FEDERAL DEPOSIT INSURANCE CORPORATION
Washington, D.C. 20429

FORM 10-K

Mark One

[x] ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the fiscal year ended December 31, 2013
or

[ ] TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from ________ to ________.

PREFERRED BANK
(Exact name of registrant as specified in its charter)

California	**33539**	**95-4340199**
(State or other jurisdiction of incorporation or organization)	*(FDIC Certificate Number)*	*(I.R.S. Employer Identification No.)*

601 S. Figueroa Street, 29th Floor, Los Angeles, California	**90017**
(Address of principal executive offices)	*(Zip Code)*

Registrant's telephone number, including area code: **(213) 891-1188**

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

Title of each class	*Name of each exchange on which registered*
Common Stock, No Par Value	**The NASDAQ Stock Market LLC**

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

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

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 [x]

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 [x] No [ ]

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes [ ] No [ ]

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 or 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 the Form 10-K or any amendment to this Form 10-K. [x]

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filed, non-accelerated filer, or a smaller reporting company. See definition of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filed [ ] Accelerated filer [x] Non-accelerated filer [ ] Smaller reporting company [ ]

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

The aggregate market value of the voting and non-voting common equity held by non-affiliates of the Registrant, computed by reference to the price at which the common equity was last sold as of the last business day of the Registrant's most recently completed second fiscal quarter (June 30, 2013) was $218,449,582.

Number of shares of common stock of the Registrant outstanding as of March 12, 2014, was 13,428,203.

The following documents are incorporated by reference herein:

Document Incorporated By Reference	Part of Form 10-K Into Which Incorporated
Definitive Proxy Statement for the Annual Meeting of Shareholders which will be filed within 120 days of the fiscal year ended December 31, 2013	Part III

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PART I

Forward-Looking Statements

Certain matters discussed in this report may constitute forward-looking statements within the meaning of Section 27A of the 1933 Act and Section 21E of the Securities Exchange Act of 1934, as amended (the "Exchange Act"), and as such, may involve risks and uncertainties. These forward-looking statements relate to, among other things, expectations of the environment in which we operate and projections of future performance. Such statements can generally be identified by the use of forward-looking language, such as "is expected to," "will likely result," "anticipated," "estimate," "forecast," "intends to," or may include other similar words, phrases, or future or conditional verbs such as "believes," "plans," "continue," "remain," "may," "will," "would," "should," "could," "can," or similar language. Our actual results, performance, or achievements may differ significantly from the results, performance, or achievements expected or implied in such forward-looking statements. When considering these statements, the reader should consider that they are subject to certain risks and uncertainties, as well as any cautionary statements made within the report, and should also note that these statements are made as of the date of the report and based only on information known to us at that time.

Factors causing risk and uncertainty, which could cause future results to be materially different from forward-looking statements contained in this report as well as from historical performance, include but are not limited to:

- Regulatory decisions regarding the bank, and impact of future regulatory and governmental agency decisions including Basel III capital standards
- Adequacy of allowance for loan and lease loss estimates in comparison to actual future losses
- Necessity of additional capital in the future, and possible unavailability of that capital on acceptable terms
- Economic and market conditions that may adversely affect the Bank and our industry
- Possible loss of members of senior management or other key employees upon which the Bank heavily relies
- Natural disasters or recurring energy shortages
- Variations in interest rates which may negatively affect the Bank's financial performance
- Strong competition from other financial service entities
- Possibility that the Bank's underwriting practices may prove not to be effective
- Possibility that appraised property values may not hold at a level greater than the amount of the debt they secure
- Adverse economic conditions in Asia which could impact the Bank's business adversely
- The economic impact of Federal budgetary policies
- Failure to attract deposits, inhibiting growth
- Interruption or break in the communication, information, operating, and financial control systems upon which the Bank relies
- Potential changes in the U.S. government's monetary policies
- Environmental liability with respect to properties to which the Bank takes title
- Negative publicity
- Possible security breaches in our online banking services

These factors are further described in this Annual Report on Form 10-K within Item 1A. We do not undertake, and we specifically disclaim any obligation to update any forward looking statements to reflect the occurrence of events or circumstances after the date of such statements except as required by law.

ITEM 1. BUSINESS

References in this Annual Report on Form 10-K to "we," "us," or "our," and the "Bank" mean Preferred Bank and its wholly-owned subsidiary, PB Investment and Consulting, Inc.

General

We are a commercial bank based in Southern California, with a niche in the Chinese-American market. We consider the Chinese-American market to encompass individuals born in the United States of Chinese ancestry, ethnic Chinese who have immigrated to the United States and ethnic Chinese who live abroad but conduct business in the United States.

We commenced operations in December 1991 as a California state-chartered bank in Los Angeles, California. Our deposits are insured by the Federal Deposit Insurance Corporation ("FDIC"). We are a member of the Federal Home Loan Bank of San Francisco ("FHLB"). At December 31, 2013, our total assets were $1.8 billion, loans were $1.3 billion, deposits were $1.5 billion and shareholders' equity grew to $206.9 million. We had net earnings per share on a diluted basis of $1.42 for the year ended December 31, 2013 as compared to net earnings of $1.78 per share for the year ended December 31, 2012. Net interest income before provision for credit losses increased from $53.8 million for the year ended December 31, 2012 to $62.0 million for the year ended December 31, 2013. We recorded a provision for credit losses of $3.3 million in 2013, which was $16.5 million less than the provision of $19.8 million recorded in 2012, the relative decrease of which is responsible for a portion of the increases in income for the year. During the years 2008 – 2010, we suffered operating losses due to losses on our loan portfolio. In June 2010, we raised $77.0 million in a private preferred stock offering in order to shore up our capital position due to the operating losses during the recession. We returned to profitability in 2011 and have been profitable in each year since, culminating in net income of $19.2 million in 2013. Also, since 2011, the Bank's nonperforming assets ("NPA's") have continued to decline. From their peak of $204.1 million, or 15.6% of total assets as of December 31, 2009, to $85.0 million or 6.5% of total assets as of the end of 2011, total NPA's now stand at $19.6 million or 1.1% of total assets. As the Bank's NPA levels have declined, so have the costs associated with holding such assets and thus profitability has improved over the same time frame. We believe that now our NPA levels have declined to the point where our profitability will not be impaired by such costs.

We provide personalized deposit services as well as real estate finance, commercial loans and trade finance to small and mid-sized businesses and their owners, entrepreneurs, real estate developers and investors, professionals and high net worth individuals. We are generally focused on businesses as opposed to retail customers and have a small number of customer relationships for whom we provide a high level of service and personal attention. We believe we have benefited, and will continue to benefit from the significant migration into California of ethnic Chinese from China and other areas of East Asia. While the majority of our business is not dependent on the Chinese-American market, it represents an important element of our operating strategy, especially for our branch network and deposit products and services.

We derive our income primarily from interest received on our loan and investment securities portfolio, and fee income we receive in connection with servicing our loan and deposit customers. Our major operating expenses are the interest we pay on deposits and borrowings, and the salaries and related benefits we pay our management and staff. We rely primarily on locally-generated deposits, approximately half of which we receive from the Chinese-American market mostly within Southern California, to fund our loan and investment activities.

We conduct operations from our main office in downtown Los Angeles, California and ten full-service branch banking offices in Los Angeles, Orange, and San Francisco Counties (San Francisco as of February 2013). We market our services and conduct our business primarily in Los Angeles, Orange, Ventura, Riverside, San Bernardino and San Francisco Counties. Additionally, the Bank opened a new branch in San Francisco, California, in February of 2013, and we are looking to further expand our services into Northern California in the future.

As a result of the rapid slowdown in the real estate market and deteriorating economic conditions, the Bank incurred net operating losses during the years 2008 through 2010 due to significant credit quality issues. Although the Bank has been profitable for the last three years, if general economic conditions and the real estate market experience a decline, the Bank could suffer future losses. Our national economy and California in particular are in the midst of a recovery from an unprecedented recession that has its roots in real estate values. Although management remains committed to improving credit quality in the loan portfolio, management has also been focused on growing the Bank's loans and deposits in light of the improvement in the economy and the credit quality of the Bank's loan portfolio over the past two years.

As a result of a regulatory examination during 2013, the Memorandum of Understanding, which the Bank entered into with the FDIC and the California Department of Business Oversight ("CBDO") on May 25, 2012, was terminated and the Bank entered into a new Memorandum of Understanding (the "MOU") with both the FDIC and the CDBO on October 1, 2013. Among other things, the MOU requires the Bank to improve its compliance with the Bank Secrecy Act ("BSA"), maintain a minimum Tier 1 Leverage Ratio of 10%, and to refrain from declaring or paying cash dividends to its shareholders and establishing new branches and offices without the prior written approval of the FDIC and CBDO. As of December 31, 2013, the Tier 1 Leverage Ratio of the Bank was 11.80%, exceeding the level required by the MOU. In response to the examination findings, management has made significant staffing investments and dedicated a significant amount of time and resources toward strengthening its BSA and compliance programs and complying with the MOU. The Board of Directors and management are committed to meeting all of the requirements of the MOU and seeing to its earliest possible termination. See "REGULATION AND SUPERVISION."

Our main office is located at 601 S. Figueroa Street, 29th Floor, Los Angeles, CA 90017 and our telephone number is (213) 891-1188. Our internet address is *www.preferredbank.com*. On our Investor Relations tab, which can be accessed through *www.preferredbank.com*, we post the following filings as soon as reasonably practicable after they are filed with or furnished to the FDIC:

- Our annual report on Form 10-K,
- Our quarterly reports on Form 10-Q,
- Our current reports on Form 8-K,
- Our proxy statement related to our annual shareholders' meeting and any amendments to those reports or statements filed with or furnished to the FDIC pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934,
- Our Form 4 statements of holdings of our directors and executive officers.

All such filings on our Investor Relations website are available free of charge. The reference to our website address does not constitute incorporation by reference of the information contained in the website and should not be considered part of this document. A copy of our Code of Personal and Business Conduct, including any amendments thereto or waivers thereof and Board Committee Charters can also be accessed on our website. We will provide, at no cost, a copy of our Code of Personal and Business Conduct and Board Committee Charters upon request by phone or in writing at the above phone number or address, attention: Edward J. Czajka, Executive Vice President and Chief Financial Officer.

Our Traditional Banking Business

We have historically provided a range of deposit and loan products and services to customers primarily within the following categories:

- *Real Estate Finance*—consisting of investors and developers within the real estate industry and of owner-occupied properties in Southern California. We have traditionally provided construction loans and mini-permanent ("mini-perm") loans for residential, commercial, industrial and other income producing properties, although construction lending is no longer a focus for new business. A portion of our real estate loans are to borrowers who are also international trade finance customers. We do not typically market single-family residential mortgages but provide them as an accommodation to our business customers.

- *Middle Market Business*—consisting of manufacturing, service and distribution companies with annual sales of approximately $5 million to $100 million and with borrowing requirements of up to approximately $12 million. We offer a range of lending products to customers in this market, including working capital loans, equipment financing and commercial real estate loans. In 2011, we increased our focus on generation of working capital and equipment financing loans. Additionally, we provide a full range of deposit products and related services including safe deposit boxes, account reconciliation, courier service and cash management services.

- *International Trade Finance*—consisting of importers and exporters based in the U.S. requiring both borrowing and operational products. We offer a full range of products to international trade finance customers, including commercial and standby letters of credit, acceptance financing, documentary collections, foreign draft collections, international wires and foreign exchange.

- *High-wealth Banking* —consisting of wealthy individuals residing in the Pacific Rim area with residences, real estate investments or businesses in Southern California. We offer all of our banking products and services to this segment through our multi-lingual team of professionals knowledgeable in the business environment and financial affairs of Pacific Rim countries. We believe our language capabilities provide us with a competitive advantage.

- *Professionals*—consisting generally of physicians, accountants, attorneys, business managers and other professionals. We provide specialized personal banking services to customers in this segment including courier service, several types of specialized deposit accounts and personal and business loans as well as lines of credit.

We provide a fully operational traditional Internet banking system with bill pay services for these customers.

Our Current Focus

As we have recovered from the high levels of NPAs and the losses associated with those assets during the economic downturn, we have been rebuilding our business development staff and more recently, our administrative staff. During 2013, as we have grown back to the asset size of we had during the year 2007, we have also been fortifying our infrastructure in order to meet the new growth and regulatory challenges facing all banks in this environment. We have made significant human resource investments in not only our BSA Department, but also our Information Technology, Operations, Credit Administration and our Compliance Departments. The bolstering of these areas is intended to support the future growth of the Bank, maintain a sound internal control structure as well as to meet the regulatory requirements of our industry.

With all of those investments being made to the infrastructure of the Bank, we were able to achieve substantial growth in loans and in profitability in 2013. This was due to the hiring of new business development and relationship officers in all regions of the Bank's market during the years 2011 through 2013 and the relationships these officers have brought with them. We now have a much larger business development staff than at any time in our history and we will look for our staff to continue to bring in new, profitable relationships, driving the future growth of the Bank.

Finally, we are in the process of negotiating a lease for a new branch office to be located on Ventura Boulevard in Encino, California. Encino is located in the Southern San Fernando Valley area of Los Angeles. The San Fernando Valley is home to a significant portion of the population of Los Angeles and we currently have no branch offices in the area. We have hired the manager for this branch and are in the process of hiring the banking team. Although the opening of this office is subject to regulatory approval, we do not believe such approval will be withheld.

Our Market

We conduct operations from our main office in downtown Los Angeles, California and 11 full-size branch banking offices in Los Angeles, Orange, and San Francisco Counties as of December 31, 2013. We market our services and conduct our business primarily in Los Angeles, Orange, Ventura, Riverside, San Bernardino, and San Francisco counties. In February 2013, we opened a branch in San Francisco and will be working to further expand into the Northern California market in 2014.

We believe that Chinese-Americans continue to be the largest Asian ethnic group in Los Angeles County. According to the U.S. Census 2010, between the years 2000 and 2010, the Chinese-American population in the United States grew by approximately 38%, with 37% of all Chinese-Americans living in California. In 2010, there were approximately 523,000 Chinese-Americans living in the five Southern California counties in which the Bank conducted business. In San Francisco County, there were approximately 172,000 Chinese Americans which represented 21% of the population of San Francisco County.

We believe we are well positioned to compete effectively with the Chinese-American community banks, the larger commercial banks and major publicly listed and foreign-owned Chinese banks operating in Southern California by offering the following:

- Deposit and cash management services to businesses and high net worth depositors with a high degree of personal service and responsiveness;

- An experienced, multi-lingual management team and staff who have an understanding of Asian markets and cultures who we believe can provide sophisticated credit solutions faster, more efficiently and with a higher degree of personal service than what is provided by our competition; and

- Loan products to customers requiring credit of a size in excess of what can be provided by our smaller competitors.

Our Lending Activities

Our current loan portfolio is comprised of the following four categories of loans:

- Real estate mini-perm loans;

- Real estate construction loans;

- Commercial loans; and

- Trade finance.

In addition to these loan types, we have historically made a small number of residential real estate and consumer loans principally as an accommodation to our business customers. We have also utilized our relationships within the banking industry to purchase and sell participations in loans that meet our underwriting criteria. As of December 31, 2013, we had a total of $115.3 million in purchased participation loans (which includes the $6.2 million loans held for sale at December 31, 2013) and $44.7 million in loans that we sold. We manage our loan portfolio to provide for an adequate return, but also to provide for diversification of risk. Due to the recessionary environment through 2009 and 2010, we pared back originating new loans as management was focused on managing existing loan relationships, specifically delinquent and non-performing loans. Although we significantly pared back lending in those years, lending activities did not stop and beginning in 2011 we began an earnest effort to build back the Bank's customer base. This culminated in small loan growth in 2011 and more robust growth in 2012 and 2013.

We have historically originated our loans from our banking offices in Los Angeles and Orange counties. For mini-perm and construction loans, we have relied on referrals from existing clients who are real estate investors, owner/operators, and developers as well as internal business development efforts. For our commercial and trade finance lending, we have sought referrals from existing banking clients as well as referrals from professionals, such as certified public accountants, attorneys and business consultants.

At December 31, 2013, 79% of our loans carried interest rates that adjust with changes in the Prime Rate, 7% carried interest rates tied to LIBOR or other indices and 14% carried a fixed rate or were tied to CD rates. Approximately 79% of our loan portfolio has an interest rate floor.

The following table sets forth information regarding our four major loan portfolios:

	At December 31, 2013 (Dollars in thousands)
Real Estate Mini Perm [3]	
Portfolio size	$ 877,746
Number of loans	397
Average loan size	$ 2,211
Average LTV[1]	60.13%
Average DCR[2]	1.72x
Weighted average rate	5.12%
Average years since origination	2.2 years
Real Estate Construction	
Portfolio size	$ 73,285
Number of loans	26
Average loan size	$ 2,819
Average LTV[1]	61.83%
Weighted average rate	5.44%
Average years since origination	2.1 years
Commercial Loans	
Portfolio size	$ 338,680
Number of loans	551
Average loan size	$ 615
Weighted average rate	4.86%
Average years since origination	2.2 years
Trade Finance	
Portfolio size	$ 39,640
Number of loans	117
Average loan size	$ 339
Weighted average rate	4.23%
Average years since origination	3.4 years

(1) Average loan-to-value at origination, or LTV, is calculated based upon a weighted average of

outstanding principal loan balances (for mini-perm loans) or commitment (for construction loans) divided by the original value.

(2) Average debt coverage ratio at origination, or DCR, is calculated based upon the net operating income of the property divided by the debt service.

(3) Real estate mini perm includes loans held for sale of $6,207.

We had 246 loans with outstanding principal balances between $1 million to $5 million, 54 loans with outstanding principal balances between $5 million and $10 million, and 13 loans with outstanding principal balances over $10 million as of December 31, 2013.

Real Estate Mini-Perm Loans

Real estate mini-perm loans are secured by retail, industrial, office, residential and residential multi-family properties and comprise 66% of our loan portfolio as of December 31, 2013. We seek diversification in our loan portfolio by maintaining a broad base of borrowers and monitoring our exposure to various property types as well as geographic and industry concentrations. Total real estate mini-perm loans were $877.7 million at December 31, 2013 as compared to $684.8 million as of December 31, 2012. Net charge-offs of mini-perm loans accounted for 5.7% of our net loan charge-offs in 2013 compared to 45.4% in 2012. We have worked to reduce the balance of land loans in our portfolio which totaled $21.4 million and $34.3 million at December 31, 2013 and 2012, respectively, which accounted for zero and 29.7% of our net charge-offs in 2013 and 2012, respectively.

The following table sets forth the breakdown of our real estate mini-perm portfolio by property type:

	At December 31, 2013	
Property Type	**Amount**	**Percentage of Loans in Each Category in Total Loan Portfolio**
	(Dollars in thousands)	
Commercial / Office	$ 146,239	11.00%
Retail	209,714	15.77
Industrial	80,265	6.04
Residential 1-4	99,290	7.47
Apartment 4+	129,200	9.72
Land	21,368	1.60
Special purpose	191,670	14.42
Total	$ 877,746	66.02%

The following table sets forth the maturity of our real estate mini-perm loan portfolio:

At December 31, 2013						
Less than					**More Than**	**Total Outstanding**
1 Year	**2 Years**	**3 Years**	**4 Years**	**5 Years**	**5-Years**	**Balance**
(In thousands)						
$115,639	$129,033	$131,974	$139,979	$211,370	$149,751	$877,746

Loan Origination: The loan origination process for mini-perm loans begins with a loan officer collecting preliminary property information and financial data from a prospective borrower. After a preliminary deal sheet is prepared and approved by management, the loan officer collects the necessary third party reports such as appraisals, credit reports, environmental assessments and preliminary title reports as well as detailed financial information. We utilize third party appraisers from an appraiser list approved by our Board of Directors' loan committee. From that list, appraisers are selected by the Chief Credit Officer or Credit Administration.

All appraisals for loans over $250,000 are reviewed by an additional outside appraiser. Appraisals for loans under that amount are reviewed by internal staff. A credit memorandum is then prepared by summarizing all third party reports and preparing an analysis of the adequacy of primary and secondary repayment sources; namely the property DCR and LTV as well as the outside financial strength and cash flow of the borrower(s) or guarantor(s). This completed credit memorandum is then submitted to an officer or committee having the appropriate authority for approval. For further information on our different levels of authority, see "—Loan Authorizations" below.

Once a loan is approved by the appropriate authority level, loan documents are drawn by our note department, which also funds the loan when approval conditions are met. On larger, relatively complex transactions, loan documents are prepared or reviewed by outside legal counsel.

Underwriting Standards: Our principal underwriting standards for real estate mini-perm loans are as follows:

- Maximum LTV of 50%-85%, depending on the property type. However, our practice is to lend at a maximum LTV of 65%.
- Minimum DCR of 1.2-1.25, depending on the property type.
- Requirements of personal guarantees from the principals of any closely-held entity.

Monitoring: We monitor our mini-perm portfolio in different ways. First, for loans over $1.5 million, we conduct site inspections and gather rent rolls and operating statements on the subject properties at least annually. Using this information, we evaluate a given property's ability to service present payment requirements, and we perform "stress-testing" to evaluate the property's ability to service debt at higher debt levels or at lower cash flow levels. Second, on an annual basis, we request updated financial information from our borrowers and/or guarantors to monitor their financial capacity. In addition, to the extent any of our mini-perm loans become delinquent 90 days or more or become adversely classified loans, we order new appraisals every six months.

The vast majority of our mini-perm loans carry a five year maturity. However, it has been our practice to renew these loans for additional five-year periods based on a satisfactory payment record and an updated underwriting profile.

Real Estate Construction

Until we began reducing the origination of construction loans in the first quarter of 2008, we were an active construction lender with construction loans comprising well over 30% of our total loan portfolio as of September 30, 2007. Given the losses experienced in this portion of the portfolio, we worked to reduce total construction loans and as a result construction loans comprised only 5.5% of the total loan portfolio as of December 31, 2013 and comprised 6.6% of the portfolio as of December 31, 2012 including one construction loan held for sale at that date. Loan policy guidelines have been significantly changed since the recession to limit total construction loans within the portfolio. Construction loans comprised 7.4% of our net loan charge-offs during 2013. We had 26 construction loans totaling $73.3 million as of December 31, 2013, and 16 construction loans totaling $75.9 million as of December 31, 2012. Our construction loans are typically short-term loans of up to 18 months for the purpose of funding the costs of constructing a building. Outstanding construction loans by property type are summarized as follows:

Property Type	At December 31, 2013 Amount	Percentage of Loans in Each Category in Total Loan Portfolio
	(Dollars in thousands)	
Commercial / Office	$ —	0.00%
Retail	3,692	0.28
Industrial	18,752	1.40
For sale attached residential	4,790	0.36
For sale detached residential	19,890	1.50
Apartment 4+	14,910	1.12
Land / Special Purpose	11,251	0.85
Total	$ 73,285	5.51%

Loan Origination: The origination process for construction loans is similar to our real estate mini-perm origination process described above under "—Real Estate Mini-Perm Loans—Loan Origination," but with one additional step. We generally require a third party review of the developer's proposed building costs.

Underwriting Standards: Our underwriting standards for construction loans are identical to those described above under "—Real Estate Mini-Perm Loans—Underwriting Standards." For the for-sale-housing projects, however, the DCR requirement is not applicable. In addition, we require that the construction loan applicant have proven experience in the type of project under consideration. Finally, notwithstanding the maximum 75%-80% LTV discussed above under "—Real Estate Mini-Perm Loans—Underwriting Standards," we generally require a maximum 70% LTV for construction loans at origination.

Monitoring: The monitoring of construction loans is accomplished under the supervision of our Chief Credit Officer and the credit administration department. We engage third-party inspectors to report on the percentage of project completion as well as to evaluate whether the project is proceeding at an acceptable pace as compared to the original construction schedule. The third-party inspector also recommends whether we should approve or disapprove disbursement request amounts based on their site inspection and their review of the project budget. The third-party inspector produces a narrative report for each disbursement that contains evaluation and recommendation for each project. The Chief Credit Officer or credit administration reviews each report and makes a final determination regarding the disbursement requests. All approved disbursements are funded by our centralized note department.

Commercial Loans

We offer a variety of commercial loan products including lines of credit for working capital, term loans for capital expenditures and commercial and stand-by letters of credit. As a matter of practice, the Bank typically requires a deposit relationship with commercial borrowers. As of December 31, 2013, we had $338.7 million of commercial loans outstanding, which represented 25.6% of the overall loan portfolio, compared to $324.8 million outstanding as of December 31, 2012. This loan category has traditionally experienced lower loss rates, particularly when compared to the loss rates on construction and land loans. Currently, the Bank is working to grow this line of business primarily because of the additional deposit relationships as well as the risk diversity that this portfolio brings to our overall loan portfolio which is typically more concentrated in real estate-related loans. Lines of credit typically have a 12 month commitment and are secured by the borrower's assets. In cases of larger commitments, an updated borrowing base certificate from the borrower may be required to determine eligibility at the time of any given advance. Term loans seldom exceed 60 months, but in no case exceed the depreciable life of the tangible asset being financed.

Trade Finance Credits: Our trade finance portfolio totaled $39.6 million, or 3.0% of our total loan portfolio as of December 31, 2013, compared to $47.4 million as of December 31, 2012. Of this amount, virtually all loans were made to U.S.-based importers who are also our current borrowers or depositors. Trade finance loans are essentially commercial loans but are typically made to importers or exporters. This portfolio has, similar to commercial loans, performed relatively well. During 2013, trade finance loans had overall net charge-offs of $11,000 and comprised 2 basis points of the Bank's 2013 net charge-offs. We also provide standby letters of credit and foreign exchange services to our clients. Our new trade finance credit relationships result from contacts and relationships with existing clients, certified public accountants and trade facilitators such as customs brokers. In many cases, the ability to generate new trade finance business is also a result of cultivated social contacts and extended family.

We offer the following services to importers:

- Commercial letters of credit;
- Import lines of credit;
- Documentary collections;
- International wire transfers; and
- Acceptances/trust receipt financing.

We offer the following services to exporters:

- Export letters of credit;
- Export finance;
- Documentary collections;
- Bills purchase program; and
- International wire transfers.

Loan Origination: A commercial or trade finance loan begins with a loan officer obtaining preliminary financial information from the borrower and guarantors and summarizing the loan request in a deal sheet. The deal sheet is then reviewed by senior management and/or those who have the loan authority to approve the credit. Following preliminary approval, the loan officer undertakes a formal underwriting analysis, including third party credit reports and asset verifications. From this information and analysis, a credit memorandum is prepared and submitted to an officer or committee having the appropriate approval authority for review. After approval, the note department prepares loan documentation reflecting the conditions of approval and funds the loan when those conditions are met.

Underwriting Standards: Our underwriting standards for commercial and trade finance loans are designed to identify, measure, and quantify the risk inherent in these types of credits. Our underwriting process and standards help us identify the primary and secondary repayment sources. The following are our major underwriting guidelines:

- Cash flow is our primary underwriting criteria. We require a minimum 1.5:1 DCR for our commercial and trade finance loans. We also review trends in the borrower’s sales levels, gross profit and expenses.

- We evaluate the borrower’s financial statements to determine whether a given borrower’s balance sheet provides for appropriate levels of equity and working capital.

- Since most of our borrowers are closely held companies, we require the principals to guarantee the company debt. Our underwriting process, therefore, includes an evaluation of the guarantor’s net worth, income and credit history. Where circumstances warrant, we may require guarantees be secured by collateral (generally real estate).

- Where there is a reliance on the accounts receivable and inventory of a company, we evaluate their condition, which may include third party onsite audits.

Monitoring: For those borrowers whose credit availability is tied to a formula based on advances as a percentage of accounts receivable and inventory (typically ranging from 40%-80% and from 0%-50%, respectively), we review monthly borrowing base certificates for both availability and turnover trends. Periodically, we also conduct third party onsite audits, the frequency of which is dependent on the individual borrower. On a quarterly basis, we monitor the financial performance of a borrower by analyzing the borrower’s financial statements for compliance with financial covenants.

Loan Concentrations

Financial instruments that potentially subject the Bank to concentrations of credit risk consist primarily of loans and investments. These concentrations may be impacted by changes in economics, industry or political factors. The Bank monitors its exposure to these financial instruments and obtains collateral as appropriate to mitigate such risk.

As of December 31, 2013 and 2012, the percentage of loans secured by real estate in our total loan portfolio was approximately 72% and 67%, respectively.

Our combined construction and mini-perm real estate loans by type of collateral including loans held for sale are as follows:

	At December 31, 2013	
Property Type	Amount	Percentage of Loans in Each Category in Total Loan Portfolio
	(Dollars in thousands)	
Commercial/Office	$ 146,239	11.00%
Retail[(1) (2)]	213,406	16.05
Industrial	99,017	7.44
Residential 1-4	123,970	9.33
Apartment 4+	144,110	10.84
Land[(2)]	21,368	1.60
Special purpose[(3)]	202,921	15.27
Total	$ 951,031	71.53%

(1) Includes shopping centers, strip malls or stand-alone properties which house retailers.
(2) Includes of loans held for sale of $6,207.
(3) Examples, other than land, include hospitality and self-storage.

To manage the risks inherent in concentrations in our loan portfolio, we have adopted a number of policies and procedures. Below is a list of the maximum loan-to-values used that must be met at loan origination, however, in practice, we rarely originate loans with loan-to-value ratios that are this high.

Collateral Type	LTV Maximum
Occupied 1-4	85%
Unimproved land	50%
Land development	60%
Improved properties	80%
Commercial construction	75%
1-4 SFR construction	80%

At December 31, 2013, the weighted average LTV of our construction and commercial real estate portfolio based on LTVs at the time of origination was 60%. Our practice is to require DCR's on commercial real estate loans of 1.2x to 1.25x, depending on the property type. We also underwrite our commercial real estate loans using a rate that is 1-2% greater than the proposed interest rate on the loan.

Our construction and mini-perm real estate loans including loans held for sale by geographic concentration are as follows.

(Dollars in thousands)

	Inland Empire	So. CA	Other CA	Out of State[1]	Total
Mini-Perm Residential	$ 2,997	$ 89,450	$ 13,209	$ 7,245	$ 112,901
Mini-Perm Commercial	37,587	564,159	111,053	52,046	764,845
Construction Residential	3,300	18,698	2,682	—	24,680
Construction Commercial	2,195	18,091	3,071	25,248	48,605
Total Real Estate Loans	$ 46,079	$ 690,398	$130,015	$ 84,539	$ 951,031

1) Includes mini-perm commercial loans held for sale of $6,207.

In addition, we have established certain concentration limits for our real estate lending activities by property type. Our other real estate loan limitations include out of area (California) lending at no more than 10% of our portfolio. At December 31, 2013, 8.9% of our real estate portfolio was secured by real estate located outside of California. At December 31, 2013, the top 20 borrowing relationships of the Bank totaled $457.7 million in loans outstanding and comprised 34% of the total loan portfolio.

