services we offer, and may subject us to increased regulation, disclosure, and reporting requirements.

Legislation and Regulatory Developments

The federal banking agencies continue to implement the remaining requirements in the Dodd-Frank Act as well as promulgating other regulations and guidelines intended to assure the financial strength and safety and soundness of banks and the stability of the U.S. banking system. On February 3, 2017 the President of the United States issued an executive order identifying certain core principles for the administration s financial services regulatory policy and directing the Secretary of the Treasury, in consultation with the heads of other financial regulatory agencies, to evaluate how the current regulatory framework promotes or inhibits the principles and what actions have been, and are being, taken to promote the principles. In response to the executive order, on June 12, 2017, October 6, 2017 and

October 26, 2017, respectively, the United States Department of the Treasury issued the first three of four reports recommending a number of comprehensive

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changes in the current regulatory system for U.S. depository institutions, the U.S. capital markets and the U.S. asset management and insurance industries, around the following principles:

- Improving regulatory efficiency and effectiveness by critically evaluating mandates and regulatory fragmentation, overlap, and duplication across regulatory agencies;
- Aligning the financial system to help support the U.S. economy;
- Reducing regulatory burden by decreasing unnecessary complexity;
- Tailoring the regulatory approach based on size and complexity of regulated firms and requiring greater regulatory cooperation and coordination among financial regulators; and
- Aligning regulations to support market liquidity, investment, and lending in the U.S. economy. The scope and breadth of regulatory changes that will be implemented in response to the President s executive order have not yet been determined.

Capital Adequacy Requirements

Bank holding companies and banks are subject to similar regulatory capital requirements administered by state and federal banking agencies. The basic capital rule changes in the new capital rules (the New Capital Rules) adopted by the federal bank regulatory agencies were fully effective on January 1, 2015, but many elements are being phased in over multiple future years. The risk-based capital guidelines for bank holding companies, and additionally for banks, require capital ratios that vary based on the perceived degree of risk associated with a banking organization s operations, both for transactions reported on the balance sheet as assets, such as loans, and for those recorded as off-balance sheet items, such as commitments, letters of credit and recourse arrangements. The risk-based capital ratio is determined by classifying assets and certain off-balance sheet financial instruments into weighted categories, with higher levels of capital being required for those categories perceived as representing greater risks, and with the applicable ratios calculated by dividing qualifying capital by total risk-adjusted assets and off-balance sheet items. Capital amounts and classifications are also subject to qualitative judgments by regulators about components, risk weighting and other factors. Bank holding companies and banks engaged in significant trading activity may also be subject to the market risk capital guidelines and be required to incorporate additional market and interest rate risk components into their risk-based capital standards. To the extent that the new rules are not fully phased in, the prior capital rules will continue to apply.

The New Capital Rules revised the previous risk-based and leverage capital requirements for banking organizations to meet the requirements of the Dodd-Frank Act and to implement the international Basel Committee on Banking Supervision Basel III agreements. Many of the requirements in the New Capital Rules and other regulations and rules are applicable only to larger or internationally active institutions and not to all banking organizations. These include required annual stress tests for institutions with $100 billion or more of assets and Enhanced Prudential Standards, Comprehensive Capital Analysis and Review requirements, Capital Plan and Resolution Plan or living will submissions. These also include an additional countercyclical capital buffer, a supplementary leverage ratio and the Liquidity Coverage Ratio rule requiring sufficient high-quality liquid assets, which may in turn apply to institutions with $50 billion or more in assets, $250 billion or more in assets, or institutions which may be identified as Global Systematically Important Banking Institutions (G-SIBs). We anticipate increased compliance costs and regulatory requirements following our acquisition of CB, which increased our asset size to over $10 billion. Under the risk-based capital guidelines in place prior to the effectiveness of the New Capital Rules, which trace back to the 1988 Basel I accord, there were three fundamental capital ratios: a total risk-based capital ratio, a Tier 1 risk-based capital ratio and a Tier 1 leverage ratio. To be deemed well capitalized, a bank must have a total risk-based capital ratio, a Tier 1 risk-based capital ratio and a Tier 1 leverage ratio of at least ten percent, six percent and five percent, respectively.

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The following are the New Capital Rules applicable to the Company and the Bank which began January 1, 2015:

- an increase in the minimum Tier 1 capital ratio from 4.00% to 6.00% of risk-weighted assets;
- a new category and a required 4.50% of risk-weighted assets ratio is established for common equity Tier 1 as a subset of Tier 1 capital limited to common equity;
- a minimum non-risk-based leverage ratio is set at 4.00%;
- changes in the permitted composition of Tier 1 capital to exclude trust preferred securities subject to certain grandfathering exceptions for organizations like CVB which were under $15 billion in assets as of December 31, 2009, mortgage servicing rights and certain deferred tax assets and include unrealized gains and losses on available for sale debt and equity securities unless the organization opts out of including such unrealized gains and losses, which election the Company made in 2015;
- the risk-weights of certain assets for purposes of calculating the risk-based capital ratios are changed for high volatility commercial real estate acquisition, development and construction loans, certain past due non-residential mortgage loans and certain mortgage-backed and other securities exposures; and
- an additional capital conservation buffer of 2.5% of risk weighted assets above the regulatory minimum capital ratios, which was phased in over four years beginning at the rate of 0.625% of risk-weighted assets per year beginning 2016 and which must be met to avoid limitations on the ability of the Bank to pay dividends, repurchase shares or pay discretionary bonuses.

Management believes that, as of December 31, 2018, the Company and the Bank meet all requirements under the New Capital Rules applicable to them.

Including the capital conservation buffer of 2.5%, the New Capital Rules result in the following minimum ratios to be considered well capitalized: (i) a Tier 1 capital ratio of 8.5%, (ii) a common equity Tier 1 capital ratio of 7.0%, and (iii) a total capital ratio of 10.5%. At December 31, 2018, the respective capital ratios of the Company and the Bank exceeded the minimum percentage requirements to be deemed well-capitalized for regulatory purposes. See Management s Discussion and Analysis of Financial Condition and Results of Operations Capital Resources.

While the New Capital Rules set higher regulatory capital standards for the Company and the Bank, bank regulators may also continue their past policies of expecting banks to maintain additional capital beyond the new minimum requirements. The implementation of the New Capital Rules or more stringent requirements to maintain higher levels of capital or to maintain higher levels of liquid assets could adversely impact the Company s net income and return on equity, restrict the ability to pay dividends or executive bonuses and require the raising of additional capital. See Management s Discussion and Analysis of Financial Condition and Results of Operations Capital Resources.

In September 2017, the federal bank regulators proposed to revise and simplify the capital treatment for certain deferred tax assets, mortgage servicing assets, investments in non-consolidated financial entities and minority interests for banking organizations, such as the Company and the Bank, that are not subject to the advanced approaches requirements. In November 2017, the federal banking regulators revised the Basel III Capital Rules to extend the current transitional treatment of these items for non-advanced approaches banking organizations until the September 2017 proposal is finalized. The September 2017 proposal would also change the capital treatment of certain commercial real estate loans under the standardized approach, which we use to calculate our capital ratios.

In December 2017, the Basel Committee published standards that it described as the finalization of the Basel III post-crisis regulatory reforms (the standards are commonly referred to as Basel IV). Among other things, these standards revise the Basel Committee s standardized approach for credit risk (including by recalibrating risk weights and introducing new capital requirements for certain unconditionally cancellable commitments, such as unused credit card lines of credit) and provides a new standardized approach for operational risk capital. Under the Basel framework, these standards will generally be effective on January 1, 2022, with an aggregate output floor phasing in through January 1, 2027. Under the current U.S. capital rules, operational risk capital requirements and a capital floor apply only to advanced approaches institutions, and not to the Company and the Bank. The impact of Basel IV on us will depend on the manner in which it is implemented by the federal bank regulators.

Prompt Corrective Action Provisions

The Federal Deposit Insurance Act requires the federal bank regulatory agencies to take prompt corrective action with respect to a depository institution if that institution does not meet certain capital adequacy standards, including requiring the prompt submission of an acceptable capital restoration plan. Depending on the bank s capital ratios, the agencies regulations define five categories in which an insured depository institution will be placed: well-capitalized, adequately capitalized, undercapitalized, significantly undercapitalized, and critically undercapitalized. At each successive lower capital category, an insured bank is subject to more restrictions, including restrictions on the bank s activities, operational practices or the ability to pay dividends or executive bonuses. Based upon its capital levels, a bank that is classified as well-capitalized, adequately capitalized, or undercapitalized may be treated as though it were in the next lower capital category if the appropriate federal banking agency, after notice and opportunity for hearing, determines that an unsafe or unsound condition, or an unsafe or unsound practice, warrants such treatment.

The prompt corrective action standards were changed to conform with the New Capital Rules. Under the new standards, in order to be considered well-capitalized, the bank will be required to meet the new common equity Tier 1 ratio of 6.5%, an increased Tier 1 ratio of 8% (increased from 6%), a total capital ratio of 10% (unchanged) and a leverage ratio of 5% (unchanged).

The federal banking agencies also may require banks and bank holding companies subject to enforcement actions to maintain capital ratios in excess of the minimum ratios otherwise required to be deemed well capitalized, in which case institutions may no longer be deemed to be well capitalized and may therefore be subject to certain restrictions such as taking brokered deposits.

Volcker Rule

In December 2013, the federal bank regulatory agencies adopted final rules that implement a part of the Dodd-Frank Act commonly referred to as the Volcker Rule. Under these rules and subject to certain exceptions, banking entities are restricted from engaging in activities that are considered proprietary trading and from sponsoring or investing in certain entities, including hedge or private equity funds that are considered covered funds. These rules became effective on April 1, 2014, although certain provisions are subject to delayed effectiveness under rules promulgated by the FRB. The Company and the Bank held no investment positions at December 31, 2018 which were subject to the final rule. Therefore, while these new rules may require us to conduct certain internal analysis and reporting to ensure continued compliance, they did not require any material changes in our operations or business.

Bank Holding Company Regulation

Bank holding companies and their subsidiaries are subject to significant regulation and restrictions by Federal and State laws and regulatory agencies, which may affect the cost of doing business, and may limit permissible activities and expansion or impact the competitive balance between banks and other financial services providers.

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A wide range of requirements and restrictions are contained in both federal and state banking laws, which together with implementing regulatory authority:

Require periodic reports and such additional reports of information as the Federal Reserve may require;

Require bank holding companies to meet or exceed increased levels of capital (See Capital Adequacy Requirements);

Require that bank holding companies serve as a source of financial and managerial strength to subsidiary banks and commit resources as necessary to support each subsidiary bank;

Limit of dividends payable to shareholders and restrict the ability of bank holding companies to obtain dividends or other distributions from their subsidiary banks. The Company s ability to pay dividends on both its common and preferred stock is subject to legal and regulatory restrictions. Substantially all of CVB s funds to pay dividends or to pay principal and interest on our debt obligations are derived from dividends paid by the Bank;

Require a bank holding company to terminate an activity or terminate control of or liquidate or divest certain subsidiaries, affiliates or investments if the Federal Reserve believes the activity or the control of the subsidiary or affiliate constitutes a significant risk to the financial safety, soundness or stability of any bank subsidiary;

Require the prior approval of senior executive officer or director changes and prohibit golden parachute payments, including change in control agreements, or new employment agreements with such payment terms, which are contingent upon termination if an institution is in troubled condition ;

Regulate provisions of certain bank holding company debt, including the authority to impose interest ceilings and reserve requirements on such debt and require prior approval to purchase or redeem securities in certain situations;

Require prior approval for the acquisition of 5% or more of the voting stock of a bank or bank holding company by bank holding companies or other acquisitions and mergers with banks and consider certain competitive, management, financial, anti-money-laundering compliance, potential impact on U.S. financial stability or other factors in granting these approvals, in addition to similar California or other state banking agency approvals which may also be required; and

Require prior notice and/or prior approval of the acquisition of control of a bank or a bank holding company by a shareholder or individuals acting in concert with ownership or control of 10% of the voting stock being a presumption of control.

Other Restrictions on the Company s Activities

Subject to prior notice or Federal Reserve approval, bank holding companies may generally engage in, or acquire shares of companies engaged in, activities determined by the Federal Reserve to be so closely related to banking or managing or controlling banks as to be a proper incident thereto. Bank holding companies which elect and retain financial holding company status pursuant to the Gramm-Leach-Bliley Act of 1999 (GLBA) may engage in these nonbanking activities and broader securities, insurance, merchant banking and other activities that are determined to be financial in nature or are incidental or complementary to activities that are financial in nature without prior Federal Reserve approval. Pursuant to GLBA and Dodd-Frank, in order to elect and retain financial holding company status, a bank holding company and all depository institution subsidiaries of a bank holding company must be considered well capitalized and well managed, and, except in limited circumstances, depository subsidiaries must be in satisfactory compliance with the Community Reinvestment Act (CRA), which requires banks to help meet the credit needs of the communities in which they operate. Failure to sustain compliance with these requirements or correct any non-compliance within a fixed time period could lead to divestiture of subsidiary banks or require all activities to conform to those permissible for a bank holding company. CVB has not elected financial holding company status and neither CVB nor the Bank has engaged in any activities determined by the Federal Reserve to be financial in nature or incidental or complementary to activities that are financial in nature.

CVB is also a bank holding company within the meaning of Section 3700 of the California Financial Code. Therefore, CVB and any of its subsidiaries are subject to examination by, and may be required to file reports with, the California Department of Business Oversight (DBO). DBO approvals may also be required for certain mergers and acquisitions.

Securities Exchange Act of 1934

CVB s common stock is publicly held and listed on the NASDAQ Stock Market (NASDAQ), and CVB is subject to the periodic reporting, information, proxy solicitation, insider trading, corporate governance and other requirements and restrictions of the Securities Exchange Act of 1934 and the regulations of the Securities and Exchange Commission (SEC) promulgated thereunder as well as listing requirements of NASDAQ.

Sarbanes-Oxley Act

The Company is subject to the accounting oversight and corporate governance requirements of the Sarbanes-Oxley Act of 2002, including, among other things, required executive certification of financial presentations, requirements for board audit committees and their members, and disclosure of controls and procedures and internal control over financial reporting.

Bank Regulation

As a California commercial bank whose deposits are insured by the FDIC, the Bank is subject to regulation, supervision, and regular examination by the DBO and by the FDIC, as the Bank s primary Federal regulator, and must additionally comply with certain applicable regulations of the Federal Reserve. Specific federal and state laws and regulations which are applicable to banks regulate, among other things, the scope of their business, their investments, their reserves against deposits, the timing of the availability of deposited funds, their activities relating to dividends, investments, loans, the nature and amount of and collateral for certain loans, servicing and foreclosing on loans, borrowings, capital requirements, certain check-clearing activities, branching, and mergers and acquisitions. California banks are also subject to statutes and regulations including Federal Reserve Regulation O and Federal Reserve Act Sections 23A and 23B and Regulation W, which restrict or limit loans or extensions of credit to insiders , including officers, directors, and principal shareholders, and loans or extension of credit by banks to affiliates or purchases of assets from affiliates, including parent bank holding companies, except pursuant to certain exceptions and only on terms and conditions at least as favorable to those prevailing for comparable transactions with unaffiliated parties. Failure to comply with applicable bank regulation or adverse results from any examinations of the Bank could affect the cost of doing business, and may limit or impede otherwise permissible activities and expansion activities by the Bank.

Pursuant to the Federal Deposit Insurance Act (FDI Act) and the California Financial Code, California state chartered commercial banks may generally engage in any activity permissible for national banks. Therefore, the Bank may form subsidiaries to engage in the many so-called closely related to banking or nonbanking activities commonly conducted by national banks in operating subsidiaries or in subsidiaries of bank holding companies. Further, California banks may conduct certain financial activities permitted under GLBA in a financial subsidiary to the same extent as may a national bank, provided the bank is and remains well-capitalized, well-managed and in satisfactory compliance with the CRA. The Bank currently has no financial subsidiaries.

FDIC and DBO Enforcement Authority

The federal and California regulatory structure gives the bank regulatory agencies extensive discretion in connection with their supervisory and enforcement activities and examination policies, including policies with respect to the classification of assets and the establishment of appropriate loan loss reserves for regulatory purposes. The regulatory agencies have adopted guidelines to assist in identifying and addressing potential safety

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and soundness concerns before an institution s capital becomes impaired. The guidelines establish operational and managerial standards generally relating to: (1) internal controls, information systems, and internal audit systems; (2) loan documentation; (3) credit underwriting; (4) interest-rate exposure; (5) asset growth and asset quality; and (6) compensation, fees, and benefits. Further, the regulatory agencies have adopted safety and soundness guidelines for asset quality and for evaluating and monitoring earnings to ensure that earnings are sufficient for the maintenance of adequate capital and reserves. If, as a result of an examination, the DBO or the FDIC should determine that the financial condition, capital resources, asset quality, earnings prospects, management, liquidity, or other aspects of the Bank s operations are unsatisfactory or that the Bank or its management is violating or has violated any law or regulation, the DBO and the FDIC, and separately the FDIC as insurer of the Bank s deposits, have residual authority to:

- Require affirmative action to correct any conditions resulting from any violation or practice;
- Direct an increase in capital and the maintenance of higher specific minimum capital ratios, which could preclude the Bank from being deemed well capitalized and restrict its ability to accept certain brokered deposits;
- Restrict the Bank s growth geographically, by products and services, or by mergers and acquisitions, including bidding in FDIC receiverships for failed banks;
- Enter into or issue informal or formal enforcement actions, including required Board resolutions, Matters Requiring Board Attention (MRBA), written agreements and consent or cease and desist orders or prompt corrective action orders to take corrective action and cease unsafe and unsound practices;
- Require prior approval of senior executive officer or director changes; remove officers and directors and assess civil monetary penalties; and
- Terminate FDIC insurance, revoke the charter and/or take possession of and close and liquidate the Bank or appoint the FDIC as receiver.

Deposit Insurance

The FDIC is an independent federal agency that insures deposits, up to prescribed statutory limits, of federally insured banks and savings institutions and safeguards the safety and soundness of the banking and savings industries. The FDIC insures our customer deposits through the DIF up to prescribed limits for each depositor. The Dodd-Frank Act revised the FDIC s DIF management authority by setting requirements for the Designated Reserve Ratio (the DIF balance divided by estimated insured deposits) and redefining the assessment base, which is used to calculate banks quarterly assessments. The amount of FDIC assessments paid by each DIF member institution is based on its asset size and relative risk of default as measured by regulatory capital ratios and other supervisory factors. The FDIC may terminate a depository institution s deposit insurance upon a finding that the institution s financial condition is unsafe or unsound or that the institution has engaged in unsafe or unsound practices that pose a risk to the DIF or that may prejudice the interest of the bank s depositors. The termination of deposit insurance for a bank would also result in the revocation of the bank s charter by the DBO.

We are generally unable to control the amount of premiums that we are required to pay for FDIC insurance, which can be affected by the cost of bank failures to the FDIC among other factors. The FDIC is an independent federal agency that insures deposits through the DIF up to prescribed statutory limits of federally insured banks and savings institutions and safeguards the safety and soundness of the banking and savings industries. The Dodd-Frank Act revised the FDIC s DIF management authority by setting requirements for the Designated Reserve Ratio (the DRR , calculated as the DIF balance divided by estimated insured deposits) and redefining the assessment base which is used to calculate banks quarterly assessments. The amount of FDIC assessments paid by each DIF member institution is based on its asset size and its relative risk of default as measured by regulatory capital ratios and other supervisory factors. As a result of our acquisition of CB our FDIC assessments will increase.

On September 30, 2018, the DRR reached 1.36%. Because the reserve ratio has exceeded 1.35%, two deposit insurance assessment changes occurred under the FDIC regulations: 1) surcharges on large banks (total consolidated assets of $10 billion or more) ended; the last surcharge on large banks was collected on December 28, 2018. and 2) small banks (total consolidated assets of less than $10 billion) were awarded assessment credits for the portion of their assessments that contributed to the growth in the reserve ratio from 1.15% to 1.35%, to be applied when the reserve ratio is at least 1.38%.The FDIC will, at least semi-annually, update its income and loss projections for the Deposit Insurance Fund and, if necessary, propose rules to further increase assessment rates. Any future increases in FDIC insurance premiums may have a material and adverse effect on our earnings and could have a material adverse effect on the value of, or market for, our common stock.

Dividends

It is the Federal Reserve s policy that bank holding companies should generally pay dividends on common stock only out of income available over the past year, and only if prospective earnings retention is consistent with the organization s expected future needs and financial condition. It is also the Federal Reserve s policy that bank holding companies should not maintain dividend levels that undermine their ability to be a source of strength to its banking subsidiaries. The Federal Reserve also discourages dividend payment ratios that are at maximum allowable levels unless both asset quality and capital are very strong. In addition, a bank holding company may be unable to pay dividends on its common stock if it fails to maintain an adequate capital conservation buffer under the New Capital Rules.

The Bank is a legal entity that is separate and distinct from its holding company. CVB relies on dividends received from the Bank for use in the operation of the Company and the ability of CVB to pay dividends to shareholders. Future cash dividends by the Bank will also depend upon management s assessment of future capital requirements, contractual restrictions, and other factors. The new Capital Rules may restrict dividends by the Bank if the additional capital conservation buffer is not achieved. See Capital Adequacy Requirements .

The ability of the Bank to declare a cash dividend to CVB is subject to California law, which restricts the amount available for cash dividends to the lesser of a bank s retained earnings or net income for its last three fiscal years (less any distributions to shareholders made during such period). Where the above test is not met, cash dividends may still be paid, with the prior approval of the DBO, in an amount not exceeding the greatest of (1) retained earnings of the bank; (2) the net income of the bank for its last fiscal year; or (3) the net income of the bank for its current fiscal year.

Compensation

The Dodd-Frank Act requires the federal bank regulators and the SEC to establish joint regulations or guidelines prohibiting incentive-based payment arrangements at specified regulated entities, including the Company and the Bank, having at least $1 billion in total assets that encourage inappropriate risks by providing an executive officer, employee, director or principal stockholder with excessive compensation, fees or benefits or that could lead to material financial loss to the entity. In addition, these regulators must establish regulations or guidelines requiring enhanced disclosure to regulators of incentive-based compensation arrangements. The agencies proposed such regulations initially in April 2011 and in April 2016, the Federal Reserve and other federal financial agencies re-proposed restrictions on incentive-based compensation. For institutions with at least $1 billion but less than $50 billion in total consolidated assets, such as the Company and the Bank, the proposal would impose principles-based restrictions that are broadly consistent with existing interagency guidance on incentive-based compensation. Such institutions would be prohibited from entering into incentive compensation arrangements that encourage inappropriate risks by the institution (1) by providing an executive officer, employee, director, or principal shareholder with excessive compensation, fees, or benefits, or (2) that could lead to material financial loss to the institution. The proposal would also impose certain governance and recordkeeping requirements on institutions of the Company s and the Bank s size. The regulatory organizations would reserve the authority to impose more stringent requirements on institutions of the Company s and the Bank s size. We are evaluating the expected impact of the proposal on our business.

Cybersecurity

Federal regulators have issued multiple statements regarding cybersecurity and that financial institutions need to design multiple layers of security controls to establish lines of defense and to ensure that their risk management processes also address the risk posed by compromised customer credentials, including security measures to reliably authenticate customers accessing internet-based services of the financial institution. In addition, a financial institution s management is expected to maintain sufficient business continuity planning processes to ensure the rapid recovery, resumption and maintenance of the institution s operations in the event of a cyber-attack. A financial institution is also expected to develop appropriate processes to enable recovery of data and business operations and address rebuilding network capabilities and restoring data if the institution or its critical service providers fall victim to a cyber-attack. If we fail to observe the regulatory guidance, we could be subject to various regulatory sanctions, including financial penalties.

State regulators have also been increasingly active in implementing privacy and cybersecurity standards and regulations. Recently, several states, notably including California where we conduct substantially all our banking business, have adopted laws and/or regulations requiring certain financial institutions to implement cybersecurity programs and providing detailed requirements with respect to these programs, including data encryption requirements. Many such states (including California) have also recently implemented or modified their data breach notification and data privacy requirements. We expect this trend of state-level activity in those areas to continue, and we continue to monitor relevant legislative and regulatory developments in California where nearly all our customers are located.

In the ordinary course of business, we rely on electronic communications and information systems to conduct our operations and to store sensitive data. We employ a layered, defensive approach that leverages people, processes and technology to manage and maintain cybersecurity controls. We employ a variety of preventative and detective tools to monitor, block, and provide alerts regarding suspicious activity, as well as to report on any suspected advanced persistent threats. Notwithstanding the strength of our defensive measures, the threat from cyber-attacks is severe, attacks are sophisticated and increasing in volume, and attackers respond rapidly to changes in defensive measures. While to date we have not detected a significant compromise, significant data loss or any material financial losses related to cybersecurity attacks, our systems and those of our customers and third-party service providers are under constant threat and it is possible that we could experience a significant event in the future. Risks and exposures related to cybersecurity attacks are expected to remain high for the foreseeable future due to the rapidly evolving nature and sophistication of these threats, as well as due to the expanding use of Internet banking, mobile banking and other technology-based products and services by us and our customers. See Item 1A. Risk Factors for a further discussion of risks related to cybersecurity.

Operations and Consumer Compliance Laws

The Bank must comply with numerous federal and state anti-money laundering and consumer protection statutes and implementing regulations, including the USA PATRIOT Act of 2001, the Bank Secrecy Act, the Foreign Account Tax Compliance Act, the CRA, the Fair Debt Collection Practices Act, the Fair Credit Reporting Act, the Equal Credit Opportunity Act, the Truth in Lending Act, the Fair Housing Act, the Home Mortgage Disclosure Act, the Real Estate Settlement Procedures Act, the National Flood Insurance Act, the California Homeowner Bill of Rights and various federal and state privacy protection laws, including the Telephone Consumer Protection Act , CAN-SPAM Act. Noncompliance with any of these laws could subject the Bank to compliance enforcement actions as well as lawsuits and could also result in administrative penalties, including, fines and reimbursements. The Bank and the Company are also subject to federal and state laws prohibiting unfair or fraudulent business practices, untrue or misleading advertising and unfair competition.

These laws and regulations mandate certain disclosure and reporting requirements and regulate the manner in which financial institutions must deal with customers when taking deposits, making loans, servicing, collecting and foreclosure of loans, and providing other services. Failure to comply with these laws and regulations can subject the Bank and the Company to various penalties, including but not limited to enforcement actions, injunctions, fines or criminal penalties, punitive damages to consumers, and the loss of certain contractual rights.

The Bank received a Satisfactory rating in its most recent FDIC overall CRA performance evaluation, which measures how financial institutions support their communities in the areas of lending, investment and service, although the Bank received Low Satisfactory ratings on certain of the components within its most recent overall CRA performance rating evaluation.

The Dodd-Frank Act provided for the creation of the Bureau of Consumer Finance Protection (CFPB) as an independent entity within the Federal Reserve with broad rulemaking, supervisory and enforcement authority over consumer financial products and services, including deposit products, residential mortgages, home-equity loans and credit cards. The CFPB s functions include investigating consumer complaints, conducting market research, rulemaking, and enforcing rules related to consumer financial products and services. CFPB regulations and guidance apply to all covered persons and banks with $10 billion or more in assets are subject to supervision including examination by the CFPB, including the Bank following completion of the acquisition of CB.

The CFPB has finalized a number of significant rules which impact nearly every aspect of the lifecycle of a residential mortgage loan. These rules implement the Dodd-Frank Act amendments to the Equal Credit Opportunity Act, the Truth in Lending Act and the Real Estate Settlement Procedures Act. Among other things, the rules adopted by the CFPB require covered persons including banks making residential mortgage loans to: (i) develop and implement procedures to ensure compliance with an ability-to-repay test and identify whether a loan meets a new definition for a qualified mortgage , in which case a rebuttable presumption exists that the creditor extending the loan has satisfied the ability-to-repay test; (ii) implement new or revised disclosures, policies and procedures for originating and servicing mortgages including, but not limited to, pre-loan counseling, early intervention with delinquent borrowers and specific loss mitigation procedures for loans secured by a borrower s principal residence; (iii) comply with additional restrictions on mortgage loan originator hiring and compensation; (iv) comply with new disclosure requirements and standards for appraisals and certain financial products; and (v) maintain escrow accounts for higher-priced mortgage loans for a longer period of time.

The review of products and practices to prevent unfair, deceptive or abusive acts or practices (UDAAP) is a continuing focus of the CFPB, and of banking regulators more broadly. The ultimate impact of this heightened scrutiny is uncertain but could result in changes to pricing, practices, products and procedures. It could also result in increased costs related to regulatory oversight, supervision and examination, additional remediation efforts and possible penalties. In addition, the Dodd-Frank Act provides the CFPB with broad supervisory, examination and enforcement authority over various consumer financial products and services, including the ability to require reimbursements and other payments to customers for alleged violations of UDAAP and other legal requirements and to impose significant penalties, as well as injunctive relief that prohibits lenders from engaging in allegedly unlawful practices. The CFPB also has the authority to obtain cease and desist orders providing for affirmative relief or monetary penalties. The Dodd-Frank Act does not prevent states from adopting stricter consumer protection standards. State regulation of financial products and potential enforcement actions could also adversely affect the Bank s business, financial condition or results of operations.

The federal bank regulators have adopted rules limiting the ability of banks and other financial institutions to disclose non-public information about consumers to unaffiliated third parties. These limitations require disclosure of privacy policies to consumers and, in some circumstances, allow consumers to prevent disclosure of certain personal information to a nonaffiliated third party. These regulations affect how consumer information is transmitted through diversified financial companies and conveyed to outside vendors. In addition, consumers

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may also prevent disclosure of certain information among affiliated companies that is assembled or used to determine eligibility for a product or service, such as that shown on consumer credit reports and asset and income information from applications. Consumers also have the option to direct banks and other financial institutions not to share information about transactions and experiences with affiliated companies for the purpose of marketing products or services.

Under the Durbin Amendment to the Dodd-Frank Act, the Federal Reserve adopted rules establishing standards for assessing whether the interchange fees that may be charged with respect to certain electronic debit transactions are reasonable and proportional to the costs incurred by issuers for processing such transactions.

Interchange fees, or swipe fees, are charges that merchants pay to us and other card-issuing banks for processing electronic payment transactions. Under the final rules, the maximum permissible interchange fee is equal to no more than 21 cents plus 5 basis points of the transaction value for many types of debit interchange transactions. The Federal Reserve also adopted a rule to allow a debit card issuer to recover one cent per transaction for fraud prevention purposes if the issuer complies with certain fraud-related requirements required by the Federal Reserve. The Federal Reserve also has rules governing routing and exclusivity that require issuers to offer two unaffiliated networks for routing transactions on each debit or prepaid product.

Currently, we qualify for the small issuer exemption from the interchange fee cap, which applies to any debit card issuer that, together with its affiliates, has total assets of less than $10 billion as of the end of the previous calendar year. However, as a result of our acquisition of CB, we will become subject to the interchange fee cap beginning July 1, 2019. We do not expect the interchange fee cap to have a material impact on our noninterest income. Reliance on the small issuer exemption does not exempt us from federal regulations prohibiting network exclusivity arrangements or from routing restrictions, however.

Commercial Real Estate Concentration Limits

In December 2006, the federal banking regulators issued guidance entitled Concentrations in Commercial Real Estate Lending, Sound Risk Management Practices to address increased concentrations in commercial real estate, or CRE, loans. In addition, in December 2015, the federal bank agencies issued additional guidance entitled Statement on Prudent Risk Management for Commercial Real Estate Lending. Together, these guidelines describe the criteria the agencies will use as indicators to identify institutions potentially exposed to CRE concentration risk. An institution that has (i) experienced rapid growth in CRE lending, (ii) notable exposure to a specific type of CRE, (iii) total reported loans for construction, land development, and other land representing 100% or more of the institution s capital, or (iv) total CRE loans representing 300% or more of the institution s capital, and the outstanding balance of the institutions CRE portfolio has increased by 50% or more in the prior 36 months, may be identified for further supervisory analysis of the level and nature of its CRE concentration risk. As of December 31, 2018, the Bank s total CRE loans and unfunded loan commitments represented 289% of its capital.

Office of Foreign Assets Control Regulation

The U.S. Treasury Department s Office of Foreign Assets Control, or OFAC, administers and enforces economic and trade sanctions against targeted foreign countries and regimes, under authority of various laws, including designated foreign countries, nationals and others. OFAC publishes lists of specially designated targets and countries. We are responsible for, among other things, blocking accounts of, and transactions with, such targets and countries, prohibiting unlicensed trade and financial transactions with them and reporting blocked transactions after their occurrence. Failure to comply with these sanctions could have serious financial, legal and reputational consequences, including causing applicable bank regulatory authorities not to approve merger or acquisition transactions when regulatory approval is required or to prohibit such transactions even if approval is not required. Regulatory authorities have imposed cease and desist orders and civil money penalties against institutions found to be violating these obligations.

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Tax Cuts and Jobs Act of 2017 (the Tax Reform Act)

On December 22, 2017, the Tax Cuts and Jobs Act of 2017 (Tax Reform Act) was signed into law. The Tax Reform Act included a number of provisions that impact us, including the following:

Tax Rate. The Tax Reform Act replaces the corporate tax rates applicable under prior law, which imposed a maximum tax rate of 35%, with a reduced 21% tax rate for 2018. Although the reduced tax rate generally should be favorable to us by resulting in lower tax expense in future periods, it decreased the value of our existing deferred tax assets as of December 31, 2017. Generally accepted accounting principles (GAAP) requires that the impact of the provisions of the Tax Reform Act be accounted for in the period of enactment. Accordingly, the incremental income tax expense recorded by the Company in the fourth quarter of 2017 related to the Tax Reform Act was $13.2 million, resulting primarily from a re-measurement of deferred tax assets;

FDIC Insurance Premiums. The Tax Reform Act prohibits taxpayers with consolidated assets over $50 billion from deducting any FDIC insurance premiums and prohibits taxpayers with consolidated assets between $10 and $50 billion from deducting the portion of their FDIC premiums equal to the ratio, expressed as a percentage, that (i) the taxpayer s total consolidated assets over $10 billion, as of the close of the taxable year, bears to (ii) $40 billion;

Employee Compensation. A publicly held company is not permitted to deduct compensation in excess of $1 million per year paid to certain employees. The Tax Reform Act eliminates certain exceptions to the $1 million limit applicable under prior law related to performance-based compensation, such as equity grants and cash bonuses that are paid only on the attainment of performance goals. As a result, our ability to deduct certain compensation paid to our most highly compensated employees is limited; and

Business Asset Expensing. The Tax Reform Act allows taxpayers immediately to expense the entire cost (instead of only 50%, as under prior law) of certain depreciable tangible property and real property improvements acquired and placed in service after September 27, 2017 and before January 1, 2023 (with an additional year for certain property). This 100% bonus depreciation is phased out proportionately for property placed in service on or after January 1, 2023 and before January 1, 2027 (with an additional year for certain property).

The foregoing description of the impact of the Tax Reform Act on us should be read in conjunction with Note 12 *Income Taxes* of the notes to consolidated financial statements for more information.

Future Legislation and Regulation

Congress may enact, modify or repeal legislation from time to time that affects the regulation of the financial services industry, and state legislatures may enact, modify or repeal legislation from time to time affecting the regulation of financial institutions chartered by or operating in those states. Federal and state regulatory agencies also periodically propose and adopt changes to their regulations or change the manner in which existing regulations are applied. The substance or impact of pending or future legislation or regulation, or the application thereof, cannot be predicted, although enactment of proposed legislation (or modification or repeal of existing legislation) could impact the regulatory structure under which the Company and Bank operate and may significantly increase its costs, impede the efficiency of its internal business processes, require the Bank to increase its regulatory capital and modify its business strategy, and limit its ability to pursue business opportunities in an efficient manner. The Company s business, financial condition, results of operations or prospects may be adversely affected, perhaps materially.

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Available Information

Reports filed with the SEC include our proxy statements, annual reports on Form 10-K, quarterly reports on Form 10-Q and current reports on Form 8-K. The SEC maintains a website that contains the reports, proxy and information statements and other information we file with them. The address of the site is http://www.sec.gov. The Company also maintains an Internet website at http://www.cbbank.com. We make available, free of charge through our website, our Proxy Statement, Annual Report on Form 10-K, Quarterly Reports on Form 10-Q, and Current Reports on Form 8-K, and any amendments thereto, as soon as reasonably practicable after we file such reports with the SEC. None of the information contained in or hyperlinked from our website is incorporated into this Form 10-K.

Executive Officers of the Company

The following sets forth certain information regarding our executive officers, their positions and their ages.

Executive Officers:

Name	Position	Age
Christopher D. Myers	President and Chief Executive Officer of the Company and the Bank	56
E. Allen Nicholson	Chief Financial Officer of the Company and Executive Vice President and Chief Financial Officer of the Bank	51
David F. Farnsworth	Executive Vice President and Chief Credit Officer of the Bank	62
David A. Brager	Executive Vice President and Sales Division Manager of the Bank	51
David C. Harvey	Executive Vice President and Chief Operations Officer of the Bank	51
Richard H. Wohl	Executive Vice President and General Counsel	60
Yamynn DeAngelis	Executive Vice President and Chief Risk Officer	62

Mr. Myers assumed the position of President and Chief Executive Officer of the Company and the Bank on August 1, 2006. Prior to that, Mr. Myers served as Chairman of the Board and Chief Executive Officer of Mellon First Business Bank from 2004 to 2006. From 1996 to 2003, Mr. Myers held several management positions with Mellon First Business Bank, including Executive Vice President, Regional Vice President, and Vice President/Group Manager.

Mr. Nicholson was appointed Chief Financial Officer of the Company and Executive Vice President and Chief Financial Officer of the Bank on May 4, 2016. Previously, Mr. Nicholson served as Executive Vice President and Chief Financial Officer of Pacific Premier Bank and its holding company, Pacific Premier Bancorp Inc. from June of 2015 to May of 2016, and from 2008 to 2014, Mr. Nicholson was Chief Financial Officer of 1st Enterprise Bank. From 2005 to 2008, he was the Chief Financial Officer of Mellon First Business Bank.

Mr. Farnsworth was appointed Executive Vice President and Chief Credit Officer of the Bank on July 18, 2016. Prior to his appointment, Mr. Farnsworth was Executive Vice President, Global Risk Management, and National CRE Risk Executive at BBVA Compass. Previously, Mr. Farnsworth held senior credit management positions with US Bank and AmSouth.

Mr. Brager assumed the position of Executive Vice President and Sales Division Manager of the Bank on November 22, 2010. From 2007 to 2010, he served as Senior Vice President and Regional Manager of the Central Valley Region for the Bank. From 2003 to 2007, he served as Senior Vice President and Manager of the Fresno Business Financial Center for the Bank. From 1997 to 2003, Mr. Brager held management positions with Westamerica

Bank.

Mr. Harvey assumed the position of Executive Vice President and Chief Operations Officer of the Bank on December 31, 2009. From 2000 to 2008, he served as Senior Vice President and Operations Manager at Bank of the West. From 2008 to 2009 he served as Executive Vice President and Commercial and Treasury Services Manager at Bank of the West.

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Mr. Wohl was initially appointed Executive Vice President and General Counsel of the Company and the Bank on October 11, 2011, and he rejoined the Company and the Bank in the same position on July 10, 2017 after a one-year hiatus at another financial institution. Prior to his initial appointment in 2011, Mr. Wohl served in senior business and legal roles at Indymac Bank, the law firm of Morrison & Foerster, and the U.S. Department of State.

Ms. DeAngelis assumed the position of Executive Vice President and Chief Risk Officer of the Bank on January 5, 2009. From 2006 to 2008, she served as Executive Vice President and Service Division Manager for the Bank. From 1995 to 2005, she served as Senior Vice President and Division Service Manager for the Bank.

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ITEM 1A. *RISK FACTORS*

Risk Factors That May Affect Future Results Together with the other information on the risks we face and our management of risk contained in this Annual Report or in our other SEC filings, the following presents significant risks which may affect us. Events or circumstances arising from one or more of these risks could adversely affect our business, financial condition, operating results and prospects and the value and price of our common stock could decline. The risks identified below are not intended to be a comprehensive list of all risks we face, and additional risks that we may currently view as not material may also impair our business operations and results.

Strategic and External Risks

Changes in economic, market and political conditions can adversely affect our liquidity, results of operations and financial condition.

Our success depends, to a certain extent, upon local, national and global economic and political conditions, as well as governmental monetary policies. Conditions such as an economic recession, rising unemployment, changes in interest rates, money supply and other factors beyond our control may adversely affect our asset quality, deposit levels and loan demand and, therefore, our earnings. Because we have a significant amount of real estate loans, decreases in real estate values could adversely affect the value of property used as collateral. Adverse changes in the economy may also have a negative effect on the ability of our borrowers to make timely repayments of their loans, which could have an adverse impact on our earnings. In addition, we may face the following risks in connection with any downward turn in the economy:

- The process we use to estimate losses inherent in our credit exposure requires difficult, subjective and complex judgments, including forecasts of economic conditions and how these economic conditions might impair the ability of our borrowers to repay their loans. The level of uncertainty concerning economic conditions may adversely affect the accuracy of our estimates which may, in turn, impact the reliability of the process;

- The Company s commercial, residential and consumer borrowers may be unable to make timely repayments of their loans, or the decrease in value of real estate collateral securing the payment of such loans could result in significant credit losses, increasing delinquencies, foreclosures and customer bankruptcies, any of which could have a material adverse effect on the Company s operating results;

- A sustained environment of low interest rates would continue to cause lending margins to stay compressed, which in turn may limit our revenues and profitability;

- The value of the portfolio of investment securities that we hold may be adversely affected by increasing interest rates and defaults by debtors;

- Further disruptions in the capital markets or other events, including actions by rating agencies and deteriorating investor expectations, may result in changes in applicable rates of interest, difficulty in accessing capital or an inability to borrow on favorable terms or at all from other financial institutions;

and

Increased competition among financial services companies due to expected further consolidation in the industry may adversely affect the Company s ability to market its products and services.

Although the Company and the Bank exceed the minimum capital ratio requirements to be deemed well capitalized for regulatory purposes and have not suffered any significant liquidity issues as a result of these types of events, the cost and availability of funds may be adversely affected by illiquid credit markets and the demand for our products and services may decline as our borrowers and customers continue to realize the impact of

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slower than customary economic growth, after-effects of the previous recession and ongoing underemployment of the workforce. In view of the concentration of our operations and the collateral securing our loan portfolio in Central and Southern California, we may be particularly susceptible to adverse economic conditions in the state of California, where our business is concentrated. In addition, adverse economic conditions may exacerbate our exposure to credit risk and adversely affect the ability of borrowers to perform, and thereby, adversely affect our liquidity, financial condition, results or operations and profitability.

Our earnings are significantly affected by the fiscal and monetary policies of the federal government and its agencies.

The policies of the Federal Reserve impact us significantly. Its policies directly and indirectly influence the rate of interest earned on loans and paid on borrowings and interest-bearing deposits and can also affect the value of financial instruments we hold. Changes in those policies are beyond our control and are difficult to predict. Federal Reserve policies can also affect our borrowers, potentially increasing the risk that they may fail to repay their loans. As an example, monetary tightening by the Federal Reserve could adversely affect our borrowers earnings and ability to repay their loans, which could have a material adverse effect on our financial condition and results of operations. In addition, the Federal Reserve s recent actions to reduce its own balance sheet of government and mortgage-backed securities could impact the credit markets and thus prevailing interest rates.

Future legislation, regulatory reform or policy changes under the current U.S. administration could have a material effect on our business and results of operations.

New legislation, regulatory reform or policy changes under the current U.S. administration, including financial services regulatory reform, U.S. oil deregulation, tax reform, government-sponsored enterprise (GSE) reform and increased infrastructure spending, could impact our business. At this time, we cannot predict the scope or nature of these changes or assess what the overall effect of such potential changes could be on our results of operations or cash flows.

We face strong competition from financial services companies and other companies that offer banking services

We conduct most of our operations in the state of California. The banking and financial services businesses in the state of California are highly competitive and increased competition in our primary market area may adversely impact the level of our loans and deposits. Ultimately, we may not be able to compete successfully against current and future competitors. These competitors include national banks, regional banks and other community banks. We also face competition from many other types of financial institutions, including savings and loan associations, finance companies, brokerage firms, insurance companies, credit unions, mortgage companies and other financial intermediaries. In addition, as noted below, we face competition from certain non-traditional entities, including so called FinTech companies which specialize in the provision of technology-based financial services, such as payment processing and lending marketplaces, and which may offer or be perceived to offer more responsive or currently desirable financial products and services.

In particular, our competitors include major financial companies whose greater resources may afford them a marketplace advantage by enabling them to offer products at lower costs, maintain numerous locations, and mount extensive promotional and advertising campaigns. Areas of competition include interest rates for loans and deposits, efforts to obtain loan and deposit customers and a range in quality of products and services provided, including new technology driven products and services. If we are unable to attract and retain banking customers, we may be unable to continue our loan growth and level of deposits.

Potential acquisitions may disrupt our business and dilute shareholder value

We generally seek merger or acquisition partners that are culturally similar and have experienced management and possess either significant market presence or have potential for improved profitability through

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financial management, economies of scale or expanded services. Acquiring other banks, businesses, or branches including our recently completed acquisition of Community Bank, involves various risks commonly associated with acquisitions, including, among other things:

- Potential exposure to unknown or contingent liabilities of the target company;
- Exposure to potential asset quality issues of the target company;
- Potential disruption to our business;
- Potential diversion of our management s time and attention;
- The possible loss of key employees and customers of the target company;
- Difficulty in estimating the value of the target company; and
- Potential changes in banking or tax laws or regulations that may affect the target company.