Except as described below, no individual or single group of related accounts is considered material in relation to our assets or deposits or in relation to our overall business. Approximately 72% of our loan portfolio at December 31, 2013 consisted of real estate secured loans. Moreover, our business activities are focused in Southern California. Consequently, our business is dependent on the trends of this regional economy, and in particular, the real estate markets. At December 31, 2013, we had 313 loans in excess of $1.0 million, totaling $1.14 billion. These loans comprise approximately 32.1% of our loan portfolio based on number of loans and 86.1% based on the total outstanding balance. Excluding credit card and consumer overdraft lines, our average loan size is $1.4 million.

Loan Maturities

In addition to measuring and monitoring concentrations in our loan portfolio, we also monitor the maturities and interest rate structure of our loan portfolio. The following table shows the amounts of loans outstanding as of December 31, 2013 which, based on remaining scheduled repayments of principal, were due in one year or less, more than one year through five years, and more than five years. The table also presents, for loans with maturities over one year, an analysis with respect to fixed interest rate loans and floating interest rate loans.

	At December 31, 2013				Rate Structure for Loans Maturing Over One Year	
	Maturity					
	One Year or Less	One through Five Years	Over Five Years	Total	Fixed Rate	Floating Rate
	(In thousands)					
Real estate mini-perm*	$ 115,639	$ 612,357	$ 149,750	$ 877,746	$ 95,612	$ 666,495
Real estate-construction	54,234	19,051	—	73,285	—	19,051
Commercial	164,131	126,359	48,190	338,680	39,715	134,834
Trade finance	32,413	7,227	—	39,640	—	7,227
Consumer	—	77	—	77	77	—
Other	210	—	—	210	—	—
Total	$ 366,627	$ 765,071	$ 197,940	$ 1,329,638	$ 135,404	$ 827,607

**Includes loans held for sale of $6,207.*

The following table shows the amounts of loans outstanding as of December 31, 2012, which, based on remaining scheduled repayments of principal, were due in one year or less, more than one year through five years, and more than five years. Demand or other loans having no stated maturity and no stated schedule of repayments are reported as due in one year or less. The table also presents, for loans with maturities over one year, an analysis with respect to fixed interest rate loans and floating interest rate loans.

	At December 31, 2012				Rate Structure for Loans Maturing Over One Year	
	Maturity					
	One Year or Less	One through Five Years	Over Five Years	Total	Fixed Rate	Floating Rate
	(In thousands)					
Real estate mini-perm	$ 127,706	$ 441,136	$ 115,955	$ 684,797	$ 78,118	$ 478,973
Real estate-construction*	50,645	23,765	—	74,410	—	23,765
Commercial	182,393	117,086	25,274	324,753	22,740	119,620
Trade finance	40,201	7,211	—	47,412	—	7,211
Consumer	99	—	—	99	—	—
Other	232	—	—	232	—	—
Total	$ 401,276	$ 589,198	$ 141,229	$ 1,131,703	$ 100,858	$ 629,569

**Includes loans held for sale of $12,150.*

As reflected in this data, the maturity of our portfolio is divided generally between loans maturing within one year or less and loans maturing between one and five years. Most of our shorter maturity loans are commercial, construction and trade finance loans. Most of the loans that have maturities between one and five years are real estate-mini-perm loans. Regardless of maturity, most of our loans have interest rates that adjust with changes in the Prime Rate.

Loan Authorizations

As a result of the deterioration of the credit portfolio during the last two years, the loan policy has been modified to reflect changes in the authorizations and approvals required to originate various loan types.

- *Individual Authorities*. Individual loan officers have approval authority up to $1.5 million for loans secured by first trust deeds or cash and up to $1,000,000 for unsecured transactions. The Chief Executive Officer, Chief Operating Officer and the Chief Credit Officer have combined approval authority up to $9.0 million for loans secured by first deeds of trust and up to $7.5 million for unsecured transactions. Loans in excess of these two limits are submitted to our Board of Directors Loan Committee for approval.

- *Board of Directors Loan Committee*. Our Board of Directors loan committee consists of five members of the Board of Directors and our Chief Executive Officer. It has approval authority up to our legal lending limit, which was approximately $56.5 million for real estate secured loans and $33.9 million for unsecured loans at December 31, 2013. The Bank has established internal loan limits which are significantly lower than these legal lending limits. The Board of Directors loan committee also reviews all loan commitments granted in excess of $1.0 million on a quarterly basis for the preceding quarter.

All individual loan authorities are granted by the Loan Committee of our Board of Directors and are based on the individual's demonstrated credit judgment and lending experience.

If a credit falls outside of the guidelines set forth in our lending policies, the loan is not approved until it is reviewed by a higher level of credit approval authority. Credit approval authority has three levels, as listed above from lowest to highest level. Policy exceptions for cash flow, waiver of guarantee, excessive LTV or poor credit require approval of the President or Chief Credit Officer regardless of size.

We believe that the current authority levels provide satisfactory management and a reasonable percentage of secondary review. Any conditions placed on loans in the approval process must be satisfied before our Chief Credit Officer will release loan documentation for execution. Our Chief Credit Officer and his staff work entirely independent of loan production and have full responsibility for all loan disbursements.

Loan Grading and Loan Review

We seek to quantify the risk in our lending portfolio by maintaining a loan grading system consisting of eight different categories (Grades 1-8). The grading system is used to determine, in part, the allowance for loan losses. The first four grades in the system are considered acceptable risk; whereas the fifth grade is a short term transition grade. Loans in this category are subjected to enhanced analysis and either demonstrate their acceptableness and are returned to an acceptable grade or are moved to a "substandard" category should the loan's underlying credit elements so dictate. The other three grades range from a "substandard" category to a "loss" category. These three grades are further discussed below under the section subtitled "classified assets."

The originating loan officer initially assigns a grade to each credit as part of the loan approval process. Such grade may be changed as a loan application moves through the approval process.

Prior to funding, all new loans of $1.0 million or over are reviewed by the Credit Administration Officer who may assign a different grade to the credit. The grade on each individual loan is reviewed at least annually by the loan officer responsible for monitoring the credit. The Board of Directors reviews monthly the aggregate amount of all loans graded as special mention (grade 5), substandard (6) or doubtful (7), and each individual loan that has a grade within such range. Additionally, changes in the grade for a loan may occur through any of the following means:

- Monthly reviews by the Credit Administration Officer of a sample of loans approved under individual loan authority;
- Bank regulatory examinations; and
- Monthly action plans submitted to the Chief Credit Officer by the responsible lending officers for each credit graded 5-8.

Loan Delinquencies: When a borrower fails to make a committed payment, we attempt to cure the deficiency by contacting the borrower to seek payment. Habitual delinquencies and loans delinquent 30 days or more are reviewed for possible changes in grading.

Classified Assets: Federal regulations require that each insured bank classify its assets on a regular basis. In addition, in connection with examinations of insured institutions, examiners have authority to identify problem assets, and, if appropriate, classify them. We use grades 6-8 of our loan grading system to identify potential problem assets.

Purchased Loan Participations

As of December 31, 2013, the Bank had $115.3 million in loans outstanding that were purchased from other financial institutions representing 8.7% of the loan portfolio. This is down from pre-recession levels when the Bank had $260.7 million or 21.1% of the loan portfolio in participations purchased as of December 31, 2007. These loans include commercial real estate, construction and commercial loans. There were no charge-offs to the Bank's purchased participations during 2013. These loans are underwritten using the same standards as loans that the Bank originates directly. In light of the performance of this part of the portfolio, the Bank has significantly curtailed purchasing new loan participations.

Deposit Products and Other Sources of Funds

Our primary sources of funds for use in our lending and investment activities consist of:

- Deposits and related services;
- Maturities and principal and interest payments on loans and securities; and
- Borrowings.

Total deposits were $1.5 billion as of December 31, 2013, of which 22.2% were demand deposits, 32.2% were in savings and interest-bearing checking, 38.6% were in CD's greater than $100,000 and 7.0% were in other CD's. We closely monitor rates and terms of competing sources of funds and utilize those sources we believe to be the most cost effective, consistent with our asset and liability management policies.

Deposits and Related Services: We have historically relied primarily upon, and expect to continue to rely primarily upon, deposits to satisfy our needs for sources of funds. An important balance sheet component impacting our net interest margin is the composition and cost of our deposit base. We can improve our net interest margin to the extent that growth in deposits can be focused in the less volatile and somewhat more traditional core deposits, or total deposits excluding CDs greater than $100,000, which are commonly referred to as Jumbo CDs.

We provide a wide array of deposit products. We offer regular checking, savings, negotiable order of withdrawal (NOW) and money market deposit accounts; fixed-rate, fixed maturity retail certificates of deposit ranging in terms from 14 days to two years; and individual retirement accounts and non-retail certificates of deposit consisting of Jumbo CDs. We attempt to price our deposit products in order to promote deposit growth and satisfy our liquidity requirements. We provide remote deposit capture service or courier service to pick up non-cash deposits and, for those customers that use large amounts of cash, we arrange for armored car and vault service.

We provide a high level of personal service to our high net worth individual customers who have significant funds available to invest. We believe our Jumbo CDs are a stable source of funding because they are based primarily on service and personal relationships with senior Bank officers rather than the interest rate. Further evidence of this is the fact that our average jumbo CD customer has been a customer of the Bank for over six years. Further, 7% of these Jumbo CDs are pledged as collateral for loans from us to the depositor or the depositor's affiliated business or family member. We monitor interest rates offered by our competitors and pay a rate we believe is competitive with the range of rates offered by such competitors.

Historically, the Bank has accessed the brokered deposit market for deposits to meet short-term liquidity requirements. In addition, we also are a member of the Certificate of Deposit Account Registry Service, or “CDARS”. Our membership ordinarily allows us to share our deposits that exceed FDIC insurance limits with other financial institutions and other financial institutions share their deposits with us in a reciprocal deposit-sharing transaction that allows our customers to receive full FDIC insurance coverage on their large deposit balances. Under the terms of a previous Memorandum of Understanding, dated March 25, 2012, the Bank could not accept brokered deposits through CDARS. As a result, the Bank’s CDARS deposit balance decreased to zero. Because the brokered deposit restriction was lifted upon the termination of the 2012 Memorandum of Understanding, the Bank was able to resume accepting brokered deposits through CDARS during 2013. Brokered deposits (including CDARS reciprocal deposits) were $17.6 million and zero as of December 31, 2013 and 2012, respectively.

The Bank has a robust Contingency Funding Plan which is designed to identify potential liquidity events, specifies monitoring requirements and also indicates steps to be taken in order to raise liquidity levels to ensure that the Bank has sufficient liquidity. Due to the high levels of cash on hand and marketable securities as well as ongoing monitoring and forecasting efforts, management is confident that the Bank has sufficient liquidity to meet all of its obligations.

At December 31, 2013, excluding government deposits, brokered deposits and deposits as direct collateral for loans, we had 58 depositors with deposits in excess of $3.0 million that totaled $434.6 million, or 28.4% of our total deposits.

We intend to focus our efforts on attracting deposits from our business lending relationships in order to reduce our cost of funds, improve our net interest margin and enhance the franchise value of the Bank

In addition to the marketing methods listed above, we seek to attract new clients and deposits by:

- Expanding long-term business customer relationships, including referrals from our customers, and
- Building deposit relationships through our branch relationship officers.

On December 31, 2012, the FDIC’s Transaction Account Guarantee (“TAG”) program ended. TAG was originally created in response to the financial crisis in 2008 and the program was renewed as part of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010. The program provided for unlimited FDIC insurance on all noninterest-bearing transaction accounts with the goal of creating stability and confidence in the financial system in a time of great stress. With the termination of this program at December 31, 2012, demand deposit accounts are now insured for up to $250,000.

Other Borrowings: In the past we have also borrowed from the FHLB pursuant to an existing commitment based on the value of the collateral pledged (both loans and securities) in our portfolio. We had $20.0 million in outstanding FHLB advances at December 31, 2013. We currently have $121.9 million in available borrowing capacity at the FHLB. In addition, we have pledged $51.7 million in securities at the Federal Reserve Bank Discount Window and may borrow against that as well.

Our Investment Activities

Our investment strategy is designed to be complementary to and interactive with our other strategies (*i.e.*, cash position; borrowed funds; quality, maturity, stability and earnings of loans; nature and stability of deposits; capital and tax planning). The target percentage for our investment portfolio is between 10% and 40% of total assets. Our general objectives with respect to our investment portfolio are to:

- Achieve an acceptable asset/liability mix;
- Provide a suitable balance of quality and diversification to our assets;
- Provide liquidity necessary to meet cyclical and long-term changes in the mix of assets and liabilities;
- Provide a stable flow of dependable earnings;
- Maintain collateral for pledging requirements;
- Manage and mitigate interest rate risk; and
- Provide funds for local community needs.

The total fair value and historical cost of investment securities (including both securities held-to-maturity and securities available-for-sale) amounted to $142.7 million and $211.7 million as of December 31, 2013 and 2012, respectively. Investment securities consist primarily of investment grade corporate notes, municipal bonds, collateralized mortgage obligations, U.S. government agency securities, and U.S agency mortgage-backed securities. In addition, for bank liquidity purposes, we use overnight federal funds, which are temporary overnight sales of excess funds to correspondent banks.

As of December 31, 2013, the bank had zero investments classified as “held-to-maturity.” As of December 31, 2012 the Bank had one investment security as “held-to-maturity” and classified the rest of its investment securities as “available-for-sale” pursuant to Investments – Debt and Equity Securities Topic of FASB ASC. Available for sale securities are reported at fair value, with unrealized gains and losses excluded from earnings and instead reported as a separate component of shareholders’ equity. Held to maturity securities are securities that we have both the intent and the ability to hold to maturity. These securities are carried at cost adjusted for amortization of premium and accretion of discount.

Our securities portfolio is managed in accordance with guidelines set by our investment policy. Specific day-to-day transactions affecting the securities portfolio are managed by our Chief Financial Officer, in accordance with our Asset/Liability and Funds Management Policy. These securities activities are reviewed monthly by our investment committee and are reported to our Board of Directors.

Our investment policy addresses strategies, types and levels of allowable investments and is reviewed and approved annually (or more often, as required) by our Board of Directors. It also limits the amount we can invest in various types of securities, places limits on average life and duration of securities, and limits the securities dealers with whom we can conduct business.

Our Competition

The banking and financial services business in Southern California is highly competitive. This increasingly competitive environment faced by banks is a result primarily of changes in laws and regulation, changes in technology and product delivery systems, and the accelerating pace of consolidation among financial services providers. We compete for loans, deposits and customers with other commercial banks, savings and loan associations, securities and brokerage companies, mortgage companies, insurance companies, finance companies, money market funds, credit unions and other nonbank financial services providers. Many of these competitors are much larger in total assets and capitalization, have greater access to capital markets, including foreign ownership and/or offer a broader range of financial services than we can offer.

We also compete with two publicly listed banks which share a partial focus on the Chinese-American market, and subsidiary banks and branches of foreign banks, from countries such as Taiwan and China, many of which have greater lending limits, and a wider variety of products and services.

Additionally, we compete with mainstream community banks and with Chinese-American community banks for both deposits and loans.

Competition for deposit and loan products remains strong from both banking and non-banking firms and this competition directly affects the rates of those products and the terms on which they are offered to customers.

Technological innovation continues to contribute to greater competition in domestic and international financial services markets. Many customers now expect a choice of several delivery systems and channels including physical branch offices, telephone, mail, Internet, ATMs, remote deposit capture and mobile banking.

Mergers between financial institutions have placed additional pressure on banks to consolidate their operations, reduce expenses and increase revenues to remain competitive. The competitive environment is also significantly impacted by federal and state legislation that make it easier for non-bank financial institutions to compete with us.

The Bank's profitability, like most financial institutions, is primarily dependent on our ability to maintain a favorable differential or "spread" between the yield on our interest-earning assets and the rate paid on our deposits and other interest-bearing liabilities. 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 our interest-earning assets, such as loans extended to customers and securities held in our investment portfolio, will comprise the major portion of the Bank's earnings. These rates are highly sensitive to many factors that are beyond the control of the Bank, such as inflation, recession and unemployment, and the impact of future changes in domestic and foreign economic conditions might have on the Bank cannot be predicted.

The Bank's business is also influenced by the monetary and fiscal policies of the federal government, and the policies of the regulatory agencies, particularly the Board of Governors of the Federal Reserve System (the "FRB"). The FRB implements national monetary policies (with objectives such as curbing inflation and combating recession) through its open-market operations in United States government securities, by adjusting the required level of reserves for financial 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 FRB in these areas influence the growth of bank loans, investments and deposits and also affect interest earned on interest-earning assets and paid on interest-bearing liabilities. The nature and impact of any future changes in monetary and fiscal policies on the Bank cannot be predicted.

REGULATION AND SUPERVISION

The following discussion of statutes and regulations affecting banks is only a summary and does not purport to be complete. This discussion is qualified in its entirety by reference to such statutes and regulations. No assurance can be given that such statutes or regulations will not change in the future.

General

The Bank is extensively regulated under both federal and state laws. Regulation and supervision by the federal and state banking agencies is intended primarily for the protection of depositors and the Deposit Insurance Fund administered by the FDIC, and not for the benefit of shareholders.

As a California state-chartered bank which is not a member of the Federal Reserve System, we are subject to supervision, periodic examination and regulation by the CDBO, as the Bank's state regulator, and by the FDIC as the Bank's primary federal regulator. The regulations of these agencies govern most aspects of our business, including the filing of periodic reports by us, and our activities relating to dividends, investments, loans, borrowings, capital requirements, certain check-clearing activities, branching, mergers and acquisitions, reserves against deposits and numerous other areas. The Bank is subject to significant regulation and restrictions by federal and state laws and regulatory agency regulations, policies and practices. If, as a result of an examination, either the CDBO 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, various remedies are available to the CDBO and the FDIC. These remedies include the power to (i) require affirmative action to correct any conditions resulting from any violation or unsafe and unsound practice; (ii) direct an increase in capital and the maintenance of higher specific minimum capital ratios, which may preclude the Bank from being deemed well capitalized and restrict its ability to accept certain brokered deposits; (iii) restrict the Bank's growth geographically, by products and services, or by mergers and acquisitions, including bidding in FDIC receiverships for failed banks; (vi) enter into informal nonpublic or formal public memoranda of understanding or written agreements and consent orders with the Bank to take corrective action; (v) issue an administrative cease and desist order that can be judicially enforced; (vi) enjoin unsafe or unsound practices; (vii) assess civil monetary penalties; and (viii) require prior approval of senior executive officers and director changes or remove officers and directors. Ultimately the FDIC could terminate the Bank's FDIC insurance and the CBDO could revoke the Bank's charter or take possession and close and liquidate the Bank.

Because California law permits commercial banks chartered by the state to engage in any activity permissible for national banks, 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 to the same extent as may a national bank, and, further, may conduct certain "financial" activities in a subsidiary as authorized by the Gramm-Leach-Bliley Act of 1999. Generally, a financial subsidiary is permitted to engage in activities that are "financial in nature" or incidental thereto, even though they are not permissible for a national bank to conduct directly within the bank. The definition of "financial in nature" includes, among other items, underwriting, dealing in or making a market in securities, including, for example, distributing shares of mutual funds. The Bank presently has no nonbanking or financial subsidiaries.

Changes in federal or state banking laws or the regulations, policies or guidance of the federal or state banking agencies could have an adverse cost or competitive impact on the Bank's operations. We cannot predict whether or when potential legislation or new regulations will 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, and may subject us to increased regulation, disclosure, and reporting requirements. Moreover, the bank regulatory agencies continue to be aggressive in responding to concerns and trends identified in examinations, and this has resulted in the increased issuance of enforcement actions to financial institutions requiring action to address credit quality, capital adequacy, liquidity and risk management, as well as other safety and soundness and compliance concerns. In addition, the outcome of any investigations initiated by federal or state authorities or the outcome of litigation may result in additional regulation, necessary changes in our operations and increased compliance costs.

Legislative and Regulatory Developments

The Dodd-Frank Act

The implementation and impact of legislation and regulations enacted since 2008 in response to the U.S. economic downturn and financial industry instability continued in 2013 as modest recovery returned to many institutions in the banking sector. Many institutions have repaid and repurchased U.S. Treasury investments under the Troubled Asset Relief Program and certain provisions of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank") are effective and have been fully implemented, including the revisions in the deposit insurance assessment base for FDIC insurance and the permanent increase in coverage to $250,000; the permissibility of paying interest on business checking accounts; the removal of barriers to interstate branching and required disclosure and shareholder advisory votes on executive compensation. Action in 2013 to implement the final Dodd-Frank provisions included (i) final new capital rules, (ii) a final rule to implement the so called Volcker rule restrictions on certain proprietary trading and investment activities and (iii) final rules and increased enforcement action by the Consumer Finance Protection Bureau ("CFPB").

Many of the regulations to implement Dodd-Frank have not yet been published for comment or adopted in final form and/or will take effect over several years, making it difficult to anticipate the overall financial impact on the Bank, our customers or the financial industry more generally. Individually and collectively, these proposed regulations resulting from Dodd-Frank may materially and adversely affect the Bank's business, financial condition, and results of operations.

Capital Standards

New Capital Rules

In July 2013, the federal bank regulatory agencies adopted final regulations which revised their risk-based and leverage capital requirements for banking organizations to meet requirements of Dodd-Frank and to implement international agreements reached by the Basel Committee on Banking Supervision intended to improve both the quality and quantity of banking organizations' capital ("Basel III"). Although many of the rules contained in these final regulations are applicable only to large, internationally active banks, some of them will apply on a phased in basis to all banking organizations, including the Bank.

The following are among the new requirements that will be phased in beginning 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% eliminating a 3.00% exception for higher rated banks
- Changes in the permitted composition of Tier 1 capital to exclude trust preferred securities, mortgage servicing rights and certain deferred tax assets and include unrealized gains and losses on available for sale debt and equity securities
- A new additional capital conservation buffer of 2.5% of risk weighted assets over each of the required capital ratios will be phased in from 2016 to 2019 must be met to avoid limitations the ability of the Bank to pay dividends, repurchase shares or pay discretionary bonuses

- 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

- An additional “countercyclical capital buffer” is required for larger and more complex institutions

Final Volcker Rule

In December 2013, the federal bank regulatory agencies adopted final rules that implement a part of Dodd-Frank commonly referred to as the “Volcker Rule.” Under these rules and subject to certain exceptions, banking entities, including the Bank, will be 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 will become effective on April 1, 2014. Certain collateralized debt obligations securities backed by trust preferred securities, which were initially defined as covered funds, were subject to the investment prohibitions of the final rule. Action taken by the Federal Reserve in January 2014 exempted many such securities to address the concern that many community banks holding such collateralized debt obligations securities may have been required to recognize losses on those securities

The Bank held no investment positions at December 31, 2013 which were subject to the final rule. Therefore, while these new rules may require us to conduct certain internal analysis and reporting, we believe that they will not require any material changes in our current operations or business.

CFPB Actions

Dodd-Frank provided for the creation of the 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 bureau’s functions include investigating consumer complaints, conducting market research, rulemaking, supervising and examining bank consumer transactions, and enforcing rules related to consumer financial products and services. CFPB regulations and guidance apply to all financial institutions and banks with $10 Billion or more in assets are subject to examination by the CFPB. Banks with less than $10 billion in assets, including the Bank, will continue to be examined for compliance by their primary federal banking agency. Significant recent CFPB developments that may affect the Bank's operations and compliance costs include:

- The issuance of final rules for residential mortgage lending, which became effective January 10, 2014, including definitions for “qualified mortgages” and detailed standards by which lenders must satisfy themselves of the borrower’s ability to repay the loan and revised forms of disclosure under the Truth in Lending Act and the Real Estate Settlement Procedures Act

- The issuance of a policy report on arbitration clauses which could result in the restriction or prohibition of lenders including arbitration clauses in consumer financial services contracts

- Actions taken to regulate and supervise credit bureaus and debt collections

- Positions taken by CFPB on fair lending, including applying the disparate impact theory in auto financing, which could make it harder for lenders to charge different rates or apply different terms to loans to different customers.

The Bank is not subject to examination by the CFPB and believes it is in material compliance with all applicable laws and regulations subject to authority of the CFPB.

Current Capital Adequacy Requirements

Banks are currently subject to various regulatory capital requirements administered by state and federal banking agencies which apply until the increased capital requirements of the new capital rules are effective and fully phased in. The currently effective risk-based capital guidelines of the regulatory agencies were based upon the 1988 capital accord ("Basel I") of the Basel Committee on Bank Supervision ("Basel Committee"), a committee of central banks and bank supervisors/regulators from the major industrialized countries that develops broad policy guidelines, which each country's supervisors can use to determine the supervisory policies they apply to their home jurisdiction. In 2004 the Basel Committee proposed a new capital accord ("Basel II") to replace Basel I that provided approaches for setting capital standards for credit risk and capital requirements for operational risk and refining the existing capital requirements for market risk exposures. U.S. banking regulators published a final rule for Basel II implementation requiring banks with over $250 billion in consolidated total assets. However, a definitive rule was not issued and instead the new capital rules to implement Basel III were first proposed in 2010.

The regulatory capital guidelines as well as the Bank's actual capitalization as of December 31, 2013, are as follows:

Tier 1 Leverage Ratio	
Preferred Bank	11.80%
Minimum requirement for "Well-Capitalized" institution	5.00%
Minimum regulatory requirement	4.00%
Tier 1 Risk-Based Capital Ratio	
Preferred Bank	13.78%
Minimum requirement for "Well-Capitalized" institution	6.00%
Minimum regulatory requirement	4.00%
Total Risk-Based Capital Ratio	
Preferred Bank	15.03%
Minimum requirement for "Well-Capitalized" institution	10.00%
Minimum regulatory requirement	8.00%

The New Capital Rule and Minimum Capital Ratios

Management believes that, as of December 31, 2013, the Bank would meet all applicable capital requirements under the new capital rules (See "*Legislature and Regulatory Developments*" above) on a fully phased-in basis if such requirements were currently in effect.

Including the capital conservation buffer of 2.5% above the new regulatory minimum capital ratios established under the new final capital rule would result in the following minimum ratios: (i) a common equity Tier 1 capital ratio of 7.0%, (ii) a Tier 1 capital ratio of 8.5%, and (iii) a total capital ratio of 10.5%. The new capital conservation buffer requirement would be phased in beginning in January 2016 at 0.625% of risk-weighted assets and would increase each year until fully implemented in January 2019. While the new final capital rule sets higher regulatory capital standards for 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 and require the raising of additional capital.

For further information regarding the capital ratios of the Bank, see the discussion under Note 11 – "Restrictions on Cash Dividends, Regulatory Capital Requirements" in the notes to the consolidated financial statements.

Memorandum of Understanding

As a result of a regulatory examination during 2013, the Memorandum of Understanding which the Bank entered into with the FDIC and CDBO on May 25, 2012 was terminated and the Bank entered into a new MOU with both the FDIC and the CDBO on October 1 2013. Among other things, the MOU requires the Bank to maintain a Tier 1 Leverage Ratio of 10%, improve its BSA compliance, maintain a minimum Tier 1 Leverage Ratio of 10%, and to refrain from declaring or paying cash dividends to its shareholders and establishing new branches and offices without the prior written approval of the FDIC and CDBO. As of December 31, 2013, the Tier 1 Leverage Ratio of the Bank was 11.80%, exceeding the level required by the MOU. In response to the examination findings, management has dedicated a significant amount of time and resources toward strengthening its BSA and compliance programs and complying with the MOU. The Board of Directors and management are committed to meeting all of the requirements of the MOU and seeing to its earliest possible termination.

Prompt Corrective Action Regulations

The FDI 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. 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 will change when the new capital rule ratios become effective. Under the new standards, in order to be considered well-capitalized, the Bank would be required to have 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).

Dividends and Other Transfers of Funds

The Bank is subject to various statutory and regulatory restrictions on its ability to pay dividends, including a prohibition in the MOU on paying cash dividends or making any other payments to our shareholders without the prior written consent of the FDIC and the CDBO. In addition, the banking agencies have the authority to prohibit the Bank from paying dividends, depending upon the Bank's financial condition, if such payment would be deemed to constitute an unsafe or unsound practice.

Deposit Insurance

The FDIC insures our customer deposits through the Deposit Insurance Fund of the FDIC up to prescribed limits for each depositor. 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 Deposit Insurance Fund or that may prejudice the interest of the bank's depositors. The termination of deposit insurance for the Bank would also result in the revocation of the Bank's charter by the CDBO.

FDIC insurance expense totaled $2.1 million for 2013. FDIC insurance expense includes deposit insurance assessments and Financing Corporation ("FICO") assessments related to outstanding FICO bonds to fund interest payments on bonds to recapitalize the predecessor to the Deposit Insurance Fund. These assessments will continue until the FICO bonds mature in 2017. The total FICO assessments we paid in 2013 was $88,000.

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

Federal Home Loan Bank System

We are a member of the FHLB. Among other benefits, each of the 12 Federal Home Loan Banks, serves as a reserve or central bank for its members within its assigned region. The FHLB makes available loans or advances to its members in compliance with the policies and procedures established by the Board of Directors of the individual FHLB. As an FHLB member, we are required to own a certain amount of restricted capital stock and maintain a certain amount of cash reserves in the FHLB. As of December 31, 2013, the Bank had $20.0 million of outstanding FHLB advances and additional borrowing capacity of $121.9 million. At December 31, 2013, the Bank was in compliance with the FHLB's stock ownership and cash reserve requirements. As of December 31, 2013 and 2012, our investment in FHLB capital stock totaled $5,296,000 and $4,282,000, respectively.

Securities Registration

The Bank's common stock is publicly held and listed on the NASDAQ Global Select Market ("NASDAQ"), and the Bank 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 as adopted by the FDIC and the regulations of the Securities and Exchange Commission (the "SEC") promulgated thereunder as well as listing requirements of NASDAQ. Dodd-Frank includes the following provisions that affect corporate governance and executive compensation, which are or, in the future, may be applicable to the Bank: (1) shareholder advisory votes on executive compensation, (2) executive compensation "clawback" requirements for companies listed on national securities exchanges in the event of materially inaccurate statements of earnings, revenues, gains or other (3) enhanced independence requirements for compensation committee members, and (4) SEC authority to adopt proxy access rules which would permit shareholders of publicly traded companies to nominate candidates for election as director and have those nominees included in a company's proxy statement.

The Sarbanes-Oxley Act

The Bank 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.

Loans-to-One Borrower Limitations

With certain limited exceptions, the maximum amount of obligations, secured or unsecured, that any borrower (including certain related entities) may owe to a California state bank at any one time may not exceed 25% of the sum of the shareholders' equity, allowance for loan losses, capital notes and debentures of the bank. Unsecured obligations may not exceed 15% of the sum of the shareholders' equity, allowance for loan losses, capital notes and debentures of the bank. The Bank has established internal loan limits which are lower than the legal lending limits for a California state chartered bank. At December 31, 2013, the Bank's largest single lending relationship had a combined outstanding balance of $50.1 million, secured predominantly by commercial real estate properties in the Bank's lending area, and which is performing in accordance with the terms of the Bank's loans.