Acquisitions typically involve the payment of a premium over book and market values, and, therefore, some dilution of our tangible book value and net income per common share may occur in connection with any future transaction. Furthermore, failure to realize the expected revenue increases, cost savings, increases in geographic or product presence, and/or other projected benefits from an acquisition could have a material adverse effect on our business, financial condition and results of operations.

Consumers may decide not to use banks to complete their financial transactions.

Technology and other changes are allowing parties to complete financial transactions through alternative methods that historically have involved banks. For example, consumers can now maintain funds that would have historically been held as bank deposits in brokerage accounts, mutual funds or general-purpose reloadable prepaid cards. Consumers can also complete transactions, such as paying bills and/or transferring funds directly without the assistance of banks. The process of eliminating banks as intermediaries, known as disintermediation, could result in the loss of fee income, as well as the loss of customer deposits and the related income generated from those deposits. The loss of these revenue streams and the lower cost of deposits as a source of funds could have a material adverse effect on our financial condition and results of operations.

Credit Risks

Our allowance for loan losses may not be sufficient to cover actual losses

A significant source of risk arises from the possibility that we could sustain losses because borrowers, guarantors, and related parties may fail to perform in accordance with the terms of their loans and leases. The underwriting and credit monitoring policies and procedures that we have adopted to address this risk may not prevent unexpected losses that could have a material adverse effect on our business, financial condition, results of operations and cash flows. We maintain an allowance for loan losses to provide for loan and lease defaults and non-performance, which also includes increases for new loan growth. While we believe that our allowance for loan losses is appropriate to cover inherent losses, we cannot assure you that we will not increase the allowance for loan losses further or that regulators will not require us to increase this allowance.

We may be required to make additional provisions for credit losses and charge-off additional loans in the future, which could adversely affect our results of operations

For the year ended December 31, 2018, we recorded $1.5 million in loan loss provision. During 2018 we experienced charge-offs of $291,000 and recoveries of $2.8 million. Because we have a significant amount of real estate loans, decreases in real estate values could adversely affect the value of property used as collateral. As of December 31, 2018, we had $5.41 billion in commercial real estate loans, $122.8 million in construction loans, $394.5 million in dairy & livestock and agribusiness loans, and $296.6 million in single-family residential mortgages. Although the U.S. economy has emerged from a prior period of severe recession followed by slower than normal growth, business activity and real estate values continue to grow more slowly than in past economic recoveries, and may not recover fully or could again decline from current levels, and this in turn could affect the ability of our loan customers to service their debts, including those customers whose loans are secured by commercial or residential real estate. This, in turn, could result in loan charge-offs and provisions for credit losses in the future, which could have a material adverse effect on our financial condition, net income and capital. In addition, the Federal Reserve Board and other government officials have expressed concerns about banks concentration in commercial real estate lending and the ability of commercial real estate borrowers to perform pursuant to the terms of their loans.

Dairy & livestock and agribusiness lending presents unique credit risks.

As of December 31, 2018, approximately 5.1% of our total gross loan portfolio was comprised of dairy & livestock and agribusiness loans. As of December 31, 2018, we had $394.5 million in dairy & livestock and agribusiness loans, including $340.5 in dairy & livestock loans, $54.0 million in agribusiness loans. Repayment of dairy & livestock and agribusiness loans depends primarily on the successful raising and feeding of livestock or planting and harvest of crops and marketing the harvested commodity (including milk production). Collateral securing these loans may be illiquid. In addition, the limited purpose of some agricultural -related collateral affects credit risk because such collateral may have limited or no other uses to support values when loan repayment problems emerge. Our dairy & livestock and agribusiness lending staff have specific technical expertise that we depend on to mitigate our lending risks for these loans and we may have difficulty retaining or replacing such individuals. Many external factors can impact our agricultural borrowers ability to repay their loans, including adverse weather conditions, water issues, commodity price volatility (i.e. milk prices), diseases, land values, production costs, changing government regulations and subsidy programs, changing tax treatment, technological changes, labor market shortages/increased wages, and changes in consumers preferences, over which our borrowers may have no control. These factors, as well as recent volatility in certain commodity prices, including milk prices, could adversely impact the ability of those to whom we have made dairy & livestock and agribusiness loans to perform under the terms of their borrowing arrangements with us, which in turn could result in credit losses and adversely affect our business, financial condition and results of operations.

The FASB has recently issued an accounting standard update that will result in a significant change in how we recognize credit losses and may have a material impact on our financial condition or results of operations.

In June 2016, the Financial Accounting Standards Board (FASB) issued an accounting standard update, Financial Instruments-Credit Losses (Topic 326), Measurement of Credit Losses on Financial Instruments, which replaces the current incurred loss model for recognizing credit losses with an expected loss model referred to as the Current Expected Credit Loss (CECL) model. Under the CECL model, we will be required to present certain financial assets carried at amortized cost, such as loans held for investment and held-to-maturity debt securities, at the net amount expected to be collected. The measurement of expected credit losses is to be based on information about past events, including historical experience, current conditions, and reasonable and supportable forecasts that affect the collectability of the reported amount. This measurement will take place at the time the financial asset is first added to the balance sheet and periodically thereafter. This differs significantly from the incurred loss model required under current generally accepted accounting principles (GAAP), which delays recognition until it is probable a loss has been incurred. Accordingly, we expect that the adoption of the CECL model will materially affect how we determine our allowance for loan losses and could require us to significantly increase our allowance. Moreover, the CECL model may create more volatility in the level of our allowance for loan losses. If we are required to materially increase our level of allowance for loan losses for any reason, such increase could adversely affect our business, financial condition and results of operations.

The new CECL standard will become effective for us for fiscal years beginning after December 15, 2019 and for interim periods within those fiscal years. We are currently evaluating the impact the CECL model will have on our accounting, but we expect to recognize a one-time cumulative-effect adjustment to our allowance for loan losses as of the beginning of the first reporting period in which the new standard is effective, consistent with regulatory expectations set forth in interagency guidance issued at the end of 2016. Under the final interagency rule released on December, 21, 2018, banking organizations that experience a reduction in retained earnings due to the adoption of CECL at the beginning of the fiscal year in which it is adopted may elect to phase in the regulatory capital impact of adopting CECL over a three-year transition period. We cannot yet determine the magnitude of any such one-time cumulative adjustment or of the overall impact of the new standard on our financial condition or results of operations.

Our loan portfolio is predominantly secured by real estate and thus we have a higher degree of risk from a downturn in our real estate markets

A renewed downturn in our real estate markets could hurt our business because many of our loans are secured by real estate. Real estate values and real estate markets are generally affected by changes in national, regional or local economic conditions, fluctuations in interest rates and the availability of loans to potential purchasers, changes in tax laws and other governmental statutes, regulations and policies, and acts of nature, such as earthquakes, prolonged drought and disasters particular to California. Substantially all of our real estate collateral is located in the state of California. If real estate values, including values of land held for development, should again start to decline, the value of real estate collateral securing our loans could be significantly reduced. Our ability to recover on defaulted loans by foreclosing and selling the real estate collateral would then be diminished and we would be more likely to suffer losses on defaulted loans. Commercial real estate loans typically involve large balances to single borrowers or a group of related borrowers. Since payments on these loans are often dependent on the successful operation or management of the properties, as well as the business and financial condition of the borrower(s), repayment of such loans may be subject to adverse conditions in the real estate market, adverse economic conditions or changes in applicable government regulations.

Additional risks associated with our real estate construction loan portfolio include failure of developers and/or contractors to complete construction on a timely basis or at all, market deterioration during construction, cost overruns and failure to sell or lease the security underlying the construction loans so as to generate the cash flow anticipated by our borrower.

A decline in the economy may cause renewed declines in real estate values and increases in unemployment, which may result in higher than expected loan delinquencies or problem assets, a decline in demand for our products and services, or a lack of growth or decrease in deposits, which may cause us to incur losses, adversely affect our capital or hurt our business.

Our commercial real estate loan portfolio exposes us to risks that may be greater than the risks related to our other loans

Federal and state banking regulators are examining commercial real estate lending activity with heightened scrutiny and may require banks with higher levels of commercial real estate loans to implement more stringent underwriting, internal controls, risk management policies and portfolio stress testing, as well as possibly higher levels of allowances for losses and capital levels as a result of commercial real estate lending growth and exposures. Because a significant portion of our loan portfolio is comprised of commercial real estate loans, the banking regulators may require us to maintain higher levels of capital than we would otherwise be expected to maintain, which could limit our ability to leverage our capital and have a material adverse effect on our business, financial condition, results of operations and prospects.

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

In the course of our business, we may foreclose and take title to real estate, and could be subject to environmental liabilities with respect to these properties. While we will take steps to mitigate this risk, we may be held liable to a governmental entity or to third parties for property damage, personal injury, investigation and clean-up costs incurred by these parties in connection with environmental contamination, or we may be required to investigate or clean-up hazardous or toxic substances, or chemical releases at one or more properties. The costs associated with investigation or remediation activities could be substantial. In addition, while there are certain statutory protections afforded lenders who take title to property through foreclosure on a loan, if we are the owner or former owner of a contaminated site, we may be subject to common law claims by third parties based on damages and costs resulting from environmental contamination emanating from the property. If we become subject to significant environmental liabilities, our business, financial condition, results of operations and prospects could be adversely affected.

Liquidity risk could impair our ability to fund operations and jeopardize our financial condition

Liquidity is essential to our business. An inability to raise funds through deposits, borrowings, the sale of loans and other sources could have a material adverse effect on our liquidity. Our access to funding sources in amounts adequate to finance our activities could be impaired by factors that affect us specifically or the financial services industry in general. Factors that could detrimentally impact our access to liquidity sources include a decrease in the level of our business activity due to a market downturn or adverse regulatory action against us. Our ability to acquire deposits or borrow could also be impaired by factors that are not specific to us, such as a severe disruption of the financial markets or negative views and expectations about the prospects for the financial services industry as a whole. Many if not all of these same factors could also significantly raise the cost of deposits to our Company and/or to the banking industry in general. This in turn could negatively affect the amount of interest we pay on our interest-bearing liabilities, which could have an adverse impact on our interest rate spread and profitability.

The actions and commercial soundness of other financial institutions could affect our ability to engage in routine funding transactions

Financial service institutions are interrelated as a result of trading, clearing, counterparty or other relationships. We have exposure to different industries and counterparties, and execute transactions with various counterparties in the financial industry, including brokers and dealers, commercial banks, investment banks, mutual funds, and other institutional clients. Defaults by financial services institutions, even rumors or questions about one or more financial institutions or the financial services industry in general, could lead to market wide liquidity problems and further, could lead to losses or defaults by the Company or other institutions. Many of these transactions expose us to credit risk in the event of default of the applicable counterparty or client. In addition, our credit risk may increase when the collateral held by us cannot be realized upon or is liquidated at prices not sufficient to recover the full amount of the loan or derivative exposure due to us. Any such losses could materially and adversely affect our consolidated financial statements.

Changes in interest rates could reduce the value of our investment securities holdings.

The Bank maintains an investment portfolio consisting of various high quality liquid fixed-income securities. The total book value of the securities portfolio as of December 31, 2018 was $2.48 billion, of which $1.73 billion is available for sale. The nature of fixed-income securities is such that changes in market interest rates impact the value of these assets.

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

A substantial portion of our income is derived from the differential or spread between the interest earned on loans, securities and other interest-earning assets, and the interest paid on deposits, borrowings and other interest-bearing liabilities. Because of the differences in the maturities and repricing characteristics of our interest-earning assets and interest-bearing liabilities, changes in interest rates do not produce equivalent changes in interest income earned on interest-earning assets and interest paid on interest-bearing liabilities. At December 31, 2018 our balance sheet was positioned with an asset sensitive bias over both a one and two-year horizon assuming no balance sheet growth, and as a result, our net interest margin tends to expand in a rising interest rate environment and decrease in a declining interest rate environment. Accordingly, fluctuations in interest rates could adversely affect our interest rate spread and, in turn, our profitability. In addition, loan origination volumes are affected by market interest rates. Rising interest rates, generally, are associated with a lower volume of loan originations while lower interest rates are usually associated with higher loan originations. Conversely, in rising interest rate environments, loan repayment rates may decline and in falling interest rate environments, loan repayment rates may increase. In addition, in a rising interest rate environment, we may need to accelerate the pace of rate increases on our deposit accounts as compared to the pace of future increases in short-term market rates. Accordingly, changes in levels of market interest rates could materially and adversely affect our net interest spread, asset quality, as well as loan origination and prepayment volume.

We may be adversely impacted by the transition from LIBOR as a reference rate

In 2017, the United Kingdom s Financial Conduct Authority announced that after 2021 it would no longer compel banks to submit the rates required to calculate the London Interbank Offered Rate (**LIBOR**). This announcement indicates that the continuation of LIBOR on the current basis cannot and will not be guaranteed after 2021. Consequently, at this time, it is not possible to predict whether and to what extent banks will continue to provide submissions for the calculation of LIBOR. Similarly, it is not possible to predict whether LIBOR will continue to be viewed as an acceptable market benchmark, what rate or rates may become accepted alternatives to LIBOR or what the effect of any such changes in views or alternatives may be on the markets for LIBOR-indexed financial instruments.

We have a number of loans, derivative contracts, borrowings and other financial instruments with attributes that are either directly or indirectly dependent on LIBOR. The transition from LIBOR could create additional costs and risk. Since proposed alternative rates are calculated differently, payments under contracts referencing new rates will differ from those referencing LIBOR. The transition could change our market risk profiles, requiring changes to risk and pricing models, valuation tools, product design and hedging strategies. Furthermore, failure to adequately manage this transition process with our customers could adversely impact our reputation. Although we are currently unable to assess what the ultimate impact of the transition from LIBOR will be, failure to adequately manage the transition could have a material adverse effect on our business, financial condition and results of operations.

We will be subject to additional regulatory scrutiny following our acquisition of CB.

Following our acquisition of CB in the third quarter of 2018, our total assets exceeded $10 billion. As a result, we will be subject to a number of additional regulatory requirements, including general oversight by the CFPB, that will impose additional compliance costs on our business. The $10 billion threshold is calculated in different ways for the various requirements (from simply reaching the $10 billion as of a certain date, to reaching it for four consecutive quarters or to reaching it by averaging total consolidated assets for four consecutive quarters) and the dates the new requirements are triggered also vary (from immediate application to a period of over two years to achieve compliance). Being subject to these additional requirements may also result in higher expectations from regulators. The CFPB has near exclusive supervision authority, including examination authority, over institutions of that size and their affiliates to assess compliance with federal consumer financial laws, to obtain information about the institutions activities and compliance systems and procedures, and to detect and assess risks to consumers and markets.

Under the Dodd-Frank Act, our assessment base for federal deposit insurance will change from the amount of insured deposits to consolidated average assets less tangible capital to a scorecard method. The scorecard method uses a performance score and a loss severity score, which are combined and converted into an initial base assessment rate. The performance score is based on measures of the bank s ability to withstand asset-related stress and funding-related stress and weighted CAMELS ratings, which are ratings ascribed under the CAMELS supervisory rating system and assigned based on a supervisory authority s analysis of a bank s financial statements and on-site examinations. The loss severity score is a measure of potential losses to the FDIC in the event of the bank s failure. Under a formula, the performance score and loss severity score are combined and converted to a total score that determines the bank s initial base assessment rate. The FDIC has the discretion to alter the total score based on factors not captured by the scorecard. The resulting initial base assessment rate is also subject to adjustments downward based on long term unsecured debt issued by the bank, to adjustment upward based on long term unsecured debt held by the bank that is issued by other FDIC-insured institutions, and to further adjustment upward if the bank s brokered deposits exceed 10% of its domestic deposits.

In addition, all financial institutions with total assets exceeding $10 billion are required to centrally clear their derivative trades through a central clearing house. This requirement will become effective for CBB at the end of 2018 and will affect trades designated as clearable transactions. This regulatory requirement will impose additional compliance costs on our business.

Further, we will be affected by the Durbin Amendment to the Dodd-Frank Act regarding limits on debit card interchange fees. The Durbin Amendment gave the FRB the authority to establish rules regarding interchange fees charged for electronic debit transactions by a payment card issuer that, together with its affiliates, has assets of $10 billion or more and to enforce a new statutory requirement that such fees be reasonable and proportional to the actual cost of a transaction to the issuer. The FRB has adopted rules under this provision that limit the swipe fees that a debit card issuer can charge a merchant for a transaction to the sum of 21 cents and five basis points times the value of the transaction, plus up to one cent for fraud prevention costs.

As a result of the above, deposit insurance assessments and expenses related to regulatory compliance are likely to increase, and interchange fee income will decrease, the cumulative effect of which may be material to our results of operations.

We may experience goodwill impairment

If our estimates of fair value change due to changes in our businesses or other factors, we may determine that impairment charges on goodwill recorded as a result of acquisitions are necessary. Estimates of fair value are determined based on a complex model using cash flows, the fair value of our Company as determined by our stock price, and company comparisons. If management s estimates of future cash flows are inaccurate, fair value determined could be inaccurate and impairment may not be recognized in a timely manner. If the fair value of the Company declines, we may need to recognize goodwill impairment in the future which would have a material adverse effect on our results of operations and capital levels.

Our accounting estimates and risk management processes rely on analytical and forecasting models

The processes we use to estimate our inherent loan losses and to measure the fair value of financial instruments, as well as the processes used to estimate the effects of changing interest rates and other market measures on our financial condition and results of operations, depends upon the use of analytical and forecasting models. These models reflect assumptions that may not be accurate, particularly in times of market stress or other unforeseen circumstances. Even if these assumptions are adequate, the models may prove to be inadequate or inaccurate because of other flaws in their design or their implementation. If the models we use for interest rate risk and asset-liability management are inadequate, we may incur increased or unexpected losses upon changes in market interest rates or other market measures. If the models we use for determining our probable loan losses are inadequate, the allowance for loan losses may not be sufficient to support future charge-offs. If the models we use to measure the fair value of financial instruments are inadequate, the fair value of such financial instruments may fluctuate unexpectedly or may not accurately reflect what we could realize upon sale or settlement of such financial instruments. Any such failure in our analytical or forecasting models could have a material adverse effect on our business, financial condition and results of operations.

Our decisions regarding the fair value of assets acquired could be different than initially estimated, which could materially and adversely affect our business, financial condition, results of operations, and future prospects

In business combinations, we acquire significant portfolios of loans that are marked to their estimated fair value. There is no assurance that the acquired loans will not suffer deterioration in value. The fluctuations in national, regional and local economic conditions, including those related to local residential, commercial real estate and construction markets, may increase the level of charge-offs in the loan portfolio that we acquire and correspondingly reduce our net income. These fluctuations are not predictable, cannot be controlled and may have a material adverse impact on our operations and financial condition, even if other favorable events occur.

Our combination with CB may be more difficult, costly or time-consuming than expected

Realizing the anticipated benefits of the acquisition of CB will depend, in part, on our ability to successfully combine the businesses of the Bank and CB. Although we completed the merger in August 2018, it is still possible that the ongoing integration process could result in:

- the loss of key employees;
- the disruption of our ongoing businesses, including from planned branch consolidation; or
- inconsistencies in standards, controls, procedures and policies that adversely affect our ability to maintain relationships with clients, customers, depositors and employees or to achieve the anticipated benefits of the merger.

If we experience difficulty with the integration process, the anticipated benefits of the merger may not be realized fully or at all, or may take longer to realize than expected. As with any merger of financial institutions, there also may be business disruptions that cause us to lose customers or cause customers to remove their accounts and move their business to competing financial institutions. These integration matters could have a material adverse effect on us for an undetermined period after consummation of the merger.

We may fail to fully realize cost savings from our acquisition of CB

Although we expect to realize cost savings from the merger when fully phased in, it is possible that these potential cost savings may not be fully realized, or may take longer to realize than expected. For example, future business developments may require us to continue to operate or maintain some facilities or support functions that we expected to be combined or reduced. Cost savings also depend on our ability to successfully combine our businesses in a manner that permits those costs savings to be realized. If we are not able to combine the two companies successfully, these anticipated cost savings may not be fully realized or realized at all, or may take longer to realize than expected. This in turn could reduce or otherwise adversely affect our profitability and our stock price.

Operational Risks

Failure to manage our growth may adversely affect our performance

Our financial performance and profitability depend on our ability to manage past and possible future growth, including the significant growth we experienced following the acquisition of CB. Future acquisitions and our continued growth may present operating, integration, regulatory, management and other issues that could have a material adverse effect on our business, financial condition, results of operations and cash flows.

The occurrence of fraudulent activity, breaches or failures of our information security controls or cybersecurity-related incidents could have a material adverse effect on our business, financial condition and results of operations

As a financial institution, we are susceptible to fraudulent activity, information security breaches and cybersecurity-related incidents that may be committed against us or our clients, which may result in financial losses or increased costs to us or our clients, disclosure or misuse of our information or our client information, misappropriation of assets, privacy breaches against our clients, litigation, or damage to our reputation. Such fraudulent activity may take many forms, including check fraud, electronic fraud, wire fraud, on-line banking, takeover, phishing, social engineering and other dishonest acts. Information security breaches and cybersecurity-related incidents may include fraudulent or unauthorized access to systems used by us or our clients, denial or degradation of service attacks, and malware or other cyber-attacks. There continues to be a rise in electronic fraudulent activity, security breaches and cyber-attacks within the financial services industry, especially in the commercial banking sector due to cyber criminals targeting commercial bank accounts. In recent periods, several large corporations, including financial institutions, medical providers and retail companies, have suffered major data breaches, in some cases exposing not only confidential and proprietary corporate information, but also sensitive financial and other personal information of their customers and employees and subjecting them to potential fraudulent activity. Some of our clients may have been affected by these breaches, which increase their risks of identity theft, credit card fraud and other fraudulent activity that could involve their accounts with us.

Information pertaining to us and our clients is maintained, and transactions are executed, such as our online banking or core systems on the networks and systems of ours, our clients and certain of our third party providers. The secure maintenance and transmission of confidential information, as well as execution of transactions over these systems, are essential to protect us and our clients against fraud and security breaches and to maintain our clients confidence. In addition, increases in criminal activity levels and sophistication, advances in computer capabilities, new discoveries, vulnerabilities in third-party technologies (including browsers and operating systems) or other developments could result in a compromise or breach of the technology, processes and controls that we use to prevent fraudulent transactions and to protect data about us, our clients and underlying transactions, as well as the technology used by our clients to access our systems. Although we continue to invest in systems and processes that are designed to detect and prevent security breaches and cyber-attacks and periodically test our security, our inability to anticipate, or failure to adequately mitigate, breaches of security could result in: losses to us or our clients; our loss of business and/or clients; damage to our reputation; the incurrence of additional expenses; disruption to our business; our inability to grow our online services or other businesses; additional regulatory scrutiny or penalties; or our exposure to civil litigation and possible financial liability any of which could have a material adverse effect on our business, financial condition and results of operations.

More generally, continued publicized information concerning security and cyber-related problems could inhibit the use or growth of electronic or web-based applications or solutions as a means of conducting commercial transactions for us and other financial institutions. Such publicity may also cause damage to our reputation as a financial institution. As a result, our business, financial condition and results of operations could be adversely affected.

Our business is exposed to the risk of changes in technology

The rapid pace of technology changes and the impact of such changes on financial services generally and on our Company specifically could impact our cost structure and our competitive position with our customers. Such developments include the rapid movement by customers and some competitor financial institutions to web-based services, mobile banking and cloud computing. Our failure or inability to anticipate, plan for or implement technology change could adversely affect our competitive position, financial condition and profitability.

Our controls and procedures could fail or be circumvented

Management regularly reviews and updates our internal controls, disclosure controls and procedures and corporate governance policies and procedures. Any system of controls, however well designed and operated, is based in part on certain assumptions and on the conduct of individuals, and can provide only reasonable, but not absolute, assurances of the effectiveness of these systems and controls, and that the objectives of these controls have been met. Any failure or circumvention of our controls and procedures, and any failure to comply with regulations related to controls and procedures could adversely affect our business, results of operations and financial condition.

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Failure to maintain effective internal control over financial reporting or disclosure controls and procedures could adversely affect our ability to report our financial condition and results of operations accurately and on a timely basis

A failure to maintain effective internal control over financial reporting or disclosure controls and procedures could adversely affect our ability to report our financial results accurately and on a timely basis, which could result in a loss of investor confidence in our financial reporting or adversely affect our access to sources of liquidity. Furthermore, because of the inherent limitations of any system of internal control over financial reporting, including the possibility of human error, the circumvention or overriding of controls and fraud, even effective internal controls may not prevent or detect all misstatements.

We rely on communications, information, operating and financial control systems technology from third-party service providers, and we may suffer an interruption in those systems

We rely heavily on third-party service providers for much of our communications, information, operating and financial control systems technology, including our internet banking services and data processing systems. Any failure or interruption of these services or systems or breaches in the security of these systems could result in failures or interruptions to serve our customers, including deposit, servicing and/or loan origination systems. The occurrence of any failures or interruptions may require us to identify alternative sources of such services, which may result in increased costs or other consequences that in turn could have an adverse effect on our business, including damage to the Bank s reputation.

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

Competition for qualified employees and personnel in the banking industry is intense and there are a limited number of qualified persons with knowledge of, and experience in, the California community banking industry. The process of recruiting personnel with the combination of skills and attributes required to carry out our strategies is often lengthy. In addition, legislation and regulations which impose restrictions on executive compensation may make it more difficult for us to retain and recruit key personnel. Our success depends to a significant degree upon our ability to attract and retain qualified management, loan origination, finance, administrative, risk management, marketing and technical personnel and upon the continued contributions of our management and personnel. In particular, our success has been and continues to be highly dependent upon the abilities of key executives, including our President and Chief Executive Officer, and certain other employees.

Legal, Regulatory, Compliance and Reputational Risks

We are subject to extensive government regulation that could limit or restrict our activities, which, in turn, may hamper our ability to increase our assets and earnings

Our operations are subject to extensive regulation by federal, state and local governmental authorities and we are subject to various laws and judicial and administrative decisions imposing requirements and restrictions on part or all of our operations. Similarly, the lending, credit and deposit products we offer are subject to broad oversight and regulation. Because our business is highly regulated, the laws, rules, regulations and supervisory guidance and policies applicable to us are subject to regular modification and change. Perennially, various laws, rules and regulations are proposed, which, if adopted, could impact our operations by making compliance much more difficult or expensive, restricting our ability to originate or sell loans or further restricting the amount of interest or other charges or fees earned on loans or other products. Current and future legal and regulatory requirements, restrictions and regulations, including those imposed under Dodd-Frank, may adversely impact our profitability and may have a material and adverse effect on our business, financial condition, and results of operations, may require us to invest significant management attention and resources to evaluate and make any changes required by the legislation and accompanying rules, and may make it more difficult for us to attract and retain qualified executive officers and employees. The implementation of certain final Dodd-Frank rules is delayed or phased in over several years; therefore, as yet we cannot definitively assess what may be the short or longer term specific or aggregate effect of the full implementation of Dodd-Frank on us.

We face a risk of noncompliance and enforcement action with the Bank Secrecy Act and other anti-money laundering statutes and regulations

The Bank Secrecy Act, the USA PATRIOT Act of 2001, and other laws and regulations require financial institutions, among other duties, to institute and maintain an effective anti-money laundering program and file suspicious activity and currency transaction reports as appropriate. The federal Financial Crimes Enforcement Network is authorized to impose significant civil money penalties for violations of those requirements and has recently engaged in coordinated enforcement efforts with the individual federal banking regulators, as well as the U.S. Department of Justice, Drug Enforcement Administration, and Internal Revenue Service. We are also subject to scrutiny of compliance with the rules enforced by the Office of Foreign Assets Control and compliance with the Foreign Corrupt Practices Act. If our policies, procedures and systems are deemed deficient, we would be subject to liability, including fines and regulatory actions, which may include restrictions on our ability to pay dividends and the necessity to obtain regulatory approvals to proceed with certain aspects of our business plan. Failure to maintain and implement adequate programs to combat money laundering and terrorist financing could also have serious reputational consequences for us. Any of these results could materially and adversely affect our business, financial condition and results of operations.

Mortgage regulations may adversely impact our business

Revisions made pursuant to Dodd-Frank to Regulation Z, which implements the Truth in Lending Act (TILA), effective in January 2014, apply to all consumer mortgages (except home equity lines of credit, timeshare plans, reverse mortgages, or temporary loans), and mandate specific underwriting criteria and ability to repay requirements for home loans. This may impact our offering and underwriting of single family residential loans in our residential mortgage lending operation and could have a resulting unknown effect on potential delinquencies. In addition, the relatively uniform requirements may make it difficult for regional and community banks to compete against the larger national banks for single family residential loan originations.

The impact of new capital rules will impose enhanced capital adequacy requirements on us and may materially affect our operations

We are subject to more stringent capital requirements. Pursuant to Dodd-Frank and to implement for U.S. banking institutions the principles of the international Basel III standards, the federal banking agencies have adopted a set of rules on minimum leverage and risk-based capital that will apply to both insured banks and their holding companies. These regulations were issued in July 2013, and have been phased in for the Bank and the Company beginning in 2016. The new capital rules, among other things:

- impose more restrictive eligibility requirements for Tier 1 and Tier 2 capital;

- introduce a new category of capital, called Common Equity Tier 1 capital, which must be at least 4.5% of risk-based assets, net of regulatory deductions, and a capital conservation buffer of an additional 2.5% of common equity to risk-weighted assets, raising the target minimum common equity ratio to 7%;

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

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

- introduce a non-risk adjusted Tier 1 leverage ratio of 3%, based on a measure of total exposure rather than total assets, and new liquidity standards.

The full implementation of the new capital rule may adversely affect our ability to pay dividends, or require us to reduce business levels or raise capital, including in ways that may adversely affect our business, liquidity, financial condition and results of operations.

The new Basel III-based capital standards could limit our ability to pay dividends or make stock repurchases and our ability to compensate our executives with discretionary bonuses. Under the new capital standards, if our Common Equity Tier 1 Capital does not include a newly required capital conservation buffer, we will be prohibited from making distributions to our stockholders. The capital conservation buffer requirement, which is measured in addition to the minimum Common Equity Tier 1 capital of 4.5%, was phased in over four years, starting at 0.625% for 2016, and is now 2.5% for 2019 and subsequent years. Additionally, under the new capital standards, if our Common Equity Tier 1 Capital does not include the newly required capital conservation buffer, we will also be prohibited from paying discretionary bonuses to our executive employees. This may affect our ability to attract or retain employees, or alter the nature of the compensation arrangements that we may enter into with them.

Managing reputational risk is important to attracting and maintaining customers, investors and employees

Threats to our reputation can come from many sources, including adverse sentiment about financial institutions generally, unethical practices, employee mistakes, misconduct or fraud, failure to deliver minimum standards of service or quality, failure of any product or service offered by us to meet our customers expectations, compliance deficiencies, government investigations, litigation, and questionable or fraudulent activities of our customers. We have policies and procedures in place to protect our reputation and promote ethical conduct, but these policies and procedures may not be fully effective. Negative publicity regarding our business, employees, or customers, with or without merit, may result in the loss of customers, investors and employees, costly litigation, a decline in revenues and increased governmental scrutiny and regulation.

We are subject to legal and litigation risk which could adversely affect us

Because our Company is extensively regulated by a variety of federal and state agencies, and because we are subject to a wide range of business, consumer and employment laws and regulations at the federal, state and local levels, we are at risk of governmental investigations and lawsuits as well as claims and litigation from private parties. We are from time to time involved in disputes with and claims from investors, customers, government agencies, vendors, employees and other business parties, and such disputes and claims may result in litigation or settlements, any one of which or in the aggregate could have an adverse impact on the Company s operating flexibility, employee relations, financial condition or results of operations, as a result of the costs of any judgment, the terms of any settlement and/or the expenses incurred in defending the applicable claim.

We are unable, at this time, to estimate our potential liability in these matters, but we may be required to pay judgments, settlements or other penalties and incur other costs and expenses in connection with any one or more of these lawsuits, which in turn could have a material adverse effect on our business, results of operations and financial condition. In addition, responding to requests for information in connection with discovery demanded by the plaintiffs in any of these lawsuits may be costly and divert internal resources away from managing our business. See Item 3 *Legal Proceedings* below.

We may be subject to customer claims and legal actions pertaining to the performance of our fiduciary responsibilities. Whether or not such customer claims and legal actions are founded or unfounded, if such claims and legal actions are not resolved in a manner favorable to us, they may result in significant financial liability and/or adversely affect the market perception of us and our products and services, as well as impact customer demand for those products and services. Any financial liability or reputation damage could have a material adverse effect on our business, which, in turn, could have a material adverse effect on our financial condition and results of operations.

Federal and state laws and regulations may restrict our ability to pay dividends

The ability of the Bank to pay dividends to the Company and of the Company to pay dividends to its shareholders is limited by applicable federal and California law and regulations. See Business Regulation and Supervision and Management s Discussion and Analysis of Financial Condition and Results of Operations Liquidity and Cash Flow.

Risks Associated with our Common Stock

The price of our common stock may be volatile or may decline

The trading price of our common stock may fluctuate widely as a result of a number of factors, many of which are outside our control. In addition, the stock market is subject to fluctuations in its share prices and trading volumes that affect the market prices of the shares of many companies. These specific and broad market fluctuations could adversely affect the market price of our common stock. Among the factors that could affect our stock price are:

- actual or anticipated fluctuations in our operating results and financial condition;
- changes in revenue or earnings estimates or publication of research reports and recommendations by financial analysts;
- credit events or losses;
- failure to meet analysts revenue or earnings estimates;
- speculation in the press or investment community;
- strategic actions by us or our competitors, such as acquisitions or restructurings;
- actions or trades by institutional shareholders or other large shareholders;
- our capital position;
- fluctuations in the stock price and operating results of our competitors;
- actions by hedge funds, short term investors, activist shareholders or shareholder representative organizations;
- general market conditions and, in particular, developments related to market conditions for the financial services industry;

proposed or adopted regulatory changes or developments;

anticipated or pending investigations, proceedings or litigation that involve or affect the Company and/or the Bank; or

domestic and international economic factors, whether related or unrelated to the Company s performance.

The stock market and, in particular, the market for financial institution stocks, has experienced significant volatility in recent years. The market price of our common stock and the trading volume in our common stock may fluctuate and cause significant price variations to occur. The trading price of the shares of our common stock and the value of our other securities will depend on many factors, which may change from time to time, including, without limitation, our financial condition, performance, creditworthiness and prospects, future sales of our equity or equity related securities, and other factors identified above in Cautionary Note Regarding Forward-Looking Statement . The capital and credit markets have been experiencing volatility and disruption for more than five years. In some cases, the markets have produced downward pressure on stock prices and credit availability for certain issuers without regard to those issuers underlying financial strength. A significant decline in our stock price could result in substantial losses for individual shareholders and could lead to costly and disruptive securities litigation. Extensive sales by large shareholders could also exert sustained downward pressure on our stock price.

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An investment in our common stock is not an insured deposit

Our common stock is not a bank deposit and, therefore, is not insured against loss by the FDIC, any other deposit insurance fund or by any other public or private entity. Investment in our common stock is inherently risky for the reasons described in this Risk Factors section and elsewhere in this report and is subject to the same market forces that affect the price of common stock in any company. As a result, if you acquire our common stock, you could lose some or all of your investment.

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

Various provisions of our articles of incorporation and by-laws and certain other actions we have taken could delay or prevent a third-party from acquiring us, even if doing so might be beneficial to our shareholders. The Bank Holding Company Act of 1956, as amended, and the Change in Bank Control Act of 1978, as amended, together with federal regulations, require that, depending on the particular circumstances, regulatory approval and/or appropriate regulatory filings may be required from either or all the Federal Reserve, the FDIC, the DBO prior to any person or entity acquiring control (as defined in the applicable regulations) of a state non-member bank, such as the Bank. These provisions may prevent a merger or acquisition that would be attractive to shareholders and could limit the price investors would be willing to pay in the future for our common stock.

Changes in stock market prices could reduce fee income from our brokerage, asset management and investment advisory businesses

We earn substantial wealth management fee income for managing assets for our clients and also providing brokerage and investment advisory services. Because investment management and advisory fees are often based on the value of assets under management, a fall in the market prices of those assets could reduce our fee income. Changes in stock market prices could affect the trading activity of investors, reducing commissions and other fees we earn from our brokerage business.

CVB is a holding company and depends on the Bank for dividends, distributions and other payments

CVB is a legal entity separate and distinct from the Bank. CVB s principal source of cash flow, including cash flow to pay dividends to our shareholders is dividends from the Bank. CVB s ability to pay dividends to its stockholders is substantially dependent upon the Bank s ability to pay dividends to CVB. Federal and state law imposes limits on the ability of the Bank to pay dividends and make other distributions and payments. If the Bank is unable to meet regulatory requirements to pay dividends or make other distributions to CVB, CVB will be unable to pay dividends to its shareholders.

We may face other risks

From time to time, we detail other risks with respect to our business and/or financial results in our filings with the SEC. For further discussion on additional areas of risk, see Item 7. *Management s Discussion and Analysis of Financial Condition and Results of Operations*.

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ITEM 1B. *UNRESOLVED STAFF COMMENTS*

None

ITEM 2. *PROPERTIES*

The principal executive offices of the Company and the Bank are located in Ontario, California, and are owned by the Company.

As of December 31, 2018, the Bank occupied a total of 70 premises consisting of (i) 68 Banking Centers (Centers) of which one Center is located at our Corporate Headquarters in Ontario California and (ii) two operation and technology centers. We own 18 of these locations and the remaining properties are leased under various agreements with expiration dates ranging from 2019 through 2028, some with lease renewal options that could extend certain leases through 2039. All properties are located in Southern and Central California.

For additional information concerning properties, see Note 10 *Premises and Equipment* of the Notes to the consolidated financial statements included in this report. See Item 8 *Financial Statements and Supplemental Data*.

ITEM 3. *LEGAL PROCEEDINGS*

The Company and its subsidiaries are parties to various lawsuits and threatened lawsuits in the ordinary and non-ordinary course of business. From time to time, such lawsuits and threatened lawsuits may include, but are not limited to, actions involving securities litigation, employment matters, wage-hour and labor law claims, consumer, lender liability claims and negligence claims, some of which may be styled as class action or representative cases. Some of these lawsuits may be similar in nature to other lawsuits pending against the Company s competitors.

The Company is a defendant and cross-complainant in an action entitled Edward A. Dunagan *et al* v. Citizens Business Bank, as successor to American Security Bank (ASB), Case No. CVDS1408287, filed in the Superior Court for San Bernardino County. The complaint was initially filed in May, 2014 against ASB, which was acquired during the same month by CBB, and a Second Amended Complaint (SAC) was filed on September 9, 2015, naming CBB as the primary defendant. The case arises out of a number of defaulted commercial real estate loans originally made by ASB to the Dunagans and various entities owned by the Dunagans (Dunagan Parties), and the SAC includes claims by the Dunagans (1) contesting their liabilities under their personal guarantees for deficiencies on certain of the defaulted loans, (2) attacking the validity of ASB s foreclosures on certain properties owned by the Dunagan Parties, and (3) claiming emotional distress caused by ASB s allegedly wrongful actions in connection with such foreclosures. The Dunagans sought compensatory damages in excess of $2 million plus punitive damages. ASB/CBB filed a cross-complaint against the Dunagans alleging breach of guaranty and demanding additional damages. A bench trial on the respective claims by the Dunagans and ASB/CBB took place in late July and early August, 2018.

On November 7, 2018, the Court issued a statement of decision finding in favor of the Dunagans and against ASB on all three claims made by the plaintiffs enumerated above, denying ASB s claims under the cross-complaint, and awarding damages and attorney s fees and costs to the Dunagans in an aggregate amount of approximately $1.34 million. The Company has filed to appeal this decision. The Company also believes that the bankers professional liability insurance policy previously obtained by ASB (which provides for a $5 million per claim limit subject to a $100,000 deductible) may cover all or a substantial portion of any final monetary award to the plaintiffs. The Company continues to believe that this adverse decision and any monetary award ultimately payable by CBB are not expected to have a material adverse impact on the Company s results of operations, financial condition or cash flows.

For lawsuits where the Company has determined that a loss is both probable and reasonably estimable, a liability representing the best estimate of the Company s financial exposure based on known facts has been recorded in accordance with FASB guidance over loss contingencies (ASC 450). However, as a result of inherent uncertainties in judicial interpretation and application of a myriad of laws applicable to the Company s business, and the unique, complex factual issues presented in any given lawsuit, the Company often cannot determine the probability of loss or estimate the amount of damages which a plaintiff might successfully prove if the Company were found to be liable. For lawsuits or threatened lawsuits where a claim has been asserted or the Company has determined that it is probable that a claim will be asserted, and there is a reasonable possibility that the outcome will be unfavorable, the Company will disclose the existence of the loss contingency, even if the Company is not able to make an estimate of the possible loss or range of possible loss with respect to the action or potential action in question, unless the Company believes that the nature, potential magnitude or potential timing (if known) of the loss contingency is not reasonably likely to be material to the Company s liquidity, consolidated financial position, and/or results of operations.

Our accruals and disclosures for loss contingencies are reviewed quarterly and adjusted as additional information becomes available. We disclose a loss contingency and/or the amount accrued if we believe it is reasonably likely to be material or if we believe such disclosure is necessary for our financial statements to not be misleading. If we determine that an exposure to loss exists in excess of an amount previously accrued or disclosed, we assess whether there is at least a reasonable possibility that a loss, or additional loss, may have been incurred, and we adjust our accruals and disclosures accordingly.

We do not presently believe that the ultimate resolution of any lawsuits currently pending against the Company will have a material adverse effect on the Company s results of operations, financial condition, or cash flows. The outcome of litigation and other legal and regulatory matters is inherently uncertain, however, and it is possible that one or more of the legal matters currently pending or threatened against the Company could have a material adverse effect on our results of operations, financial condition or cash flows

ITEM 4. ***MINE SAFETY DISCLOSURES***

Not applicable.

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PART II

ITEM 5. *MARKET FOR THE REGISTRANT S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES*

CVB s common stock is traded on the NASDAQ Global Select National Market under the symbol CVBF. CVB had approximately 139,973,017 shares of common stock outstanding with 1,630 registered shareholders of record as of February 15, 2019. Refer to the section entitled Information about the Annual Meeting and Voting of our definitive Proxy Statement to be filed pursuant to Regulation 14A within 120 days after the end of the last fiscal year.

For information on the statutory and regulatory limitations on the ability of the Company to pay dividends to its shareholders and on the Bank to pay dividends to CVB, see Item 1. *Business-Regulation and Supervision Dividends* and Item 7. *Management s Discussion and Analysis of Financial Condition and Results of Operations Liquidity and Cash Flow*.

Issuer Purchases of Equity Securities

On July 16, 2008, our Board of Directors approved a program to repurchase up to 10,000,000 shares of CVB common stock (such number will not be adjusted for stock splits, stock dividends, and the like) in the open market or in privately negotiated transactions, at times and at prices considered appropriate by us, depending upon prevailing market conditions and other corporate and legal considerations. As a result of various repurchases made under the 2008 repurchase program, on August 11, 2016, our Board of Directors authorized an increase in CVB s common stock repurchase program back to 10,000,000 shares, or approximately 9.3% of CVB s currently outstanding shares at the time of authorization, and adopted a 10b5-1 plan. There is no expiration date for this repurchase program. The Company terminated its 10b5-1 plan in January 2017 in order to comply with Regulation M. A new 10b5-1 plan was approved by the Board of Directors effective as of May 2, 2017. On March 30, 2018, the Company terminated its 10b5-1 plan in order to comply with Regulation M, due to the then-pending CB acquisition and contemplated issuance of shares of CVB. A new 10b5-1 plan was approved by the Board of Directors effective as of November 1, 2018. During the fourth quarter and for the year ended December 31, 2018, the Company repurchased 340,283 shares of CVB common stock outstanding. As of December 31, 2018, we have 9,577,917 shares of CVB common stock remaining that are eligible for repurchase under the common stock repurchase program.

Period	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Average Price Paid Per Share	Maximum Number of Shares Available for Repurchase Under the Plans or Programs
October 1 - 31, 2018	-	$ -	9,918,200
November 1 - 30, 2018	-	$ -	9,918,200
December 1 - 31, 2018	340,283	$ 19.49	9,577,917
Total	340,283	$ 19.49	9,577,917

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Performance Graph

The following Performance Graph and related information shall not be deemed soliciting material or be filed with the Securities and Exchange Commission, nor shall such information be incorporated by reference into any future filing under the Securities Act of 1933 or Securities Exchange Act of 1934, each as amended, except to the extent that the Company specifically incorporates it by reference into such filing.

The following graph compares the yearly percentage change in CVB s cumulative total shareholder return (stock price appreciation plus reinvested dividends) on common stock (i) the cumulative total return of the Nasdaq Composite Index; and (ii) a published index comprised by Morningstar (formerly Hemscott, Inc.) of banks and bank holding companies in the Pacific region (the peer group line depicted below). The graph assumes an initial investment of $100 on December 31, 2013, and reinvestment of dividends through December 31, 2018. Points on the graph represent the performance as of the last business day of each of the years indicated. The graph is not necessarily indicative of future price performance.