Extensions of Credit to Insiders and Transactions with Affiliates

The Bank is subject to Federal Reserve Regulation O and companion California banking law limitations and conditions on loans or extensions of credit to:

- The Bank's executive officers, directors and principal shareholders (*i.e.*, in most cases, those persons who own, control or have power to vote more than 10% of any class of voting securities);
- Any company controlled by any such executive officer, director or shareholder; or
- Any political or campaign committee controlled by such executive officer, director or principal shareholder.

Loans extended to any of the above persons must comply with loan-to-one-borrower limits, require prior full board approval when aggregate extensions of credit to the person exceed specified amounts, must be made on substantially the same terms (including interest rates and collateral) as, and follow credit-underwriting procedures that are not less stringent than those prevailing at the time for comparable transactions with non-insiders, and must not involve more than the normal risk of repayment or present other unfavorable features. In addition, Regulation O provides that the aggregate limit on extensions of credit to all insiders of a bank as a group cannot exceed the bank's unimpaired capital and unimpaired surplus. Regulation O also prohibits a bank from paying an overdraft on an account of an executive officer or director, except pursuant to a written pre-authorized interest-bearing extension of credit plan that specifies a method of repayment or a written pre-authorized transfer of funds from another account of the officer or director at the bank. California has laws and the CDBO has regulations which adopt and also apply Regulation O to the Bank.

The Bank also is subject to certain restrictions imposed by Federal Reserve Act Sections 23A and 23B and Federal Reserve Regulation W on any extensions of credit to, or the issuance of a guarantee or letter of credit on behalf of, any affiliates, the purchase of, or investments in, stock or other securities thereof, the taking of such securities as collateral for loans, and the purchase of assets of any affiliates. Such restrictions prevent any affiliates from borrowing from the Bank unless the loans are secured by marketable obligations of designated amounts. Further, such secured loans and investments to or in any affiliate are limited, individually, to 10.0% of the Bank's capital and surplus (as defined by federal regulations), and such secured loans and investments are limited, in the aggregate, to 20.0% of the Bank's capital and surplus. A financial subsidiary is considered an affiliate subject to these restrictions whereas other nonbanking subsidiaries are not considered affiliates. Additional restrictions on transactions with affiliates may be imposed on the Bank under the FDI Act prompt corrective action provisions and the supervisory authority of the federal and state banking agencies.

Operations and Consumer Compliance

The Bank must comply with numerous federal anti-money laundering and consumer privacy and protection statutes and implementing regulations, including the USA PATRIOT Act of 2001, the Bank Secrecy Act, the Foreign Account Tax Compliance Act, the Community Reinvestment Act, the Fair Credit Reporting Act, as amended by the Fair and Accurate Credit Transactions Act, the Electronic Fund Transfer 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 Americans with Disabilities Act and various other federal and state consumer banking and privacy protection laws.

These laws and regulations mandate certain disclosure and other requirements and regulate the manner in which financial institutions must deal with customers when taking deposits, making loans, collecting loans, and providing other services. Failure to comply with these laws and regulations can subject the Bank 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 is also subject to federal and state laws prohibiting unfair or fraudulent business practices, untrue or misleading advertising and unfair competition.

Employees

As of December 31, 2013, the Bank had a total of 148 full-time equivalent employees. None of the employees are represented by a union or collective bargaining group. Management believes that employee relations are satisfactory.

Executive Officers of the Bank

The following table sets forth our executive officers, their positions and their ages. Each officer is appointed by, and serves at the pleasure of the Board of Directors.

Name	Age [(1)]	Position with Bank
Li Yu	[73]	Chairman of the Board and Chief Executive Officer
Wellington Chen	[54]	President and Chief Operating Officer
Edward J. Czajka......	[49]	Executive Vice President and Chief Financial Officer
Lucilio Couto	[45]	Executive Vice President and Chief Credit Officer
Robert Kosof............	[70]	Executive Vice President and Head of Commercial and Industrial Loans and Regional Branch Manager

[(1)] *As of March 1, 2014.*

Li Yu has been our Chief Executive Officer since 1993. From December 1991 to the present, he has served as Chairman of our Board of Directors. From 1987 to 1991, he was involved in several privately held companies of which he was the owner. From 1982 to 1987, he served as Chairman of the Board of California Pacific National Bank, which became a part of Bank of America. Mr. Yu received a Masters of Business Administration, or MBA, from the University of California, Los Angeles. He was also the past President of the National Association of Chinese American Bankers, and is currently a member of the Board of Visitors of UCLA’s Anderson Graduate School of Management.

Wellington Chen has been the Bank’s Senior Executive Vice President since June 22, 2011 and was promoted to President on August 21, 2012, and has been the Bank’s Chief Operating Officer since August 9, 2011. Prior to joining Preferred Bank, Mr. Chen was Executive Vice President and Director of Corporate Banking for East-West Bank in Pasadena, California where he oversaw a significant portion of the loan and deposit production activities. Prior to that, he was Senior Executive Vice President and a Director of Far East National Bank in Los Angeles.

Edward J. Czajka has been Senior Vice President and Chief Financial Officer since 2006 and was promoted to Executive Vice President since 2008. Before joining Preferred Bank, Mr. Czajka was Chief Financial Officer of Presidio Bank, a San Francisco-based bank that was then in organization. Prior to this, Mr. Czajka was Executive Vice President and Chief Financial Officer of North Valley Bancorp, (Nasdaq: NOVB) a publicly-traded multi-bank holding company located in Redding, California. From 1994 through 2000, Mr. Czajka held the position of Vice President, Corporate Controller for Pacific Capital Bancorp in Santa Barbara, California. Mr. Czajka graduated summa cum laude from Capella University with a BS in Business Administration and is a graduate of the Bank Administration Institute Graduate School of Banking at Vanderbilt University.

Lucilio Couto was appointed Executive Vice President on February 2, 2010 and on August 9, 2011 was appointed Chief Credit Officer. Prior to that, he was Senior Vice President and Special Assistant to the Chairman. Before joining Preferred Bank he served in senior management positions at two other Southern California financial institutions including Vineyard Bank, NA. Mr. Couto served as the Chief Risk Officer of Vineyard Bank from July 2007 to April 2009 and Executive Vice President and Chief Credit Officer from September 2008 to April 2009. Prior to joining Vineyard Bank, Mr. Couto spent 16 years working for the FDIC in a variety of positions, including most recently as Senior Risk Management Examiner. He has expertise in risk management, regulatory compliance, credit analysis and financial statement analysis. Mr. Couto received his Bachelor's degree of finance from California State University San Bernardino in 1991 and graduated from the University of Wisconsin's Graduate School of Banking in 2004.

Robert Kosof was appointed on February 22, 2010 as Executive Vice President and Head of Commercial and Industrial Loans and Regional Branch Manager. Prior to that, he served as Executive Vice President and Chief Credit Officer and he has been with Preferred Bank since 2008. Before joining Preferred Bank he was Executive Vice President and Chief Credit Officer of RP Realty Partners Entrepreneurial Fund from 2006 to 2008. Prior to that, he was Senior Vice President and Chief Lending Officer for Bank Leumi USA from 1987 to 2006. His responsibilities included credit approval and credit quality for the California branches of the Bank. From 1985 to 1987 he was Executive Vice President and Director for Olympic National Bank. From 1974 to 1985 he was Senior Vice President and head of Loan Administration which included Loan Adjustments for Imperial Bank.

Available Information

The Bank also maintains an Internet website at *www.preferredbank.com.* The Bank makes its website content available for information purposes only. It should not be relied upon for investment purposes.

We are subject to the reporting and other requirements of the Securities Exchange Act of 1934, as amended and as adopted by the FDIC (the "Exchange Act"). In accordance with Sections 12, 13 and 14 of the Exchange Act and as a bank that is not a member of the Federal Reserve System, we file certain reports, proxy materials, information statements and other information with the FDIC, copies of which can be inspected and copied at the public reference facilities maintained by the FDIC, at the Accounting and Securities Disclosure Section, Division of Supervision and Consumer Protection, 550 17th Street, N.W., Washington, DC 20429. Requests for copies may be made by telephone at (202) 898-8913 or by fax at (202) 898-3909. Forms 3, 4 and 5 are filed electronically with FDIC, at the FDIC's website at *http://www.fdic.gov.*

ITEM 1A. RISK FACTORS

Risk Factors That May Affect Future Results

In addition to the other information on the risks we face and our management of risk contained in this annual report or in our other filings, the following are significant risks which may affect us. Events or circumstances arising from one or more of these risks could adversely affect our business, financial condition, operations 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.

We are subject to certain requirements and prohibitions under the MOU and we cannot assure you whether or when the MOU will be terminated.

The Bank has been subject to the current MOU since October 2013, which requires us to maintain a higher tier 1 leverage capital ratio than statutorily required and to improve Bank Secrecy Act compliance. The MOU also prohibits the Bank from paying cash dividends or making any other payments to its shareholders without prior written consent of the FDIC and the CDBO.

As of the date of this filing, we believe we are in compliance with all the requirements of the MOU. We will continue to work to maintain compliance with all provisions of the MOU. Although we believe we are in compliance with the provisions of the MOU, we cannot assure that we will maintain full compliance with the requirements in the MOU and whether or when the MOU will be terminated. Although the requirements and restrictions of the MOU are not judicially enforceable, the failure to comply with the MOU could result in the entry into a formal enforceable consent order. The Bank is committed to comply with all provisions of the MOU and to maintain good relations with its regulators.

Pursuant to the MOU, we are prohibited from paying cash dividends or any other payments to our shareholders.

Under the terms of the MOU, we are prohibited from paying cash dividends or any other payments to our shareholders without the prior written consent of the FDIC and the CDBO. We do not know when the Bank will receive regulatory approval to pay dividends to our shareholders. These restrictions could have a negative effect on the value of our common stock.

If our allowance for loan and lease losses is inadequate to cover actual losses, our financial results would be harmed.

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. Although a substantial amount of loan losses were incurred between 2008 and 2012, the underwriting and credit monitoring policies and procedures that we have adopted to address this risk may not prevent additional losses that could have an adverse effect on our business, financial condition, results of operations and cash flows. Additional losses may arise for a wide variety of reasons, many of which are beyond our ability to predict, influence or control. Some of these reasons could include a continued economic downturn in the State of California, a reversal of the recent gains made in the California real estate market, changes in the interest rate environment, adverse economic conditions in Asia and natural disasters.

Like all financial institutions, we maintain an allowance for loan and lease losses to provide for loan and lease defaults and non-performance. Our allowance for loan and lease losses may not be adequate to cover actual loan and lease losses, and future provisions for loan and lease losses could materially and adversely affect our business, financial condition, results of operations and cash flows. Our allowance for loan and lease losses reflects our best estimate of the losses inherent in the existing loan and lease portfolio at the relevant balance sheet date and is based on management's evaluation of the collectability of the loan and lease portfolio, which evaluation is based on historical loss experience and other significant factors. For the year ended December 31, 2013, we recorded a provision for loan and lease losses and net loan charge-offs of $3.3 million and $4.4 million, respectively, compared to $19.8 million and $22.9 million for the year ended December 31, 2012.

The determination of an appropriate level of loan and lease loss allowance is an inherently difficult process and is based on numerous assumptions. The amount of future losses is susceptible to changes in economic, operating and other conditions, including changes in interest rates, that may be beyond our control and future losses may exceed current estimates. While we believe that our allowance for loan and lease losses is adequate to cover current losses, we cannot ensure that we will not increase the allowance for loan and lease losses further or that regulators will not require us to increase our allowance. Either of these occurrences could materially adversely affect our business, financial condition and results of operations but would not affect cash flow directly.

If the risks inherent in construction lending are further realized, our net income could be adversely affected.

At December 31, 2013, our construction loans were $73.3 million, or 5.4% of our total loans held, and the average loan size of our construction loans was $2.8 million. The risks inherent in construction lending include, among other things, the possibility that contractors may fail to complete, or fail to complete on a timely basis, construction of the relevant properties; substantial cost overruns in excess of original estimates and financing; market deterioration during construction; and a lack of permanent take-out financing. Loans secured by these properties also involve additional risk because the properties have no operating histories. In these loans funds are advanced upon the security of the project under construction, which is of uncertain value prior to completion of construction, and the estimated operating cash flow to be generated, by the completed project. The borrowers' ability to repay their obligations to us and the value of our security interest in the collateral will be materially adversely affected if the projects do not generate sufficient cash flow by being either sold or leased. Construction lending was a significant source of our loan losses incurred in 2009 and 2010.

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

We will be 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 new 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 will be phased in, for the Bank, over a period of five years, beginning in 2015. 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 percent of risk-based assets, net of regulatory deductions, and a capital conservation buffer of an additional 2.5 percent of common equity to risk-weighted assets, raising the target minimum common equity ratio to 7 percent;
- increase the minimum Tier 1 capital ratio to 8.5 percent inclusive of the capital conservation buffer;
- increase the minimum total capital ratio to 10.5 percent inclusive of the capital conservation buffer; and
- introduce a non-risk adjusted Tier 1 leverage ratio of 3 percent, 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 shareholders. The capital conservation buffer requirement, which is measured in addition to the minimum Common Equity Tier 1 capital of 4.5%, will be phased in over four years, starting at 0.625% for 2016, and rising to 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.

Future regulatory requirements could adversely affect us.

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.

Difficult economic and market conditions have adversely affected our industry and us.

During 2008-2010, dramatic declines in the housing market, with decreasing home prices and increasing delinquencies and foreclosures, negatively impacted the credit performance of mortgage and construction loans and resulted in significant write-downs of assets by many financial institutions.

Although 2012 and 2013 saw national and local economic conditions improve, a weak employment market continues to be a soft spot in the economy. A worsening of these conditions would likely exacerbate the adverse effects of these difficult market conditions on us and others in the financial institutions industry. In particular, we may face the following risks in connection with these events:

- We potentially face increased regulation of our industry. Compliance with such regulation may increase our costs and limit our ability to pursue business opportunities. Proposals have been discussed that call for a complete overhaul of the current regulatory framework applicable to commercial banks. We cannot assess the impact of any such changes on our business at this time.
- 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 classification of our criticized loans as substandard, doubtful and loss and the related provision for loan losses, and the estimated losses inherent in our loan portfolio, could be increased by our primary regulators in connection with an examination of our loan portfolio, which could subject us to restrictions on our operations and require us to increase our capital.
- Our banking operations are concentrated primarily in Southern California. Adverse economic conditions in this region in particular could impair borrowers’ ability to service their loans, decrease the level and duration of deposits by customers, and erode the value of loan collateral. This could increase the amount of our non-performing assets and have an adverse effect on our efforts to collect our non-performing loans or otherwise liquidate our non-performing assets (including other real estate owned) on terms favorable to us, if at all, and could also cause a decline in demand for our products and services, or a lack of growth or a decrease in deposits, any of which may cause us to incur losses, adversely affect our capital, and hurt our business.

As of December 31, 2013, approximately 72% of the book value of our loan portfolio consisted of loans collateralized by various types of 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 laws, regulations and policies and acts of nature. In addition, real estate values in California could be affected by, among other things, earthquakes and national disasters particular to the state. If real estate prices decline, particularly in California, the value of real estate collateral securing our loans could be significantly reduced. As a result, we may experience greater charge-offs and, similarly, 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.

As a result of these financial and economic crises, we have experienced substantial increases in non-performing loans in recent years. However, total non-performing loans decreased to $14.0 million at December 31, 2013 from $26.1 million at December 31, 2012 and $47.5 million at December 31, 2011, representing 1.1%, 1.7% and 5.0% of total loans owned at December 31, 2013, December 31, 2012 and December 31, 2011, respectively. Total non-performing assets decreased to $19.6 million at December 31, 2013 from $47.3 million at December 31, 2012 and $85.5 million at December 31, 2011, representing 1.1%, 3.0% and 6.5% of total assets at December 31, 2013, December 31, 2012 and December 31, 2011, respectively.

Declines in the volume of sales, especially in certain parts of California, along with the reduced availability of certain types of credit, have resulted in increases in delinquencies and losses in our portfolio of construction loans. Further declines in real estate prices with the continued economic recession in our markets and continued high or increased unemployment levels could cause additional losses which could continue to adversely affect our earnings and financial condition.

We rely heavily on our senior management team and other key employees, the loss of whom could materially and adversely affect our business.

Our success depends heavily on the abilities and continued service of our executive officers, especially Li Yu, our founder, Chairman and Chief Executive Officer. Mr. Yu, who founded the Bank, is integral to implementing our business plan. We currently do not have an employment agreement or non-competition agreement with Mr. Yu nor our other executives. Accordingly, members of our senior management team are not contractually prohibited from leaving or joining one of our competitors. If we lose the services of any of our executive officers, especially Mr. Yu, our business, financial condition, results of operations and cash flows may be adversely affected. Furthermore, attracting suitable replacements may be difficult and may require significant management time and resources.

We also rely to a significant degree on the abilities and continued service of our private banking, loan origination, underwriting, administrative, marketing and technical personnel. 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. If we fail to attract and retain qualified management personnel and the necessary deposit generation, loan origination, underwriting, administrative, finance, marketing and technical personnel, our business, financial condition, results of operations and cash flows may be materially adversely affected.

A natural disaster or recurring energy shortage, especially in California, could harm our business.

Historically, Southern California has been vulnerable to natural disasters. Therefore, we are susceptible to the risks of natural disasters, such as earthquakes, wildfires, floods and mudslides. Natural disasters could harm our operations directly through interference with communications, as well as through the destruction of facilities and our operational, financial and management information systems. Uninsured or underinsured disasters may reduce a borrower's ability to repay mortgage loans. Disasters may also reduce the value of the real estate securing our loans, impairing our ability to recover on defaulted loans. Southern California has also experienced energy shortages which, if they recur, could impair the value of the real estate in those areas affected. The occurrence of natural disasters or energy shortages in Southern California could have a material adverse effect on our business, financial condition, results of operations and cash flows.

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

Market interest rates are affected by many factors that are beyond our control and are hard to predict, including inflation, recession, performance of the stock markets, a rise in unemployment, tightening money supply, exchange rates, monetary and other policies of various governmental and regulatory agencies, domestic and international disorder and instability in domestic and foreign financial markets.

Changes in the interest rate environment may reduce our profits. Changes in interest rates will influence not only the interest we receive on our loans and investment securities and the amount of interest we pay on deposits, it will also affect our ability to originate loans and obtain deposits and our costs in doing so. Rising interest rates, generally, are associated with a lower volume of loan originations, while lower interest rates are usually associated with higher loan originations.

We expect that we will continue to realize a substantial portion of our income from the differential or "spread" between the interest earned on loans, securities and other interest-earning assets, and interest paid on deposits, borrowings and other interest-bearing liabilities. Because interest rates are based on the maturity, re-pricing and other characteristics of an instrument, conditions that trigger changes in interest rates do not produce equivalent changes in interest income earned on our interest-earning assets and interest expense paid on our interest-bearing liabilities. Although management measures the impact of changing interest rates on the Bank's net interest income and believes that current interest rate risk is low, fluctuations in interest rates could adversely affect our interest rate spread and, in turn, our profitability.

In addition, an increase in the general level of interest rates may adversely affect the ability of some borrowers to pay the interest on and principal of their obligations, which could reduce our cash flows and harm our asset quality. In rising interest rate environments, loan repayment rates may decline and in falling interest rate environments, loan repayment rates may increase.

We face strong competition from financial services companies and other companies that offer banking services, and our failure to compete effectively with these companies could have a material adverse effect on our business, financial condition, results of operations and cash flows.

We conduct our operations primarily in California. The banking and financial services businesses in California are highly competitive and increased competition within California may result in reduced loan originations and deposits. Ultimately, we may not be able to compete successfully against current and future competitors. Many competitors offer the types of loans and banking services that we offer in our service areas. These competitors include national banks, regional banks and other community banks. We also face competition from many other types of financial institutions, including saving and loan associations, finance companies, brokerage firms, insurance companies, credit unions, mortgage banks and other financial intermediaries. In particular, our competitors include financial institutions whose greater resources may afford them a marketplace advantage by enabling them to maintain numerous banking 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. Competitive conditions may intensify as continued merger activity in the financial services industry produces larger, better-capitalized and more geographically diverse companies. Additionally, banks and other financial institutions with larger capitalization and financial intermediaries not subject to bank regulatory restrictions may have larger lending limits which would allow them to serve the credit needs of larger customers. These institutions, particularly to the extent they are more diversified than we are, may be able to offer the same loan products and services we offer at more competitive rates and prices.

We also face competition from out-of-state financial intermediaries that have opened loan production offices or that solicit deposits in our market areas. If we are unable to attract and retain banking customers, we may be unable to continue our loan growth and level of deposits, and our business, financial condition, results of operations and cash flows may be materially adversely affected.

If our underwriting practices are not effective, we may suffer further losses in our loan portfolio and our results of operations may be harmed.

We seek to mitigate the risks inherent in our loan portfolio by adhering to specific underwriting practices. Depending on the type of loan, these practices include analysis of a borrower's prior credit history, financial statements, tax returns and cash flow projections, valuation of collateral based on reports of independent appraisers, verification of liquid assets and any other information deemed relevant. Although we believe that our underwriting criteria are appropriate for the types of loans we make, we cannot assure you that they will be effective in mitigating all risks. If our conservative underwriting criteria in effect when loans were granted proves to be ineffective, we may incur additional losses in our loan portfolio, and these losses may exceed the amounts set aside as reserves in our allowance for loan losses.

If the appraised value of our real property collateral is greater than the proceeds we realize from a sale or foreclosure of the property, we may suffer a loss in our loan portfolio.

In considering whether to make a loan on or secured by real property, we require an appraisal on such property. However, an appraisal is only an estimate of the value of the property at the time the appraisal is made. If the appraisal does not reflect the amount that may be obtained upon any sale or foreclosure of the property, we may not realize an amount equal to the indebtedness secured by the property and we may suffer further losses in our loan portfolio.

Adverse economic conditions in Asia could impact our business adversely.

We believe that our Chinese-American customers maintain significant ties to many Asian countries and, therefore, could be affected by economic and other conditions in those countries. We cannot predict the behavior of the Asian economies. U.S. economic policies, the economic policies of countries in Asia, domestic unrest and/or military tensions, crises in leadership succession, currency devaluations, and an unfavorable global economic condition may among other things adversely impact the Asian economies. We generally do not loan to customers or take collateral located outside of Southern California. However, if Asian economic conditions should deteriorate, we could experience an outflow of deposits by our Chinese-American customers. In addition, adverse economic conditions could prevent or delay these customers from meeting their obligations to us. This may adversely impact the recoverability of investments with or loans made to these customers. Adverse economic conditions may also negatively impact asset values and the profitability and liquidity of companies operating in Asia, which will also impact the Bank’s liquidity.

At December 31, 2013, approximately \$39.6 million, or 3.0%, of our loan portfolio consisted of loans made to finance international trade activities. Changes in monetary policy, including changes in interest rates, governmental regulation of international trade activities, currency valuation, price competition, competition from other financial institutions and general economic and political conditions could negatively impact the amount of goods imported to and exported from the United States, the ability of borrowers to repay loans made by us, and the number and extent of importers’ and exporters’ need for our trade finance products and services. It is possible that if the U.S. dollar weakens against other foreign currencies, the cost of imported goods will increase, which could have an adverse impact on some of our customers who import goods for resale in the United States. Such factors could have a material adverse effect on our business, financial condition, results of operations and cash flows.

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

Although we are planning to continue to grow the balance sheet, we intend to seek additional deposits by continuing to establish and strengthen our personal relationships with our customers and by offering deposit products that are competitive with those offered by other financial institutions in our markets. Although we are confident that our liquidity is sufficient, we cannot assure you that our liquidity management efforts will be successful. Our inability to attract additional deposits at competitive rates could have a material adverse effect on our business, financial condition, results of operations and cash flows.

We rely to a certain degree on large certificates of deposits (over \$250,000) to fund our operations, and the potential volatility of such deposits and the unavailability of any such funds in the future could adversely impact our growth strategy and prospects.

Our average jumbo deposit customer has been a customer of the Bank for over six years which indicates that these are long-term customers who consistently renew their CDs with the Bank. At December 31, 2013, we held \$213.4 million of Jumbo CDs, representing 14.0% of total deposits. These deposits are considered by the banking industry to be volatile and could be subject to withdrawal. Withdrawal of a material amount of such deposits would adversely impact our liquidity, profitability, business, financial condition, results of operations and cash flows.

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

We rely on communications, information, operating and financial control systems technology from third-party service providers, and we may suffer an interruption in or break of those systems that may result in lost business and we may not be able to obtain substitute providers on terms that are as favorable if our relationships with our existing service providers are interrupted. We rely heavily on third-party service providers for much of our communications, information, operating and financial control systems technology, including customer relationship management, general ledger, deposit, servicing and loan origination systems. Any failure, interruption or breach in security of these systems could result in failures or interruptions in our customer relationship management, general ledger, deposit, servicing and/or loan origination systems. We cannot assure you that such failures or interruptions will not occur or, if they do occur, that they will be adequately addressed by us or the third parties on which we rely. The occurrence of any failures or interruptions could have a material adverse effect on our business, financial condition, results of operations and cash flows. If any of our third-party service providers experience financial, operational or technological difficulties, or if there is any other disruption in our relationships with them, we may be required to locate alternative sources of such services, and we cannot assure you that we could negotiate terms that are as favorable to us, or could obtain services with similar functionality as found in our existing systems without the need to expend substantial resources, if at all. Any of these circumstances could have a material adverse effect on our business, financial condition, results of operations and cash flows.

The U.S. government's monetary policies or changes in those policies could have a major effect on our operating results, and we cannot predict what those policies will be or any changes in such policies or the effect of such policies on us.

Our earnings will be affected by domestic economic conditions and the monetary and fiscal policies of the U.S. government and its agencies. The monetary policies of the Federal Reserve Bank, or the FRB, have had, and will continue to have, an important effect on the operating results of commercial banks and other financial institutions through its power to implement national monetary policy in order, among other things, to curb inflation or combat a recession.

The monetary policies of the FRB, implemented principally through open market operations and regulation of the discount rate and reserve requirements, have had major effects upon the levels of bank loans, investments and deposits. For example, in 2008-2009, multiple rate decreases in the Fed Funds rate by the Federal Open Market Committee placed tremendous pressure on the profitability of many financial institutions because of the resulting contraction of net interest margins due to high levels of adjustable rate loans. It is not possible to predict the nature or effect of future changes in monetary and fiscal policies.

Governmental regulation and any further enforcement actions against us may further impair our operations or restrict our growth and could result in a decrease in the value of your shares.

In addition to the requirements of the MOU, we are subject to significant governmental supervision and regulation. Because our business is highly regulated, the laws, rules and regulations and supervisory guidance and policies applicable to us are subject to regular modification and change, which may have the effect of increasing or decreasing the cost of doing business, modifying permissible activities or enhancing the competitive position of other financial institutions. These laws are primarily intended for the protection of consumers, depositors and not for the protection of shareholders of bank holding companies or banks. 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. We cannot assure you that these proposed laws, rules and regulations or any other laws, rules or regulations will not be adopted in the future, which could make compliance much more difficult or expensive, restrict our ability to originate loans, further limit or restrict the amount of commissions, interest or other charges earned on loans originated by us or otherwise adversely affect our business, financial condition, results of operations or cash flows.

Federal and state governments could pass additional legislation responsive to current credit conditions. As an example, we could experience higher credit losses because of federal or state legislation or regulatory action that reduces the principal amount or interest rate under existing loan contracts. Also, we could experience higher credit losses because of federal or state legislation or regulatory action that limits the Bank's ability to foreclose on property or other collateral or makes foreclosure less economically feasible.

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

In the course of our business, we may foreclose on and take title to properties securing our loans. If hazardous substances were discovered on any of the properties, we may be held liable to governmental entities or to third parties for property damage, personal injury, investigation and clean-up costs incurred by these parties in connection with environmental contamination or may be required to investigate or clean up hazardous or toxic substances or chemical releases at a property. Many environmental laws can impose liability regardless of whether we knew of or were responsible for the contamination. In addition, if we arrange for the disposal of hazardous or toxic substances at another site, we may be liable for the costs of cleaning up and removing those substances from the site, even if we neither own nor operate the disposal site. Environmental laws may require us to incur substantial expenses and may materially limit use of properties we acquire through foreclosure, reduce their value or limit our ability to sell them in the event of a default on the loans they secure. In addition, future laws or more stringent interpretations or enforcement policies with respect to existing laws may increase our exposure to environmental liability.

Negative publicity could damage our reputation.

Reputation risk, or the risk to our earnings and capital from negative publicity or public opinion, is inherent in our business. Negative publicity or public opinion could adversely affect our ability to keep and attract customers and expose us to adverse legal and regulatory consequences. Negative public opinion could result from our actual or perceived conduct in any number of activities, including lending practices, corporate governance, regulatory compliance, mergers and acquisitions, and disclosure, sharing or inadequate protection of customer information, and from actions taken by government regulators and community organizations in response to that conduct.

Terrorist attacks may have depressed the economy in the past and if there are additional terrorist events especially in our market, the economy could be adversely affected.

The possibility of further terrorist attacks, as well as continued terrorist threats, may create and perpetuate this economic uncertainty. Future terrorist acts and responses to such activities could adversely affect us in a number of ways, including an increase in delinquencies, bankruptcies or defaults that could result in a higher level of non-performing assets, net charge-offs and provision for loan losses.

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

The trading price of our common stock has fluctuated and may in the future 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 the share prices and trading volumes that affect the market prices of the shares of many companies. These 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 quarterly fluctuations in our operating results and financial condition;
- Changes in revenue or earnings estimates or publication of research reports and recommendations by financial analysts;
- 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 by institutional shareholders;
- Fluctuations in the stock price and operating results of our competitors;
- 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 us; or
- Domestic and international economic factors unrelated to our performance.

The stock market and, in particular, the market for financial institution stocks, has experienced significant volatility. As a result, the market price of our common stock has been and in the future may be volatile. In addition, the trading volume in our common stock may fluctuate more than usual 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 “Forward-Looking Statements”. Current levels of market volatility are still historically high. The capital and credit markets have been experiencing volatility and disruption for more than two 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.

Your share ownership may be diluted by the issuance of additional shares of our common stock in the future.

Your share ownership may be diluted by the issuance of additional shares of our common stock in the future. Our amended and restated articles of incorporation do not provide for preemptive rights to the holders of our common stock. Any authorized but unissued shares are available for issuance by our Board of Directors. As a result, if we issue additional shares of common stock to raise additional capital or for other corporate purposes, you may be unable to maintain your pro rata ownership in the Bank.

We could be liable for breaches of security in our online banking services. Fear of security breaches could limit the growth of our online services.