ASSUMES $100 INVESTED ON DECEMBER 31, 2013

ASSUMES DIVIDEND REINVESTED

FISCAL YEAR ENDING DECEMBER 31, 2018

Company/Market/Peer Group	12/31/2013	12/31/2014	12/31/2015	12/31/2016	12/31/2017	12/31/2018
CVB Financial Corp.	**100.00**	**96.27**	**104.59**	**144.83**	**152.20**	**133.97**
NASDAQ Composite	**100.00**	**114.62**	**122.81**	**133.19**	**172.11**	**165.84**
Peer Group Index	**100.00**	**103.41**	**109.73**	**151.58**	**173.71**	**139.83**

Source: Research Data Group, Inc., www.researchdatagroup.com

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ITEM 6. ***SELECTED FINANCIAL DATA***

The following table reflects selected financial information at and for the five years ended December 31. Throughout the past five years, the Company has acquired other banks. This may affect the comparability of the data.

	At or For the Year Ended December 31,				
	2018	**2017**	**2016**	**2015**	**2014**
	(Dollars in thousands, except per share amounts)				
Interest income	$ 361,860	$ 287,226	$ 265,050	$ 261,513	$ 252,903
Interest expense	12,815	8,296	7,976	8,571	16,389
Net interest income	349,045	278,930	257,074	252,942	236,514
Provision for (recapture of) loan losses	1,500	(8,500)	(6,400)	(5,600)	(16,100)
Noninterest income	43,481	42,118	35,552	33,483	36,412
Noninterest expense	179,911	140,753	136,740	140,659	126,229
Earnings before income taxes	211,115	188,795	162,286	151,366	162,797
Income taxes	59,112	84,384	60,857	52,221	58,776
NET EARNINGS	$ 152,003	$ 104,411	$ 101,429	$ 99,145	$ 104,021
Basic earnings per common share	$ 1.25	$ 0.95	$ 0.94	$ 0.93	$ 0.98
Diluted earnings per common share	$ 1.24	$ 0.95	$ 0.94	$ 0.93	$ 0.98
Cash dividends declared per common share	$ 0.560	$ 0.540	$ 0.480	$ 0.480	$ 0.400
Cash dividends declared on common shares	$ 70,203	$ 59,483	$ 51,849	$ 51,040	$ 42,356
Dividend pay-out ratio (1)	46.19%	56.97%	51.12%	51.48%	40.72%
Weighted average common shares:					
Basic	121,670,113	109,409,301	107,282,332	105,715,247	105,239,421
Diluted	121,957,364	109,806,710	107,686,955	106,192,472	105,759,523
Common Stock Data:					
Common shares outstanding at year end	140,000,017	110,184,922	108,251,981	106,384,982	105,893,216
Book value per share	$ 13.22	$ 9.70	$ 9.15	$ 8.68	$ 8.29
Financial Position:					
Assets	$ 11,529,153	$ 8,270,586	$ 8,073,707	$ 7,671,200	$ 7,377,920
Investment securities available-for-sale	1,734,085	2,080,985	2,270,466	2,368,646	3,137,158

Investment securities held-to-maturity	744,440	829,890	911,676	850,989	1,528
Net loans, excluding PCI loans (2)	7,683,988	4,742,531	4,263,158	3,867,941	3,630,875
Net PCI loans (3)	17,010	28,515	70,366	89,840	126,367
Deposits	8,827,490	6,546,853	6,309,680	5,917,260	5,604,658
Borrowings	722,255	553,773	656,028	736,704	809,106
Junior subordinated debentures	25,774	25,774	25,774	25,774	25,774
Stockholders' equity	1,851,190	1,069,266	990,862	923,399	878,109
Equity-to-assets ratio (4)	16.06%	12.93%	12.27%	12.04%	11.90%
Financial Performance:					
Return on beginning equity	14.22%	10.54%	10.98%	11.29%	13.48%
Return on average equity (ROAE)	11.00%	9.84%	10.26%	10.87%	12.50%
Return on average assets (ROAA)	1.60%	1.26%	1.26%	1.31%	1.45%
Net interest margin, tax-equivalent (TE) (5)	4.03%	3.63%	3.46%	3.62%	3.62%
Efficiency ratio (6)	45.83%	43.84%	46.73%	49.11%	46.25%
Noninterest expense to average assets	1.89%	1.70%	1.70%	1.86%	1.77%
Credit Quality:					
Allowance for loan losses	$ 63,613	$ 59,585	$ 61,540	$ 59,156	$ 59,825
Allowance/gross loans	0.82%	1.23%	1.40%	1.47%	1.57%
Total nonaccrual loans	$ 19,951	$ 10,716	$ 7,152	$ 21,019	$ 32,186
Nonaccrual loans/gross loans, net of deferred loan fees	0.26%	0.22%	0.16%	0.52%	0.84%
Allowance/nonaccrual loans	318.85%	556.04%	860.46%	281.44%	185.87%
Net recoveries	$ 2,528	$ 6,545	$ 8,784	$ 4,931	$ 690
Net recoveries/average loans	0.04%	0.14%	0.21%	0.13%	0.02%
Regulatory Capital Ratios:					
Company:					
Tier 1 leverage ratio	10.98%	11.88%	11.49%	11.22%	10.86%
Common equity Tier 1 risk-based capital ratio	13.04%	16.43%	16.48%	16.49%	N/A
Tier 1 risk-based capital ratio	13.32%	16.87%	16.94%	16.98%	16.99%
Total risk-based capital ratio	14.13%	18.01%	18.19%	18.23%	18.24%
Bank:					
Tier 1 leverage ratio	10.90%	11.77%	11.36%	11.11%	10.77%
Common equity Tier 1 risk-based capital ratio	13.22%	16.71%	16.76%	16.81%	N/A
Tier 1 risk-based capital ratio	13.22%	16.71%	16.76%	16.81%	16.85%
Total risk-based capital ratio	14.03%	17.86%	18.01%	18.06%	18.11%

(1) Dividends declared on common stock divided by net earnings.
(2) Net loans, excluding Purchase Credit Impaired (PCI) loans.
(3) Excludes loans held-for-sale. PCI loans are those loans acquired from SJB and previously covered by a loss sharing agreement with the FDIC.
(4) Stockholders equity divided by total assets.
(5) Net interest income (TE) divided by average interest-earning assets.

(6) Noninterest expense divided by net interest income before provision for loan losses plus noninterest income. Also refer to Noninterest Expense and Efficiency Ratio Reconciliation (non-GAAP) under *Analysis of the Results of Operations* of Item 7 of this Form 10-K.

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ITEM 7. *MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS*

The following discussion provides information about the results of operations, financial condition, liquidity, and capital resources of CVB Financial Corp. and its wholly owned subsidiary. This information is intended to facilitate the understanding and assessment of significant changes and trends related to our financial condition and the results of our operations. This discussion and analysis should be read in conjunction with this Annual Report on Form 10-K, and the audited consolidated financial statements and accompanying notes presented elsewhere in this report.

CRITICAL ACCOUNTING POLICIES

The preparation of these consolidated financial statements requires management to make estimates and judgments that affect the reported amounts of assets and liabilities, revenues and expenses, and related disclosures of contingent assets and liabilities at the date of our financial statements. Actual results may differ from these estimates under different assumptions or conditions.

Critical accounting policies are defined as those that are reflective of significant judgments and uncertainties, and are essential to understanding Management s Discussion and Analysis of Financial Condition and Results of Operations. The following is a summary of the more judgmental and complex accounting estimates and principles. In each area, we have identified the variables most important in the estimation process. We have used the best information available to make the necessary estimates to value the related assets and liabilities. Actual performance that differs from our estimates and future changes in the key variables could change future valuations and impact the results of operations.

Allowance for Loan Losses (ALLL) Arriving at an appropriate level of allowance for loan losses involves a high degree of judgment. Our allowance for loan losses provides for probable losses based upon evaluations of known and inherent risks in the loan and lease portfolio. The determination of the balance in the allowance for loan losses is based on an analysis of the loan and lease finance receivables portfolio using a systematic methodology and reflects an amount that, in our judgment, is appropriate to provide for probable credit losses inherent in the portfolio, after giving consideration to the character of the loan portfolio, current economic conditions, past credit loss experience, and such other factors as deserve current recognition in estimating inherent credit losses. The provision for loan losses is charged to expense. For a full discussion of our methodology of assessing the adequacy of the allowance for loan losses, see Item 7, *Management s Discussion and Analysis of Financial Condition and Results of Operation Risk Management* and Note 3 *Summary of Significant Accounting Policies* and Note 7 *Loans and Lease Finance Receivables and Allowance for Loan Losses* of our consolidated financial statements presented elsewhere in this report.

Business Combinations The Company applies the acquisition method of accounting for business combinations. Under the acquisition method, the acquiring entity in a business combination recognizes the assets acquired and liabilities assumed at their acquisition date fair values. Management utilizes prevailing valuation techniques appropriate for the asset or liability being measured in determining these fair values. These fair values are estimates and are subject to adjustment for up to one year after the acquisition date or when additional information relative to the closing date fair values becomes available and such information is considered final, whichever is earlier. Any excess of the purchase price over amounts allocated to assets acquired, including identifiable intangible assets, and liabilities assumed is recorded as goodwill. Where amounts allocated to assets acquired and liabilities assumed is greater than the purchase price, a bargain purchase gain would be recognized. Acquisition related costs are expensed as incurred. Refer to Note 4 *Business Combinations* of our consolidated financial statements presented elsewhere in this report.

Valuation and Recoverability of Goodwill Goodwill represented $666.5 million of our $11.53 billion in total assets as of December 31, 2018. The Company has one reportable segment. Goodwill has an indefinite useful life and is not amortized, but is tested for impairment at least annually, or more frequently, if events and circumstances exist that indicate that a goodwill impairment test should be performed. Such events and circumstances may include among others, a significant adverse change in legal factors or in the general business climate, significant decline in our stock price and market capitalization, unanticipated competition, the testing for recoverability of a significant asset group within the reporting unit, and an adverse action or assessment by a regulating body. Any adverse change in these factors could have a significant impact on the recoverability of goodwill and could have a material impact on our consolidated financial statements.

Based on the results of our annual goodwill impairment test, we determined that no goodwill impairment charges were required as our single reportable segment s fair value exceeded its carrying amount. As of December 31, 2018, we determined there were no events or circumstances which would more likely than not reduce the fair value of our reportable segment below its carrying amount. Note 3 *Summary of Significant Accounting Policies* of our consolidated financial statements presented elsewhere in this report

Income Taxes Income taxes are accounted for under the asset and liability method. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. Future realization of deferred tax assets ultimately depends on the existence of sufficient taxable income of the appropriate character (for example, ordinary income or capital gain) within the carryback or carryforward periods available under the tax law. Based on historical and future expected taxable earnings and available strategies, the Company considers the future realization of these deferred tax assets more likely than not.

The tax effects from an uncertain tax position are recognized in the financial statements only if, based on its merits, the position is more likely than not to be sustained on audit by the taxing authorities. Interest and penalties related to uncertain tax positions are recorded as part of other operating expense.

For complete discussion and disclosure of other accounting policies see Note 3 *Summary of Significant Accounting Policies* of the Company s consolidated financial statements presented elsewhere in this report.

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OVERVIEW

For the year ended December 31, 2018, we reported net earnings of $152.0 million, compared with $104.4 million for 2017. This represented an increase of $47.6 million, or 45.58%. Diluted earnings per share were $1.24 for the year ended December 31, 2018, compared to $0.95 for 2017. Income tax expense for 2017 included a one-time charge of $13.2 million due to the re-measurement of the Company s net deferred tax asset (DTA) resulting from the Tax Cuts and Jobs Act of 2017 (Tax Reform Act). Excluding the impact of the $13.2 million DTA revaluation, net income totaled $117.6 million for 2017, or $1.07 per share. Net earnings grew by $34.4 million from 2017, or 29.23%, when the impact of the DTA revaluation is excluded.

On August 10, 2018, we completed the acquisition of Community Bank (CB). Our financial statements for the year ended 2018 include 143 days of CB operations, post-merger. At close, Citizens Business Bank acquired $2.73 billion of loans. We also assumed $1.26 billion of noninterest-bearing deposits and $2.87 billion of total deposits.

At December 31, 2018, total assets of $11.53 billion increased $3.26 billion, or 39.40%, from total assets of $8.27 billion at December 31, 2017. Interest-earning assets of $10.29 billion at December 31, 2018 increased by$2.49 billion, or 31.87%, when compared with earning assets of $7.80 billion at December 31, 2017. The increase in interest-earning assets was primarily due to a $2.93 billion increase in total loans, partially offset by a $432.4 million decrease in investment securities. The increase in total loans included $2.73 billion of loans acquired from CB in the third quarter of 2018.

Total investment securities were $2.48 billion at December 31, 2018, a decrease of $432.4 million, or 14.85%, from $2.57 billion at December 31, 2017. At December 31, 2018, investment securities HTM totaled $744.4 million. At December 31, 2018, investment securities AFS totaled $1.73 billion, inclusive of a pre-tax unrealized loss of $23.6 million. HTM securities declined by $85.5 million, or 10.30%, and AFS securities declined by $346.9 million, or 16.67%, from December 31, 2017.

Total loans and leases, net of deferred fees and discount, of $7.76 billion at December 31, 2018, increased by $2.93 billion, or 60.74%, from $4.83 billion at December 31, 2017. Excluding the $2.73 billion of acquired CB loans, total loans increased by $199.9 million or 4.14% for 2018. Commercial real estate loans grew by $223.1 million and dairy & livestock and agribusiness loans increased by $34.1 million. This growth was partially offset by a decrease of $46.6 million in commercial and industrial loans and a decrease of $13.5 million in consumer and other loans.

Noninterest-bearing deposits were $5.20 billion at December 31, 2018, an increase of $1.36 billion, or 35.31%, compared to $3.85 billion at December 31, 2017. At December 31, 2018, noninterest-bearing deposits were 58.96% of total deposits, compared to 58.75% at December 31, 2017. The increase in total deposits from the end of 2017 included $1.26 billion of noninterest-bearing deposits and $2.87 billion of total deposits assumed from CB during the third quarter of 2018. Our average cost of total deposits was 0.13% for 2018, compared to 0.09% for 2017.

Customer repurchase agreements totaled $442.3 million at December 31, 2018, compared to $553.8 million at December 31, 2017. Our average cost of total deposits including customer repurchase agreements was 0.14% for 2018, compared to 0.10% for 2017.

At December 31, 2018, we had $280.0 million in short-term borrowings, compared to zero at December 31, 2017. At December 31, 2018, we had $25.8 million of junior subordinated debentures, unchanged from December 31, 2017. These debentures bear interest at three-month LIBOR plus 1.38% and mature in 2036. Our average cost of funds was 0.16% for 2018, compared to 0.12% for 2017.

The allowance for loan losses totaled $63.6 million at December 31, 2018, compared to $59.6 million at December 31, 2017. The allowance for loan losses was increased by net recoveries on loans of $2.5 million for

2018 and was increased by a $1.5 million loan loss provision for 2018. The allowance for loan losses was 0.82% and 1.23% of total loans and leases outstanding at December 31, 2018 and 2017, respectively. The ratio as of December 31, 2018 was impacted by the $2.73 billion in loans acquired from CB that were recorded at fair market value, without a corresponding loan loss allowance.

Our capital ratios under the revised capital framework referred to as Basel III remain well-above regulatory standards. As of December 31, 2018, the Company s Tier 1 leverage capital ratio totaled 10.98%, our common equity Tier 1 ratio totaled 13.04%, our Tier 1 risk-based capital ratio totaled 13.32%, and our total risk-based capital ratio totaled 14.13%. Refer to our *Analysis of Financial Condition-Capital Resources* for discussion of the new capital rules which were effective beginning with the first quarter ended March 31, 2015.

Recent Acquisitions

On August 10, 2018, we completed the acquisition of CB with approximately $4.09 billion in total assets and 16 banking centers. The increase in total assets at December 31, 2018 included $2.73 billion of acquired loans, net of an $86.7 million discount, $717.0 million of investment securities, and $70.9 million in bank-owned life insurance. The acquisition resulted in approximately $550.0 million of goodwill and $52.2 million in core deposit premium. At the close of the merger, the entire CB security portfolio was liquidated at fair market value, as was $297.6 million of FHLB term advances and $166.0 million of overnight borrowings assumed from CB. These fair values are estimates and are subject to adjustment for up to one year after the acquisition date or when additional information relative to the closing date fair values becomes available and such information is considered final, whichever is earlier. As the initial estimate of fair value of impaired loans was incomplete as of December 31, 2018, the fair value reflected in the financial statements has been determined provisionally.

We have included the financial results of the business combination in the consolidated statement of earnings and comprehensive income beginning on the acquisition date.

Business Segments

For the years ended December 31, 2016 through December 31, 2017, we operated as two reportable segments: Banking Centers and Dairy & Livestock and Agribusiness. As a result of the Community Bank acquisition, along with changes in personnel, reporting structure, and operations, we re-evaluated our segment reporting for the third quarter ended September 30, 2018.

As of December 31, 2018, we operated as one reportable segment. The factors considered in making this determination included the nature of products and offered services, geographic regions in which we operate, the applicable regulatory environment, and the materiality of discrete financial information reviewed by our key decision makers.

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ANALYSIS OF THE RESULTS OF OPERATIONS

Financial Performance

	For the Year Ended December 31,			Variance			
				2018		2017	
	2018	2017	2016	$	%	$	%
	(Dollars in thousands, except per share amounts)						
Net interest income	$ 349,045	$ 278,930	$ 257,074	$ 70,115	25.14%	$ 21,856	8.50%
(Provision for) recapture of provision for loan losses	(1,500)	8,500	6,400	(10,000)	-117.65%	2,100	32.81%
Noninterest income	43,481	42,118	35,552	1,363	3.24%	6,566	18.47%
Noninterest expense	(179,911)	(140,753)	(136,740)	(39,158)	-27.82%	(4,013)	-2.93%
Income taxes	(59,112)	(84,384) **(1)**	(60,857)	25,272	29.95%	(23,527)	-38.66%
Net earnings	$ 152,003	$ 104,411	$ 101,429	$ 47,592	45.58%	$ 2,982	2.94%
Earnings per common share:							
Basic	$ 1.25	$ 0.95	$ 0.94	$ 0.30		$ 0.01	
Diluted	$ 1.24	$ 0.95	$ 0.94	$ 0.29		$ 0.01	
Return on average assets	1.60%	1.26% **(1)**	1.26%	0.34%		-	
Return on average shareholders' equity	11.00%	9.84% **(1)**	10.26%	1.16%		-0.42%	
Efficiency ratio	45.83%	43.84%	46.73%	1.99%		-2.89%	
Noninterest expense to average assets	1.89%	1.70%	1.70%	0.19%		-	

(1) Includes $13.2 million DTA revaluation resulting from the Tax Reform Act.

Reconciliations of Adjusted Efficiency Ratio and Noninterest Expense to Average Assets Ratio (Non-GAAP)

We use certain non-GAAP financial measures to provide supplemental information regarding our performance. Noninterest expense for the years ended December 31, 2018, 2017 and 2016 included acquisition related expenses of $16.4 million, $2.3 million and $1.9 million, respectively. We believe that presenting the efficiency ratio and noninterest expense to average assets ratio, excluding acquisition expenses, provides additional clarity to the users of financial statements regarding core net income.

	For the Year Ended December 31,		
	2018	2017	2016
		(Dollars in thousands)	
Total noninterest expense	$ 179,911	$ 140,753	$ 136,740

Acquisition related expenses	(16,404)	(2,251)	(1,897)
Adjusted total noninterest expense, excluding acquisition expenses	$ 163,507	$ 138,502	$ 134,843
Net interest income before provision for (recapture of) loan losses	$ 349,045	$ 278,930	$ 257,074
Total noninterest income	43,481	42,118	35,552
Average total assets	9,512,669	8,301,721	8,022,994
Efficiency ratio [1]	45.83%	43.84%	46.73%
Adjusted efficiency ratio, excluding acquisition expenses	41.66%	43.14%	46.08%
Noninterest expense to average assets, annualized	1.89%	1.70%	1.70%
Adjusted noninterest expense to average assets, annualized, excluding acquisition expenses	1.72%	1.67%	1.68%

(1) Noninterest expense divided by net interest income before provision for loan losses plus noninterest income.

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Tax Reform and Effect of Tax Rate Change Reconciliations (Non-GAAP)

The year ended December 31, 2017 includes a one-time charge of $13.2 million as a result of the December 22, 2017 enactment of the Tax Reform Act of 2017. We believe that presenting the effective tax rate, earnings, ROAA, ROAE, and earnings per common share, excluding the impact of the re-measurement of our net deferred tax asset, provides additional clarity to the users of financial statements regarding core financial performance.

	For the Year Ended December 31,		
	2018	2017	2016
	(Dollars in thousands, except per share amounts)		
Income tax expense	$ 59,112	$ 84,384	$ 60,857
Less: Effect of income tax rate change-DTA revaluation	-	(13,208)	-
Adjusted income tax expense	$ 59,112	$ 71,176	$ 60,857
Effective Tax Rate	28.00%	44.70%	37.50%
Adjusted effective tax rate	28.00%	37.70%	37.50%
Net earnings	$ 152,003	$ 104,411	$ 101,429
Effect of income tax rate change-DTA revaluation	-	13,208	-
Adjusted net earnings	$ 152,003	$ 117,619	$ 101,429
Average assets	$ 9,512,669	$ 8,301,721	$ 8,022,994
Return on average assets	1.60%	1.26%	1.26%
Adjusted return on average assets	1.60%	1.42%	1.26%
Average equity	$ 1,382,392	$ 1,061,557	$ 988,732
Return on average equity	11.00%	9.84%	10.26%
Adjusted return on average equity	11.00%	11.08%	10.26%
Weighted average shares outstanding			
Basic	121,670,113	109,409,301	107,282,332
Diluted	121,957,364	109,806,710	107,686,955
Earnings per common share:			
Basic	$ 1.25	$ 0.95	$ 0.94
Diluted	$ 1.24	$ 0.95	$ 0.94
Adjusted earnings per common share:			
Basic	$ 1.25	$ 1.07	$ 0.94
Diluted	$ 1.24	$ 1.07	$ 0.94

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Reconciliations of Adjusted Yield on Average Loans, Yield on Average Earning Assets and NIM (Non-GAAP)

We use certain non-GAAP financial measures to provide supplemental information regarding our performance. Net interest income for the years ended December 31, 2018, 2017 and 2016 included a yield adjustment of $18.6 million, $7.4 million and $7.4 million, respectively. These yield adjustments relate to discount accretion on acquired loans and nonrecurring nonaccrual interest paid, and are reflected in the Company s net interest margin. We believe that presenting net interest income and the net interest margin excluding these yield adjustments provides additional clarity to the users of financial statements regarding core net interest income and net interest margin.