We offer various Internet-based services to our clients, including online banking services. The secure transmission of confidential information over the Internet is essential to maintain our clients' confidence in our online services. Advances in computer capabilities, new discoveries or other developments could result in a compromise or breach of the technology we use to protect client transaction data. In addition, individuals may seek to intentionally disrupt our online banking services or compromise the confidentiality of customer information with criminal intent. Although we have developed systems and processes that are designed to prevent security breaches and periodically test our security, failure to mitigate breaches of security could adversely affect our ability to offer and grow our online services, result in costly litigation and loss of customer relationships and could have an adverse effect on our business.

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 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.

ITEM 1B. UNRESOLVED STAFF COMMENTS

None.

ITEM 2. PROPERTIES

Our headquarters and main branch office are located at 601 S. Figueroa Street, Los Angeles, California, 90017. This lease expires in August of 2020.

At December 31, 2013, we maintained eleven full-service branch offices in Alhambra, Arcadia, Century City, City of Industry, Diamond Bar, Los Angeles, Pico Rivera, San Francisco, Torrance, Anaheim, and Irvine, California all of which we lease, except the Irvine branch which we own. On February 6, 2013, we opened a new branch office in San Francisco, California. We believe that no single lease is material to our operations. Leases for branch offices are generally 3 to 12 years in length and generally provide renewal terms of 3 to 5 additional years.

We believe that our existing facilities are adequate for our present purposes. We believe that, if necessary, we could secure alternative facilities on similar terms without adversely affecting our operations. Total lease expense was $1.8 million for the year ended December 31, 2013 and $1.6 million for December 31, 2012.

The Bank accounts for its leases under the provision of ASC 840, Leases. Certain leases have scheduled rent increases, and certain leases include an initial period of free or reduced rent as an inducement to enter into the lease agreement ("rent holiday"). The Bank recognizes rent expense for rent increases and rent holiday on a straight line basis over the terms of the underlying lease without regard to when rent payments are made.

The following table provides certain information with respect to our owned and leased branch locations.

Location	Address	Current Lease Term Expiration Date	Square Footage	Total Deposits at December 31, 2013
				(in thousands)
Los Angeles County				
Alhambra	325 E. Valley Blvd.	05/31/19	6,000	$231,098
Arcadia	1469 S. Baldwin Avenue	03/01/19	2,600	107,897
Century City	1801 Century Park East, Suite 100	06/30/16	4,416	146,705
City of Industry	17515-A Colima Road	03/14/15	5,610	161,968
Diamond Bar	1373 S. Diamond Bar Blvd.	11/30/16	3,440	98,304
Los Angeles (Head Office & branch)	601 S. Figueroa Street, 29th Floor	08/31/20	22,627	479,853
Pico Rivera	7004 Rosemead Blvd.	02/10/19	2,850	22,146
Torrance	21615 Hawthorne Boulevard, Suite 100	06/30/16	4,800	157,049
Orange County				
Anaheim	1055 N. Tustin Avenue	7/15/18	2,750	23,660
Irvine (Owned Branch Premises)	890 Roosevelt Avenue	N/A	4,960	57,281
Northern California				
San Francisco	600 California Street, Suite 550	12/19/17	3,679	43,353

ITEM 3. LEGAL PROCEEDINGS

From time to time we are a party to claims and legal proceedings arising in the ordinary course of business. We accrue for any probable loss contingencies that are estimable and disclose any possible losses in accordance with ASC 450, "*Contingencies*." There are no pending legal proceedings or, to the best of our knowledge, threatened legal proceedings, to which we are a party which may have a material adverse effect upon our financial condition, results of operations and business prospects.

ITEM 4. MINE SAFETY DISCLOSURES

Not applicable

PART II

ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY AND RELATED SHAREHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

Market Information

Our common stock is listed on the NASDAQ Global Select Market under the symbol "PFBC." Our common stock closed at $24.49 on March 12, 2014 and there were 13,428,203 outstanding shares of our common stock on that date. The number of shares and per share data has been adjusted to reflect our June 17, 2011 one-for-five reverse stock split.

The following table sets forth the high and low sales prices for our common stock for the periods indicated as reported by the NASDAQ, as well as the cash dividends declared per share during the last two years:

	High	Low	Cash Dividends Declared
2012			
First Quarter………….	$12.49	$ 7.40	*
Second Quarter……….	$13.36	$ 11.16	*
Third Quarter…………	$14.50	$ 10.52	*
Fourth Quarter………..	$14.57	$ 12.95	*
2013			
First Quarter………….	$16.74	$ 14.24	*
Second Quarter……….	$17.33	$ 14.64	*
Third Quarter…………	$17.96	$ 15.89	*
Fourth Quarter………..	$21.29	$ 17.53	*

*On April 16, 2009, the Bank's Board of Directors elected to indefinitely suspend the Bank's cash dividend in order to preserve the Bank's capital. In addition, the MOU prohibits the payment of dividends to our shareholders without the prior approval of the FDIC and CDBO.

Holders

As of March 12, 2014, 13,428,203 shares of the Bank's common stock were held by 146 shareholders of record.

Reverse Stock Split

At the May 24, 2011 Annual Meeting of Shareholders, the shareholders of the Bank approved the proposal to authorize the Board of Directors in its discretion, without further authorization of the Bank's shareholders, to amend the Bank's Articles of Incorporation to effect a reverse split of the Bank's common stock by a ratio of one for five ("Reverse Stock Split"). The Reverse Stock Split was also subject to receipt of an Order of Exemption from the California Department of Business Oversight, which the Bank received on June 17, 2011. Upon receipt of the Order of Exemption, the Bank's Board of Directors amended the Bank's Articles of Incorporation to reflect the effect of the Reverse Stock Split of the Bank's common stock effective with respect to the shareholders of record at the close of business on June 17, 2011 (the "Effective Time"). At the Effective Time every five shares of Preferred Bank's pre-split common shares automatically were converted into one post-split share. The Reverse Stock Split affected all holders of common stock uniformly and did not affect any shareholder's percentage ownership interest in the Bank, except record holders of common stock otherwise entitled to a fractional share as a result of the Reverse

Stock Split received a cash payment in lieu of such fractional share in a proportional amount based on the closing price of the common stock on the NASDAQ Stock Exchange at the Effective Time. Under the terms of the Bank's equity incentive plans, at the Effective Time, the number of shares reserved for issuance under the plans was proportionately decreased in accordance with the exchange ratio. Under the terms of the options granted under the plans, at the Effective Time, the number of shares covered by each option decreased and the conversion or exercise price per share increased in accordance with the exchange ratio. Accordingly, all references in the accompanying consolidated statements of financial condition, statements of operations and statements of changes in shareholders' equity to the number of common stock shares and earnings per share amounts have been retroactively adjusted for all periods presented. The number of authorized common shares remains at 20,000,000 subsequent to the Reverse Stock Split.

Dividends

On April 16, 2009, the Bank's Board of Directors elected to indefinitely suspend the Bank's cash dividend in order to preserve the Bank's capital. Further, under the terms of the MOU, we are prohibited from paying cash dividends or any other payments to our shareholders without the prior written consent of the FDIC and the CDBO. With the eventual termination of the MOU, dividend payments will depend upon our earnings, financial condition, results of operations, capital requirements, available investment opportunities, regulatory restrictions, contractual restrictions and other factors that our Board of Directors may deem relevant. Accordingly, there can be no assurance that any stock or cash dividends will be declared in the future, and if any are declared, what amount they will be.

Because we are a California state-chartered bank, our ability to pay dividends or make distributions to shareholders are subject to restrictions set forth in the California Financial Code in addition to the requirements of the MOU. California Financial Code Section 1132 restricts the amount available for cash dividends by state-chartered banks to the lesser of: (1) retained earnings; or (2) the bank's net income for its last three fiscal years (less any distributions to shareholders made during such period).

However, Section 1133 of the California Financial Code provides that notwithstanding the provisions of Section 1132, a state-chartered bank may, with the prior approval of the California Commissioner, make a distribution to its shareholders in an amount not exceeding the greater of:

- Retained earnings;
- Net income for a bank's last preceding fiscal year; or
- Net income of the bank for its current fiscal year.

If the California Commissioner finds that the shareholders' equity of the Bank is not adequate or that the payment of a dividend would be unsafe or unsound for the Bank, the California Commissioner may order the Bank not to pay a dividend to the Bank's shareholders.

In addition, under California law, the California Commissioner has the authority to prohibit a bank from engaging in business practices which the California Commissioner considers to be unsafe or injurious to its business or financial condition. It is possible, depending on our financial condition and other factors, that the California Commissioner could assert that the payment of dividends or other payments to our shareholders might under some circumstances be unsafe or injurious to our business or financial condition and prohibit such payment.

The FDIC also has the authority to prohibit a bank from engaging in business practices which the FDIC considers to be unsafe or unsound. It is possible, depending upon our financial condition and other factors, that the FDIC could assert that the payment of dividends or other payments might under some circumstances be such an unsafe or unsound practice and prohibit such payment.

Recent Sales of Unregistered Securities

There were no sales of unregistered securities in 2013.

Issuer's Purchases of Equity Securities.

No repurchases of the Bank's common stock were made by or on behalf of the Bank in 2013**.**

Securities Authorized for Issuance Under Equity Compensation Plans.

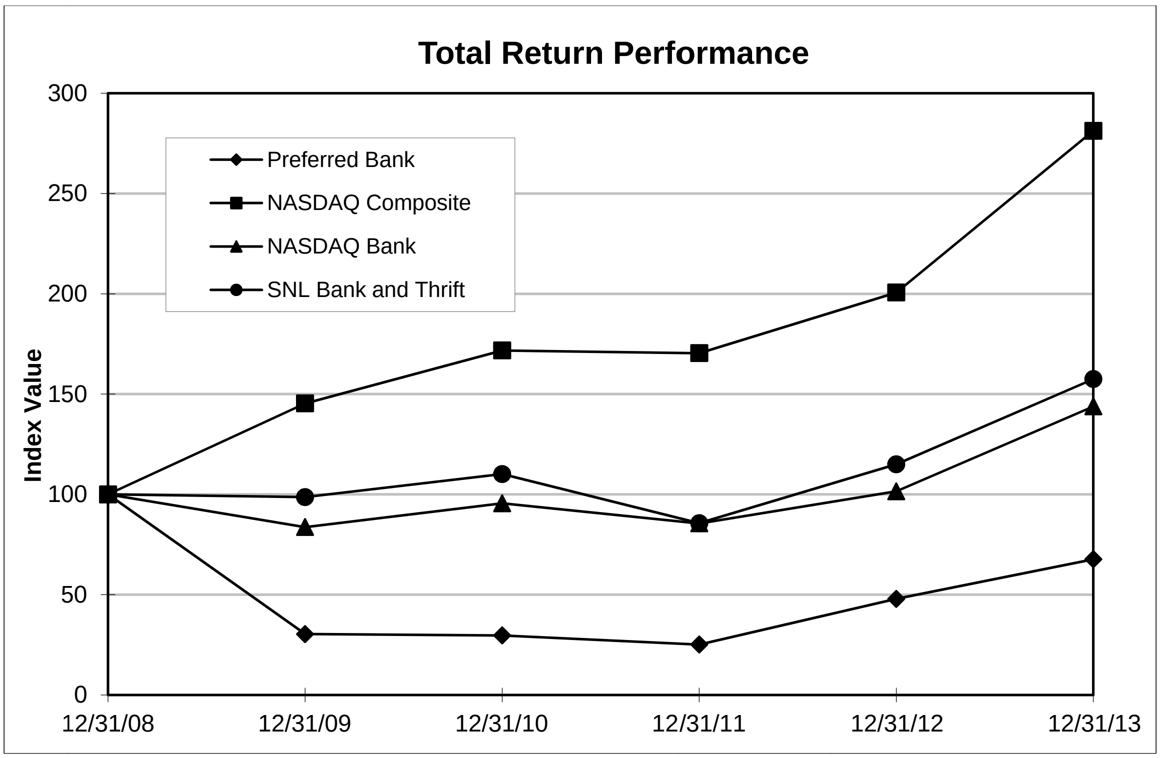
The following table provides information as of December 31, 2013, regarding equity compensation plans under which equity securities of the Bank were authorized for issuance.

Plan Category	**Number of securities to be issued upon exercise of outstanding options (a)**	**Weighted average exercise price of outstanding options (b)**	**Number of securities available for future issuance under equity compensation plans excluding securities reflected in column (a) (c)**
Equity incentive plans approved by security holders	790,152	$15.69	399,371
Equity incentive plans not approved by security holders	—	—	—
	790,152		399,371

The shares data reflected above has been adjusted to reflect our June 2011 one-for-five stock split; and shares under the 2004 Equity Plan available as a result of the Bank's tender offer and repurchase of certain options on October 29, 2010.

__Stock Performance Graph__

The following graph shows a comparison of shareholder return on the Bank's common stock based on the market price of the common stock assuming the reinvestment of dividends, for the period beginning December 31, 2008 assuming an investment of $100 in each as of December 31, 2008. The Bank is not included in either of these indices. Total shareholder return for the Bank, as well as for the indices, is based on the cumulative amount of dividends for a given period (assuming dividend reinvestment) and the difference between the share price at the beginning and at the end of the period. This graph is historical only and may not be indicative of possible future performance of the common stock.



	__Period Ending__					
__Index__	**12/31/08**	**12/31/09**	**12/31/10**	**12/31/11**	**12/31/12**	**12/31/13**
Preferred Bank	100.00	30.37	29.70	25.14	47.92	67.66
NASDAQ Composite	100.00	145.36	171.74	170.38	200.63	281.22
NASDAQ Bank	100.00	83.70	95.55	85.52	101.50	143.84
SNL Bank and Thrift	100.00	98.66	110.14	85.64	115.00	157.46

ITEM 6. SELECTED FINANCIAL DATA

The following table shows our selected historical financial data for the periods indicated. You should read our selected historical financial data, together with the notes thereto, in conjunction with the more detailed information in our consolidated financial statements and related notes and "Management's Discussion and Analysis of Financial Condition and Results of Operations" included elsewhere in this Form 10-K

Our financial condition data as of December 31, 2013 and 2012 and our statement of operations data for the years ended December 31, 2013, 2012 and 2011 have been derived from our audited historical financial statements included elsewhere in this Form 10-K.

	At or for the Year Ended December 31,				
	2013	2012	2011	2010	2009
	(Dollars in thousands, except per share data)				
Financial Condition Data:					
Total assets	$ 1,768,959	$ 1,554,856	$ 1,309,797	$ 1,255,866	$ 1,306,781
Total deposits	1,529,314	1,357,527	1,117,953	1,081,265	1,160,412
Investment securities held-to-maturity	—	979	3,021	—	—
Investments securities available-for-sale, at fair value sale	142,670	210,742	166,083	183,269	114,464
Loans and leases, gross	1,323,431	1,131,703	953,627	915,410	1,043,299
Cash and cash equivalents	246,615	151,995	142,466	108,233	68,071
Other real estate owned[(1)]	5,602	28,280	37,577	53,268	59,190
Shareholders' equity	206,916	187,838	158,048	141,334	85,374
Statement of Operations Data:					
Interest income	$ 69,726	$ 61,542	$ 53,790	$ 52,088	$ 58,876
Interest expense	7,729	7,783	10,303	14,822	22,812
Net interest income	61,997	53,759	43,487	37,266	36,064
Provision for credit losses	3,250	19,800	5,700	16,550	71,250
Net interest income (loss) after provision for loan and lease losses	58,747	33,959	37,787	20,716	(35,186)
Noninterest income	2,003	3,508	2,790	2,807	6,476
Noninterest expense	29,261	34,178	33,392	41,037	51,953
Income (loss) before provision for income taxes	31,489	3,289	7,185	(17,514)	(80,663)
(Benefit) provision for income taxes	12,290	(20,583)	(5,049)	(704)	(8,128)
Net income (loss)	$ 19,199	$ 23,872	$ 12,234	$ (16,810)	$ (72,535)
Accretion of beneficial conversion feature	—	—	—	(25,600)	—
Income allocated to participating securities	(201)	(323)	(195)	—	—
Net income (loss) available to common shareholders	$ 18,998	$ 23,549	$ 12,039	$ (42,410)	$ (72,535)

	At or for the Year Ended December 31,				
	2013	2012	2011	2010	2009
	(Dollars in thousands, except per share data)				
Share Data:					
Net (loss)income per share, basic[2] [10]	$ 1.45	$ 1.80	$ 0.93	$ (6.21)	$ (31.49)
Net (loss) income per share, diluted[2] [10]	$ 1.42	$ 1.78	$ 0.93	$ (6.21)	$ (31.49)
Book value per share[3] [10]	$ 15.58	$ 14.19	$ 11.95	$ 10.72	$ 27.05
Shares outstanding at period end[10]	13,280,653	13,234,608	13,220,955	13,188,305	3,153,425
Weighted average number of shares outstanding, basic[2] [10]	13,116,563	13,050,559	12,995,525	6,829,734	2,303,629
Weighted average number of shares outstanding, diluted[2] [10]	13,364,320	13,247,389	12,995,525	6,829,734	2,303,629
Selected Other Balance Sheet Data[4]:					
Average assets	$ 1,633,710	$ 1,426,053	$1,237,034	$1,343,450	$ 1,440,279
Average earning assets	1,578,570	1,367,496	1,192,942	1,276,478	1,357,385
Average shareholders' equity	196,981	178,257	148,817	127,289	129,959
Selected Financial Ratios[4]:					
Return on average assets	1.18%	1.67%	0.99%	(1.25)%	(5.04)%
Return on average shareholders' equity[3]	9.75	13.39	8.22	(13.21)	(55.81)
Shareholders' equity to assets[5]	11.70	12.08	12.07	11.25	6.53
Net interest margin[6]	3.95	3.96	3.69	2.98	2.72
Efficiency ratio[7]	45.72	59.68	72.16	102.41	122.13
Selected Asset Quality Ratios:					
Non-performing loans to total loans and leases[8]	1.06%	2.31%	4.98%	11.13%	13.89%
Non-performing assets to total assets[9]	1.11	3.50	6.49	12.30	15.62
Allowance for loans and lease losses to total loans and leases	1.47	1.84	2.50	3.60	4.10
Allowance for loans and lease losses to non-performing loans	138.80	78.82	49.98	32.30	29.55
Net charge-offs (recoveries) to average loans and leases	0.36	2.25	1.65	2.71	4.76

(1) These amounts include all property held by us as a result of foreclosure.

(2) Net income per share, basic is computed by dividing net income adjusted by presumed dividend payments and earnings on unvested restricted stock by the weighted average number of common shares outstanding. Losses are not allocated to participating securities. Unvested shares of restricted stock are excluded from basic shares outstanding. Net income per share, diluted reflects the potential dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock or resulted in the issuance of common stock that then shares in the loss or earnings of the Bank. The net loss available to common shareholders was $6.21 per common share for year ended December 31, 2010, and included $3.75 loss per share due to the recognition of the intrinsic value of the beneficial conversion feature of the preferred stock.

(3) Book value per share represents our shareholders' equity divided by the number of shares of common stock issued and outstanding at the end of the period indicated (exclusive of shares exercisable under our stock option plans).

(4) Average balances used in this chart and throughout this annual report are based on daily averages. Percentages as used throughout this annual report have been rounded to the closest whole number, tenth or hundredth as the case may be.

(5) For a discussion of the components of the capital ratios, see "Management's Discussion and Analysis of Financial Condition and Results of Operations—Capital Resources."

(6) Net interest margin is net interest income expressed as a percentage of average total interest-earning assets.

(7) The efficiency ratio is the ratio of noninterest expense divided by the sum of net interest income before the provision for credit losses plus noninterest income.

(8) Non-performing loans consist of loans on non-accrual and loans past due 90 days or more and restructured debt.

(9) Non-performing assets consist of non-performing loans and other real estate owned.

(10) Adjusted to reflect 1-for-5 stock split, effective on June 2011.

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

Our discussion and analysis of earnings and related financial data are presented herein to assist investors in understanding the financial condition of our Company at December 31, 2013 and 2012, and the results of operations for the years ended December 31, 2013, 2012 and 2011. This discussion should be read in conjunction with the consolidated financial statements and related footnotes of our Company presented elsewhere herein. Historical share and per share data has been adjusted to reflect our June 2011 one-for-five stock split, and the conversion of preferred stock to common shares in August 2010.

Overview

We experienced fairly significant growth in loans and net income in 2013. The national economy is improving and the local economy is gaining strength. The real estate market in Southern California could now be considered to be strong however there is still weakness in some outlying areas of Southern California. During 2013, the Bank posted a high level of net income due growth in loans, a reduction in the provision for loan losses and a reduction in the Bank's non-interest expenses. The reduction in expenses was mainly due to lower costs associated with NPA's.

We derive our income primarily from interest received on our loan and investment securities portfolios, and fee income we receive in connection with servicing our loan and deposit customers. Our major operating expenses are the interest we pay on deposits and borrowings, and the salaries and related benefits we pay our management and staff. We rely primarily on locally-generated deposits, approximately half of which we receive from the Chinese-American market within California, to fund our loan and investment activities.

For the year ended December 31, 2013, the Bank recorded net income of $19.2 million as compared to net income of $23.9 million for 2012. Net income in 2012 was larger due to the reversal of the valuation allowance on deferred tax assets during the period, resulting in a net tax benefit of $20.6 million for the year. See —"Results of Operations".

For the year ended December 31, 2012, the Bank recorded net income of $23.9 million as compared to net income of $12.2 million for December 31, 2011. Pre-tax income in 2012 was only $3.3 million due mainly to the $19.8 million provision for loan losses recorded for 2012. However, the Bank released its valuation allowance on its deferred tax asset in the first quarter which resulted in a tax benefit for the year of $20.6 million. See —"Results of Operations".

Regulatory Matters

As a result of a regulatory examination during 2013, the Memorandum of Understanding which the Bank entered into with the FDIC and CDBO on May 25, 2012 was terminated and the Bank entered into a new MOU with both the FDIC and the CDBO on October 1 2013. Among other things, the MOU requires the Bank to maintain a Tier 1 Leverage Ratio of 10%, improve its BSA compliance, maintain a minimum Tier 1 Leverage Ratio of 10%, and to refrain from declaring or paying cash dividends to its shareholders and establishing new branches and offices without the prior written approval of the FDIC and CDBO. As of December 31, 2013, the Tier 1 Leverage Ratio of the Bank was 11.80%, exceeding the level required by the MOU. In response to the examination findings, management has dedicated a significant amount of time and resources toward strengthening its BSA and compliance programs and complying with the MOU. The Board of Directors and management are committed to meeting all of the requirements of the MOU and seeing to its earliest possible termination.

Critical Accounting Policies

Our accounting policies are integral to understanding the financial results reported. Our most complex accounting policies require management's judgment to ascertain the valuation of assets, liabilities, commitments and contingencies. We have established detailed policies and control procedures that are intended to ensure valuation methods are well controlled and consistently applied from period to period. In addition, these policies and procedures are intended to ensure that the process for changing methodologies occurs in an appropriate manner. The following is a brief description of our current accounting policies involving significant management valuation judgments.

Allowance for Loan and Lease Losses

The allowance for loan and lease losses, or ALLL, represents our best estimate of losses inherent in the existing loan and lease portfolio. The allowance for loan and lease losses is increased by the provision for credit losses charged to expense and reduced by loans and leases charged off, net of recoveries.

We evaluate our allowance for loan and lease losses quarterly. We believe that the allowance for loan and lease losses is a "critical accounting estimate" because it is based upon management's assessment of various factors affecting the collectability of the loans and leases, including current economic conditions, past credit experience, delinquency status, the value of the underlying collateral, if any, and a continuing review of the portfolio of loans and leases. On a recurring basis, the Bank measures the fair value of impaired collateral dependent loans based on fair value of the collateral value which is derived from appraisals that take into consideration prices in observable transactions involving similar assets in similar locations in accordance with Receivables Topic of FASB ASC covering loan impairments.

Like all financial institutions, we maintain an ALLL based on a number of quantitative and qualitative factors. The amount of the allowance is based on management's evaluation of the collectability of the loan and lease portfolio and that evaluation is based on historical loss experience and other significant factors. These other significant factors include the level and trends in delinquent, non-accrual and adversely classified loans and leases, trends in volume and terms of loans and leases, levels and trends in credit concentrations, effects of changes in underwriting standards, policies, procedures and practices, national and local economic trends and conditions, changes in capabilities and experience of lending management and staff and other external factors including industry conditions, competition and regulatory requirements.

The allowance adequacy analysis requires a significant amount of judgment and subjectivity by management especially in regards to the qualitative portion of the analysis. We cannot provide you with any assurance that further economic difficulties or other circumstances which would adversely affect our borrowers and their ability to repay outstanding loans and leases will not occur. These difficulties or other circumstances could result in increased losses in our loan and lease portfolio, which could result in actual losses that exceed reserves previously established.

Other Real Estate Owned (OREO)

Upon acquisition, OREO is stated at the fair value of the property based on appraisal, less estimated selling costs. Any cost in excess of the fair value at the time of acquisition is accounted for as a loan charge-off and deducted from the allowance for loan and lease losses. Based on appraisals obtained every 6-12 months, valuation allowance is established for any subsequent declines in value through a charge to earnings, on an individual basis by property. Operating expenses of such properties, net of related income, and gains and losses on their disposition are included in noninterest income or expense, as appropriate.

Investment Securities

The classification and accounting for investment securities are discussed in detail in Note 1 of the Consolidated Financial Statements presented elsewhere herein. Under Investments – Debt and Equity Securities Topic of FASB ASC, investment securities must be classified as held-to-maturity, available-for-sale, or trading. The appropriate classification is based partially on our ability to hold the securities to maturity and largely on management's intentions with respect to either holding or selling the securities. The classification of investment securities is significant since it directly impacts the accounting for unrealized gains and losses on securities. Unrealized gains and losses on trading securities flow directly through earnings during the periods in which they arise, whereas unrealized gains and losses on available-for-sale securities are recorded as a separate component of shareholders' equity (accumulated other comprehensive income or loss) and do not affect earnings until realized. The fair values of our investment securities are generally determined by an independent pricing service and are considered to be level 2 or 3 categories as defined by Fair Value Measurements and Disclosures Topic of FASB ASC. The fair values of investment securities are generally determined by reference to market prices obtained from an independent external pricing service. In obtaining such valuation information from third parties, we have evaluated the methodologies used to develop the resulting fair values. The procedures include, but are not limited to, initial and on-going review of third party pricing methodologies, review of pricing trends, and monitoring of trading volumes. We ensure whether prices received from independent brokers represent a reasonable estimate of fair value through the use of external cash flow model developed based on spreads, and when available, market indices. As a result of this analysis, if we determine there is a more appropriate fair value based upon the available market data, the price received from the third party maybe adjusted accordingly. Management reviews the fair value of investment securities on a monthly basis for reasonableness. In addition, management has a separate fixed income broker/dealer review the fair values received from the pricing service on a quarterly basis as an additional control over the process of determining fair values. On a quarterly basis, management thoroughly assesses the fair values of impaired investment securities by looking at other data regarding the fair values such as: recent trading levels of the same or similarly rated securities, reviewing assumptions used in discounted cash flow analyses for reasonableness and other information such as general market conditions.

We are obligated to assess, at each reporting date, whether there is an "other-than-temporary" impairment to our investment securities. For debt securities, we assess whether (a) we have the intent to sell the security and (b) it is more likely than not that we will be required to sell the security prior to its anticipated recovery. These steps are done before assessing whether we will recover the cost basis of the investment. This assessment requires us to assert we have both the intent and the ability to hold a security for a period of time sufficient to allow for an anticipated recovery in fair value to avoid recognizing an other-than-temporary impairment. In instances when a determination is made that an other-than-temporary impairment exists but we do not intend to sell the debt security and it is not more likely than not that we will be required to sell the debt security prior to its anticipated recovery, the FASB guidance covering recognition and presentation of other-than-temporary impairments, changes the presentation and amount of the other-than-temporary impairment recognized in the income statement. The other-than-temporary impairment is separated into (a) the amount of the total other-than-temporary impairment related to a decrease in cash flows expected to be collected from the debt security (the credit loss) and (b) the amount of the total other-than-temporary impairment related to all other factors. The amount of the total other-than-temporary impairment related to the credit loss is recognized in earnings. The amount of the total other-than-temporary impairment related to all other factors is recognized in other comprehensive income. The determination of other-than-temporary impairment is a subjective process, requiring the use of judgments and assumptions. We examine all individual securities that are in an unrealized loss position at each reporting date for other-than-temporary impairment. Specific investment-related factors we examine to assess impairment include the nature of the investment, severity and duration of the loss, the probability that we will be unable to collect all amounts due, an analysis of the issuers of the securities and whether there has been any cause for default on the securities and any change in the rating of the securities by the various rating agencies. Additionally, we evaluate whether the creditworthiness of the issuer calls the realization of contractual cash flows into question.

The Bank considers all available information relevant to the collectability of the pooled trust preferred securities, including information about past events, current conditions, and reasonable and supportable forecasts, when developing the estimate of future cash flows and making its other-than-temporary impairment assessment for our portfolio of pooled trust preferred securities. The Bank considers factors such as remaining payment terms of the security, prepayment speeds, the financial condition of the underlying issuers and expected deferrals, defaults and recoveries.

We re-examine the financial resources, intent and the overall ability of the Bank to hold the securities until their fair values recover. Management does not believe that there are any investment securities, other than those identified in the current and previous periods, which are deemed to be "other-than-temporarily" impaired as of December 31, 2013. Investment securities are discussed in more detail in Note 2 to the Bank's consolidated financial statements presented elsewhere in this report.

Income Taxes

We accounted for income taxes under the asset and liability method, which requires the recognition of deferred tax assets and liabilities for the expected future tax consequences of events that have been included in the financial statements. Under this method, deferred tax assets and liabilities are determined based on the differences between the financial statements and tax basis of assets and liabilities using enacted tax rates in effect for the year in which the differences are expected to reverse. The effect of a change in tax rates on deferred tax rates on deferred tax assets and liabilities is recognized in income in the period that includes the enacted date. Income taxes are discussed in more detail in *"Notes to Consolidated Financial Statements, Note 1 — Summary of Significant Accounting Policies"* and *"Note 6 — Income Taxes"*

Results of Operations

The following tables summarize key financial results for the periods indicated:

	Year Ended December 31,		
	2013	**2012**	**2011**
	(Dollars in thousands, except per share data)		
Net income	$ 19,199	$ 23,872	$ 12,234
Net income per share, basic[1]	$ 1.45	$ 1.80	$ 0.93
Net income per share, diluted[1]	$ 1.42	$ 1.78	$ 0.93
Return on average assets	1.18%	1.67%	0.99%
Return on average shareholders' equity	9.75%	13.39%	8.22%

(1) Adjusted to reflect 1-for-5 reverse stock split effective June, 2011.

Year Ended December 31, 2013 Compared to Year Ended December 31, 2012

	Year Ended December 31,		
	2013	**2012**	**Increase (Decrease)**
	(Dollars in thousands, except per share data)		
Statement of Operations Data:			
Interest income	$ 69,726	$ 61,542	$ 8,184
Interest expense	7,729	7,783	(54)
Net interest income	61,997	53,759	8,238
Provision for credit losses	3,250	19,800	(16,550)
Net interest income after provision for loan and lease losses	58,747	33,959	24,788
Noninterest income	2,003	3,508	(1,505)
Noninterest expense	29,261	34,178	(4,917)
Income before income taxes	31,489	3,289	28,200
Income tax expense (benefit)	12,290	(20,583)	32,873
Net income	$ 19,199	$ 23,872	$ (4,673)
Income allocated to participating securities	(201)	(323)	122
Net income available to common shareholders	$ 18,998	$ 23,549	$ (4,551)
Net income per share, basic	$ 1.45	$ 1.80	$ (0.35)
Net income per share, diluted	$ 1.42	$ 1.78	$ (0.36)

The Bank's net income decreased to $19.2 million, or $1.42 per diluted share, for the year ended December 31, 2013, from a net income of $23.9 million, or $1.78 per diluted share, for the year ended December 31, 2012. Our return on average assets was 1.18% and return on average shareholders' equity was 9.75% for the year ended December 31, 2013, compared to 1.67% and 13.39%, respectively, for the year ended December 31, 2012.

Net income decreased from 2012 to 2013, principally as a result of income tax benefit resulting from the full reversal of the valuation allowance on the deferred tax asset during 2012, compared to net income tax expense of $12.3 million recognized in 2013. This was offset by an $8.2 million increase in net interest income from 2012 to 2013, a $4.9 million decrease in noninterest expense, and a $16.6 million decrease in provision for credit losses between the periods.

The $8.2 million, or 15.3%, increase in net interest income was due primarily to growth of the loan portfolio, as well as lower rates paid on deposits despite overall deposit growth, and lower levels of non-accrual loans. Our overall cost of funds in 2013 decreased by 16 basis points to 0.73%, compared to 0.89% for 2012 while average yields on earning assets decreased by 9 basis points to 4.44% from 4.53%. The impact of the low interest rate environment in 2013 was the primary driver of our decreased cost of funds during 2013 as higher-rate CD's continue to mature and renew at lower rates. Yield on earning assets saw a slight decrease primarily due to lower average yields on investments during the year, as well as a decrease in average interest rate on loans of 21 basis points, from 5.44% for 2012 to 5.23% for 2013.

As of December 31, 2013, 79% of our loan portfolio was tied to the Prime Rate, which has the potential to re-price daily, and 7% was tied to the London Interbank Offered Rate, or LIBOR, or other indices, which re-price periodically. Approximately 79% of our loan portfolio had a floor interest rate at various levels, which provides us with some protection in the current environment with the Prime Rate at a level below the floor interest rate. Approximately 2% of our loan portfolio had interest rate ceilings at various rates limiting the amount of interest rate increases that can be passed on to the borrower. Our weighted average maturity of certificates of deposit at December 31, 2013 was 11.2 months.

Year Ended December 31, 2012 Compared to Year Ended December 31, 2011

	Year Ended December 31,		
	2012	2011	Increase (Decrease)
	(Dollars in thousands, except per share data)		
Statement of Operations Data:			
Interest income	$ 61,542	$ 53,790	$ 7,752
Interest expense	7,783	10,303	(2,520)
Net interest income	53,759	43,487	10,272
Provision for credit losses	19,800	5,700	14,100
Net interest income after provision for loan and lease losses	33,959	37,787	(3,828)
Noninterest income	3,508	2,790	718
Noninterest expense	34,178	33,392	786
Income before income taxes	3,289	7,185	(3,896)
Income tax benefit	(20,583)	(5,049)	(15,534)
Net income	$ 23,872	$ 12,234	$ 11,638
Accretion of beneficial conversion feature	(323)	—	(323)
Net income available to common shareholders	$ 23,549	$ 12,234	$ 11,315
Net income per share, basic	$ 1.80	$ 0.93	$ 0.87
Net income per share, diluted	$ 1.78	$ 0.93	$ 0.85

The Bank's net income increased to $23.9 million, or $1.78 per diluted share, for the year ended December 31, 2012, from a net income of $12.2 million, or $0.93 per diluted share, for the year ended December 31, 2011. Our return on average assets was 1.67% and return on average shareholders' equity was 13.39% for the year ended December 31, 2012, compared to 0.99% and 8.22%, respectively, for the year ended December 31, 2011.

Net income increased from 2011 to 2012, principally as a result of income tax benefit resulting from the full reversal of the valuation allowance on the deferred tax asset during 2012. While net interest income increased by $10.3 million, this was offset by an increase in provision for credit losses during 2012 resulting in a decrease in net income before income taxes of $3.9 million.

The $10.3 million, or 23.6%, increase in net interest income was due primarily to lower rates paid on deposits and lower levels of non-accrual loans. Our overall cost of funds in 2012 decreased by 32 basis points to 0.89%, compared to 1.21% for 2011 while average yields on earning assets decreased by 2 basis points to 4.53% from 4.55%. The impact of the low interest rate environment in 2012 was the primary driver of our decreased cost of funds during 2012 as higher-rate CD's continue to mature and renew at lower rates. Yield on earning assets remained relatively constant, with the slight decrease primarily due to lower average yields on investments during the year, offset by a higher average interest rate on loans.

As of December 31, 2012, 79% of our loan portfolio was tied to the Prime Rate, which has the potential to re-price daily, and 8% was tied to the London Interbank Offered Rate, or LIBOR, or other indices, which re-price periodically. Approximately 76% of our loan portfolio had a floor interest rate at various levels, which provides us with some protection in the current environment with the Prime Rate at a level below the floor interest rate. Approximately 3% of our loan portfolio had interest rate ceilings at various rates limiting the amount of interest rate increases that can be passed on to the borrower. Our weighted average maturity of certificates of deposit at December 31, 2012 was 8.7 months.

Net Interest Income and Net Interest Margin

Year ended December 31, 2013 compared to 2012

Net interest income before the provision for credit losses for the year ended December 31, 2013 increased $8.2 million, or 15.3%, to $62.0 million from $53.8 million for the year ended December 31, 2012. This increase was due to a decrease in interest expense of $54,000 and increase in interest income of $8.2 million. Total increase in interest income is primarily due to the higher average loan balance of $1.22 billion in 2013, an increase from $1.02 billion average balance in 2012, offset by a decreased average loan interest rate from 5.44% to 5.23% between the periods. This increase is also partially offset by decreased investment securities interest income due to lower yields during 2013.

The average yield on our interest-earning assets decreased by 9 basis points to 4.44% in the year ended December 31, 2013 from 4.53% in the year ended December 31, 2012. The decrease was mainly due to a lower average yield on loans during the year offset by increased volume of loans, as well as a decreased yield on investments.

The cost of average interest-bearing liabilities decreased to 0.73% in the year ended December 31, 2013 from 0.89% in the year ended December 31, 2012. The decrease was primarily driven by generally lower rates paid on deposits during 2013 versus 2012.

Year ended December 31, 2012 compared to 2011

Net interest income before the provision for credit losses for the year ended December 31, 2012 increased $10.3 million, or 23.6%, to $53.8 million from $43.5 million for the year ended December 31, 2011. This increase was due to a decrease in interest expense of $2.5 million and increase in interest income of $7.8 million. Total increase in interest income is primarily due to the higher average loan balance of $1.02 billion in 2012, an increase from $902 million average balance in 2011, as well as an increased average loan interest rate from 5.15% to 5.44% between the periods This increase is partially offset by decreased investment securities interest income due to lower yields and lower average investment securities balance during 2012.

The average yield on our interest-earning assets decreased slightly to 4.53% in the year ended December 31, 2012 from 4.55% in the year ended December 31, 2011. The decrease was mainly due to a lower yield on investment securities during the year, as well as an increased average balance of other earning assets, which is primarily cash earning a very low interest rate. These decreases are partially offset by an increase in average yield on loans, from 5.15% for the year ended December 31, 2011 to 5.44% for the year ended December 31, 2012.

The cost of average interest-bearing liabilities decreased to 0.89% in the year ended December 31, 2012 from 1.21% in the year ended December 31, 2011. The decrease was primarily driven by generally lower rates paid on deposits during 2012 versus 2011.

	Year Ended December 31, 2013			Year Ended December 31, 2012			Year Ended December 31, 2011		
	Average Balance	Interest Income or Expense	Average Yield or Cost	Average Balance	Interest Income or Expense	Average Yield or Cost	Average Balance	Interest Income or Expense	Average Yield or Cost
				(Dollars in thousands)					
ASSETS									
Interest-earning assets:									
Loans and leases [(2)] [(3)]	$ 1,217,383	$ 63,718	5.23%	$ 1,018,366	$ 55,400	5.44%	$ 902,346	$ 46,464	5.15%
Investment securities [(1)]	186,084	6,003	3.23%	155,199	6,141	3.96%	173,733	7,585	4.37%
Federal funds sold	13,241	55	0.41%	4,344	26	0.60%	—	—	0.00%
Other earning assets	161,862	383	0.24%	189,586	435	0.23%	116,863	257	0.22%
Total interest-earning assets	$ 1,578,570	$ 70,159	4.44%	$ 1,367,495	$ 62,002	4.53%	$1,192,942	$ 54,306	4.55%
Noninterest-earning assets:									
Cash and due from banks	5,490			4,556			4,374		
Other assets	49,650			54,002			39,718		
Total assets	$ 1,633,710			$ 1,426,053			$1,237,034		
LIABILITIES AND SHAREHOLDERS' EQUITY									
Interest-bearing liabilities:									
Deposits									
Interest-bearing demand	$ 102,169	$ 545	0.53%	$ 54,534	$ 290	0.49%	$ 42,933	$ 254	0.59%
Money market	280,108	1,654	0.59%	216,916	1,456	0.80%	133,056	1,041	0.78%
Savings	22,783	89	0.39%	21,007	75	0.38%	23,307	92	0.39%
Time certificates of deposit	650,155	5,373	0.83%	581,265	5,868	1.01%	625,657	8,163	1.30%
Total interest-bearing deposits	1,055,215	7,661	0.73%	873,722	7,689	0.88%	824,953	9,550	1.16%
Short-term borrowings	1	—	0.51%	—	—	0.00%	—	—	0.00%
Long-term debt (FHLB and Senior debt)	10,630	68	0.64%	3,125	94	3.00%	25,996	753	2.90%
Total interest-bearing liabilities	1,065,846	7,729	0.73%	876,847	7,783	0.89%	850,949	10,303	1.21%
Noninterest-bearing liabilities:									
Demand deposits	359,205			362,118			230,088		
Other liabilities	11,678			8,831			7,180		
Total liabilities	1,436,729			1,247,796			1,088,217		
Shareholders' equity	196,981			178,257			148,817		
Total liabilities and shareholders' equity	$1,633,710			$1,426,053			$1,237,034		
Net interest income		$ 62,431			$ 54,219			$ 44,003	
Net interest spread			3.72%			3.65%			3.34%
Net interest margin			3.95%			3.96%			3.69%

(1)Yields on securities have been adjusted to a tax-equivalent basis.
(2)Includes average non-accrual loans and leases.
(3)Net loan and lease fees income of $2.0 million, $1.1 million and 367,000 for the year ended December 31, 2013, 2012 and 2011, respectively, are included in the yield computations.

The increase in interest income from loans and decrease in interest expense on time certificate deposits, largely offset each other to drive the slight decrease of net interest margin to 3.95% for 2013 compared to 3.96% for 2012. In addition to the distribution, yields and costs of our assets and liabilities, our net income is also affected by changes in the volume of and rates on our assets and liabilities. The following table shows the change in interest income and interest expense and the amount of change attributable to variances in volume, rates and the combination of volume and rates based on the relative changes of volume and rates.

	Year Ended December 31,					
	2013 vs. 2012			2012 vs. 2011		
	Net Change	Rate	Volume	Net Change	Rate	Volume
	(In thousands)					
Interest income:						
Loans and leases	$ 8,318	$ (2,165)	$ 10,483	$ 8,936	$ 2,728	$ 6,208
Investment securities[1]	(138)	(1,242)	1,104	(1,444)	(675)	(769)
Federal funds sold	29	(10)	39	26	—	26
Other earning assets	(52)	13	(65)	178	12	166
Total interest income	8,157	(3,404)	11,561	7,696	2,065	5,631
Interest expense:						
Interest-bearing demand	255	1	254	36	(28)	64
Money market	198	(190)	388	415	(165)	580
Savings	14	7	7	(17)	(8)	(9)
Time certificates of Deposit	(495)	(1,130)	635	(2,296)	(1,789)	(507)
Short-term borrowings	—	—	—	—	—	—
Long-term debt	(26)	(118)	92	(658)	27	(685)
Total interest expense	(54)	(1,430)	1,376	(2,520)	(1,963)	(557)
Net interest income	$ 8,211	$ (1,974)	$ 10,185	$ 10,216	$ 4,028	$ 6,188

(1) Amounts have been adjusted to a tax-equivalent basis.

Provision for Credit Losses

In response to the credit risk inherent in our lending business and the recent ongoing sluggish economy, we set aside allowances for loan losses through charges to earnings. Such charges were not made only for our outstanding loan portfolio, but also for off-balance sheet items, such as commitments to extend credits or letters of credit. The charges made for our outstanding loan portfolio were credited to allowance for loan losses, whereas charges for off-balance sheet items were credited to the reserve for off-balance sheet items, which is presented as a component of other liabilities.

The provision for credit losses for 2013 decreased $16.5 million to $3.3 million from $19.8 million for 2012. The Bank’s net loans and lease charge-offs decreased to $4.4 million during 2013 from $22.9 million in 2012. The decrease in the provision for credit losses during 2013 is due to a relatively large provision in 2012 attributed to two significant loan relationships which were written down in the second quarter of 2012. Since 2009, the Bank has made significant refinements in the assumptions for calculating its adequacy of allowance for loan losses as prescribed under Contingencies Topic of FASB ASC as well as prescribed by regulatory guidelines. In calculating the need for allowance levels based on historical losses, the Bank uses a 2-year historical loss measurement period. Also, the Bank utilizes qualitative factors used in calculating allowance levels, such as the mix of the loan portfolio, concentration levels and trends, local and national economic conditions, changes in capabilities and experience of lending management and staff and other external factors including industry conditions, competition and regulatory requirements. Non-performing loans decreased from $26.1 million as of December 31, 2012 to $14.0 million as of December 31, 2013, as this area continues to be the primary focus of management. The ratio of allowance for loan losses to total loans decreased from 1.84% of total loans at December 31, 2012 to 1.47% at December 31, 2013, directionally consistent with non-performing loan trends over the same period. Management believes that through the application of the allowance methodology’s quantitative and qualitative components, that the provision and overall level of allowance is adequate for losses estimated to be inherent in the portfolio as of December 31, 2013.

The provision for credit losses for 2012 increased $14.1 million to $19.8 million from $5.7 million for 2011. The Bank’s net loans and lease charge-offs increased to $22.9 million during 2012 from $14.8 million in 2011. The increase in the provision for credit losses during 2012 is due to two significant loan relationships which were written down in the second quarter of 2012. Non-performing loans decreased from $47.5 million as of December 31, 2011 to $26.1 million as of December 31, 2012, as this area continues to be the primary focus of management. The ratio of allowance for loan losses to total loans decreased from 2.50% of total loans at December 31, 2011 to 1.84% at December 31, 2012, directionally consistent with non-performing loan trends over the same period.

Noninterest Income

We earn noninterest income primarily through fees related to:

- Services provided to deposit customers
- Services provided in connection with trade finance
- Services provided to current loan customers
- Rental income from OREO property
- Increases in the cash surrender value of bank owned life insurance policies ("BOLI")
- Sale of investment securities

The following table presents, for the periods indicated, the major categories of noninterest income:

	Year Ended December 31,		
	2013	2012	2011
		(In thousands)	
Service charges and fees on deposit accounts	$ 2,101	$ 1,792	$ 1,742
Trade finance income	612	309	241
Increase in cash surrender value of life insurance	331	329	333
Net gain (loss) on sale of investment securities	(1,957)	575	81
Other income	916	503	393
Total noninterest income	$ 2,003	$ 3,508	$ 2,790

Total noninterest income decreased by $1.5 million or 43%, to $2.0 million during 2013 from $3.5 million during 2012. The overall decrease in noninterest income was due mainly to a net loss of $2.0 million on sale of investment securities in 2013, compared to a net gain of $575,000 on sale of investment securities in 2012. Service charges and fees on deposit accounts increased by $309,000 year over year, primarily due to increased Account Analysis Fees. The $413,000 increase in other income between 2012 and 2013 was mostly attributable to loan-related income.

Total noninterest income increased by $718,000 or 26%, to $3.5 million during 2012 from $2.8 million during 2011. The overall increase in noninterest income was due mainly to an increase in net gain on sale of investment securities in 2012 and net gain on loan sales of $290,000 compared to 2011.

Our results can be influenced by the unpredictable nature of gains and losses in connection with the sale of investment securities and other real estate owned. We do not engage in active securities trading; however, from time to time we sell securities in our available-for-sale portfolio to change the duration of the portfolio or to re-position the portfolio for various reasons. We plan to continue this practice judgmentally for the foreseeable future. From time to time, we acquire real estate in connection with non-performing loans, and sell such real estate to recoup the principal amount of the defaulted loans. These sales can result in gains or losses from time to time that are not expected to occur in predictable patterns during future periods.

Noninterest Expense

Noninterest expense is the cost, other than interest expense and the provision for credit losses, associated with providing banking and financial services to customers and conducting our business.

The following table presents, for the periods indicated, the major categories of noninterest expense:

	Year Ended December 31,		
	2013	2012	2011
		(In thousands)	
Salaries and employee benefits	$ 16,226	$ 12,523	$ 11,155
Net occupancy expense	3,206	2,990	3,060
Business development and promotion expense	366	294	335
Professional services	3,597	3,227	2,267
Office supplies and equipment expense	1,186	1,154	1,061
Total other-than-temporary impairment losses	7	24	32
Portion of loss recognized in other comprehensive income	—	—	—
Loss (gain) on sale of OREO and related expense	(449)	8,580	8,303
Other expense	5,122	5,386	7,179
Total noninterest expense	29,261	34,178	$ 33,392

Total noninterest expense decreased by $4.9 million, or 14%, to $29.3 million during 2013 from $34.2 million during 2012. Salaries and benefits increased $3.7 million over 2012 levels due to the addition of business development and Bank Secrecy Act compliance staff, additional loan production staff as well as staff for the new branch in San Francisco, California, which opened in February 2013, and increased levels of bonus accruals in line with the bank's performance. Net occupancy expense increased $216,000 between the periods primarily as a result of the new branch in San Francisco. Professional fees increased by $370,000 to $3.6 million during 2013 from $3.2 million in 2012 due primarily to an increase in legal costs associated with non-performing loans. Net other-than-temporary impairment ("OTTI") credit-related charges were $7,000 in 2013 compared to $24,000 in 2012. OREO related expenses totaled a net gain of $1.2 million in 2013, increasing $9.8 million from $8.6 million in 2012. This net gain consisted of $3.8 million net gain on sale of OREO properties, offset by $1.7 million in OREO valuation charges as well as $1.1 million in other OREO related costs. Other expenses were $5.9 million in 2013, an increase of $511,000 from the $5.4 million in 2012 due mainly to valuation write-downs on loans held for sale of $775,000 during 2013 compared to $387,000 during 2012, and $376,000 in amortization of investment in low income housing in 2013, compared to zero in 2012.

Total noninterest expense increased by $786,000, or 2.4% to $34.2 million during 2012 from $33.4 million during 2011. Salaries and benefits increased $1.4 million over 2011 levels due to the addition of business development staff and reinstatement of bonus accruals which had been suspended in 2008. Professional fees increased by $960,000 to $3.2 million during 2012 from $2.3 million in 2011 due primarily to an increase in legal costs associated with non-performing loans and OREO as significant efforts to reduce these balances continued through 2012, as well as an increase in audit fees compared to 2011, resulting from the 2011 utilization of excess audit fee accruals recorded due to an overestimation of the expense in 2010. Net other-than-temporary impairment ("OTTI") credit-related charges were $24,000 in 2012 compared to $32,000 in 2011. OREO related expenses totaled $8.6 million in 2012, increasing $277,000 from $8.3 million in 2011. OREO expenses in 2012 consisted of $4.0 million in OREO valuation charges, loss on sale of OREO of $387,000, and other net OREO related charges of $4.2 million. Other expenses were $5.4 million in 2012, a decrease of $1.8 million from the $7.2 million in 2011 due mainly to a gain on loan sale of $290,000 for 2012 compared to a loss on loan sale of $656,000 in 2011, and a decrease in FDIC insurance premiums.

Provision for Income Taxes

We accounted for income taxes under the asset and liability method, which requires the recognition of deferred tax assets and liabilities for the expected future tax consequences of events that have been included in the financial statements. Under this method, deferred tax assets and liabilities are determined based on the differences between the financial statements and tax basis of assets and liabilities using enacted tax rates in effect for the year in which the differences are expected to reverse. The effect of a change in tax rates on deferred tax rates on deferred tax assets and liabilities is recognized in income in the period that includes the enacted date.

We record net tax assets to the extent we believe these assets will more likely than not be realized. In making such determination, we consider all available positive and negative evidence, including scheduled reversals of deferred tax liabilities, projected future taxable income, tax planning strategies and recent financial operations. During 2012, we reversed the valuation allowance of $25.7 million and the allowance balance is zero as of December 31, 2012 and December 31, 2013. This recognition was the result of an evaluation of our historical net operating losses and our more recent history of consecutive quarters of profitability. We assessed the likelihood that our deferred tax asset would be recovered from taxable income and determined that recovery was more likely than not based upon the totality of the evidence, both positive and negative.

We recorded a provision of $12.3 million for income taxes related to the pre-tax income for the year ended December 31, 2013 at an effective tax rate of 39.0%. In 2012, we recorded a benefit provision of $20.6 million as the result of eliminating the valuation allowance against the bank's deferred tax assets. Accounting Standards Codification Topic 740, "*Income Taxes*," provides for the recognition of deferred tax assets, such as the future benefit of net operating loss deductions against future taxable income, if realization of such tax-related assets is more likely than not. Based upon the weight of available evidence, which includes our historical operating performance, we reversed the full valuation allowance against our net deferred tax assets in 2012.

As of December 31, 2013 we had federal and state net operating loss (NOL) carryforwards of $0.3 million and $13.9 million, respectively.

Pursuant to Sections 382 and 383 of the Internal Revenue Code, annual use of net operating loss and credit carryforwards may be limited in the event a cumulative change in ownership of more than 50 percent points occurs within a three-year period. We determined that such an ownership change occurred as of June 21, 2010 as a result of stock issuances in 2010 and 2009. This ownership change resulted in estimated limitations on the utilization of tax attributes, including net operating loss carryforwards and tax credits. Although we fully expect to utilize all of the federal net operating loss carryforward prior to their expiration, the California net operating loss carryover has been significantly impacted by the IRC Sec. 382 limitation. We estimate that of approximately $83.5 million of the California net operating losses as of December 31, 2013 subject to $69.6 million are expected to expire in 2029 as they will be unutilized as a result of IRS Sec 382 limitation. This amounts to approximately $4.9 million of deferred tax assets which would not be realized. The remaining California net operating loss carryforward of the approximately $13.9 million at December 31, 2013, is subject to IRC Sec. 382 annual limitation amount of approximately $1.5 million.

Financial Condition

For the period between December 31, 2013 and December 31, 2012, our assets, loans and deposits grew at the rate of 13.8%, 18.6% and 12.7%, respectively. Our total assets at December 31, 2013 were $1.77 billion compared to $1.55 billion at December 31, 2012. Our earning assets at December 31, 2013 totaled $1.72 billion compared to $1.50 billion at December 31, 2012. Total deposits at December 31, 2013 and December 31, 2012 were $1.53 billion and $1.36 billion, respectively.

Loans and Leases

The largest component of our assets and largest source of interest income is our loan portfolio. The following table sets forth the amount of our loans and leases outstanding at the end of each of the periods indicated, and the percentages of the overall loan pool represented. We had no foreign loans or energy-related loans as of the dates indicated.

	Year Ended December 31,														
	2013			2012			2011			2010			2009		
							(in thousands)								
Loans and leases (by portfolio and class):															
Real Estate - Mini-perm:															
Real Estate - Residential	$ 242,101	18.3	%	$ 177,948	15.7	%	$ 143,344	15.0	%	$ 162,000	17.8	%	$ 201,285	19.3	%
Real Estate - Commercial	629,438	47.6		494,699	44.8		431,828	45.3		369,640	40.4		363,988	34.9	
Total Real Estate - Mini-perm	$ 871,539			$ 672,647			$ 575,172			$ 531,640			$ 565,273		
Real Estate - Construction:															
R/E Construction - Residential	24,997	1.9		36,347	3.2		39,537	4.6		87,611	9.8		143,905	13.8	
R/E Construction - Commercial	48,288	3.7		38,063	3.4		32,405	3.4		33,214	3.6		58,282	5.6	
Total Real Estate - Construction	$ 73,285			$ 74,410			$ 71,942			$ 120,825			$ 202,187		
Commercial & Industrial	338,680	25.6		324,753	28.7		252,161	26.4		209,520	22.9		227,421	21.8	
Trade Finance	39,640	3.0		47,413	4.2		49,750	5.2		50,520	5.5		47,998	4.6	
Other Loans	287	0.0		330	0.0		606	0.1		349	0.0		420	0.0	
Total gross loans and leases	$ 1,323,431	100.0	%	$ 1,119,553	100.0	%	$ 949,631	100.0	%	$ 912,854	100.0	%	$ 1,043,299	100.0	%
Less: allowance for loan and lease losses	(19,494)			(20,607)			(23,718)			(32,898)			(42,810)		
Deferred loan and lease fees, net	(2,562)			(2,019)			(1,037)			58			585		
Total loan excluding loans held for sale	$ 1,301,375			$ 1,096,927			$ 924,876			$ 880,014			$ 1,001,074		
Loans held for sale	6,207			12,150			3,996			2,556			—		
Total net loans and leases	$ 1,307,582			$ 1,109,077			$ 928,872			$ 882,570			$ 1,001,074		

Total gross loans at December 31, 2013, net of loans held for sale, were $1.32 billion, up from the $1.12 billion as of December 31, 2012. Real estate mini-perm loans which are real estate loans collateralized by various types of commercial and residential real estate, were up from $672.6 million as of December 31, 2012 to $871.5 million at December 31, 2013. Real estate construction loans, which are loans made to developers for the purpose of constructing residential or commercial properties, decreased slightly by $1.1 million from December 31, 2012. Commercial & industrial loans increased $13.9 million and trade finance loans, which are primarily working capital revolving and term loans for business operations, decreased by $7.8 million from December 31, 2012 to December 31, 2013. Management's focus from a lending perspective is on prime-owner-occupied, income-producing commercial real estate and multi-family real estate as well as commercial & industrial loans as seen in the results of the loan portfolio changes from December 31, 2012. Management continually evaluates the mix of loan types in the loan portfolio in order to minimize risk and maximize returns within the portfolio.

There were six loans with a recorded investment of $26.2 million sold during 2013 for a net gain of $514,000. During 2012, five loans with a recorded investment of $9.3 million were sold for a net gain of $290,000. Five loans with a recorded investment of $21.7 million were transferred to held for sale status in 2013 and were subsequently sold, and one loan transferred to held for sale status during 2012 remained in the balance as of December 31, 2013.

Our real estate mini-perm loan portfolio increased in 2013 by $198.9 million or 29.6% to $871.5 million from $672.6 million at December 31, 2012. The overall increase was due to management's focus from a lending perspective on prime owner-occupied, income-producing commercial real estate as well as commercial & industrial loans as seen in the results of the loan portfolio changes from December 31, 2012. Residential real estate loans increased by $64.2 million, or 36.1%, and commercial real estate loans grew by $134.7 million or 27.2%. Retail-purpose continued to grow during 2013, with an increase of $46.7 million, or 28.7%, land loans decreased $12.9 million, or 37.7%, and special purpose loans increased $19.0 million, or 11.0%. Further detail regarding the real estate mini perm portfolio by property type is provided in the table below. Following is a summary of the trends in our real estate mini-perm loan portfolio over the prior four years: During 2012, mini-perm loans increased by $109.6 million or 19.1% to $684.8 million from $575.2 million at December 31, 2011; during 2011, mini-perm loans increased by $43.5 million or

8.2% to $575.2 million from $531.6 million at December 31, 2010; during 2010, it decreased by $33.6 million, or 5.9%, to $531.6 million from $565.3 million at December 31, 2009.

The following table provides information about our real estate mini-perm portfolio by property type:

		At December 31, 2013			At December 31, 2012	
Property Type		**Amount**	**Percentage of Loans in Each Category in Total Loan Portfolio**		**Amount**	**Percentage of Loans in Each Category in Total Loan Portfolio**
		(Dollars in thousands)			(Dollars in thousands)	
Commercial/Office	$	146,239	11.00%	$	101,113	8.93%
Retail		209,714	15.76		162,983	14.40
Industrial		80,265	6.03		61,325	5.42
Residential 1-4		99,290	7.46		33,961	3.00
Apartment 4+		129,200	9.71		118,427	10.46
Land		21,368	1.60		34,308	3.03
Special purpose		191,670	14.41		172,680	15.26
Total	$	877,746	65.97%	$	684,797	60.50%

During 2013, real estate construction loans decreased by $1.1 million or 1.5% to $73.3 million at December 31, 2013 from $74.4 million at December 31, 2012; and increased by $2.5 million or 3.5% to $74.4 million at December 31, 2012 from $71.9 million at December 31, 2011; and declined by $48.9 million or 40.5% to $71.9 million at December 31, 2011 from $120.8 million at December 31, 2010; and declined in 2010 by $81.4 million or 40.2%, to $120.8 million from $202.2 million at December 31, 2009. Real estate construction-residential was one of the hardest hit of our loan segments in the harsh economic climate due to the combination of deterioration in residential real estate values and lack of available financing.

Commercial & industrial loans outstanding at December 31, 2013 increased by $13.9 million, or 4.3%, to $338.7 million from $324.8 million as of December 31, 2012; increased by $72.6 million, or 28.8%, to $324.8 million from $252.2 million as of December 31, 2011; increased by $42.6 million, or 20.4%, to $252.1 million from $209.5 million at December 31, 2010; and decreased by $17.9 million, or 7.9% to $209.5 million from $227.4 million at December 31, 2009. Total commercial loan commitments (including undisbursed amounts) at December 31, 2013 increased $64.4 million or 14.2% to $516.8 million from $452.4 million at December 31, 2012 while the rate of credit utilization decreased to 65.5% as of December 31, 2013 from 71.8% at December 31, 2012. We believe that this increase in utilization is primarily incidental and secondarily due to the increased need for funding by our business customers.