	For the Year Ended December 31,		
	2018	**2017**	**2016**
	(Dollars in thousands)		
Yield on Average Loans			
Loan interest income	$ 293,284	$ 214,126	$ 192,992
Less: Discount accretion on acquired loans	(15,400)	(5,159)	(4,028)
Less: Nonrecurring nonaccrual interest paid	(3,183)	(2,194)	(3,330)
Adjusted loan interest income	$ 274,701	$ 206,773	$ 185,634
Average loans and lease finance receivables, net of discount on acquired loans	$ 5,905,674	$ 4,623,244	$ 4,195,129
Add: Average discount on acquired loans	39,674	9,514	7,838
Average gross loans and lease finance receivables	$ 5,945,348	$ 4,632,758	$ 4,202,967
Yield on average loans	4.97%	4.63%	4.60%
Adjusted yield on average loans	4.62%	4.46%	4.41%
Yield on Average Earning Assets (TE)			
Total interest income (TE)	$ 363,864	$ 291,234	$ 270,358
Less: Discount accretion on acquired loans	(15,400)	(5,159)	(4,028)
Less: Nonrecurring nonaccrual interest paid	(3,183)	(2,194)	(3,330)
Adjusted total interest income (TE)	$ 345,281	$ 283,881	$ 263,000
Average total interest-earning assets	$ 8,723,370	$ 7,798,463	$ 7,584,909
Add: Average discount on acquired loans	39,674	9,514	7,838
Adjusted average total interest-earning assets	$ 8,763,044	$ 7,807,977	$ 7,592,747
Yield on average earning assets (TE)	4.17%	3.74%	3.57%
Adjusted yield on average earning assets (TE)	3.94%	3.64%	3.47%

Net Interest Margin (TE)			
Net interest income (TE)	$ 351,049	$ 282,938	$ 262,382
Less: Discount accretion on acquired loans	(15,400)	(5,159)	(4,028)
Less: Nonrecurring nonaccrual interest paid	(3,183)	(2,194)	(3,330)
Adjusted net interest income (TE)	$ 332,466	$ 275,585	$ 255,024
Average net interest-earning assets	$ 8,723,370	$ 7,798,463	$ 7,584,909
Add: Average discount on acquired loans	39,674	9,514	7,838
Adjusted average net interest-earning assets	$ 8,763,044	$ 7,807,977	$ 7,592,747
Net interest margin (TE)	4.03%	3.63%	3.46%
Adjusted net interest margin (TE)	3.80%	3.53%	3.36%

Return on Average Tangible Common Equity Reconciliations (Non-GAAP)

The return on average tangible common equity is a non-GAAP disclosure. The Company uses certain non-GAAP financial measures to provide supplemental information regarding the Company s performance. The following is a reconciliation of net income, adjusted for tax-effected amortization of intangibles and the impact of the $13.2 million DTA revaluation, to net income computed in accordance with GAAP; a reconciliation of average tangible common equity to the Company s average stockholders equity computed in accordance with GAAP; as well as a calculation of return on average tangible common equity.

	For the Year Ended December 31,		
	2018	**2017**	**2016**
	(Dollars in thousands)		
Net Income	$ 152,003	$ 104,411	$ 101,429
Add: Amortization of intangible assets	5,254	1,329	1,106
Less: Tax effect of amortization of intangible assets [1]	(1,553)	(559)	(465)
Tangible net income	155,704	105,181	102,070
Add: Effect of income tax rate change-DTA revaluation	-	13,208	-
Adjusted tangible net income	$ 155,704	$ 118,389	$ 102,070
Average stockholders' equity	$ 1,382,392	$ 1,061,557	$ 988,732
Less: Average goodwill	(330,613)	(112,916)	(85,894)
Less: Average intangible assets	(26,055)	(6,957)	(4,937)
Average tangible common equity	$ 1,025,724	$ 941,684	$ 897,901
Return on average equity	11.00%	9.84%	10.26%
Return on average tangible common equity	15.18%	11.17%	11.37%
Adjusted return on average tangible common equity	15.18%	12.57%	11.37%

(1) Tax effected at respective statutory rates.

Net Interest Income

The principal component of our earnings is net interest income, which is the difference between the interest and fees earned on loans and investments (interest-earning assets) and the interest paid on deposits and borrowed funds (interest-bearing liabilities). Net interest margin is net interest income as a percentage of average interest-earning assets for the period. The level of interest rates and the volume and mix of interest-earning assets and interest-bearing liabilities impact net interest income and net interest margin. The net interest spread is the yield on average interest-earning assets minus the cost of average interest-bearing liabilities. Net interest margin and net interest spread are included on a tax equivalent (TE) basis by adjusting interest income utilizing the federal statutory tax rates of 21%, 35% and 35% in effect for the years ended December 31, 2018, 2017 and 2016, respectively. The substantial change in rates were due to the Tax Reform Act. Our net interest income, interest spread, and net interest margin are sensitive to general business and economic conditions. These conditions include short-term and long-term interest rates, inflation, monetary supply, and the strength of the international, national and state economies, in general, and more specifically, the local economies in which we conduct business. Our ability to manage net interest income during changing interest rate environments will have a significant impact on our overall performance. We manage net interest income through affecting changes in the mix of interest-earning assets as well as the mix of interest-bearing liabilities, changes in the level of interest-bearing liabilities in proportion to interest-earning assets, and in the growth and maturity of earning assets. See Item 7 *Management s Discussion and Analysis of Financial Condition and Results of Operations Asset/Liability and Market Risk Management Interest Rate Sensitivity Management* included herein.

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The table below presents the interest rate spread, net interest margin and the composition of average interest-earning assets and average interest-bearing liabilities by category for the periods indicated, including the changes in average balance, composition, and average yield/rate between these respective periods.

Interest-Earning Assets and Interest-Bearing Liabilities

	For the Year Ended December 31,								
	2018			2017			2016		
	Average Balance	Interest	Yield/ Rate	Average Balance	Interest	Yield/ Rate	Average Balance	Interest	Yiel Rat
				(Dollars in thousands)					
EREST-EARNING SETS									
estment securities									
ilable-for-sale rities:									
able	$ 1,869,842	$ 44,423	2.38%	$ 2,137,332	$ 47,596	2.24%	$ 2,126,733	$ 43,538	2.0
-advantaged	52,550	1,565	3.98%	68,522	2,182	4.73%	123,844	4,164	4.9
d-to-maturity rities:									
able	534,642	11,848	2.22%	586,673	12,558	2.14%	500,557	10,183	2.0
-advantaged	243,955	7,053	3.50%	278,109	8,457	4.11%	300,484	10,044	4.5
estment in FHLB k	19,441	2,045(4)	10.52%	18,046	1,375	7.62%	17,873	2,224(5)	12.2
rest-earning osits with other tutions	97,266	1,642	1.69%	86,537	932	1.08%	320,289	1,905	0.5
ns (2)	5,905,674	293,284	4.97%	4,623,244	214,126	4.63%	4,195,129	192,992	4.6
al interest-earning ts	8,723,370	361,860	4.17%	7,798,463	287,226	3.74%	7,584,909	265,050	3.5
al interest-earning ts	789,299			503,258			438,085		
al assets	$ 9,512,669			$ 8,301,721			$ 8,022,994		
EREST-BEARING BILITIES									
ings deposits (3)	$ 2,656,660	7,250	0.27%	$ 2,337,142	4,903	0.21%	$ 2,185,493	4,354	0.2
e deposits	453,031	2,575	0.57%	401,033	1,141	0.28%	584,149	1,603	0.2
al interest-bearing osits	3,109,691	9,825	0.32%	2,738,175	6,044	0.22%	2,769,642	5,957	0.2

LB advances, other owings, and omer repurchase eements	499,526	2,990	0.60%	571,991	2,252	0.39%	637,585	2,019	0.3
rest-bearing ilities	3,609,217	12,815	0.35%	3,310,166	8,296	0.25%	3,407,227	7,976	0.2
interest-bearing osits	4,449,110			3,856,987			3,539,707		
er liabilities	71,950			73,011			87,328		
kholders' equity	1,382,392			1,061,557			988,732		
al liabilities and kholders' equity	$ 9,512,669			$ 8,301,721			$ 8,022,994		
interest income		$ 349,045			$ 278,930			$ 257,074	
t interest spread - equivalent			3.82%			3.49%			3.3
t interest margin			4.00%			3.58%			3.3
t interest margin - equivalent			4.03%			3.63%			3.4

(1) Includes tax equivalent (TE) adjustments utilizing a federal statutory rate of 21%, 35% and 35% in effect for the years ended December 31, 2018, 2017 and 2016, respectively. Non tax-equivalent (TE) rate was 2.41%, 2.31% and 2.24% for the years ended December 31, 2018, 2017 and 2016, respectively.
(2) Includes loan fees of $3.4 million, $3.6 million and $4.0 million for the years ended December 31, 2018, 2017 and 2016, respectively. Prepayment penalty fees of $3.0 million, $2.7 million and $3.5 million are included in interest income for the years ended December 31, 2018, 2017 and 2016, respectively.
(3) Includes interest-bearing demand and money market accounts.
(4) Includes a special dividend from the FHLB of $520,000.
(5) Includes a special dividend from the FHLB of $588,000.

The following table presents a comparison of interest income and interest expense resulting from changes in the volumes and rates on average interest-earning assets and average interest-bearing liabilities for the periods indicated. Changes in interest income or expense attributable to volume changes are calculated by multiplying

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the change in volume by the initial average interest rate. The change in interest income or expense attributable to changes in interest rates is calculated by multiplying the change in interest rate by the initial volume. The changes attributable to interest rate and volume changes are calculated by multiplying the change in rate times the change in volume.

Rate and Volume Analysis for Changes in Interest Income, Interest Expense and Net Interest Income

	Comparision of Year Ended December 31,							
	2018 Compared to 2017 Increase (Decrease) Due to				2017 Compared to 2016 Increase (Decrease) Due to			
	Volume	Rate	Rate/ Volume	Total	Volume	Rate	Rate/ Volume	Total
	(Dollars in thousands)							
Interest income:								
Available-for-sale securities:								
Taxable investment securities	$ (5,743)	$ 2,929	$ (359)	$ (3,173)	$ 468	$ 3,552	$ 38	$ 4,058
Tax-advantaged investment securities	(509)	(141)	33	(617)	(1,824)	(281)	123	(1,982)
Held-to-maturity securities:								
Taxable investment securities	(1,118)	448	(40)	(710)	1,753	531	91	2,375
Tax-advantaged investment securities	(1,022)	(434)	52	(1,404)	(766)	(889)	68	(1,587)
Investment in FHLB stock	106	524	40	670	21	(862)	(8)	(849)
Interest-earning deposits with other institutions	117	528	65	710	(1,390)	1,544	(1,127)	(973)
Loans	59,330	15,522	4,306	79,158	19,620	1,373	141	21,134
Total interest income	51,161	19,376	4,097	74,634	17,882	4,968	(674)	22,176
Interest expense:								
Savings deposits	673	1,473	201	2,347	295	237	17	549
Time deposits	144	1,142	148	1,434	(506)	64	(20)	(462)
FHLB advances, other borrowings, and customer	(279)	1,164	(147)	738	(203)	486	(50)	233

repurchase agreements								
Total interest expense	538	3,779	202	4,519	(414)	787	(53)	320
Net interest income	$ 50,623	$ 15,597	$ 3,895	$ 70,115	$ 18,296	$ 4,181	$ (621)	$ 21,856

2018 Compared to 2017

Net interest income, before provision for (recapture of) loan losses, of $349.0 million for 2018 increased $70.1 million, or 25.14%, compared to $278.9 million for 2017. Interest-earning assets increased on average by $924.9 million, or 11.86%, from $7.80 billion for 2017 to $8.72 billion for 2018. Our net interest margin (TE) was 4.03% for 2018, compared to 3.63% for 2017. On a nominal basis, excluding the impact from tax-exempt interest, the net interest margin for 2018 grew by 42 basis points over 2017. The increase in our net interest margin was primarily the result of loan growth from the acquisition of CB and a higher level of discount accretion from the acquired loans.

Interest income for 2018 was $361.9 million, which represented a $74.63 million, or 25.98%, increase when compared to 2017. Average interest-earning assets increased by $924.9 million and the average interest-earning asset yield of 4.17% increased by 43 basis points compared to 2017, primarily due to loans acquired from CB. The 43 basis point increase in the interest-earning asset yield over 2017 resulted from the combination of a 34 basis point increase in loan yields, a four basis point increase in investment yields and the change in mix of earning assets, represented by an increase in average loans as a percentage of earning assets from 59.3% in 2017 to 67.7% in 2018. Conversely, average investment securities declined as a percentage of earning assets from 39.4% in the prior year to 31.0% in 2018.

Interest income and fees on loans for 2018 of $293.3 million increased $79.2 million, or 36.97% when compared to 2017 primarily due to loans acquired from CB. Average loans increased $1.28 billion for 2018 when compared with 2017. As a result of higher levels of discount accretion on acquired loans and nonaccrual interest paid, 2018 interest income increased by $11.2 million in comparison to 2017. Also contributing to the 34 basis point increase in loan yield were increases in the rate on loans indexed to variable interest rates, such as the Bank s Prime rate, which increased by 1.00% when compared to the end of 2017. Excluding discount accretion on acquired loans and nonaccrual interest paid, our loan yields grew by 18 basis points over the prior year.

In general, we stop accruing interest on a loan after its principal or interest becomes 90 days or more past due. When a loan is placed on nonaccrual, all interest previously accrued but not collected is charged against earnings. There was no interest income that was accrued and not reversed on nonaccrual loans at December 31, 2018 and 2017. As of December 31, 2018 and 2017, we had $20.0 million and $10.7 million of nonaccrual loans (excluding PCI loans), respectively. Had these nonaccrual loans for which interest was no longer accruing complied with the original terms and conditions, interest income would have been approximately $1.3 million and $889,000 greater for 2018 and 2017, respectively.

Interest income from investment securities was $64.9 million for 2018, a $5.9 million, or 8.34%, decrease from $70.8 million for 2017. This decrease was primarily the result of a $369.6 million decrease in the average investment securities for 2018, compared to 2017. The nominal yield on investments increased by 9 basis points compared to 2017, while the tax equivalent yield increased by only four basis points due to the reduction of the federal tax rate on tax-exempt investments resulting from the Tax Reform Act. Dividend income from FHLB stock increased by $670,000 from 2017, due to a special dividend of $520,000 received from the FHLB in the fourth quarter of 2018.

Interest expense of $12.8 million for 2018 increased $4.5 million, or 54.47%, compared to $8.3 million for 2017. The average rate paid on interest-bearing liabilities increased 10 basis points, to 0.35% for 2018, from 0.25% for 2017. Average interest-bearing liabilities were $299.1 million higher in 2018, compared to 2017, as we assumed $1.61 billion interest-bearing deposits from CB during the third quarter of 2018. Average noninterest-bearing deposits represented 58.86% of our total deposits for 2018, compared to 58.48% for 2017. Our total cost of funds in 2018 was 0.16%, compared to 0.12% in 2017.

2017 Compared to 2016

Net interest income, before recapture of provision for loan losses, was $278.9 million for 2017, an increase of $21.9 million, or 8.50%, compared to $257.1 million for 2016. Interest-earning assets grew on average by $213.6 million, or 2.82%, from $7.58 billion for 2016 to $7.80 billion for 2017. Our net interest margin (TE) was 3.63% for 2017, compared to 3.46% for 2016.

Interest income for 2017 was $287.2 million, which represented a $22.2 million, or 8.37%, increase when compared to 2016. Compared to 2016, average interest-earning assets increased by $213.6 million and the yield on interest-earning assets increased by 17 basis points. The 17 basis point increase in the interest-earning asset yield over 2016 resulted from the combination of a seven basis point increase in investment yields, a three basis point increase in loan yields and the change in mix of earning assets represented by an increase in loans as a percentage of earning assets growing from 55.3% in 2016 to 59.3% in 2017. Excluding interest recaptured on nonaccrual loans and additional discount accretion on a PCI loan, interest income grew by about $23.3 million, or 8.91%, year-over-year. When the impact of the recaptured interest and additional discount accretion is excluded, the yield on interest-earning assets increased from 3.52% for 2016 to 3.71% for 2017.

Interest income and fees on loans for 2017 totaled $214.1 million which represented a $21.1 million, or 10.95%, increase when compared to 2016. Average loans increased $428.1 million for 2017 when compared with 2016, and included approximately $238 million of acquired VBB loans.

For the year ended December 31, 2017, there were three nonperforming, troubled debt restructuring (TDR) loans that were paid in full resulting in the recognition of $1.4 million of interest income and additional discount accretion of $762,000 resulted from the payoff of a PCI loan. This compares to four nonperforming loans paid in full resulting in a $3.3 million increase in interest income in 2016. Excluding the impact of

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recaptured interest and additional discount accretion, the net interest margin (TE) was 3.60% for 2017, compared to 3.42% for 2016.

There was no interest income that was accrued and not reversed on nonaccrual loans at December 31, 2017 and 2016. As of December 31, 2017 and 2016, we had $10.7 million and $7.2 million of nonaccrual loans (excluding PCI loans), respectively. Had these nonaccrual loans for which interest was no longer accruing complied with the original terms and conditions, interest income would have been approximately $889,000 and $493,000 greater for 2017 and 2016, respectively.

Interest income from investment securities was $70.8 million for 2017, a $2.9 million, or 4.22%, increase from $67.9 million for 2016. This increase was the result of a $19.0 million increase in the average investment securities for 2017, compared to 2016 and a seven basis point increase in the non-TE yield on securities. Dividend income from FHLB stock decreased by $849,000 from 2016, due to a special dividend of $588,000 from the FHLB in 2016.

Interest expense of $8.3 million for 2017 increased $320,000, or 4.01%, compared to $8.0 million for 2016. The average rate paid on interest-bearing liabilities increased two basis points, to 0.25% for 2017, from 0.23% for 2016. Average interest-bearing liabilities were $97.1 million lower in 2017, compared to 2016, as repurchase agreements and other borrowings declined by $65.6 million. Excluding a $183.1 million decline in average time deposits primarily due to the Bank s decision in 2016 to not renew certificates of deposit with the State of California, interest-bearing liabilities increased by $86.1 million. Our total cost of funds in 2017 was 0.12%, compared to 0.11% in 2016.

Provision for Loan Losses

The allowance for loan losses is increased by the provision for loan losses and recoveries of prior losses, and is decreased by recapture of provisions and by charge-offs taken when management believes the uncollectability of any loan is confirmed. The provision for loan losses is determined by management as the amount to be added to (subtracted from) the allowance for loan losses after net charge-offs have been deducted to bring the allowance to an appropriate level which, in management s best estimate, is necessary to absorb probable loan losses within the existing loan portfolio.

The allowance for loan losses totaled $63.6 million at December 31, 2018, compared to $59.6 million at December 31, 2017. The allowance for loan losses was increased by a $1.5 million loan loss provision for 2018 and by net recoveries of $2.5 million. This compares to a $8.5 million loan loss provision recapture and net recoveries of $6.5 million for 2017 and a $6.4 million loan loss provision recapture and net recoveries of $4.9 million for 2016. We periodically assess the credit quality of our portfolio to determine whether additional provisions for loan losses are necessary. The ratio of the allowance for loan losses to total loans and leases outstanding, net of deferred fees and discount, as of December 31, 2018, 2017 and 2016 was 0.82%, 1.23% and 1.40%, respectively. The ratio as of December 31, 2018 was impacted by the $2.73 billion in loans acquired from CB that were recorded at fair market value, without a corresponding loan loss allowance. Refer to the discussion of Allowance for Loan Losses in Item 7 *Management s Discussion and Analysis of Financial Condition and Results of Operations* contained herein for discussion concerning observed changes in the credit quality of various components of our loan portfolio as well as changes and refinements to our methodology.

No assurance can be given that economic conditions which adversely affect the Company s service areas or other circumstances will not be reflected in increased provisions for loan losses in the future, as the nature of this process requires considerable judgment. See Allowance for Loan Losses under *Analysis of Financial Condition* herein.

PCI loans acquired in the FDIC-assisted transaction were initially recorded at their fair value and were covered by a loss sharing agreement with the FDIC, which expired in October 2014 for commercial loans. Refer to Note 3 *Summary of Significant Accounting Policies* of the consolidated financial statements. During the

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year ended December 31, 2018, 2017, and 2016, there were no charge-offs or recoveries, for loans in excess of the amount originally expected in the fair value of the loans at acquisition.

Noninterest Income

Noninterest income includes income derived from financial services offered, such as CitizensTrust, BankCard services, international banking, and other business services. Also included in noninterest income are service charges and fees, primarily from deposit accounts, gains (net of losses) from the disposition of investment securities, loans, other real estate owned, and fixed assets, and other revenues not included as interest on earning assets.

The following table sets forth the various components of noninterest income for the periods presented.

	For the Year Ended December 31,			Variance 2018		Variance 2017	
	2018	**2017**	**2016**	**$**	**%**	**$**	**%**
	(Dollars in thousands)						
Noninterest income:							
Service charges on deposit accounts	$ 17,070	$ 15,809	$ 15,066	$ 1,261	7.98%	$ 743	4.93%
Trust and investment services	8,774	9,845	9,595	(1,071)	-10.88%	250	2.61%
Bankcard services	3,485	3,406	2,921	79	2.32%	485	16.60%
BOLI income	4,018	3,420	2,612	598	17.49%	808	30.93%
Gain on sale of investment securities, net	-	402	548	(402)	-100.00%	(146)	-26.64%
Gain (loss) on OREO, net	3,546	6	(20)	3,540	59000.00%	26	130.00%
Gain on sale of loans	-	-	1,101	-	-	(1,101)	-100.00%
Gain on sale of asset held-for-sale, net	-	542	-	(542)	-100.00%	542	-
Gain on sale of branches, net	-	906	272	(906)	-100.00%	634	233.09%
Gain on eminent domain condemnation, net	-	2,894	-	(2,894)	-100.00%	2,894	-
Other	6,588	4,888	3,457	1,700	34.78%	1,431	41.39%
Total noninterest income	$ 43,481	$ 42,118	$ 35,552	$ 1,363	3.24%	$ 6,566	18.47%

2018 Compared to 2017

The $43.5 million in noninterest income included $3.5 million of net gain on the sale of one OREO. 2017 included $2.9 million in one-time gains related to an eminent domain condemnation of one of our banking center buildings, a $906,000 net gain on the sale of a branch acquired from VBB, a $542,000 net gain on the sale of our former operations and technology center, and a $402,000 gain on sale of an investment security. Excluding the net gains realized in 2018 and 2017, noninterest income increased by $2.5 million over 2017. Service charges on deposit accounts increased by $1.3 million over 2017, primarily due to the acquisition of CB.

CitizensTrust consists of Wealth Management and Investment Services income. The Wealth Management group provides a variety of services, which include asset management, financial planning, estate planning, retirement planning, private, and corporate trustee services, and probate services. Investment Services provides self-directed brokerage, 401(k) plans, mutual funds, insurance and other non-insured investment products. At December 31, 2018, CitizensTrust had approximately $2.54 billion in assets under management and administration, including $1.80 billion in assets under management. CitizensTrust generated fees of $8.8 million for 2018, a decrease of $1.1 million compared to $9.8 million for 2017.

The Bank s investment in BOLI includes life insurance policies acquired through acquisitions and the purchase of life insurance by the Bank on a selected group of employees. The Bank is the owner and beneficiary of these policies. BOLI is recorded as an asset at its cash surrender value. Increases in the cash value of these policies, as well as insurance proceeds received, are recorded in noninterest income and are not subject to income tax, as long as they are held for the life of the covered parties. The $598,000 increase in BOLI income included $706,000 in BOLI income from $70.9 million of BOLI policies acquired from CB in the third quarter of 2018, which partially offset the $775,000 in income recorded in 2017 on the death benefit of a former director.

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2017 Compared to 2016

The $6.6 million increase in noninterest income was primarily due to a $2.9 million net gain from an eminent domain condemnation of one of our banking center buildings, a $906,000 net gain on the sale of a branch acquired from VBB, and a $542,000 net gain on the sale of our former operations and technology center that was classified as an asset held-for-sale at December 31, 2016. Service charges on deposit accounts and Bankcard services increased $743,000 and $485,000, respectively. Noninterest income for 2016 included a $1.1 million net gain on the sale of loans during the first quarter of 2016 and a $272,000 net gain on the sale of our Porterville branch in the second quarter of 2016.

At December 31, 2017, CitizensTrust had approximately $2.88 billion in assets under management and administration, including $2.15 billion in assets under management. CitizensTrust generated fees of $9.8 million for 2017, an increase of $250,000 compared to $9.6 million for 2016.

The $808,000 increase in BOLI income was due to $775,000 in tax free income on the death benefit of a former director.

Noninterest Expense

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

	For the Year Ended December 31,			Variance			
				2018		2017	
	2018	2017	2016	$	%	$	%
			(Dollars in thousands)				
Noninterest expense:							
Salaries and employee benefits	$ 100,601	$ 87,065	$ 82,630	$ 13,536	15.55%	$ 4,435	5.37%
Occupancy	16,386	13,188	12,138	3,198	24.25%	1,050	8.65%
Equipment	4,455	3,568	3,503	887	24.86%	65	1.86%
Professional services	6,477	5,940	5,054	537	9.04%	886	17.53%
Software licenses and maintenance	8,655	6,385	5,465	2,270	35.55%	920	16.83%
Stationery and supplies	1,207	1,246	1,178	(39)	-3.13%	68	5.77%
Telecommunications expense	2,564	2,352	2,222	212	9.01%	130	5.85%
Marketing and promotion	5,302	4,839	5,027	463	9.57%	(188)	-3.74%
Amortization of intangible assets	5,254	1,329	1,106	3,925	295.33%	223	20.16%
Regulatory assessments	3,218	3,119	3,785	99	3.17%	(666)	-17.60%
Insurance	1,735	1,780	1,719	(45)	-2.53%	61	3.55%
Loan expense	1,103	752	991	351	46.68%	(239)	-24.12%
OREO expense	7	128	500	(121)	-94.53%	(372)	-74.40%
Recapture of provision for unfunded loan commitments	(250)	(400)	(450)	150	37.50%	50	11.11%
Directors' expenses	1,073	954	797	119	12.47%	157	19.70%
Acquisition related expenses	16,404	2,251	1,897	14,153	628.74%	354	18.66%

Impairment loss on asset held-for-sale	-	-	2,558	-	-	(2,558)	-100.00%
Legal settlement	-	-	1,500	-	-	(1,500)	-100.00%
Other	5,720	6,257	5,120	(537)	-8.58%	1,137	22.21%
Total noninterest expense	$ 179,911	$ 140,753	$ 136,740	$ 39,158	27.82%	$ 4,013	2.93%
Noninterest expense to average assets	1.89%	1.70%	1.70%				
Noninterest expense to average assets, excluding acquisition related expenses	1.72%	1.67%	1.68%				
Efficiency ratio (1)	45.83%	43.84%	46.73%				
Efficiency ratio, excluding acquisition related expenses (1)	41.66%	43.14%	46.08%				

(1) Noninterest expense divided by net interest income before provision for loan losses plus noninterest income.

Our ability to control noninterest expenses in relation to asset growth can be measured in terms of total noninterest expenses as a percentage of average assets. Excluding acquisition related expenses, noninterest expense as a percentage of average assets was 1.72% for 2018, compared to 1.67% and 1.68% for 2017 and 2016, respectively.

Our ability to control noninterest expenses in relation to the level of total revenue (net interest income before provision for loan losses plus noninterest income) is measured by the efficiency ratio and indicates the percentage of net revenue that is used to cover expenses. For 2018, the efficiency ratio, excluding acquisition related expenses, was 41.66%, compared to 43.14% for 2017 and 46.08% for 2016.

2018 Compared to 2017

Noninterest expense of $179.9 million for the year ended December 31, 2018 was $39.2 million higher than 2017. The year-over-year increase included $16.4 million in merger related expenses for the acquisition of CB in 2018, compared to $2.1 million in acquisition costs related to the integration and systems conversion of VBB for the same period of 2017. Salaries and benefit costs increased by $13.5 million due to additional compensation related expenses for the newly hired and former CB employees. CB related expenses were the primary driver of a $3.2 million increase in occupancy expense and a $2.3 million increase in software licenses and maintenance. The year-over-year increase also included a $3.9 million increase in amortization of intangible assets due to core deposits assumed from CB.

2017 Compared to 2016

Noninterest expense of $140.8 million for the year ended December 31, 2017 was $4.0 million higher than 2016. The $4.4 million, or 5.37%, increase in compensation and benefit expense includes additional staff from the acquisition of VBB and normal year-over-year escalation in wages. The $1.1 million year-over-year increase in occupancy and equipment expense included both temporary and permanent expenses related to the acquisition of VBB and the build-out and relocation to our new operations and technology building. Acquisition related expenses were $2.3 million, up $354,000 from the prior year. Software licenses and maintenance and professional service expense increased $920,000 and $886,000, respectively. Increases in professional services included $300,000 in higher legal expenses. Partially offsetting these expense increases were $4.1 million in nonrecurring expenses in the fourth quarter of 2016 resulting from a fair value adjustment of $2.6 million for our operations and technology center and a $1.5 million accrual for the settlement of a wage-hour class action lawsuit.

Income Taxes

The Company s effective tax rate for the year ended December 31, 2018 was 28.00%, compared with 44.70% for the year ended December 31, 2017. On December 22, 2017, the Tax Reform Act was enacted into law. Beginning in 2018, the Tax Reform Act reduces the federal tax rate for corporations from 35% to 21% and changes or limits certain tax deductions. During the fourth quarter of 2017, we recorded a $13.2 million one-time charge to income tax expense due to the tax rate reduction and re-measurement of our net DTA. Our estimated annual effective tax rate also varies depending upon the level of tax-advantaged income as well as available tax credits. Refer to Note 12 *Income Taxes* of the notes to consolidated financial statements for more information.

The effective tax rates are below the nominal combined Federal and State tax rate as a result of tax-advantaged income from certain municipal security investments, municipal loans and leases and BOLI, as well as available tax credits for each period.

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ANALYSIS OF FINANCIAL CONDITION

The Company reported total assets of $11.53 billion at December 31, 2018. This represented an increase of $3.26 billion, or 39.40%, from total assets of $8.27 billion at December 31, 2017. Interest-earning assets of $10.29 billion at December 31, 2018 increased $2.49 billion, or 31.87%, when compared with interest-earning assets of $7.80 billion at December 31, 2017. The increase in interest-earning assets was primarily due to a $2.93 billion increase in total loans. This increase was partially offset by a $432.4 million decrease in investment securities. The increase in total loans included $2.73 billion of loans acquired from CB in the third quarter of 2018. Total liabilities were $9.68 billion at December 31, 2018, an increase of $2.48 billion, or 34.39%, from total liabilities of $7.20 billion at December 31, 2017. The increase in total liabilities at December 31, 2018 included $2.87 billion of total deposits assumed from CB during the third quarter of 2018. Total equity increased $781.9 million, or 73.13%, to $1.85 billion at December 31, 2018, compared to total equity of $1.07 billion at December 31, 2017. The $781.9 million increase in equity was due to $722.8 million for the issuance of common stock for the acquisition of CB, $152.0 million in net earnings and $2.8 million for various stock based compensation items. This was offset by $70.2 million in cash dividends declared, a $20.1 million decrease in other comprehensive income, net of tax, resulting from the net change in fair value of our investment securities portfolio, and $7.8 million for the repurchase of common stock. In December 2018, under our common stock repurchase program, we repurchased 340,000 shares of common stock at an average price of $19.49.

Investment Securities

The Company maintains a portfolio of investment securities to provide interest income and to serve as a source of liquidity for its ongoing operations. At December 31, 2018, we reported total investment securities of $2.48 billion. This represented a decrease of $432.4 million, or 14.85%, from total investment securities of $2.91 billion at December 31, 2017. At December 31, 2018, investment securities HTM totaled $744.4 million. At December 31, 2018, our investment securities AFS totaled $1.73 billion, inclusive of a pre-tax unrealized loss of $23.6 million. The after-tax unrealized loss reported in AOCI on investment securities AFS was $16.6 million.

As of December 31, 2018, the Company had a pre-tax net unrealized holding loss on total investment securities of $23.6 million, compared to a pre-tax net unrealized holding gain of $2.9 million at December 31, 2017. The changes in the net unrealized holding gain resulted primarily from fluctuations in market interest rates. For 2018, total repayments/maturities and proceeds from sales of investment securities totaled $489.6 million, compared to $572.8 million for 2017. The Company purchased additional investment securities totaling $98.7 million and $362.0 million for 2018 and 2017, respectively. At the close of the merger in the third quarter of 2018, we liquidated the entire investment security portfolio of $717.0 million acquired from CB. No other investment securities were sold in 2018. This compares to one investment security sold in 2017 with a recognized gain of $402,000, and two investment securities sold in 2016 with a recognized gain of $548,000.

The tables below summarize the fair value of AFS and HTM investment securities for the periods presented.

	December 31,					
	2018		2017		2016	
	Fair Value	**Percent**	**Fair Value**	**Percent**	**Fair Value**	**Percent**
	(Dollars in thousands)					
Investment securities available-for-sale						

Government agency/GSE	$ -	-	$ -	-	$ 2,752	0.12%
Residential mortgage-backed securities	1,474,508	85.03%	1,750,909	84.14%	1,834,748	80.81%
CMO/REMIC - residential	214,051	12.34%	273,829	13.16%	347,189	15.29%
Municipal bonds	44,810	2.59%	55,496	2.66%	80,071	3.53%
Other securities	716	0.04%	751	0.04%	5,706	0.25%
Total available-for-sale securities	$ 1,734,085	100.00%	$ 2,080,985	100.00%	$ 2,270,466	100.00%

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	December 31, 2018 Amortized Cost	2018 Percent	2017 Amortized Cost	2017 Percent	2016 Amortized Cost	2016 Percent
	(Dollars in thousands)					
Investment securities held-to-maturity						
Government agency/GSE	$ 138,274	18.57%	$ 159,716	19.25%	$ 182,648	20.03%
Residential mortgage-backed securities	153,874	20.67%	176,427	21.26%	193,699	21.25%
CMO	215,336	28.93%	225,072	27.12%	244,419	26.81%
Municipal bonds	236,956	31.83%	268,675	32.37%	290,910	31.91%
Total held-to-maturity securities	$ 744,440	100.00%	$ 829,890	100.00%	$ 911,676	100.00%
Fair Value	$ 721,537		$ 819,215		$ 897,374	

The maturity distribution of the AFS and HTM portfolios consist of the following for the period presented.

	December 31, 2018 One Year or Less	After One Year Through Five Years	After Five Years Through Ten Years	After Ten Years	Total	Percent to Total
	(Dollars in thousands)					
Investment securities available-for-sale:						
Residential mortgage-backed securities	$ 7,645	$ 1,348,584	$ 117,988	$ 291	$ 1,474,508	85.03%
CMO/REMIC - residential	2,220	197,811	14,020	-	214,051	12.34%
Municipal bonds (1)	3,489	8,291	8,492	24,538	44,810	2.59%
Other securities	716	-	-	-	716	0.04%
Total	$ 14,070	$ 1,554,686	$ 140,500	$ 24,829	$ 1,734,085	100.00%
Weighted average yield:						
Residential mortgage-backed securities	3.56%	2.57%	2.51%	5.36%	2.57%	
CMO/REMIC - residential	3.42%	2.48%	2.46%	-	2.49%	
Municipal bonds (1)	4.33%	1.92%	3.56%	2.44%	2.70%	
Other securities	2.31%	-	-	-	2.31%	
Total	3.55%	2.56%	2.57%	2.48%	2.56%	

(1) The weighted average yield for the portfolio is based on projected duration and is not tax-equivalent. The tax-equivalent yield at December 31, 2018 was 3.41%.

	December 31, 2018					
	One Year or Less	After One Year Through Five Years	After Five Years Through Ten Years	After Ten Years	Total	Percent to Total
	(Dollars in thousands)					
Investment securities held-to-maturity:						
Government agency/GSE	$ -	$ -	$ -	$ 138,274	$ 138,274	18.57%
Residential mortgage-backed securities	-	68,845	80,765	4,264	153,874	20.67%
CMO	-	202,033	13,303	-	215,336	28.93%
Municipal bonds (1)	500	18,089	102,993	115,374	236,956	31.83%
Total	$ 500	$ 288,967	$ 197,061	$ 257,912	$ 744,440	100.00%
Weighted average yield:						
Government agency/GSE	-	-	-	1.89%	1.89%	
Residential mortgage-backed securities	-	2.41%	2.56%	3.05%	2.51%	
CMO	-	2.09%	2.00%	-	2.08%	
Municipal bonds (1)	4.07%	3.09%	3.05%	2.59%	2.83%	
Total	4.07%	2.23%	2.78%	2.22%	2.37%	

(1) The weighted average yield for the portfolio is not tax-equivalent. The tax equivalent yield at December 31, 2018 was 3.59%.

The maturity of each security category is defined as the contractual maturity except for the categories of mortgage-backed securities and CMO/REMIC whose maturities are defined as the estimated average life. The final maturity of mortgage-backed securities and CMO/REMIC will differ from their contractual maturities because the underlying mortgages have the right to repay such obligations without penalty. The speed at which the underlying mortgages repay is influenced by many factors, one of which is interest rates. Mortgages tend to repay faster as interest rates fall and slower as interest rate rise. This will either shorten or extend the estimated average life. Also, the yield on mortgage-backed securities and CMO/REMIC are affected by the speed at which the underlying mortgages repay. This is caused by the change in the amount of amortization of premiums or accretion of discounts of each security as repayments increase or decrease. The Company obtains the estimated average life of each security from independent third parties.

The weighted-average yield on the total investment portfolio at December 31, 2018 was 2.55% with a weighted-average life of 4.3 years. This compares to a weighted-average yield of 2.50% at December 31, 2017 with a weighted-average life of 4.3 years. The weighted average life is the average number of years that each dollar of unpaid principal due remains outstanding. Average life is computed as the weighted-average time to the receipt of all future cash flows, using as the weights the dollar amounts of the principal pay-downs.

Approximately 89% of the securities in the total investment portfolio, at December 31, 2018, are issued by the U.S. government or U.S. government-sponsored agencies and enterprises, which have the implied guarantee of payment of principal and interest. As of December 31, 2018, approximately $89.7 million in U.S. government agency bonds are callable. The Agency CMO/REMIC are backed by agency-pooled collateral. Municipal bonds, which represented approximately 11% of the total investment portfolio, are predominately AA or higher rated securities.

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The Company held investment securities in excess of 10% of shareholders equity from the following issuers for the periods presented.

	December 31, 2018		December 31, 2017	
	Book Value	Market Value	Book Value	Market Value
	(Dollars in thousands)			
Major issuer:				
Federal National Mortgage Association	$ 955,546	$ 944,989	$ 1,164,683	$ 1,170,306
Federal Home Loan Mortgage Corporation	871,257	856,427	991,287	988,480
Government National Mortgage Association	253,735	241,130	268,369	259,521
Small Business Administration (1)	138,274	136,224	159,291	158,011

(1) Investment securities from this issuer were no longer in excess of 10% of shareholders equity as of December 31, 2018.

Municipal securities held by the Company are issued by various states and their various local municipalities. The following tables present municipal securities by the top holdings by state for the periods presented.

	December 31, 2018			
	Amortized Cost	Percent of Total	Fair Value	Percent of Total
	(Dollars in thousands)			
Municipal Securities available-for-sale:				
Minnesota	$ 11,078	24.3%	$ 10,599	23.7%
Iowa	8,617	18.9%	8,615	19.2%
Connecticut	6,305	13.8%	6,167	13.8%
California	5,641	12.4%	5,758	12.8%
Massachusetts	4,153	9.1%	3,934	8.8%
Ohio	2,135	4.7%	2,141	4.8%
All other states (9 states)	7,692	16.8%	7,596	16.9%
Total	$ 45,621	100.0%	$ 44,810	100.0%
Municipal Securities held-to-maturity:				
Minnesota	$ 54,370	22.9%	$ 52,732	22.8%
Texas	28,510	12.0%	27,893	12.1%
Massachusetts	27,191	11.5%	26,369	11.4%
Louisiana	12,804	5.4%	12,364	5.3%
Wisconsin	12,315	5.2%	11,777	5.1%
Pennsylvania	11,682	4.9%	11,731	5.1%
All other states (21 states)	90,084	38.1%	88,458	38.2%
Total	$ 236,956	100.0%	$ 231,324	100.0%

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	December 31, 2017			
	Amortized Cost	Percent of Total	Fair Value	Percent of Total
	(Dollars in thousands)			
Municipal Securities available-for-sale:				
Minnesota	$ 11,089	20.2%	$ 10,992	19.8%
Iowa	8,618	15.7%	8,865	16.0%
Connecticut	6,639	12.1%	6,672	12.0%
California	5,609	10.2%	5,751	10.4%
Massachusetts	5,061	9.2%	5,040	9.1%
Arizona	2,698	4.9%	2,733	4.9%
All other states (9 states)	15,252	27.7%	15,443	27.8%
Total	$ 54,966	100.0%	$ 55,496	100.0%
Municipal Securities held-to-maturity:				
Minnesota	$ 59,813	22.3%	$ 59,213	22.1%
Texas	32,025	11.9%	31,929	11.9%
Massachusetts	27,281	10.2%	27,217	10.2%
New York	14,718	5.5%	14,727	5.5%
Wisconsin	12,675	4.7%	12,472	4.7%
Louisiana	12,906	4.8%	12,652	4.7%
All other states (21 states)	109,257	40.6%	109,426	40.9%
Total	$ 268,675	100.0%	$ 267,636	100.0%

The tables below show the Company s investment securities gross unrealized losses and fair value by investment category and length of time that individual securities have been in a continuous unrealized loss position, at December 31, 2018 and 2017. The unrealized losses on these securities were primarily attributed to changes in interest rates. The issuers of these securities have not, to our knowledge, evidenced any cause for default on these securities. These securities have fluctuated in value since their purchase dates as market rates have fluctuated. However, we have the ability and the intention to hold these securities until their fair values recover to cost or maturity. As such, management does not deem these securities to be other-than-temporarily- impaired (OTTI). A summary of our analysis of these securities and the unrealized losses is described more fully in Note 5 *Investment Securities* of the notes to the consolidated financial statements. Economic trends may adversely affect the value of the portfolio of investment securities that we hold.

	December 31, 2018					
	Less Than 12 Months		12 Months or Longer		Total	
	Fair Value	Gross Unrealized Holding Losses	Fair Value	Gross Unrealized Holding Losses	Fair Value	Gross Unrealized Holding Losses
	(Dollars in thousands)					

Investment securities available-for-sale:						
Residential mortgage-backed securities	$ 692,311	$ (4,864)	$ 593,367	$ (16,082)	$ 1,285,678	$ (20,946)
CMO/REMIC - residential	36,582	(365)	135,062	(3,160)	171,644	(3,525)
Municipal bonds	9,568	(188)	14,181	(955)	23,749	(1,143)
Total available-for-sale securities	$ 738,461	$ (5,417)	$ 742,610	$ (20,197)	$ 1,481,071	$ (25,614)
Investment securities held-to-maturity:						
Government agency/GSE	$ 7,479	$ (15)	$ 54,944	$ (2,607)	$ 62,423	$ (2,622)
Residential mortgage-backed securities	59,871	(484)	90,863	(2,656)	150,734	(3,140)
CMO	-	-	203,254	(12,081)	203,254	(12,081)
Municipal bonds	70,989	(778)	77,723	(5,410)	148,712	(6,188)
Total held-to-maturity securities	$ 138,339	$ (1,277)	$ 426,784	$ (22,754)	$ 565,123	$ (24,031)

	December 31, 2017					
	Less Than 12 Months		12 Months or Longer		Total	
	Fair Value	Gross Unrealized Holding Losses	Fair Value	Gross Unrealized Holding Losses	Fair Value	Gross Unrealized Holding Losses
			(Dollars in thousands)			
Investment securities available-for-sale:						
Residential mortgage-backed securities	$ 414,091	$ (1,828)	$ 303,746	$ (6,274)	$ 717,837	$ (8,102)
CMO/REMIC - residential	95,137	(487)	71,223	(1,595)	166,360	(2,082)
Municipal bonds	946	(4)	13,956	(240)	14,902	(244)
Total available-for-sale securities	$ 510,174	$ (2,319)	$ 388,925	$ (8,109)	$ 899,099	$ (10,428)
Investment securities held-to-maturity:						
Government agency/GSE	$ 18,950	$ (27)	$ 43,495	$ (2,107)	$ 62,445	$ (2,134)
Residential mortgage-backed securities	51,297	(188)	55,306	(194)	106,603	(382)
CMO	-	-	216,431	(8,641)	216,431	(8,641)
Municipal bonds	32,069	(492)	66,217	(3,298)	98,286	(3,790)
Total held-to-maturity securities	$ 102,316	$ (707)	$ 381,449	$ (14,240)	$ 483,765	$ (14,947)

The Company did not record any charges for other-than-temporary impairment losses for the years ended December 31, 2018 and 2017.

Loans

Total loans and leases, net of deferred fees and discounts, of $7.76 billion at December 31, 2018, increased by $2.93 billion, or 60.74%, from $4.83 billion at December 31, 2017. The increase in total loans included $2.73 billion of loans acquired from CB in the third quarter of 2018. Excluding the acquired CB loans, total loans increased by $199.9 million, or 4.14%, for 2018. Commercial real estate loans grew by $223.1 million and dairy & livestock and agribusiness loans increased by $34.1 million. This growth was partially offset by decreases of $46.6 million in commercial and industrial loans, and $13.5 million in consumer and other loans.