Trade finance loans decreased in 2013 by $7.8 million or 16.4% during 2013, from $47.4 million to $39.6 million as of December 31, 2013; and decreased by $2.4 million or 4.8% during 2012, from $49.8 million to $47.4 million as of December 31, 2012; and decreased by $770,000 during 2011 to $49.8 million from $50.5 million at December 31, 2010; and grew $2.5 million or 5.3% during 2010 to $50.5 million from $48.0 million at December 31, 2009.

Other loans, which include installment/consumer debt, leases receivable and other unallocated loans, are relatively insignificant.

Non-Performing Assets

Non-performing assets are comprised of loans on non-accrual status and OREO, and certain Troubled Debt Restructurings (“TDRs”). TDRs that are on non-accrual status are included in non-performing assets while TDRs that are performing according to their revised terms are not included in non-performing asset and evaluated for impairment in accordance with ASC 310-10-35. Generally, loans and leases are placed on non-accrual status when they become 90 days or more past due or at such earlier time as management determines timely recognition of interest to be in doubt, unless they are both fully secured and in process of collection. Accrual of interest is discontinued on a loan or lease when management believes, after considering economic and business conditions and collection efforts that the borrower’s financial condition is such that collection of principal and contractually due interest is not likely. OREO consists of real property acquired through foreclosure or similar means that the Bank intends to offer for sale.

A TDR is a debt restructuring in which a bank, for economic or legal reasons specifically related to a borrower’s financial condition, grants a concession to the borrower that it would not otherwise consider. At December 31, 2013, loans classified as TDRs totaled $8.1 million, of which $7.7 million was on non-accrual status and $403,000 was performing as agreed. At December 31, 2012, loans classified as TDRs totaled $7.9 million, of which $7.2 million were on non-accrual status and $727,000 were on accrual status.

The following table summarizes the loans and leases for which the accrual of interest has been discontinued and loans and leases more than 90 days past due and still accruing interest and OREO:

	Year Ended December 31,				
	2013	2012	2011	2010	2009
	(Dollars in thousands)				
Non-accrual loans and leases*	$ 14,044	$ 26,145	$ 47,453	$ 101,860	$ 137,301
Accruing loans and leases past due 90 days or more	—	—	—	7	7,571
Total non-performing loans (NPLs)	14,044	26,145	47,453	101,867	144,872
OREO	5,602	28,280	37,577	52,663	59,190
Total non-performing assets (NPAs)	$ 19,646	$ 54,425	$ 85,030	$ 154,530	$ 204,062
Selected ratios:					
NPLs to total gross loans and leases held for investment	1.06%	2.31%	4.98%	11.15%	13.88%
NPAs to total assets	1.11%	3.50%	6.49%	12.30%	15.61%

*Non-accrual Troubled Debt Restructurings (TDRs) that are included in non-accrual loans are as follows: 2013 - $7,665; 2012 - $7,150; 2011 - $11,482; 2010 - $34,681; 2009 - $34,875. TDRs that are performing according to their revised terms are not reflected as non-performing loans (NPLs).

The amount of interest income that we would have been recorded on impaired loans that were non-accrual loans and leases had the loans and leases been current totaled $1,132,000, $1,769,000, and $3,369,000, for 2013, 2012, and 2011, respectively. When an asset is placed on non-accrual status, previously accrued but unpaid interest is reversed against current income. Subsequent collections of cash are applied as principal reductions when received, except when the ultimate collectability of principal is probable, in which case interest payments are credited to income. See Note 3 of the Consolidated Financial Statements for further details regarding non-accrual and past due loans by loan class.

As of December 31, 2013, we had 3 OREO properties for $5.6 million as compared 16 OREO properties for $28.3 million as of December 31, 2012. During 2013, the Bank sold 13 OREO properties at a net gain of $3.8 million. The following table summarizes the Bank’s OREO as of the periods presented.

Foreclosed assets (OREO) as of December 31, 2013 and 2012 were as follows:

Loan Class	2013		2012	
	#	$	#	$
(Dollars in thousands)				
Real Estate-Mini-Perm:				
Residential	2	$ 3,351	11	$ 15,127
Commercial	1	2,251	3	7,829
Real Estate-Construction:				
Residential	—	—	1	3,051
Commercial	—	—	1	2,273
Real Estate-Housing	—	—	—	—
Commercial & Industrial	—	—	—	—
Total as of December 31	3	$ 5,602	16	$ 28,280

Management continued to work to reduce OREO balances and has made good progress throughout 2013. As market conditions dictate, the Bank will continue to dispose of these properties with an eye toward capital preservation. Although management anticipates the disposition of these properties, it is likely that non-performing real estate loans will be foreclosed upon, thus partially offsetting the OREO disposition efforts We have placed a particular emphasis on the effort of disposing of OREO properties as soon as is practicable, but with the intention to minimize losses on sales.

OREO is initially stated at fair value of the property based on appraisal, less estimated selling cost. Any cost in excess of the fair value at the time of acquisition is accounted for as a loan charge-off and deducted from the allowance for loan and lease losses. A valuation allowance is established for any subsequent declines in value through a charge to earnings. Operating expenses of such properties, net of related income, and gains and losses on their disposition are included in other operating income or expense, as appropriate.

Impaired Loans and Leases

Impaired loans and leases are considered impaired when it is probable that we will not be able to collect all amounts due according to the contractual terms of the loan or lease agreement. The category of impaired loans and leases is not comparable with the category of non-accrual loans and leases. Management may choose to place a loan or lease on non-accrual status due to payment delinquency or uncertain collectability, while not classifying the loan or lease as impaired if it is probable that we will collect all amounts due in accordance with the original contractual terms of the loan or lease or the loan.

In determining whether or not a loan or lease is impaired, we apply our normal loan and lease review procedures on a case-by-case basis taking into consideration the circumstances surrounding the loan or lease and borrower, including the collateral value, the reasons for the delay, the borrower's prior payment record, the amount of the shortfall in relation to the principal and interest owed and the length of the delay. We measure impairment on a loan-by-loan basis using either the present value of expected future cash flows discounted at the loan's or lease's effective interest rate or at the fair value of the collateral if the loan or lease is collateral dependent, less estimated selling costs. Loans or leases for which an insignificant shortfall in amount of payments is anticipated, but where we expect to collect all amounts due, are not considered impaired.

TDR loans are defined by ASC 310-40, *"Troubled Debt Restructurings by Creditors"* and ASC 470-60, *"Troubled Debt Restructurings by Debtors,"* and evaluated for impairment in accordance with ASC 310-10-35. The concessions may be granted in various forms, including reduction in the stated interest rate, reduction in the amount of principal amortization, forgiveness of a portion of a loan balance or accrued interest, or extension of the maturity date.

We had $14.4 million, $25.0 million and $73.4 million of impaired loans or leases at December 31, 2013, 2012, and 2011, respectively. The total allowance for loan and lease losses related to these loans and leases was zero, $2.3 million and $4.9 million at December 31, 2013, 2012 and 2011, respectively. Interest income recognized on such loans and leases during 2013, 2012 and 2011 was $105,000, $615,000, and $1.2 million, respectively. The average recorded investment on impaired loans and leases including loans held for sale during 2013, 2012 and 2011 was $22.6 million, $36.2 million and $101.6 million, respectively.

Allowance for Loan and Lease Losses

The allowance for loan and lease losses is maintained at a level which, in management's judgment, is adequate to absorb loan and lease losses inherent in the loan and lease portfolio. The amount of the allowance is based on management's evaluation of the collectability of the loan and lease portfolio and that evaluation is based on historical loss experience and other significant factors.

The methodology we use to estimate the amount of our allowance for loan and lease losses is based on both objective and subjective criteria. While some criteria are formula driven, other criteria are subjective inputs included to capture environmental and general economic risk elements which may trigger losses in the loan portfolio,.

Specifically, our allowance methodology contains four elements: (a) amounts based on specific evaluations of impaired loans; (b) amounts of estimated losses on loans classified as 'special mention' and 'substandard' that are not already included in impaired loan analysis; (c) amounts of estimated losses on loans not adversely classified which we refer to as 'pass' based on historical loss rates by loan type; and (d) amounts for estimated losses on loans rated as pass based on economic and other factors that indicate probable losses were incurred but were not captured through the other elements of our allowance process.

Impaired loans are identified at each reporting date based on certain criteria and individually reviewed for impairment. A loan is considered impaired when it is probable that a creditor will be unable to collect all amounts due according to the original contractual terms of the loan agreement. We measure impairment of a loan based upon the fair value of the loan's collateral if the loan is collateral dependent or the present value of cash flows, discounted at the loan's effective interest rate, if the loan is not collateralized or is not collateral dependent. The impairment amount on a collateralized loan and a non-collateralized loan is set up as a specific reserve or is charged off.

Our loan portfolio, excluding impaired loans which are evaluated individually, is categorized into several pools for purposes of determining allowance amounts by loan pool. The loan pools we currently evaluate are: commercial & industrial, international trade finance, real estate and real estate construction. Real estate is further segmented by individual product type with a general class, residential or commercial. The commercial class is represented by–office, industrial, retail, special purpose and land commercial product types. The residential class is represented by multi family, SFR, land residential. Real estate construction is similarly further segmented by the office, industrial, and retail product types; with multifamily and SFR product types representing the commercial loan class. Within these loan pools, we then evaluate loans rated as pass credits, separately from adversely classified loans. The allowance amounts for pass rated loans, which are not reviewed individually, are determined using historical loss rates developed through migration analyses. The adversely classified loans are further grouped into three credit risk rating categories: substandard, doubtful and loss.

Finally, in order to ensure our allowance methodology is incorporating recent trends and economic conditions, we apply environmental and general economic factors to our allowance methodology including: credit concentrations; delinquency trends; economic and business conditions; the quality of lending management and staff; lending policies and procedures; loss and recovery trends; nature and volume of the portfolio; non-accrual and problem loan trends; and other adjustments for items not covered by other factors.

Although we believe that our allowance for loan losses is adequate and believe that we have considered all risks within the loan portfolio, there can be no assurance that our allowance will be adequate to absorb future losses. Factors such as a prolonged and deepened recession, higher unemployment rates than we have already anticipated, continued deterioration of California real estate values as well as natural disasters, civil unrest and terrorism can have a significantly negative impact on the performance of our loan portfolio and the occurrence of any single one of these factors may lead to additional future losses which can negatively impact our earnings, capital and liquidity.

The table below summarizes loans and leases, average loans and leases, non-performing loans and leases and changes in the allowance for loan and lease losses arising from loan and lease losses and additions to the allowance from provisions charged to operating expense:

Allowance for Loan and Lease Loss History

	Year Ended December 31,				
	2013	2012	2011	2010	2009
			(Dollars in thousands)		
Allowance for loan losses:					
Balance at beginning of period	$ 20,607	$ 23,718	$ 32,898	$ 42,810	$ 26,935
Actual charge-offs:					
Commercial	4,147	10,328	5,126	6,672	7,716
Trade finance	11	197	—	—	3,246
Real estate-construction	2,438	2,184	2,329	12,600	24,293
Real estate -mini-perm	1,668	10,772	8,637	7,806	24,456
Other (credit card)	—	—			—
Total charge-offs	8,264	23,481	16,097	27,095	59,711
Less recoveries:					
Commercial	366	64	823	289	3,924
Trade finance	—	—	117	—	—
Real estate-construction	2,114	147	173	316	397
Real estate -mini-perm	1,421	359	104	28	15
Other	—	—	—	—	—
Total recoveries	3,901	570	1,217	633	4,336
Net loans charged-off	4,363	22,911	14,880	26,462	55,375
Provision for credit losses	3,250	19,800	5,700	16,550	71,250
Balance at end of period	$ 19,494	$ 20,607	$ 23,718	$ 32,898	$ 42,810
Total gross loans and leases at end of period *	1,329,638	1,131,703	953,627	915,410	1,043,299
Average total loans and leases **	1,217,383	1,018,366	902,346	977,188	1,162,221
Non-performing loans and leases	14,044	26,145	47,453	101,867	144,872
Selected ratios:					
Net charge-offs (recoveries) to average loans and leases	0.36%	2.25%	1.65%	2.71%	4.76%
Provision for loan losses to average loans and leases	0.27%	1.94%	0.63%	1.69%	6.13%
Allowance for loan losses to loans and leases at end of period	1.47%	1.84%	2.50%	3.60%	4.10%
Allowance for loan losses to non-performing loans and leases	138.80%	78.82%	49.98%	32.29%	29.55%

* Includes loans held for sale of $6,207 as of December 31, 2013, $12,150 as of December 31, 2012, $3,996 as of December 31, 2011, $2,556 as of December 31, 2010, and zero as of December 30, 2009.
** Includes average loans held for sale balance of $12,495 for the year ended December 31, 2013, $12,381 for the year ended December 31, 2012, $6,993 for the year ended December 31, 2011, $8,431 for the year ended December 31, 2010, and zero for the year ended December 31, 2009.

The allowance for loan losses of $19.5 million at December 31, 2013, represented 1.47% of total loans and 138.80% of non-performing loans. The allowance for loan losses of $20.6 million at December 31, 2012, represented 1.84% of total loans and 78.82% of non-performing loans. The increase in the coverage ratio for the allowance for loan losses to non-performing loans from 78.82% at December 31, 2012 to 138.80% at December 31, 2012 was primarily a result of decline in adversely classified and non-performing loans in 2013. Net charge-offs to average loans were 0.32% for the year ended December 31, 2013 compared to 2.25% for the year ended December 31, 2012. See "Critical Accounting Policies," and Note 4 of the "Notes to Consolidated Financial Statements."

In allocating our allowance for loan and lease losses, management has considered the credit risk in the various loan and lease categories in our portfolio. As such, the allocations of the allowance for loan and lease losses are based upon our historical net loan and lease loss experience and the other factors discussed above. While every effort has been made to allocate the allowance to specific categories of loans, management believes that any allocation of the allowance for loan and lease losses into loan categories lends an appearance of precision that does not exist.

The following table reflects management's allocation of the allowance and the percent of loans in each portfolio to total loans and leases as of each of the following dates:

	At December 31,									
	2013		2012		2011		2010		2009	
	Allocation of the Allowance	Percent of Loans in Each Category in Total Loans	Allocation of the Allowance	Percent of Loans in Each Category in Total Loans	Allocation of the Allowance	Percent of Loans in Each Category in Total Loans	Allocation of the Allowance	Percent of Loans in Each Category in Total Loans	Allocation of the Allowance	Percent of Loans in Each Category in Total Loans
	(Dollars in thousands)									
Real estate-Mini-perm	$ 9,234	66.0%	$ 10,973	60.1%	$ 14,831	60.6%	$ 16,400	58.3%	$ 17,376	54.2%
Real estate-construction	1,355	5.5	1,655	6.7	2,353	7.6	6,501	13.2	14,885	19.4
Commercial	4,264	25.5	5,069	29.0	3,156	26.6	8,215	23.0	8,314	21.8
Trade finance	393	3.0	427	4.2	523	5.2	1,559	5.5	1,411	4.6
Other	3	0.0	4	0.0	7	0.0	5	0.0	7	0.0
Unallocated	4,245	0.0	2,479	0.0	2,848	0.0	218	0.0	817	0.0
Total	$ 19,494	100%	$ 20,607	100%	$ 23,718	100%	$ 32,898	100%	$42,810	100%

Allowance for Losses Related to Undisbursed Loan and Lease Commitments

We maintain a reserve for undisbursed loan and lease commitments. Management estimates the amount of probable losses by applying the loss factors used in our allowance for loan and lease loss methodology to our estimate of the expected usage of undisbursed commitments for each loan and lease type. Provisions for allowance for undisbursed loan and lease commitments are recorded in other expense. The allowance for undisbursed loan and lease commitments totaled $100,000 and $100,000 at December 31, 2013 and 2012, respectively.

Investment Securities, Available-for-Sale and Held-to-Maturity

The Bank classifies its debt and equity securities in two categories: held-to-maturity or available-for-sale. Securities that could be sold in response to changes in interest rates, increased loan demand, liquidity needs, capital requirements, or other similar factors are classified as securities available-for-sale. These securities are carried at fair value. Unrealized holding gains or losses, net of the related tax effect, on available-for-sale securities are excluded from income and are reported as a separate component of shareholders' equity as other comprehensive income net of applicable taxes until realized. Realized gains and losses from the sale of available-for-sale securities are determined on a specific-identification basis. Securities classified as held-to-maturity are those that the Bank has the positive intent and ability to hold until maturity. These securities are carried at amortized cost, adjusted for the amortization or accretion of premiums or discounts.

The Bank performs regular impairment analysis on its investment securities portfolio, following FASB standards which provide guidance on: identifying whether a market for an asset or liability is distressed or inactive, determining whether an entity has the intent and ability to hold a security to its anticipated recovery and whether an investment is other-than-temporarily-impaired. If it is determined that the impairment is other than temporary for equity securities, the impairment loss is recognized in earnings equal to the difference between the investment's cost and its fair value. If it is determined that the impairment is other-than-temporary for debt securities, the Bank will recognize the credit component of an other-than-temporary impairment in earnings and the non-credit component in other comprehensive income when the Bank does not intend to sell the security and it is more likely than not that the Bank will not be required to sell the security prior to recovery. The new cost basis is not changed for subsequent recoveries in fair value.

Premiums and discounts are amortized or accreted over the life of the related held-to-maturity or available-for-sale security as an adjustment to yield using the effective-interest method. Dividend and interest income are recognized when earned.

Our portfolio of investment securities consists primarily of investment grade corporate notes, U.S Agency mortgage-backed securities (MBS), municipal bonds, collateralized mortgage obligations (CMO's) and U.S. Government agency securities. We have traditionally categorized our entire securities portfolio as available-for-sale securities. We invest in securities to generate interest income and to maintain a liquid source of funding for our lending and other operations, including withdrawals of deposits. We do not engage in active trading in our investment securities portfolio. While management has the intent and ability to hold all securities until maturity, we have realized and from time to time may realize gains from sales of selected securities primarily in response to changes in interest rates. The Bank purchased a security considered held-to-maturity in 2011, and the security was called during 2013 resulting in a balance of zero at December 31, 2013. At December 31, 2013, investment securities classified as available-for-sale with a carrying value of $35.2 million were pledged to secure public deposits.

The carrying value of our held-to-maturity investment securities was zero at December 31, 2013 and $979,000 at December 31, 2012. The carrying value of our available-for-sale investment securities at December 31, 2013 totaled $142.7 million compared to $210.7 million at December 31, 2012. The decrease was primarily due sales of asset- and mortgage-backed securities and principal paydowns of securities during the year, in addition to a small decline of the fair market value of the portfolio of securities.

The carrying value of our portfolio of available-for-sale investment securities at December 31, 2013 and 2012 was as follows:

	Estimated Fair Value At December 31, 2013	2012
	(In thousands)	
Mutual Fund	4,840	4,973
Corporate notes	51,075	50,981
Mortgage-backed securities	51,342	96,924
Collateralized mortgage obligations	9,858	24,660
Municipal securities	21,049	25,811
Principal-only strip securities	4,506	5,846
Collateralized debt obligations	—	1,547
Total securities available-for-sale	$ 142,670	$ 210,742

The following table shows the maturities of available-for-sale investment securities at December 31, 2013, and the weighted average yields of such securities. The table does not consider the impact of prepayments on the maturities:

At December 31, 2013	Within One Year		After One Year but within Five Years		After Five Years but within Ten Years		After Ten Years		Total	
	Amount	Yield	Amount	Yield	Amount	Yield	Amount	Yield	Amount	Yield
	(Dollars in thousands)									
Corporate notes	—	—	6,070	4.78	36,184	4.21	8,821	4.42	51,075	4.32
Principal only strips	—	—	—	—	—	—	4,506	2.20	4,506	2.20
Mortgage-backed securities	—	—	997	3.42	12,453	4.12	37,892	1.62	51,342	2.26
Municipal securities	—	—	—	—	—	—	21,049	7.03	21,049	7.03
Collateralized mortgage obligations	—	—	1,413	3.76	—	—	8,445	1.20	9,858	1.57
Mutual Fund	—	—	—	—	—	—	4,840	1.74	4,840	1.74
Total securities available-for-sale	$ —	—%	$ 8,480	4.45%	$ 48,637	4.19%	$ 85,553	3.33%	$142,670	3.57%

During 2013, the Bank sold all three collateralized debt obligations ("CDO's") which were in its available-for-sale portfolio as of December 31, 2012, which consisted of pools of bank trust preferred securities. As of December 31, 2012, the amortized cost of all three CDO's exceeded the fair value. The sale of these securities was due to what was then named the Final Volcker Rule of the Dodd-Frank Act of 2010 (The rule was later amended to allow for Banks to own this type of asset class).

Management recognized credit-related OTTI for the CDO securities, based on the guidance of the Investments – Debt and Equity Securities Topic of FASB ASC, of $7,000 and $24,000 for the years ended December 31, 2013 and 2012 respectively.

As of December 31, 2013, the Bank owned 4 corporate securities where the amortized cost exceeded fair value. The total amortized cost of these securities was $15.6 million and their fair value was $14.6 million. Management performed an analysis on all of the issuers of these securities which focused on the recent financial results of the companies, capital ratios and long-term prospects of the issuer and deemed all 4 corporate securities to be temporarily impaired. The Bank had recorded no credit-related OTTI charges on corporate securities during 2013, and also had zero OTTI charges relating to corporate securities in 2012 and 2011.

As of December 31, 2013, the Bank owned 2 collateralized mortgage obligations ("CMO") where the amortized cost exceeded fair value. The total amortized cost of these securities was $8.6 million and the total fair value was $8.4 million. Management determined that the CMO securities were not other-than-temporarily impaired as of December 31, 2013. This determination was made based on several factors such as debt rating of the securities, amount of credit protection, the Bank's intent and ability to hold the securities until a recovery in value and the determination that it is not more likely than not that the Bank will be required to sell the securities prior to recovery of amortized cost basis.

The Bank owns 20 municipal investment securities. Each of these securities carries an investment-grade rating. As of December 31, 2013, 17 of these issues were in an unrealized loss position. The total amortized cost of these securities was $20.2 million and the total fair value was $18.9 million. Management determined that none of the municipal securities was other-than-temporarily impaired as of December 31, 2013. This determination was made based on several factors such as the Bank's intent and ability to hold the securities until a recovery in value and the determination that it is not more likely than not that the Bank will be required to sell the securities prior to recovery of amortized cost basis. In addition, management reviews all of the ratings on the municipal investment securities, recent ratings changes, as well as the length of time that the security has been impaired to determine whether the security is other than temporary impaired.

At December 31, 2013, the Bank held one agency-backed principal-only (PO) strip security with an amortized cost of $4.6 million and a fair value of $4.5 million. Based on factors including the Bank's intent and ability to hold the security until a recovery in value and the determination that it is not more likely than not that the Bank will be required to sell the security prior to recovery of amortized cost basis, management determined that the security was not other-than-temporarily impaired as of December 31, 2013.

At December 31, 2013, there were 24 and 8 investment securities that were in an unrealized loss position for less than 12 months and for 12 months or greater, respectively. Temporary impairments related to corporate notes, mortgage-backed securities, and municipal securities are primarily attributable to declining market prices caused by lack of trading liquidity in these instruments and in the case of corporate notes, resulted from increases in credit spreads between U.S. Treasuries and corporate bonds subsequent to the date that these securities were purchased. None of the securities in the Bank's investment portfolio rely on an insurance wrap as a credit enhancement. Management believes that it is not probable that the Bank will not receive all amounts due under the contractual terms of these securities. If economic conditions worsen, or if the financial condition of specific issuers within these portfolios deteriorates, then the Bank could record OTTI charges in 2014 on specific investments within these portfolios.

It is possible that we may recognize OTTI in future periods. We do not intend to sell these securities until recovery and have determined that it is not more likely than not that we will be required to sell the securities prior to recovery of their amortized cost basis. Additional information concerning investment securities is provided in Note 3 of the "Notes to Consolidated Financial Statements" in this annual report.

Deposits

Total deposits were $1.53 billion at December 31, 2013 compared to $1.36 billion at December 31, 2012. Noninterest-bearing demand deposits decreased $108.2 million or 24.2%. This decrease was due to the termination of a program whereby the Bank received DDA deposits but those deposits required FDIC insurance or AAA collateral. Upon the expiration of the TAG Program at the end of 2012, management opted not to collateralize these deposits and so the program was terminated. The ratio of noninterest-bearing deposits to total deposits was 22.1% at December 31, 2013 and 32.9% at December 31, 2012. Interest-bearing deposits are comprised of interest-bearing demand deposits, money market accounts, regular savings accounts, time deposits of under $250,000 and time deposits of $250,000 or more. Interest-bearing demand and savings deposits increased by $146.1 million or 42.1%, and time deposits decreased $133.9 million or 23.7%. The increase in demand and interest-bearing demand deposits is a direct result of management's desire to grow this segment of the deposit base as these deposits are typically related to long-term customer relationships and also carry the lowest interest costs.

The following table shows the average amount and average rate paid on the categories of deposits for each of the periods indicated:

	Year Ended December 31,					
	2013		2012		2011	
	Average Balance	**Average Rate**	**Average Balance**	**Average Rate**	**Average Balance**	**Average Rate**
	(Dollars in thousands)					
Noninterest-bearing deposits	$ 359,205	0.00%	$ 362,118	0.00%	$ 230,088	0.00%
Interest-bearing demand	102,169	0.52	54,534	0.53	42,933	0.59
Money market	280,108	0.60	216,916	0.67	133,056	0.78
Savings	22,783	0.39	21,007	0.36	23,307	0.39
Time certificates of deposit	650,155	0.83	581,265	1.01	625,657	1.30
Total	$ 1,414,420	0.54%	$ 1,235,840	0.62%	$1,055,041	0.91%

Average total deposits increased in 2013. The increase in average total deposits for 2013 was primarily driven by increases of $68.9 million in average time certificates of deposit, $63.2 million in average money market accounts, and $47.6 million in average interest-bearing demand between the years.

The largest single component of our deposits has been, and in the near term is likely to be, time certificates of deposit. We market and receive time certificates of deposit from our existing and new high net worth customers, especially from the Chinese communities within our branch network. While we do not attempt to be a market leader in offered interest rates, we attempt to offer competitive rates on these time certificates of deposit within a range offered by other competing banks.

The following table shows the maturities of time certificates of deposit at December 31, 2013 and 2012:

	At December 31, 2013	At December 31, 2012
	(In thousands)	
Three months or less	$ 187,398	$ 172,477
Over three months through six months	153,886	114,245
Over six months through twelve months	205,878	191,142
Over twelve months	150,662	80,956
Total	$ 697,824	$ 558,820

Capital Resources

Current risk-based regulatory capital standards generally require banks to maintain a ratio of "core" or "Tier 1" capital (consisting principally of common equity) to risk-weighted assets of at least 4%, a ratio of Tier 1 capital to adjusted total assets (leverage ratio) of at least 4% and a ratio of total capital (which includes Tier 1 capital plus certain forms of subordinated debt, a portion of the allowance for loan and lease losses and preferred stock) to risk-weighted assets of at least 8%. Risk-weighted assets are calculated by multiplying the balance in each category of assets by a risk factor, which ranges from zero for cash assets and certain government obligations to 100% for some types of loans, and adding the products together.

Our goal is to exceed the minimum regulatory capital requirements for well-capitalized institutions as well as maintain a tier 1 leverage ratio above 10% as required by the MOU. At December 31, 2013 and 2012, our capital ratios were above the minimum requirements for well capitalized institutions. On a quarterly basis, we perform a stress test on our capital to determine our level of capital in various economic circumstances looking out twenty-four months into the future.

	At December 31, 2013	At December 31, 2012
Leverage Ratio		
Preferred Bank	11.80%	11.96%
Minimum requirement for "Well-Capitalized" institution	5.00%	5.00%
Minimum regulatory requirement	4.00%	4.00%
Tier 1 Risk-Based Capital Ratio		
Preferred Bank	13.78%	13.73%
Minimum requirement for "Well-Capitalized" institution	6.00%	6.00%
Minimum regulatory requirement	4.00%	4.00%
Total Risk-Based Capital Ratio		
Preferred Bank	15.03%	14.98%
Minimum requirement for "Well-Capitalized" institution	10.00%	10.00%
Minimum regulatory requirement	8.00%	8.00%

Contractual Obligations and Off-Balance Sheet Arrangements

The following table presents our contractual cash obligations, excluding deposits and unrecognized tax benefits, as of December 31, 2013:

Contractual Obligations [1]	Amount of Commitment Expiring per Period Total Amounts Committed	Less Than 1 year	1-3 Years	3-5 Years	After 5 Years
			(In thousands)		
Operating Lease Obligations	$ 12,748	$ 2,814	$ 5,272	$ 3,384	$ 1,278
Total	$ 12,748	$ 2,814	$ 5,272	$ 3,384	$ 1,278

[1] *Contractual obligations do not include interest.*

In the normal course of business, we enter into off-balance sheet arrangements consisting of commitments to extend credit, to fund commercial letters of credit and standby letters of credit. Commercial letters of credit are originated to facilitate transactions both domestic and foreign while standby letters of credit are originated to issue payments on behalf of the Bank's customers when specific future events occur. Historically, the Bank has rarely issued payment under standby letters of credit, which the Bank's customer is obligated to reimburse the Bank. The Bank could also liquidate collateral or offset a customer's deposit accounts to satisfy this payment.

Financial instrument transactions are subject to our normal credit standards, financial controls and risk-limiting and monitoring procedures. Collateral requirements are based on a case-by-case evaluation of each customer and product.

The following table presents these off-balance sheet arrangements at December 31, 2013:

Off-balance sheet arrangements	Amount of off-balance sheet Expiring per Period Total Amounts Committed	Less Than 1 year	1-3 Years	3-5 Years	After 5 Years
			(In thousands)		
Commitments to extend credit	$ 354,463	$ 221,456	$ 95,170	$ 34,278	$ 3,559
Commercial letters of credit	5,764	5,764	—	—	—
Standby letter of credit	12,057	12,057	—	—	—
Total	$ 372,284	$ 239,277	$ 95,170	$ 34,278	$ 3,559

Liquidity

Based on our existing business plan, we believe that our level of liquid assets is sufficient to meet our current and presently anticipated funding needs. We rely on deposits as the principal source of funds and, therefore, must be in a position to service depositors' needs as they arise. We attempt to maintain a loan-to-deposit ratio below approximately 95%. Our loan-to-deposit ratio was 86.9% at December 31, 2013 compared to 83.2% at December 31, 2012.

Borrowings from the FHLB are another source of funding for our loan and investment activities. At December 31, 2013, we had $20.0 million of outstanding FLHB borrowings, and we could additionally borrow up to $139.8 million with collateral of specifically identified loans and securities. In addition, we have pledged securities with a fair value of $51.7 million at the Federal Reserve Discount Window which we may borrow from on an overnight basis. We have one uncommitted borrowing line with a financial institution for $20.0 million. As an additional condition of borrowing from the FHLB, we are required to purchase FHLB stock. For the year ended December 31, 2013, the Bank was required to maintain the minimum stock requirement of $5,296,200 of FHLB stock based on the volume of "membership assets" as defined by the FHLB. At December 31, 2013, the Bank held $5,296,200 in FHLB stock.

We also attempt to maintain a liquidity ratio (liquid assets, including cash and due from banks, federal funds sold and investment securities not pledged as collateral expressed as a percentage of total deposits) above approximately 18%. Our liquidity ratios were 32% at December 31, 2013 and 36% at December 31, 2012. We believe that in the event the level of liquid assets (our primary liquidity) does not meet our liquidity needs, other available sources of liquid assets (our secondary liquidity), including the sales of securities under agreements to repurchase, sales of unpledged investment securities or loans, utilizing the discount window borrowings from the Federal Reserve Bank as well as borrowing from the FHLB could be employed to meet those funding needs. We have a Contingency Funding Plan which is reviewed annually by the Board of Directors which sets forth actions to be taken in the event that our liquidity ratios fall below Board-established guidelines. We also perform quarterly liquidity stress tests to review various adverse scenarios. Although we believe that our funding resources will be more than adequate to meet our obligations, we cannot be certain of this adequacy if further economic deterioration or other negative events occur that could impair our ability to meet our funding obligations.

Quantitative and Qualitative Disclosures about Market Risk

Market risk is the risk of loss in a financial instrument arising from adverse changes in market prices and rates, foreign currency exchange rates, commodity prices and equity prices. Our market risk arises primarily from interest rate risk inherent in our lending and deposit taking activities. To that end, management actively monitors and manages our interest rate risk exposure. We do not have any market risk sensitive instruments entered into for trading purposes. We manage our interest rate sensitivity by matching the re-pricing opportunities on our earning assets to those on our funding liabilities. Management uses various asset/liability strategies to manage the re-pricing characteristics of our assets and liabilities designed to ensure that exposure to interest rate fluctuations is limited and within our guidelines of acceptable levels of risk-taking. Hedging strategies, including the terms and pricing of loans and deposits and managing the deployment of our securities, are used to reduce mismatches in interest rate re-pricing opportunities of portfolio assets and their funding sources.

Interest rate risk is addressed by our Investment Committee which is comprised of the Chief Executive Officer and members of the Board of Directors. The Investment Committee monitors interest rate risk by analyzing the potential impact on the net portfolio of equity value and net interest income from potential changes in interest rates, and considers the impact of alternative strategies or changes in balance sheet structure. The Investment Committee manages our balance sheet in part to maintain the potential impact on net portfolio value and net interest income within acceptable ranges despite rate changes in interest rates.

Exposure to interest rate risk is monitored continuously by senior management and is reviewed by the Investment Committee at least quarterly by management and our Board of Directors. Interest rate risk exposure is measured using interest rate sensitivity analysis to determine our change in net portfolio value and net interest income in the event of hypothetical changes in interest rates. If potential changes to net portfolio value and net interest income resulting from our analysis of hypothetical interest rate changes are not within board-approved limits, the board may direct management to adjust the asset and liability mix to bring interest rate risk within board-approved limits. This analysis of hypothetical interest rate changes is performed on a monthly basis by a third party vendor utilizing detailed data that we provide to them.

Market Value of Portfolio Equity

We measure the impact of market interest rate changes on the net present value of estimated cash flows from our assets and liabilities defined as market value of portfolio equity, using a simulation model. This simulation model assesses the changes in the market value of interest rate sensitive financial instruments that would occur in response to an instantaneous and sustained increase or decrease in market interest rates.

The following table presents forecasted changes in net portfolio value using a base market rate and the estimated change to the base scenario given an immediate and sustained upward movement in interest rates of 100, 200, 300 and 400 basis points and an immediate and sustained downward movement in interest rates of 100 and 300 basis points at December 31, 2013.

Market Value of Portfolio Equity

Interest Rate Scenario	Market Value	Percentage Change from Base	Percentage of Total Assets	Percentage of Portfolio Equity Book Value
		(Dollars in thousands)		
Up 400 basis points	$ 337,394	19.94%	19.32%	163.06%
Up 300 basis points	$ 324,156	15.23%	18.46%	156.66%
Up 200 basis points	$ 309,557	10.04%	17.52%	149.60%
Up 100 basis points	$ 294,151	4.57%	16.55%	142.16%
Base	$ 281,305	— %	15.68%	135.95%
Down 100 basis points	$ 269,074	(4.35%)	14.87%	130.04%
Down 300 basis points	$ 243,046	(13.60%)	13.35%	117.46%

The computation of prospective effects of hypothetical interest rate changes are based on numerous assumptions, including relative levels of market interest rates, asset prepayments and deposit decay, and should not be relied upon as indicative of actual results. Further, the computations do not contemplate any actions we may undertake in response to changes in interest rates. Actual amounts may differ from the projections set forth above should market conditions vary from the underlying assumptions.

Net Interest Income

In order to measure interest rate risk at December 31, 2013, we used a simulation model to project changes in net interest income that result from forecasted changes in interest rates. This analysis calculates the difference between net interest income forecasted using a rising and a falling interest rate scenario and a net interest income forecast using a base market interest rate derived from the current treasury yield curve. The income simulation model includes various assumptions regarding the re-pricing relationships for each of our products. Many of our assets are floating rate loans, which are assumed to re-price immediately, and to the same extent as the change in market rates according to their contracted index. Some loans and investment vehicles include the opportunity of prepayment (embedded options), and accordingly the simulation model uses national indexes to estimate these prepayments and reinvest their proceeds at current yields. Non-term deposit products reprice more slowly, usually changing less than the change in market rates and at management discretion.

This analysis indicates the impact of changes in net interest income for the given set of rate changes and assumptions. It assumes no growth in the balance sheet and that its structure will remain similar to the structure at year end. It does not account for all factors that impact this analysis, including changes by management to mitigate the impact of interest rate changes or secondary impacts such as changes to our credit risk profile as interest rates change. Furthermore, loan prepayment rate estimates and spread relationships change regularly. Interest rate changes create changes in actual loan prepayment rates that will differ from the market estimates incorporated in this analysis. Changes that vary significantly from the assumptions may have significant effects on our net interest income.

For the rising and falling interest rate scenarios, the base market interest rate forecast was increased or decreased on an instantaneous and sustained basis.

Sensitivity of Net Interest Income December 31, 2013

Interest Rate Scenario	Adjusted Net Interest Income	Percentage Change from Base	Net Interest Margin Percent	Net Interest Margin Change
		(Dollars in thousands)		
Up 400 basis points	$ 105,950	65.30%	6.05%	2.36
Up 300 basis points	$ 94,201	46.97%	5.39%	1.70
Up 200 basis points	$ 82,488	28.69%	4.73%	1.04
Up 100 basis points	$ 71,388	11.38%	4.10%	0.41
Base	$ 64,097	— %	3.69%	—
Down 100 basis points	$ 62,982	(1.74)%	3.62%	(0.06)
Down 300 basis points	$ 63,266	(1.30)%	3.64%	(0.04)

Inflation

The majority of our assets and liabilities are monetary items held by us, the dollar value of which is not affected by inflation. Only a small portion of total assets is in premises and equipment. The lower inflation rate of recent years has not had the positive impact on us that was felt in many other industries. Our small fixed asset investment minimizes any material effect of asset values and depreciation expenses that may result from fluctuating market values due to inflation. Higher inflation rates may increase operating expenses or have other adverse effects on borrowers of the banks, making collection on extensions of credit more difficult for us. Rates of interest paid or charged generally rise if the marketplace believes inflation rates will increase.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES OF MARKET RISKS

For quantitative and qualitative disclosures regarding market risks in our portfolio, see, "Management's Discussion and Analysis of Financial Condition and Results of Operations—Quantitative and Qualitative Disclosure About Market Risk."

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

The financial statements of the Bank, including the "Report of Independent Registered Public Accounting Firm," are included in this report immediately following Part IV.

ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

None.

ITEM 9A. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

As of December 31, 2013, we carried out an evaluation, under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures and internal controls over financial reporting pursuant to SEC rules, as such rules are adopted by the FDIC. Based upon that evaluation, and the identification of the material weakness in our internal control over financial reporting as described below under "Management's Report on Internal Control over Financial Reporting", the Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were effective as of December 31, 2013. Based on a number of factors, including the performance of additional procedures by management designed to ensure the reliability of our financial reporting, we believe that the financial statements in this Annual Report on Form 10-K fairly present, in all material respects, our financial position, results of operations and cash flows for the periods presented in conformity with GAAP.

Management's Report on Internal Control over Financial Reporting

The Management of the Bank is responsible for establishing and maintaining adequate internal control over financial reporting pursuant to the rules and regulations of the SEC. The Bank's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with U.S. generally accepted accounting principles. Internal control over financial reporting includes those written policies and procedures that:

- pertain to the maintenance of records that in reasonable detail accurately and fairly reflect the transactions and dispositions of the assets of the company;
- provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles;
- provide reasonable assurance that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and
- provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the company's assets that could have a material effect on the consolidated financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Management under the supervision and with the participation of the Bank's principal executive officer and principal financial officer assessed the effectiveness of the Bank's internal control over financial reporting as of December 31, 2013. Management based this assessment on criteria for effective internal control over financial reporting described in *Internal Control-Integrated Framework (1992)* issued by the Committee of Sponsoring Organizations of the Treadway Commission. Management's assessment included an evaluation of the design of Preferred Bank's internal control over financial reporting and testing of the operational effectiveness of its internal control over financial reporting. Management reviewed the results of its assessment with the Audit Committee of our Board of Directors. Based on this evaluation, management determined that the Bank's system of internal controls over financial reporting was effective as of December 31, 2013.

Report of Independent Registered Public Accounting Firm

The Board of Directors and Shareholders
Preferred Bank:

We have audited Preferred Bank and subsidiary's (the Bank) internal control over financial reporting as of December 31, 2013, based on criteria established in *Internal Control – Integrated Framework (1992)* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The Bank's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management's Report on Internal Control over Financial Reporting. Our responsibility is to express an opinion on the Bank's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audit also included performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, the Bank maintained, in all material respects, effective internal control over financial reporting as of December 31, 2013, based on criteria established in *Internal Control – Integrated Framework (1992)* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated statements of financial condition of Preferred Bank and subsidiary as of December 31, 2013 and 2012, and the related consolidated statements of operations and comprehensive income, changes in shareholders' equity, and cash flows for each of the years in the three-year period ended December 31, 2013, and our report dated March 17, 2014 expressed an unqualified opinion on those consolidated financial statements.

/s/ KPMG LLP

Los Angeles, California
March 17, 2014

ITEM 9B. OTHER INFORMATION

None

PART III

ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE

Information concerning directors and executive officers of the Bank, to the extent not included under "Item 1 under the heading "*Executive Officers of the Bank*", will appear in the Bank's definitive proxy statement for the 2014 Annual Meeting of Shareholders (the "2014 Proxy Statement"), and such information either shall be (i) deemed to be incorporated herein by reference from the section entitled "ELECTION OF DIRECTORS" AND **"**SECTION 16(a) BENEFICIAL OWNERSHIP REPORTING COMPLIANCE" and "THE COMMITTEES OF THE BOARD," if filed with the Federal Deposit Insurance Corporation pursuant to Regulation 14A not later than 120 days after the end of the Bank's most recently completed fiscal year or (ii) included in an amendment to this report filed with the Federal Deposit Insurance Corporation on Form 10-K/A not later than the end of such 120 day period.

Code of Ethics

The Bank has adopted a code of ethics that applies to its principal executive officer, principal financial and accounting officer, controller, and persons performing similar functions. The code of ethics is posted on our internet website at www.preferredbank.com.

ITEM 11. EXECUTIVE COMPENSATION

Information concerning executive compensation will appear in the 2014 Proxy Statement, and such information either shall be (i) deemed to be incorporated herein by reference from the sections entitled "COMPENSATION COMMITTEE INTERLOCKS AND INSIDER PARTICIPATION," "COMPENSATION COMMITTEE'S REPORT," "COMPENSATION DISCUSSION AND ANALYSIS," "SUMMARY COMPENSATION TABLE," "OUTSTANDING EQUITY AWARDS, " "NON-QUALIFIED DEFERRED COMPENSATION," "CHANGE OF CONTROL AGREEMENTS, " and "COMPENSATION OF DIRECTORS," if filed with the Federal Deposit Insurance Corporation pursuant to Regulation 14A not later than 120 days after the end of the Bank's most recently completed fiscal year or (ii) included in an amendment to this report filed with the Federal Deposit Insurance Corporation on Form 10-K not later than the end of such 120 day period.

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED SHAREHOLDER MATTERS

Information concerning security ownership of certain beneficial owners and management and information related to the Bank's equity compensation plans will appear in the 2013 Proxy Statement, and such information either shall be (i) deemed to be incorporated herein by reference from the sections entitled "SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT" and "EQUITY COMPENSATION PLANS," if filed with the Federal Deposit Insurance Corporation pursuant to Regulation 14A not later than 120 days after the end of the Bank's most recently completed fiscal year or (ii) included in an amendment to this report filed with the Federal Deposit Insurance Corporation on Form 10-K/A not later than the end of such 120 day period.

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE

Information concerning certain relationships and related transactions will appear in the 2014 Proxy Statement, and such information either shall be (i) deemed to be incorporated herein by reference from the section entitled "CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS and "BOARD INDEPENDENCE," if filed with the Federal Deposit Insurance Corporation pursuant to Regulation 14A not later than 120 days after the end of the Bank's most recently completed fiscal year, or (ii) included in an amendment to this report filed with the Federal Deposit Insurance Corporation on Form 10-K/A not later than the end of such 120 day period.

ITEM 14. PRINCIPAL ACCOUNTING FEES AND SERVICES

Information concerning principal accountant fees and services will appear in the 2014 Proxy Statement, and such information either shall be (i) deemed to be incorporated herein by reference from the section entitled “INDEPENDENT AUDITOR FEES,” and “AUDIT COMMITTEE PRE-APPROVAL POLICY” if filed with the Federal Deposit Insurance Corporation pursuant to Regulation 14A not later than 120 days after the end of the Bank’s most recently completed fiscal year or (ii) included in an amendment to this report filed with the Federal Deposit Insurance Corporation on Form 10-K/A not later than the end of such 120 day period.

PART IV

ITEM 15. EXHIBITS, FINANCIAL STATEMENT SCHEDULES

(a)(1) Financial Statements

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(a)(2) Financial Statement schedules

Schedules have been omitted because they are not applicable, not material or because the information is included in the consolidated financial statements or the notes thereto.

(a)(3) Exhibits

Exhibit No.	**Exhibit Description**
3.1	Amended and Restated Articles of Incorporation(1)
3.2	Certificate of Determination of the Series A preferred Stock(4)
3.3	Amended and Restated Bylaws(1)
4.1	Common Stock Certificate(3)
10.1*	1992 Stock Option Plan(1)
10.2*	Management Incentive Bonus Plan(1)
10.3*	Deferred Compensation Plan(1)
10.4*	Stock Option Gain Deferred Compensation Plan(1)
10.5*	2004 Equity Incentive Plan(1)
10.6*	Form of Indemnification Agreement for directors and executive officers(1)
10.7*	Revised Bonus Plan(2)
10.8*	Deferred Compensation Plan-Deferred Stock Unit Agreement and Rabbi Trust
10.9*	Retention and Severance Agreement-Li Yu
12.1	Computation of Ratio of Earnings to Fixed Charges
31.1	Chief Executive Officer Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
31.2	Chief Financial Officer Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
32.1	Chief Executive Officer Certification Pursuant to 18 U.S.C. Section 1350, As Adopted Pursuant To Section 906 of the Sarbanes-Oxley Act of 2002
32.2	Chief Financial Officer Certification Pursuant to 18 U.S.C. Section 1350, As Adopted Pursuant To Section 906 of the Sarbanes-Oxley Act of 2002

(1) Incorporated by reference from Registrant's Registration Statement on Form 10 filed with the Federal Deposit Insurance Corporation on January 18, 2006.

(2) Incorporated by reference from Registrant's Registration Statement on Form 10 filed with the Federal Deposit Insurance Corporation on March 13, 2007.

(3) Incorporated by reference from Registrant's Registration Statement on Form 10 Amendment No. 1 filed with the Federal Deposit Insurance Corporation on February 2, 2006.

(4) Incorporated by reference from Current Report on Form 8-K filed with the Federal Deposit Insurance Corporation on June 10, 2010.

* Denotes management contract or compensatory plan or arrangement.

Report of Independent Registered Public Accounting Firm

The Board of Directors and Shareholders
Preferred Bank:

We have audited the accompanying consolidated statements of financial condition of Preferred Bank and subsidiary (the Bank) as of December 31, 2013 and 2012, and the related consolidated statements of income and comprehensive income, changes in shareholders' equity, and cash flows for each of the years in the three-year period ended December 31, 2013. These consolidated financial statements are the responsibility of the Bank's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Preferred Bank and subsidiary as of December 31, 2013 and 2012, and the results of their operations and their cash flows for each of the years in the three-year period ended December 31, 2013, in conformity with U.S. generally accepted accounting principles.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the Bank's internal control over financial reporting as of December 31, 2013, based on criteria established in *Internal Control – Integrated Framework (1992)* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO), and our report dated March 17, 2014 expressed an unqualified opinion on the effectiveness of the Company's internal control over financial reporting.

/s/ KPMG LLP

Los Angeles, California
March 17, 2014

PREFERRED BANK
Consolidated Statements of Financial Condition
December 31, 2013 and 2012
(In thousands, except for shares)

	2013	2012
Assets		
Cash and due from banks	$ 226,615	$ 151,995
Federal funds sold	20,000	—
Cash and cash equivalents	246,615	151,995
Securities held-to-maturity, at amortized cost	—	979
Securities available-for-sale, at fair value	142,670	210,742
Loans and leases	1,323,431	1,119,553
Less allowance for loan and lease losses	(19,494)	(20,607)
Less unamortized deferred loan costs, net	(2,562)	(2,019)
Net loans and leases	1,301,375	1,096,927
Loans held for sale, at lower of cost or fair value	6,207	12,150
Other real estate owned	5,602	28,280
Customers' liability on acceptances	2,061	1,961
Bank furniture and fixtures, net	4,205	4,383
Bank-owned life insurance	8,290	8,049
Investment in affordable housing	6,411	—
Accrued interest receivable	5,378	5,646
Federal Home Loan Bank ("FHLB") stock, at cost	5,296	4,282
Net deferred tax assets	23,331	26,975
Income tax receivable	1,784	542
Other assets	9,734	1,943
Total assets	$ 1,768,959	$ 1,554,856
Liabilities and Shareholders' Equity		
Deposits:		
Demand	$ 338,530	$ 446,734
Interest-bearing demand	469,976	325,018
Savings	22,984	21,844
Time certificates of $100,000 or more	590,721	463,171
Other time certificates	107,103	100,760
Total deposits	1,529,314	1,357,527
Acceptances outstanding	2,061	1,961
Advances from Federal Home Loan Bank	20,000	—
Accrued interest payable	983	968
Other liabilities	9,685	6,562
Total liabilities	1,562,043	1,367,018
Commitments and contingencies		
Shareholders' equity:		
Preferred stock. Authorized 25,000,000 shares; no shares issued and outstanding at December 31, 2013 and 2012.	—	—
Common stock, no par value. Authorized 20,000,000 shares; issued and outstanding 13,280,653 and 13,234,608 shares at December 31, 2013 and 2012, respectively.	163,237	162,927
Treasury stock, at cost 153,251 and 152,985 shares at December 31, 2013 and 2012, respectively)	(19,115)	(19,115)
Additional paid-in capital	25,974	24,544
Retained earnings	36,680	17,481
Accumulated other comprehensive loss:		
Non-credit portion of other-than-temporary impairment on securities available-for-sale, net of tax of $0 and $133 at December 31, 2013 and December 31, 2012, respectively.	—	(184)
Unrealized gain on securities available-for-sale, net of tax of $102 and $1,585 at December 31, 2013 and December 31, 2012, respectively.	140	2,185
Total shareholders' equity	206,916	187,838
Total liabilities and shareholders' equity	$ 1,768,959	$ 1,554,856

See accompanying notes to the consolidated financial statements.

PREFERRED BANK
Consolidated Statements of Operations and Comprehensive Income
Years Ended December 31, 2013, 2012 and 2011
(In thousands, except share and per share data)

	2013	2012	2011
Interest income:			
Loans and leases	$ 63,718	$ 55,400	$ 46,464
Investment securities, available for sale	5,953	6,116	7,326
Federal funds sold	55	26	—
Total interest income	69,726	61,542	53,790
Interest expense:			
Interest-bearing demand	2,199	1,746	1,295
Savings	89	75	92
Time certificates of $100,000 or more	4,557	4,667	4,956
Other time certificates	816	1,201	3,207
FHLB borrowings	68	—	—
Senior debt	—	94	753
Total interest expense	7,729	7,783	10,303
Net interest income before provision for credit losses	61,997	53,759	43,487
Provision for credit losses	3,250	19,800	5,700
Net interest income after provision for credit losses	58,747	33,959	37,787
Noninterest income:			
Fees and service charges on deposit accounts	2,101	1,792	1,742
Trade finance income	612	309	241
BOLI income	331	329	333
Net (loss) gain on sale of investment securities	(1,957)	575	81
Other income	916	503	393
Total noninterest income	2,003	3,508	2,790
Noninterest expense:			
Salaries and employee benefits	16,226	12,523	11,155
Net occupancy expense	3,206	2,990	3,060
Business development and promotion expense	366	294	335
Professional services	3,597	3,227	2,267
Office supplies and equipment expense	1,186	1,154	1,061
Total other-than-temporary impairment losses	99	24	32
Portion of loss reclassified in other comprehensive income	(92)	—	—
Net of other-than-temporary impairment losses	7	24	32
(Gain) loss on sale of OREO and related expense	(449)	8,580	8,303
Other	5,122	5,386	7,179
Total noninterest expense	29,261	34,178	33,392
Income before income taxes	31,489	3,289	7,185
Income tax expense (benefit)	12,290	(20,583)	(5,049)
Net income	$ 19,199	$ 23,872	$ 12,234
Income allocated to participating shares	(201)	(323)	(195)
Net income available to common shareholders	$ 18,998	$ 23,549	$ 12,039
Other comprehensive income:			
Unrealized net gain (loss) on securities available-for-sale	(5,175)	8,710	4,286
Less reclassification adjustments included in net (loss) income	(1,964)	551	(840)
Other comprehensive (loss) income, before tax	(3,211)	8,159	3,446
Income taxes (benefits) related to items of other comprehensive income (loss)	1,350	(3,372)	(25)
Other comprehensive income (loss) , net of tax	(1,861)	4,787	3,421
Comprehensive income	$ 17,337	$ 28,659	$ 15,655
Net income per share			
Basic	$ 1.45	$ 1.80	$ 0.93
Diluted	$ 1.42	$ 1.78	$ 0.93
Weighted-average common shares outstanding			
Basic	13,116,713	13,050,559	12,995,525
Diluted	13,364,320	13,247,389	12,995,525
Dividends per share	$ 0.00	$ 0.00	$ 0.00

See accompanying notes to the consolidated financial statements.

PREFERRED BANK
Consolidated Statements of Changes in Shareholders' Equity
Years Ended December 31, 2013, 2012 and 2011
(In thousands, except share and dividends declared per share data)

	Preferred Stock	Common Stock Shares	Common Stock Amount	Treasury Stock	Additional Paid-In Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total Shareholders' Equity
Balance as of December 31, 2011	$ —	13,220,955	$162,884	$ (19,115)	$ 23,456	$ (6,391)	$ (2,786)	$ 158,048
Restricted stock award grant	—	8,600	—	—	542	—	—	542
Restricted stock award forfeitures	—	(416)	—	—	—	—	—	—
Stock options exercised	—	5,469	43	—	—	—	—	43
Share-based compensation	—	—	—	—	546	—	—	546
Net income	—	—	—	—	—	23,872	—	23,872
Change in Non-credit OTTI in AOCI, net of taxes	—	—	—	—	—	—	296	296
Change in unrealized gain, net of tax	—	—	—	—	—	—	4,491	4,491
Balance as of December 31, 2012	$ —	13,234,608	$162,927	$ (19,115)	$ 24,544	$ 17,481	$ 2,001	$ 187,838
Restricted stock award grant	—	11,250	—	—	409	—	—	409
Restricted stock award forfeitures	—	—	—	—	—	—	—	—
Stock options exercised	—	34,795	310	—	—	—	—	310
Tax effect of stock plans, net	—	—	—	—	(232)	—	—	(232)
Share-based compensation	—	—	—	—	1,253	—	—	1,253
Net income	—	—	—	—	—	19,199	—	19,199
Change in Non-credit OTTI in AOCI, net of taxes	—	—	—	—	—	—	184	184
Change in unrealized gain, net of tax	—	—	—	—	—	—	(2,045)	(2,045)
Balance as of December 31, 2013	$ —	13,280,653	$163,237	$ (19,115)	$ 25,974	$ 36,680	$ 140	$ 206,916

PREFERRED BANK
Consolidated Statements of Cash Flows
Years Ended December 31, 2013, 2012 and 2011
(In thousands)

	2013	2012	2011
Cash flows from operating activities:			
Net income	$ 19,199	$ 23,872	$ 12,234
Adjustments to reconcile net income to net cash provided by operating activities:			
Provision for credit losses	3,250	19,800	5,700
Net change in deferred loan fees	544	982	1,095
Loss (gain) on sale and call of securities available-for-sale	1,957	(575)	(81)
Amortization of investment securities discounts and premiums, net	1,022	595	530
Amortization of investments in affordable housing partnerships	376	—	—
Depreciation and amortization	686	650	738
Impairment of securities available for sale	7	24	32
Federal Home Loan Bank stock dividends	—	(119)	276
Share-based compensation expense	1,430	1,087	1,059
Write-down on other real estate owned	1,706	4,018	4,870
Net (gain) loss on sale of loans	(514)	(290)	656
Deferred tax expense (benefit)	4,994	(19,996)	(6,979)
(Increase) decrease in income taxes receivable	(1,241)	—	—
Net (gain) loss on sale of other real estate owned	(3,793)	387	1,090
Decrease (increase) in BOLI, accrued interest receivable, and other assets	377	(4,135)	3,737
Increase in accrued interest payable and other liabilities	3,138	158	194
Net cash provided by operating activities	33,138	26,460	25,150
Cash flows from investing activities:			
Proceeds from maturities and redemptions of securities held-to-maturity	988	2,062	33,761
Proceeds from maturities and redemptions of securities available-for-sale	28,459	28,386	3,002
Proceeds from sale of securities available-for-sale	28,962	11,096	20,453
Purchase of securities held-to-maturity	—	—	(6,052)
Purchase of securities available-for-sale	(3,697)	(82,848)	(34,034)
Purchase of investments in affordable housing partnerships	(6,787)	—	—
Purchase of FHLB stock	(1,014)	(119)	—
Proceeds from sale of other real estate owned	24,766	7,945	14,982
Proceeds from sale of loans	12,355	2,534	35,642
Proceeds from recoveries of written off loans	3,901	570	1,217
Net increase in loans	(218,040)	(199,932)	(96,468)
Purchase of bank premises and equipment	(508)	(244)	(109)
Net cash used in investing activities	(130,615)	(230,550)	(27,606)
Cash flows from financing activities:			
Increase in deposits	171,787	239,574	36,688
Increase in other borrowings	20,000	—	—
Decrease in senior debt	—	(25,996)	—
Net proceeds from stock issuance	—	—	—
Proceeds from the exercise of stock options	310	43	—
Net cash provided by financing activities	192,097	213,620	36,688
Net increase in cash and cash equivalents	94,620	9,530	34,233
Cash and cash equivalents at beginning of year	151,995	142,466	108,233
Cash and cash equivalents at end of year	246,615	151,995	142,466
Supplemental disclosure of cash flow information			
Cash paid during the period for:			
Interest	$ 7,714	$ 8,107	$ 10,727
Income taxes	$ 8,769	$ 4,410	$ 154
Noncash activities:			
Real estate acquired in settlement of loans	$ —	$ 6,103	$ 6,107
Loans to facilitate the sale of other real estate owned	$ —	$ 3,050	$ 4,535
Transfer of loans receivable to loans held for sale	$ 21,701	$ 31,784	$ 40,806

See accompanying notes to consolidated financial statements.

(1) Summary of Significant Accounting Policies

Preferred Bank (the Bank) is a full service commercial bank and is engaged primarily in commercial, real estate, and international lending to customers with businesses domiciled in the state of California. The accounting and reporting policies of the Bank are in accordance with accounting principles generally accepted in the United States of America and conform to general practices in the banking industry. The following is a summary of the Bank's significant accounting policies.

(a) Basis of Presentation

The financial statements include the accounts of Preferred Bank and its subsidiary, PB Investment and Consulting, Inc. (collectively the "Bank" or the "Company"). The consolidated financial statements of the Company have been prepared in conformity with accounting principles generally accepted in the United States of America.

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions. These estimates and assumptions affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting periods.

Material estimates that are particularly susceptible to significant changes in the near-term relate to the determination of the allowance for loan losses, and the fair value of loans, real estate owned, and securities. In connection with the determination of the allowance for loan losses, management obtains independent appraisals for significant properties, evaluates overall loan portfolio characteristics and delinquencies and monitors economic conditions.

The consolidated financial statements reflect management's evaluation of subsequent events through the date of issuance of this Annual Report on Form 10-K.

(b) Reverse Stock Split

At the May 24, 2011 Annual Meeting of Shareholders, the shareholders of the Bank approved the proposal to authorize the Board of Directors in its discretion, without further authorization of the Bank's shareholders, to amend the Bank's Articles of Incorporation to effect a reverse split of the Bank's common stock by a ratio of one for five ("Reverse Stock Split"). The approval of the Reverse Stock Split was also subject to receipt of an Order of Exemption from the California Department of Business Oversight, which the Bank received on June 17, 2011. Upon receipt of the Order of Exemption, the Bank's Board of Directors amended the Bank's Articles of Incorporation to reflect the effect of the Reverse Stock Split of the Bank's common stock effective with respect to the shareholders of record at the close of business on June 17, 2011 (the "Effective Time"). At the Effective Time every five shares of Preferred Bank's pre-split common shares automatically were converted into one post-split share. The Reverse Stock Split affected all holders of common stock uniformly and did not affect any shareholder's percentage ownership interest in the Bank, except record holders of common stock otherwise entitled to a fractional share as a result of the Reverse Stock Split received a cash payment in lieu of such fractional share in a proportional amount based on the closing price of the common stock on the NASDAQ Stock Exchange at the Effective Time. Under the terms of the Bank's equity incentive plans, at the Effective Time, the number of shares reserved for issuance under the plans was proportionately decreased in accordance with the exchange ratio. Under the terms of the options granted under the plans, at the Effective Time, the number of shares covered by each option decreased and the conversion or exercise price per share increased in accordance with the exchange ratio. After giving effect to the Reverse Stock Split, we have retroactively adjusted the number of common shares outstanding at December 31, 2010 to 13,188,305. Accordingly, all references in the accompanying consolidated statements of financial condition, statements of operations and statements of changes in shareholders' equity to the number of common stock shares and earnings per share amounts have been retroactively adjusted for all periods presented. The number of authorized common shares is 20,000,000 subsequent to the Reverse Stock Split.