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Total loans, net of deferred loan fees, comprise 75.47% of our total earning assets as of December 31, 2018. The following table presents our loan portfolio, excluding PCI loans, by type for the periods presented.

Distribution of Loan Portfolio by Type

	December 31,				
	2018	**2017**	**2016**	**2015**	**2014**
	(Dollars in thousands)				
Commercial and industrial	$ 1,002,209	$ 513,325	$ 485,078	$ 434,099	$ 390,011
SBA	350,043	122,055	97,184	106,867	134,265
Real estate:					
Commercial real estate	5,394,229	3,376,713	2,930,141	2,643,184	2,487,803
Construction	122,782	77,982	85,879	68,563	55,173
SFR mortgage	296,504	236,202	250,605	233,754	205,124
Dairy & livestock and agribusiness	393,843	347,289	338,631	305,509	279,173
Municipal lease finance receivables	64,186	70,243	64,639	74,135	77,834
Consumer and other loans	128,429	64,229	78,274	69,278	69,884
Gross loans, excluding PCI loans	7,752,225	4,808,038	4,330,431	3,935,389	3,699,267
Less: Deferred loan fees, net	(4,828)	(6,289)	(6,952)	(8,292)	(8,567)
Gross loans, excluding PCI loans, net of deferred loan fees	7,747,397	4,801,749	4,323,479	3,927,097	3,690,700
Less: Allowance for loan losses	(63,409)	(59,218)	(60,321)	(59,156)	(59,825)
Net loans, excluding PCI loans	7,683,988	4,742,531	4,263,158	3,867,941	3,630,875
PCI Loans	$ 17,214	$ 30,908	$ 73,093	$ 93,712	$ 133,496
Discount on PCI loans	-	(2,026)	(1,508)	(3,872)	(7,129)
Less: Allowance for loan losses	(204)	(367)	(1,219)	-	-
PCI loans, net	17,010	28,515	70,366	89,840	126,367
Total loans and lease finance receivables	$ 7,700,998	$ 4,771,046	$ 4,333,524	$ 3,957,781	$ 3,757,242

As of December 31, 2018, $229.8 million, or 4.26% of the total commercial real estate loans included loans secured by farmland, compared to $206.1 million, or 6.10%, at December 31, 2017. The loans secured by farmland included $126.9 million for loans secured by dairy & livestock land and $102.9 million for loans secured by agricultural land at December 31, 2018, compared to $118.2 million for loans secured by dairy & livestock land and $87.9 million for loans secured by agricultural land at December 31, 2017. As of December 31, 2018, dairy & livestock and agribusiness loans of $393.8 million were comprised of $340.5 million for dairy & livestock loans and $53.3 million for agribusiness loans, compared to $310.6 million for dairy & livestock loans and $36.7 million for agribusiness loans at December 31, 2017.

Real estate loans are loans secured by conforming trust deeds on real property, including property under construction, land development, commercial property and single-family and multi-family residences. Our real estate loans are comprised of industrial, office, retail, medical, single-family residences, multi-family residences, and farmland. Consumer loans include auto and equipment leases, installment loans to consumers as well as home equity loans and other loans secured by junior liens on real property. Municipal lease finance receivables are leases to municipalities. Dairy & livestock and agribusiness loans are loans to finance the operating needs of wholesale dairy farm operations, cattle feeders, livestock raisers, and farmers.

As of December 31, 2018, the Company had $181.2 million of total SBA 504 loans. SBA 504 loans include term loans to finance capital expenditures and for the purchase of commercial real estate. Initially the Bank provides two separate loans to the borrower representing a first and second lien on the collateral. The loan with the first lien is typically at a 50% advance to the acquisition costs and the second lien loan provides the financing for 40% of the acquisition costs with the borrower s down payment of 10%. When the loans are funded the Bank retains the first lien loan for its term and sells the second lien loan to the SBA subordinated debenture program.

A majority of the Bank s 504 loans are granted for the purpose of commercial real estate acquisition. As of December 31, 2018, the Company had $170.1 million of total SBA 7(a) loans. The SBA 7(a) loans include revolving lines of credit (SBA Express) and term loans to finance long term working capital requirements, capital expenditures, and/or for the purchase or refinance of commercial real estate.

As of December 31, 2018, the Company had $122.8 million in construction loans. This represents 1.58% of total gross loans held-for-investment. There were no PCI construction loans at December 31, 2018. Although our construction loans are located throughout our market footprint, the majority of construction loans consist of commercial land development and construction projects in Los Angeles County, Orange County, and the Inland Empire region of Southern California. At December 31, 2018, construction loans consisted of $66.9 million in SFR construction loans and $55.9 million in commercial construction loans. There were no nonperforming construction loans at December 31, 2018.

PCI Loans from the SJB Acquisition

These PCI loans were acquired from SJB on October 16, 2009 and were subject to a loss sharing agreement with the FDIC. Under the terms of such loss sharing agreement, the FDIC absorbed 80% of losses and shared in 80% of loss recoveries up to $144.0 million in losses with respect to covered assets, after a first loss amount of $26.7 million. The loss sharing agreement covered 5 years for commercial loans and covers 10 years for single-family residential loans from the October 16, 2009 acquisition date and the loss recovery provisions are in effect for 8 and 10 years, respectively, for commercial and single-family residential loans from the acquisition date. The loss sharing agreement for commercial loans expired October 16, 2014. The loss sharing agreement with the FDIC for single-family residential loans, which would have expired on October 16, 2019, was terminated by the Bank on July 20, 2018.

The following table presents PCI loans by type for the periods presented.

Distribution of Loan Portfolio by Type

	December 31,				
	2018	**2017**	**2016**	**2015**	**2014**
	(Dollars in thousands)				
Commercial and industrial	$ 519	$ 934	$ 2,309	$ 7,473	$ 14,605
SBA	1,258	1,383	327	393	1,110
Real estate:					
Commercial real estate	14,407	27,431	67,594	81,786	109,350
Construction	-	-	-	-	-
SFR mortgage	145	162	178	193	205
Dairy & livestock and agribusiness	700	770	1,216	1,429	4,890
Municipal lease finance receivables	-	-	-	-	-
Consumer and other loans	185	228	1,469	2,438	3,336
Gross PCI loans	17,214	30,908	73,093	93,712	133,496
Less: Purchase accounting discount	-	(2,026)	(1,508)	(3,872)	(7,129)
Gross PCI loans, net of discount	17,214	28,882	71,585	89,840	126,367
Less: Allowance for PCI loan losses	(204)	(367)	(1,219)	-	-

Net PCI loans	$ 17,010	$ 28,515	$ 70,366	$ 89,840	$ 126,367

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Our loan portfolio is geographically disbursed throughout our marketplace, with less than 5% located outside of California. The following is the breakdown of our total held-for-investment commercial real estate loans, excluding PCI loans, by region as of December 31, 2018.

	December 31, 2018			
	Total Loans		Commercial Real Estate Loans	
	(Dollars in thousands)			
Los Angeles County	$ 3,414,138	44.1%	$ 2,352,477	43.6%
Central Valley	1,095,139	14.1%	777,399	14.4%
Inland Empire	1,061,652	13.7%	902,730	16.7%
Orange County	1,020,748	13.2%	660,900	12.2%
Central Coast	443,700	5.7%	343,790	6.4%
San Diego	243,277	3.1%	127,579	2.4%
Other California	156,906	2.0%	67,989	1.3%
Out of State	316,665	4.1%	161,365	3.0%
	$ 7,752,225	100.0%	$ 5,394,229	100.0%

The following is the breakdown of total PCI held-for-investment commercial real estate loans by region as of December 31, 2018.

	December 31, 2018			
	Total PCI Loans		Commercial Real Estate Loans	
	(Dollars in thousands)			
Central Valley	$ 17,214	100.0%	$ 14,407	100.0%
Los Angeles County	-	-	-	-
Central Coast	-	-	-	-
Other California	-	-	-	-
Out of State	-	-	-	-
	$ 17,214	100.0%	$ 14,407	100.0%

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The table below breaks down our real estate portfolio, excluding PCI loans.

	December 31, 2018			
	Loan Balance	Percent	Percent Owner-Occupied (1)	Average Loan Balance
	(Dollars in thousands)			
SFR mortgage:				
SFR mortgage - Direct	$ 280,872	4.9%	100.0%	$ 617
SFR mortgage - Mortgage pools	15,632	0.3%	100.0%	252
Total SFR mortgage	296,504	5.2%		
Commercial real estate:				
Multi-family	537,644	9.4%	0.6%	1,591
Industrial	1,933,155	34.0%	56.2%	1,443
Office	914,192	16.1%	27.4%	1,451
Retail	828,040	14.5%	12.2%	1,714
Medical	276,955	4.9%	46.4%	1,822
Secured by farmland (2)	229,789	4.0%	98.6%	2,108
Other (3)	674,454	11.9%	48.5%	1,457
Total commercial real estate	5,394,229	94.8%		
Total SFR mortgage and commercial real estate loans	$ 5,690,733	100.0%	42.5%	1,411

(1) Represents percentage of reported owner-occupied at origination in each real estate loan category.
(2) The loans secured by farmland included $126.9 million for loans secured by dairy & livestock land and $102.9 million for loans secured by agricultural land at December 31, 2018.
(3) Other loans consist of a variety of loan types, none of which exceeds 2.0% of total commercial real estate loans.

In the table above, SFR mortgage - Direct loans include SFR mortgage loans which are currently generated through an internal program in our Centers. This program is focused on owner-occupied SFR s with defined loan-to-value, debt-to-income and other credit criteria, such as FICO credit scores, that we believe are appropriate for loans which are primarily intended for retention in our Bank s loan portfolio. We originated loan volume in the aggregate principal amount of $45.4 million under this program during 2018.

In addition, we previously purchased pools of owner-occupied single-family loans from real estate lenders, SFR mortgage Mortgage Pools, with a remaining balance totaling $15.6 million at December 31, 2018. These loans were purchased with average FICO scores predominantly ranging from 700 to over 800 and overall original loan-to-value ratios of 60% to 80%. We have not purchased any mortgage pools since August 2007.

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The table below breaks down our PCI real estate portfolio.

	December 31, 2018			
	Loan Balance	Percent	Percent Owner-Occupied (1)	Average Loan Balance
	(Dollars in thousands)			
SFR mortgage				
SFR mortgage - Direct	$ 145	1.0%	100.0%	$ 145
SFR mortgage - Mortgage pools	-	-	-	-
Total SFR mortgage	145	1.0%		
Commercial real estate:				
Multi-family	552	3.8%	-	552
Industrial	2,426	16.6%	77.6%	303
Office	1,265	8.7%	100.0%	422
Retail	1,393	9.6%	-	348
Medical	1,951	13.4%	100.0%	650
Secured by farmland	1,163	8.0%	100.0%	291
Other (2)	5,657	38.9%	76.2%	435
Total commercial real estate	14,407	99.0%		
Total SFR mortgage and commercial real estate loans	$ 14,552	100.0%	73.7%	393

(1) Represents percentage of reported owner-occupied at origination in each real estate loan category.
(2) Includes loans associated with hospitality, churches and gas stations, which represents approximately 76% of other loans.

The table below provides the maturity distribution for held-for-investment total gross loans, including PCI loans, as of December 31, 2018. The loan amounts are based on contractual maturities although the borrowers have the ability to prepay the loans. Amounts are also classified according to repricing opportunities or rate sensitivity.

Loan Maturities and Interest Rate Category at December 31, 2018

	Within One Year	After One But Within Five Years	After Five Years	Total
	(Dollars in thousands)			
Types of Loans:				
Commercial and industrial	$ 445,699	$ 379,867	$ 177,162	$ 1,002,728
SBA	2,137	20,474	328,690	351,301

Real estate:				
Commercial real estate	264,715	1,644,371	3,499,550	5,408,636
Construction	97,833	24,672	277	122,782
SFR mortgage	6,316	14,425	275,908	296,649
Dairy & livestock and agribusiness	341,483	37,485	15,575	394,543
Municipal lease finance receivables	585	7,285	56,316	64,186
Consumer and other loans	12,605	20,453	95,556	128,614
Total gross loans	$ 1,171,373	$ 2,149,032	$ 4,449,034	$ 7,769,439
Amount of Loans based upon:				
Fixed Rates	$ 227,900	$ 1,441,432	$ 2,094,774	$ 3,764,106
Floating or adjustable rates	943,473	707,600	2,354,260	4,005,333
Total gross loans	$ 1,171,373	$ 2,149,032	$ 4,449,034	$ 7,769,439

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As a normal practice in extending credit for commercial and industrial purposes, we may accept trust deeds on real property as collateral. In some cases, when the primary source of repayment for the loan is anticipated to come from the cash flow from normal operations of the borrower, and real property has been taken as collateral, the real property is considered a secondary source of repayment for the loan. Since we lend primarily in Southern and Central California, our real estate loan collateral is concentrated in this region. At December 31, 2018, substantially all of our loans secured by real estate were collateralized by properties located in California. This concentration is considered when determining the adequacy of our allowance for loan losses.

Nonperforming Assets

The following table provides information on nonperforming assets, excluding PCI loans, as of December 31 for each of the last five years.

	December 31,				
	2018	**2017**	**2016**	**2015**	**2014**
	(Dollars in thousands)				
Nonaccrual loans	$ 16,442	$ 6,516	$ 5,526	$ 8,397	$ 11,901
Troubled debt restructured loans (nonperforming)	3,509	4,200	1,626	12,622	20,285
OREO, net	420	4,527	4,527	6,993	5,637
Total nonperforming assets	$ 20,371	$ 15,243	$ 11,679	$ 28,012	$ 37,823
Troubled debt restructured performing loans	$ 3,594	$ 4,809	$ 19,233	$ 42,687	$ 53,589
Percentage of nonperforming assets to total loans outstanding, net of deferred fees, and OREO	0.26%	0.32%	0.27%	0.70%	0.99%
Percentage of nonperforming assets to total assets	0.18%	0.18%	0.14%	0.37%	0.51%

At December 31, 2018, loans classified as impaired, excluding PCI loans, totaled $23.5 million, or 0.30% of total gross loans, compared to $15.5 million, or 0.32% of total loans at December 31, 2017. At December 31, 2018, nonperforming loans of $20.0 million included $12.3 million of loans acquired from CB in the third quarter of 2018. At December 31, 2018, impaired loans which were restructured in a TDR represented $7.1 million, of which $3.5 million were nonperforming and $3.6 million were performing.

Of the $23.5 million total impaired loans as of December 31, 2018, $20.5 million were considered collateral dependent and measured using the fair value of the collateral based on current appraisals (obtained within 1 year). The amount of impaired loans measured using the present value of expected future cash flows discounted at the loans effective rate were $3.0 million.

Troubled Debt Restructurings

Total TDRs were $7.1 million at December 31, 2018, compared to $9.0 million at December 31, 2017. At December 31, 2018, we had $3.5 million in nonperforming TDRs and $3.6 million of performing TDRs were accruing interest as restructured loans. Performing TDRs were granted in response to borrower financial difficulty and generally provide for a modification of loan repayment terms. The performing restructured loans represent the only impaired loans accruing interest at each respective reporting date. A performing restructured loan is reasonably assured of repayment and is performing in accordance with the modified terms. We have not restructured loans into multiple loans in what is typically referred to as an A/B note structure, where normally the A note meets current underwriting standards and the B note is typically immediately charged off upon restructuring.

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The following table provides a summary of TDRs, excluding PCI loans, for the periods presented.

	December 31, 2018		December 31, 2017	
	Balance	Number of Loans	Balance	Number of Loans
	(Dollars in thousands)			
Performing TDRs:				
Commercial and industrial	$ 135	2	$ 190	3
SBA	575	1	625	1
Real Estate:				
Commercial real estate	472	1	1,291	2
Construction	-	-	-	-
SFR mortgage	2,412	9	2,703	10
Dairy & livestock and agribusiness	-	-	-	-
Consumer and other	-	-	-	-
Total performing TDRs	$ 3,594	13	$ 4,809	16
Nonperforming TDRs:				
Commercial and industrial	$ 21	1	$ 50	1
SBA	-	-	281	2
Real Estate:				
Commercial real estate	3,143	1	3,791	2
Construction	-	-	-	-
SFR mortgage	-	-	-	-
Dairy & livestock and agribusiness	78	1	78	1
Consumer and other	267	1	-	-
Total nonperforming TDRs	$ 3,509	4	$ 4,200	6
Total TDRs	$ 7,103	17	$ 9,009	22

At December 31, 2018 and 2017, $490,000 and $1,000 of the allowance for loan losses was specifically allocated to TDRs, respectively. Impairment amounts identified are typically charged off against the allowance at the time a probable loss is determined. During the years ended December 31, 2018 and 2017, there were no charge-offs on TDRs.

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Nonperforming Assets and Delinquencies

The table below provides trends in our nonperforming assets and delinquencies, excluding PCI loans, for the periods presented.

	December 31, 2018	September 30, 2018	June 30, 2018	March 31, 2018	December 31, 2017
			(Dollars in thousands)		
Nonperforming loans:					
Commercial and industrial	$ 7,490	$ 3,026	$ 204	$ 272	$ 250
SBA	2,892	3,005	574	589	906
Real estate:					
Commercial real estate	6,068	5,856	6,517	6,746	6,842
Construction	-	-	-	-	-
SFR mortgage	2,937	2,961	1,578	1,309	1,337
Dairy & livestock and agribusiness	78	775	800	818	829
Consumer and other loans	486	807	509	438	552
Total	**$ 19,951**	**$ 16,430**	**$ 10,182**	**$ 10,172**	**$ 10,716**
% of Total gross loans	**0.26%**	**0.22%**	**0.21%**	**0.21%**	**0.22%**
Past due 30-89 days:					
Commercial and industrial	$ 909	$ 274	$ -	$ -	$ 768
SBA	1,307	123	-	-	403
Real estate:					
Commercial real estate	2,789	-	-	-	-
Construction	-	-	-	-	-
SFR mortgage	285	-	-	680	-
Dairy & livestock and agribusiness	-	-	-	-	-
Consumer and other loans	-	98	47	63	1
Total	**$ 5,290**	**$ 495**	**$ 47**	**$ 743**	**$ 1,172**
% of Total gross loans	**0.07%**	**0.01%**	**0.001%**	**0.02%**	**0.02%**
OREO:					
Real estate:					
Commercial real estate	$ -	$ -	$ -	$ -	$ -
Construction	-	-	-	-	4,527
SFR mortgage	420	420	-	-	-
Total	**$ 420**	**$ 420**	**$ -**	**$ -**	**$ 4,527**
	$ 25,661	**$ 17,345**	**$ 10,229**	**$ 10,915**	**$ 16,415**

Total nonperforming, past due, and OREO					
% of Total gross loans	**0.33%**	**0.23%**	**0.21%**	**0.23%**	**0.34%**

Nonperforming loans, defined as nonaccrual loans plus nonperforming TDR loans, were $20.0 million at December 31, 2018, or 0.26% of total loans. Total nonperforming loans at December 31, 2018 included $12.3 million of nonperforming loans acquired from CB in the third quarter of 2018. This compares to nonperforming loans of $10.7 million, or 0.22% of total loans, at December 31, 2017. The $9.2 million increase in nonperforming loans was primarily due to a $7.2 million increase in nonperforming commercial and industrial loans, a $2.0 million increase in nonperforming SBA loans, and a $1.6 million increase in nonperforming SFR mortgage loans, partially offset by a $774,000 decrease in nonperforming commercial real estate loans and a $751,000 decrease in nonperforming dairy & livestock and agribusiness loans.

At December 31, 2018, we had one OREO property with a carrying value of $420,000, compared to one property with a carrying value of $4.5 million at December 31, 2017. During 2018, we sold one OREO property, realizing a net gain on sale of $3.5 million. There was one addition to OREO for the twelve months ended December 31, 2018.

Changes in economic and business conditions have had an impact on our market area and on our loan portfolio. We continually monitor these conditions in determining our estimates of needed reserves. However, we

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cannot predict the extent to which the deterioration in general economic conditions, real estate values, increases in general rates of interest and changes in the financial conditions or business of a borrower may adversely affect a borrower s ability to pay or the value of our collateral. See *Risk Management Credit Risk Management* included herein.

Acquired SJB Assets

Loans acquired through the SJB acquisition are accounted for under ASC Topic 310-30, *Loans and Debt Securities Acquired with Deteriorated Credit Quality* (ASC 310-30). PCI loans accounted for under ASC 310-30 are generally considered accruing and performing loans as the loans accrete interest income over the estimated life of the loan when cash flows are reasonably estimable. Accordingly, acquired impaired loans that are contractually past due are still considered to be accruing and performing loans. If the timing and amount of future cash flows is not reasonably estimable, the loans may be classified as nonperforming loans and interest income is not recognized until the timing and amount of future cash flows can be reasonably estimated. As of December 31, 2018, there were no PCI loans considered as nonperforming as described above.

There were no acquired SJB OREO properties remaining as of December 31, 2018 and 2017.

Allowance for Loan Losses

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

The allowance for loan losses totaled $63.6 million as of December 31, 2018, compared to $59.6 million as of December 31, 2017. The allowance for loan losses was increased by net recoveries of $2.5 million and $1.5 million in provision for loan losses for the year ended December 31, 2018. This compares to an $8.5 million loan loss provision recapture, offset by net recoveries of $6.5 million for the same period of 2017.

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The table below presents a summary of net charge-offs and recoveries by type and the resulting allowance for loan losses and recapture of provision for loan losses for the periods presented.

	As of and For the Year Ended December 31,				
	2018	2017	2016	2015	2014
	(Dollars in thousands)				
Allowance for loan losses at beginning of period	$ 59,585	$ 61,540	$ 59,156	$ 59,825	$ 75,235
Charge-offs:					
Commercial and industrial	(10)	(138)	(120)	(411)	(888)
SBA	(257)	-	-	(37)	(50)
Commercial real estate	-	-	-	(117)	(353)
Construction	-	-	-	-	-
SFR mortgage	(13)	-	(102)	(215)	-
Dairy & livestock and agribusiness	-	-	-	-	(1,061)
Consumer and other loans	(11)	(13)	(16)	(229)	(17)
Total charge-offs	(291)	(151)	(238)	(1,009)	(2,369)
Recoveries:					
Commercial and industrial	82	118	630	319	873
SBA	20	78	40	41	114
Commercial real estate	-	154	792	4,330	140
Construction	2,506	6,036	7,174	581	885
SFR mortgage	51	212	-	186	401
Dairy & livestock and agribusiness	19	19	216	407	492
Consumer and other loans	141	79	170	76	154
Total recoveries	2,819	6,696	9,022	5,940	3,059
Net recoveries	2,528	6,545	8,784	4,931	690
Provision for (recapture of) loan losses	1,500	(8,500)	(6,400)	(5,600)	(16,100)
Allowance for loan losses at end of period	$ 63,613	$ 59,585	$ 61,540	$	