(c) Principles of Consolidation

The financial statements include the accounts of the Company and its subsidiary, PB Investment and Consulting, Inc. All intercompany transactions and accounts have been eliminated in consolidation.

(d) Cash and Cash Equivalents

Cash and cash equivalents include cash and due from banks, and federal funds sold, all of which have original or purchased maturities of less than 90 days. Included in the Bank's cash balances are cash reserves required by FRB in the amounts of $2.3 million and $3.1 million as of December 31, 2013 and 2012, respectively.

(e) Investment Securities

The Bank classifies its debt and equity securities in two categories: held-to-maturity or available-for-sale. Securities that could be sold in response to changes in interest rates, increased loan demand, liquidity needs, capital requirements, or other similar factors are classified as securities available-for-sale. These securities are carried at fair value. Unrealized holding gains or losses, net of the related tax effect, on available-for-sale securities are excluded from income and are reported as a separate component of shareholders' equity as other comprehensive income net of applicable taxes until realized. Realized gains and losses from the sale of available-for-sale securities are determined on a specific-identification basis. Securities classified as held-to-maturity are those that the Bank has the positive intent and ability to hold until maturity. These securities are carried at amortized cost, adjusted for the amortization or accretion of premiums or discounts. At December 31, 2013 and 2012, there were zero and $979,000 classified in the held-to-maturity portfolio.

At each reporting date, the Bank performs an impairment analysis on its investment securities portfolio, following FASB standards in identifying whether a market for an asset or liability is distressed or inactive, determining whether an entity has the intent and ability to hold a security to its anticipated recovery and whether an investment is other-than-temporarily-impaired. If it is determined that the impairment is other than temporary for equity securities, the impairment loss is recognized in earnings equal to the difference between the investment's cost and its fair value. If it is determined that the impairment is other-than-temporary for debt securities, the Bank will recognize the credit component of an other-than-temporary impairment in earnings and the non-credit component in other comprehensive income when the Bank does not intend to sell the security and it is more likely than not that the Bank will not be required to sell the security prior to recovery. The new cost basis is not changed for subsequent recoveries in fair value.

Premiums and discounts are amortized or accreted over the life of the related held-to-maturity or available-for-sale security as an adjustment to yield using the effective-interest method. Dividend and interest income are recognized when earned.

(f) Loans and Loan Origination Fees and Costs

Loans that the Bank has both the intent and ability to hold for the foreseeable future, or until maturity, are held at carrying value, less related allowance for loan loss and deferred loan fees. Interest income is recorded on an accrual basis in accordance with the terms of the loans.

Loan origination fees, offset by certain direct loan origination costs and commitment fees, are deferred and recognized in income as a yield adjustment using the effective interest yield method over the contractual life of the loan, which approximates the interest method. If a commitment expires unexercised, the commitment fee is recognized as income.

Loans on which the accrual of interest has been discontinued are designated as non-accrual loans. The accrual of interest on loans is discontinued when principal or interest is past due 90 days or more unless the loan is both well secured and in the process of collection. In addition, a loan that is current may be placed on non-accrual status if the Bank believes substantial doubt exists as to whether the Bank will collect all principal and contractual due interest. When loans are placed on non-accrual status, all interest previously accrued, but not collected, is reversed against current period interest income. Interest received on non-accrual loans is subsequently recognized as interest income or applied against the principal balance of the loan. The loan is generally returned to accrual status when the borrower has brought the past due principal and interest payments current and, in the opinion of management, the borrower has demonstrated the ability to make future payments of principal and interest as scheduled.

Loans are considered for full or partial charge-offs in the event that they are impaired, considered collateral dependent, principal or interest is over 90 days past due, the loan lacks sufficient collateral protection and are not in the process of collection. The Bank also considers charging off loans in the event of any of the following circumstances: 1) the impaired loan balances are not covered by the fair value of the collateral or discounted cash flow; 2) the loan has been identified for charge-off by regulatory authorities; and 3) any overdrafts greater than 90 days.

The Bank measures a loan for impairment when it is “probable” that it will be unable to collect all amounts due (i.e. both principal and interest) according to the contractual terms of the loan agreement. A loan is also considered impaired when the recorded investment in the loan is less than the present value of expected future cash flows (discounted at the loan’s effective interest rate). By definition, all loans classified as troubled debt restructures are considered impaired and measured for impairment. The measurement of impairment is based on (1) the present value of the expected future cash flows of the impaired loan discounted at the loan’s original effective interest rate, (2) the observable market price of the impaired loan, or (3) the fair value of the collateral of a collateral-dependent loan. The amount by which the recorded investment of the loan exceeds the measure of the impaired loan is recognized by recording a valuation allowance with a corresponding charge to the provision for loan losses. All loans classified as “substandard” or “doubtful” are analyzed for impairment. The Bank recognizes interest income on impaired loans based on its existing methods of recognizing interest income on non-accrual loans.

Troubled Debt Restructured (“TDR”) loans are defined by ASC 310-40, “Troubled Debt Restructurings by Creditors” and ASC 470-60, “Troubled Debt Restructurings by Debtors,” and evaluated for impairment in accordance with ASC 310-10-35. The concessions may be granted in various forms, including reduction in the stated interest rate, reduction in the amount of principal amortization, forgiveness of a portion of a loan balance or accrued interest, or extension of the maturity date.

(g) Allowance for Loan and Lease Losses

The allowance for loan and lease losses is maintained at a level considered adequate to provide for losses that are probable and reasonably estimable. The adequacy of the allowance for loan losses is based on management’s evaluation of the collectability of the loan and lease portfolio and that evaluation is based on historical loss experience and other significant factors.

The methodology we use to estimate the amount of our allowance for loan and lease losses is based on both objective and subjective criteria. While some criteria are formula driven, other criteria are subjective inputs included to capture environmental and general economic risk elements which may trigger losses in the loan portfolio.

Specifically, our allowance methodology contains four elements: (a) amounts based on specific evaluations of impaired loans; (b) amounts of estimated losses on loans classified as ‘special mention’ and ‘substandard’ that are not already included in impaired loan analysis; (c) amounts of estimated losses on loans not adversely classified which we refer to as ‘pass’ based on historical loss rates by loan type; and (d) amounts for estimated losses on loans rated as pass and substandard that are not already included in impaired analysis based on economic and other qualitative factors that indicate probable losses were incurred but were not captured through the other elements of our allowance adequacy analysis.

Impaired loans are identified at each reporting date based on certain criteria and individually reviewed for impairment. A loan is considered impaired when it is probable that the Bank will be unable to collect all amounts due according to the original contractual terms of the loan agreement.

Our loan portfolio, excluding impaired loans which are evaluated individually, is categorized into several segments for purposes of determining allowance amounts by loan segment. The loan pools we currently evaluate are: commercial & industrial, trade finance, real estate – land, mini-perm, real estate construction and other loans. Each of these segments is then further broken down based on industry, geography or property type or a combination thereof. Within these loan pools, we then evaluate loans rated as pass credits, separately from adversely classified loans. The allowance amounts for pass rated loans are determined using historical loss rates developed through migration analyses. The adversely classified loans are further grouped into three credit risk rating categories: special mention, substandard and doubtful.

Finally, in order to ensure our allowance methodology is incorporating recent trends and economic conditions, we apply environmental and general economic factors to our allowance methodology including: credit concentrations; delinquency trends; economic and business conditions; the quality of lending management and staff; lending policies and procedures; loss and recovery trends; nature and volume of the portfolio; non-accrual and problem loan trends; and other adjustments for items not covered by other factors. We base our allowance for loan losses on an estimation of probable losses inherent in our loan portfolio.

(h) Other Real Estate Owned (OREO)

Other real estate owned, consisting of real estate acquired through foreclosure or other proceedings, is initially stated at fair value of the property based on appraisal, less estimated selling costs. Any cost in excess of the fair value at the time of acquisition is accounted for as a loan charge-off and deducted from the allowance for loan and lease losses. A valuation allowance is established for any subsequent declines in value through a charge to earnings. Operating expenses of such properties, net of related income, and gains and losses on their disposition are included in loss on sale of REO and related expense, as appropriate.

(i) Bank Furniture and Fixtures

Bank furniture and fixtures are stated at cost, less accumulated depreciation and amortization. Depreciation on furniture and equipment is computed on a straight-line method over the estimated useful lives of the assets, generally three to five years. Leasehold improvements are capitalized and amortized on the straight-line method over the estimated useful life of the improvement or the term of lease, whichever is shorter. Buildings are amortized on the straight-line method over 30 years.

(j) Comprehensive Income

Comprehensive income consists of net income and net unrealized gains (losses) on securities available-for-sale and is presented in the statements of operations and comprehensive (loss) income.

(k) Income Taxes

The Bank accounts for income taxes using the asset and liability method. The objective of the asset and liability method is to establish deferred tax assets and liabilities for the temporary differences between the financial reporting basis and the tax basis of the Bank's assets and liabilities at enacted tax rates expected to be in effect when such amounts are realized or settled. A valuation allowance is established for deferred tax assets if based on the weight of available evidence, it is more likely than not that some portion or all of the deferred tax assets will not be realized. The valuation allowance is sufficient to reduce the deferred tax assets to the amount that is more likely than not to be realized.

(l) Earnings per Share

Earnings per share (EPS) are computed on a basic and diluted basis. Basic EPS is computed by dividing net income adjusted by presumed dividend payments and earnings on unvested restricted stock by the weighted average number of common shares outstanding. Losses are not allocated to participating securities. Unvested shares of restricted stock are excluded from basic shares outstanding. Diluted EPS reflects the potential dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock or resulted in the issuance of common stock that shares in the earnings of the Bank.

(m) Share-Based Compensation

Employees and directors participate in the following stock option compensation plans--the 1992 Stock Option Plan, Interim Stock Option Plan and the 2004 Equity Incentive Plan. Share-based compensation expense for all share-based payment awards is based on the grant-date fair value estimated in accordance with the provisions of ASC 718. The Bank recognizes these compensation costs on a straight-line basis over the requisite service period for the entire award of generally three to five years, and options expire between four and ten years from the date of grant. See Note 13 for further discussion.

(n) Bank-Owned Life Insurance (BOLI)

Bank-owned life insurance policies are carried at their cash surrender value. Income from BOLI is recognized when earned.

(o) Use of Estimates

Management of the Bank has made a number of estimates and assumptions relating to the reporting of assets and liabilities and the disclosure of contingent assets and liabilities to prepare these financial statements in conformity with accounting principles generally accepted in the United States of America. Actual results could differ from these estimates. The most significant estimates subject to change relates to the allowance for loan losses, the valuation of other real estate owned, and accounting for deferred tax assets. If the allowance is not adequate as of December 31, 2013 then additional losses could be realized in 2014. The carrying value of other real estate owned; if real estate values deteriorate further then the Bank could suffer additional losses on the disposition of its other real estate owned. If estimates related to future cash flows used to determine fair value of investment securities is incorrect then the Bank could be subject to further other-than-temporary impairment charges.

(p) Risk and Uncertainties

Preferred Bank is a commercial bank which takes in deposits from businesses and individuals and provides loans to real estate developers/owners and individuals. The Bank’s main source of revenue is interest income from loans and investment securities and its main expenses are interest expense paid on deposits and borrowings and compensation expenses to its employees. The Bank’s operations are located and concentrated primarily in Southern California and are likely to remain so for the foreseeable future.

As of December 31, 2013, approximately 91% of the total dollar amount of the Bank’s loans and commitments was related to collateral or borrowers located within California. Because the Bank’s loan portfolio is concentrated in commercial and residential real estate, the performance of these loans may be affected by further continued weakness or further negative changes in California’s economic and business conditions and the real estate market of Southern California. Deterioration in economic conditions could have a material adverse effect on the quality of the Bank’s loan portfolio and the demand for its products and services. In addition, during this period of economic slowdown, the Bank has experienced a decline in collateral values and an increase in delinquencies and defaults. Further declines in collateral values and an increase in delinquencies and defaults increase the possibilities and severity of losses. California real estate is also subject to certain natural disasters, such as earthquakes, fires, floods and mud slides, as well as civil unrest, which are typically not covered by the standard hazard insurance policies maintained by the Bank’s borrowers. Uninsured disasters may render borrowers unable to repay loans made by the Bank and lower collateral values.

(q) Segment Reporting

Through our branch network, the Bank provides a broad range of financial services to individuals and companies located primarily in Southern California. Their services include demand, time and savings deposits and real estate, business and consumer lending. While our chief decision makers monitor the revenue streams of our various products and services, operations are managed and financial performance is evaluated on a company-wide basis. Accordingly, the Bank considers all of our operations are aggregated in one reportable operating segment.

(r) Recently Issued Accounting Standards

Following are the recently issued updates to the codification of U.S. Accounting Standards (ASUs), which are the most relevant to the Bank.

In May 2011, the FASB issued ASC update No. 2011-04, “Fair Value Measurement (Topic 820), Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs.” The amendments in this Update result in common fair value measurement and disclosure requirements in U.S. GAAP and IFRSs. Consequently, the amendments change the wording used to describe many of the requirements in U.S. GAAP for measuring fair value and for disclosing information about fair value measurements. Some of the amendments clarify the application of existing fair value measurement requirements. Other amendments change a particular principle or requirement for measuring fair value or for disclosing information about fair value measurements. The amendments that clarify the application of existing fair value measurements and disclosure requirements include the following: 1) application of the highest and best use and valuation premise concepts, 2) measuring the fair value of an instrument classified in a reporting entity’s shareholders’ equity, and 3) disclosures about fair value measurements that clarify that a reporting entity should disclose quantitative information about the unobservable inputs used in a fair value measurement that is categorized within Level 3 of the fair value hierarchy. The amendments in this Update that change a particular principle or requirement for measuring fair value or disclosing information about fair value measurements include the following: 1) measuring the fair value of financial instruments that are managed within a portfolio, 2) application of premiums and discounts in a fair value measurement, and 3) additional disclosures about fair value measurements. The amendments in this Update are to be applied prospectively and are effective during interim and annual periods beginning after December 15, 2011. The adoption of this guidance did not have a material impact on the Bank.

In December 2011, the Financial Accounting Standards Board ("FASB") issued authoritative guidance related to balance sheet offsetting. The new guidance requires disclosures about assets and liabilities that are offset or have the potential to be offset. These disclosures are intended to address differences in the asset and liability offsetting requirements under U.S. GAAP and International Financial Reporting Standards. This new guidance will be effective for the Bank for interim and annual reporting periods beginning January 1, 2013, with retrospective application required and has not had a material impact on the Bank’s consolidated financial statements.

In February 2013, the FASB issued ASU 2013-02, Comprehensive Income (Topic 220), which amends authoritative guidance related to reporting of amounts reclassified out of Accumulated Other Comprehensive Income (Loss). The amendment requires all private and public companies to present the effects of significant income amounts reclassified on the face of the Statement of Operations if the reclassification is required by U.S. GAAP. The amendment is effective for annual and interim reporting periods beginning after December 15, 2012 for public companies, and does not have a material impact on the Bank’s consolidated financial statements.

(2) Securities Available-for-Sale and Held-to-Maturity

Financial instruments that potentially subject the Bank to concentrations of credit risk consist primarily of loans and investments. The Bank monitors its exposure to such risks and the concentrations may be impacted by changes in economic, industry or political factors.

The Bank aims to maintain a diversified investment portfolio including issuer, sector and geographic stratification, where applicable, and has established certain exposure limits, diversification standards and review procedures to mitigate credit risk.

Other than U.S. government agencies (Fannie Mae and Freddie Mac, when combined), the Bank has no exposure within its investment portfolio to any single issuer greater that 10% of equity capital.

The carrying value of our held-to-maturity investment securities was zero at December 31, 2013 and $979,000 at December 31, 2012. The table below shows the amortized cost, gross unrealized gains and losses and estimated fair value of securities held-to-maturity as of December 31, 2013 and 2012:

	December 31, 2013			
	Amortized cost	Gross unrealized gains	Gross unrealized losses	Estimated fair value
	(In thousands)			
Collateralized debt obligations	$ —	$ —	$ —	$ —

	December 31, 2012			
	Amortized cost	Gross unrealized gains	Gross unrealized losses	Estimated fair value
	(In thousands)			
Collateralized debt obligations	$ 979	$ 3	$ —	$ 982

The table below shows the amortized cost, the total other-than-temporary impairment recognized in accumulated other comprehensive income, gross unrealized gains and losses, and estimated fair value of securities available for sale as of December 31, 2013 and 2012.

	December 31, 2013				
	Amortized cost	Gross unrealized gains	Gross unrealized losses	Non-credit other-than-temporary impairment	Estimated fair value
	(In thousands)				
Corporate notes	$ 49,319	$ 2,831	$ (1,075)	$ —	$ 51,075
Mortgage-backed securities	51,240	656	(554)	—	51,342
Collateralized mortgage obligations	9,978	15	(135)	—	9,858
Municipal securities	22,332	25	(1,308)	—	21,049
Principal-only strip securities	4,559	—	(53)	—	4,506
Mutual funds – government bond funds	5,000	—	(160)	—	4,840
Total securities available-for-sale	$ 142,428	$ 3,527	$ (3,285)	$ —	$ 142,670

	December 31, 2012				
	Amortized cost	Gross unrealized gains	Gross unrealized losses	Non-credit other-than-temporary impairment	Estimated fair value
			(In thousands)		
Corporate notes	$ 49,347	$ 3,092	$ (1,458)	$ —	$ 50,981
Mortgage-backed securities	95,873	1,103	(52)	—	96,924
Collateralized mortgage obligations	24,664	67	(71)	—	24,660
Municipal securities	24,823	988	—	—	25,811
Principal-only strip securities	5,719	127	—	—	5,846
Mutual funds – government bond funds	5,000	—	(27)	—	4,973
Collateralized debt obligations	1,863	1	—	(317)	1,547
Total securities available-for-sale	$ 207,289	$ 5,378	$ (1,608)	$ (317)	$ 210,742

Gross unrealized losses on securities available-for-sale and the fair value of the related securities, aggregated by investment category and length of time that the individual securities have been in a continuous unrealized loss position, at December 31, 2013 and 2012 are as follows:

	December 31, 2013					
	Less than 12 months		12 months or greater		Total	
	Estimated fair value	Unrealized losses	Estimated fair value	Unrealized losses	Estimated fair value	Unrealized losses
			(In thousands)			
Corporate notes	$ 4,895	$ (105)	$ 9,655	$ (970)	$ 14,550	$ (1,075)
Mortgage-backed securities	4,634	(53)	10,540	(554)	15,174	(607)
Collateralized mortgage obligations	8,445	(135)	—	—	8,445	(135)
Municipal securities	18,897	(1,308)	—	—	18,897	(1,308)
Mutual funds – government bond funds	—	—	4,840	(160)	4,840	(160)
Principal-only strip securities	—	—	—	—	—	—
Total securities available-for-sale	$ 36,871	$ (1,601)	$ 25,035	$ (1,684)	$ 61,906	$ (3,285)

	December 31, 2012					
	Less than 12 months		12 months or greater		Total	
	Estimated fair value	Unrealized losses	Estimated fair value	Unrealized losses	Estimated fair value	Unrealized losses
	(In thousands)					
Corporate notes	$ —	$ —	$ 18,217	$ (1,458)	$ 18,217	$ (1,458)
Mortgage-backed securities	10,148	(52)	—	—	10,148	(52)
Collateralized mortgage obligations	3,519	(71)	—	—	3,519	(71)
Municipal securities	—	—	—	—	—	—
Mutual funds – government bond funds	—	—	4,973	(27)	4,973	(27)
Principal-only strip securities	—	—	—	—	—	—
Collateralized debt obligations	—	—	1,100	(317)	1,100	(317)
Total securities available-for-sale	$ 13,667	$ (123)	$ 24,290	$ (1,802)	$ 37,957	$ (1,925)

The Bank's investment portfolio is primarily comprised of corporate notes, U.S. government securities, collateralized mortgage obligations, municipal securities, and mortgage-backed securities.

Preferred Bank performs a regular impairment analysis on its investment securities portfolio and management has analyzed all investment securities which have an amortized cost that exceeds fair value as of December 31, 2012.

During 2013, the Bank sold all three collateralized debt obligations ("CDO's") which were in its available-for-sale portfolio as of December 31, 2012, which consisted of pools of bank trust preferred securities. As of December 31, 2012, the amortized cost of all three CDO's exceeded the fair value. The sale of these securities was due to what was then named the Final Volcker Rule of the Dodd-Frank Act of 2010 (The rule was later amended to allow for Banks to own this type of asset class).

Management recognized credit-related OTTI for the CDO securities, based on the guidance of the Investments – Debt and Equity Securities Topic of FASB ASC, of $7,000 and $24,000 for the years ended December 31, 2013 and 2012 respectively.

As of December 31, 2013, the Bank owned 4 corporate securities where the amortized cost exceeded fair value. The total amortized cost of these securities was $15.6 million and their fair value was $14.6 million. Management performed an analysis on all of the issuers of these securities which focused on the recent financial results of the companies, capital ratios and long-term prospects of the issuer and deemed all 4 corporate securities to be temporarily impaired. The Bank had recorded no credit-related OTTI charges on corporate securities during 2013, and also had zero OTTI charges relating to corporate securities in 2012 and 2011.

As of December 31, 2013, the Bank owned 2 collateralized mortgage obligations ("CMO") where the amortized cost exceeded fair value. The total amortized cost of these securities was $8.6 million and the total fair value was $8.4 million. Management determined that the CMO securities were not other-than-temporarily impaired as of December 31, 2013. This determination was made based on several factors such as debt rating of the securities, amount of credit protection, the Bank's intent and ability to hold the securities until a recovery in value and the determination that it is not more likely than not that the Bank will be required to sell the securities prior to recovery of amortized cost basis.

The Bank owns 20 municipal investment securities. Each of these securities carries an investment-grade rating. As of December 31, 2013, 17 of these issues were in an unrealized loss position. The total amortized cost of these securities was $20.2 million and the total fair value was $18.9 million. Management determined that none of the municipal securities was other-than-temporarily impaired as of December 31, 2013. This determination was made based on several factors such as the Bank's intent and ability to hold the securities until a recovery in value and the determination that it is not more likely than not that the Bank will be required to sell the securities prior to recovery of amortized cost basis. In addition, management reviews all of the ratings on the municipal investment securities, recent ratings changes, as well as the length of time that the security has been impaired to determine whether the security is other than temporary impaired.

At December 31, 2013, the Bank held one agency-backed principal-only (PO) strip security with an amortized cost of $4.6 million and a fair value of $4.5 million. Based on factors including the Bank's intent and ability to hold the security until a recovery in value and the determination that it is not more likely than not that the Bank will be required to sell the security prior to recovery of amortized cost basis, management determined that the security was not other-than-temporarily impaired as of December 31, 2013.

At December 31, 2013, there were 24 and 8 investment securities that were in an unrealized loss position for less than 12 months and for 12 months or greater, respectively. Temporary impairments related to corporate notes, mortgage-backed securities, and municipal securities are primarily attributable to declining market prices caused by lack of trading liquidity in these instruments and in the case of corporate notes, resulted from increases in credit spreads between U.S. Treasuries and corporate bonds subsequent to the date that these securities were purchased. None of the securities in the Bank's investment portfolio rely on an insurance wrap as a credit enhancement. Management believes that it is not probable that the Bank will not receive all amounts due under the contractual terms of these securities. If economic conditions worsen, or if the financial condition of specific issuers within these portfolios deteriorates, then the Bank could record OTTI charges in 2014 on specific investments within these portfolios.

Cash proceeds from sales of securities available-for-sale totaled $37.1 million, $11.1 million and $20.5 million in 2013, 2012, and 2011, respectively. Net realized gains or losses for sales and calls of securities totaled a loss of $2.0 million, a gain of $554,000, and a gain of $81,000 for the years ended December 31, 2013, 2012, and 2011 respectively. Gain from mutual funds was $0, $21,000, and $0 for the years ended December 31, 2013, 2012, and 2011, respectively. Investment securities having a fair value of approximately $107.7 million and $125.0 million were pledged to secure governmental deposits, treasury tax and loan deposits, borrowing lines from the Federal Reserve Bank and FHLB as of December 31, 2013 and 2012, respectively.

The amortized cost and estimated fair value of securities at December 31, 2013 and 2012, by contractual maturity, are shown below. Mortgage-backed securities are classified in accordance with their estimated average life. Expected maturities differ from contractual maturities mainly due to prepayment rates; changes in prepayment rates will affect a security's average life.

	2013		**2012**	
	Available-for-Sale		**Available-for-Sale**	
	Amortized cost	**Estimated fair value**	**Amortized cost**	**Estimated fair value**
	(In thousands)			
Due in one year or less	$ —	$ —	$ —	$ —
Due after one year through five years	7,821	8,480	6,464	7,061
Due after five years through ten years	46,568	48,637	49,867	51,974
Due after ten years	88,039	85,553	150,958	151,707
Total	$ 142,428	$ 142,670	$ 207,289	$ 210,742

The following table provides a roll-forward of the amounts recognized in earnings for those debt securities that have been other-than-temporarily impaired because of credit losses which also have an other-than-temporary impairment due to non-credit factors recorded as a component of other comprehensive income for the year ended December 31, 2013 and 2012:

	Beginning Balance as of December 31, 2012	Additions for the amount related to the credit loss for which OTTI was not previously recognized	Reductions for Securities Sold	Reductions for securities for which the amount previously recognized in OCI was recognized in earnings	Additional increases to the amount related to credit loss for which OTTI loss was previously recognized	Reductions for increases in cash flows expected to be collected that are recognized over the remaining life of the security	Ending Balance as of December 31, 2013
				(in thousands)			
Amounts related to credit losses on debt securities for which a portion of OTTI was recognized in OCI	$ 1,641	$ —	$ (1,648)	$ —	$ 7	$ —	$ —

	Beginning Balance as of December 31, 2011	Additions for the amount related to the credit loss for which OTTI was not previously recognized	Reductions for Securities Sold	Reductions for securities for which the amount previously recognized in OCI was recognized in earnings	Additional increases to the amount related to credit loss for which OTTI loss was previously recognized	Reductions for increases in cash flows expected to be collected that are recognized over the remaining life of the security	Ending Balance as of December 31, 2012
				(in thousands)			
Amounts related to credit losses on debt securities for which a portion of OTTI was recognized in OCI	$ 1,617	$ —	$ —	$ —	$ 24	$ —	$ 1,641

(3) Loans and Leases and Allowance for Loan and Lease Losses

The loans and leases portfolio as of December 31, 2013 and 2012 is summarized as follows:

	2013	2012
	(In thousands)	
Real estate-mini perm	$ 871,539	$ 672,647
Real estate-construction	73,285	74,410
Commercial	338,680	324,753
Trade finance	39,640	47,413
Other Loans	287	330
Gross loans	1,323,431	1,119,553
Less:		
Allowance for loan and lease losses	(19,494)	(20,607)
Deferred loan fees, net	(2,562)	(2,019)
Loans excluding loans held for sale	1,301,375	1,096,927
Loans held for sale	6,207	12,150
Total loans, net	$ 1,307,582	$ 1,109,077

The majority of the Bank's loans is to customers and businesses in the state of California and/or secured by properties located primarily in the greater Los Angeles metropolitan area. All loans are made based on the same credit standards regardless of where the customers and/or collateral properties are located.

The Bank had $14.0 million of non-accrual loans and leases at December 31, 2013 compared to $26.1 million at December 31, 2012. These loans and leases had interest due, but not recognized, of approximately $1.1 million and $1.8

million in 2013 and 2012, respectively. The Bank had zero loans past due 90 or more days and still accruing interest as of both December 31, 2013 and December 31, 2012.

The following tables depict the Bank's past due loans by class as of December 31, 2013 and 2012:

December 31, 2013 Loan Class:	30-89 Days Accruing	90+ Days Still Accruing	Non-accrual & Non-current	Total Past Due	Non-accrual Current
			(in thousands)		
Real estate - Mini-perm					
R/E - Residential	$ —	$ —	$ —	$ —	$ —
R/E - Commercial	—	—	597	597	1,458
Total R/E - Mini-perm	—	—	597	597	1,458
Real Estate - Construction					
Construction - Residential	—	—	3,300	3,300	—
Construction - Commercial	—	—	—	—	—
Total R/E - Construction	—	—	3,300	3,300	—
Commercial and Industrial	—	—	2,482	2,482	—
Trade Finance	—	—	—	—	—
Other	—	—	—	—	—
Loans held for sale	$ —	$ —	$ 6,207	$ 6,207	$ —
Total as of December 31, 2012	$ —	$ —	$ 12,586	$ 12,586	$ 1,458

December 31, 2012 Loan Class:	30-89 Days Accruing	90+ Days Still Accruing	Non-accrual & Non-current	Total Past Due	Non-accrual Current
			(in thousands)		
Real estate - Mini-perm					
R/E - Residential	$ —	$ —	$ 727	$ 727	$ —
R/E - Commercial	5,382	—	1,265	6,647	—
Total R/E - Mini-perm	5,382	—	1,992	7,374	—
Real Estate - Construction					
Construction - Residential	—	—	5,543	5,543	—
Construction - Commercial	5,400	—	—	5,400	—
Total R/E - Construction	5,400	—	5,543	10,943	—
Commercial and Industrial	376	—	11,460	11,836	—
Trade Finance	—	—	—	—	—
Other	—	—	—	—	—
Loans held for sale	$ —	$ —	$ 7,150	$ 7,150	$ —
Total as of December 31, 2011	$ 11,158	$ —	$ 26,145	$ 37,303	$ —

The following tables depict the Bank's total non-accrual loans by class for the years ended December 31, 2013 and 2012:

Loan Class	**December 31, 2013**	**2012**
	(In thousands)	
Real Estate-Mini-Perm:		
R/E - Residential	$ —	$ 727
R/E - Commercial	2,055	1,265
Total R/E-Mini-Perm	2,055	1,992
Real Estate - Construction:		
Construction-Residential	3,300	5,543
Construction-Commercial	—	—
Total R/E - Construction	3,300	5,543
Commercial and Industrial	2,482	11,460
Trade Finance	—	—
Other	—	—
Loans held for sale	6,207	7,150
Total non-accrual loans	$ 14,044	$ 26,145

A troubled debt restructuring ("TDR") is a formal modification of the terms of a loan when the lender, for economic or legal reasons related to the borrower's financial condition, grants a concession to the borrower. The concessions may be granted in various forms, including change in the stated interest rate, reduction in the loan balance or accrued interest, or extension of the maturity date with a stated interest rate lower than the current market rate.

TDRs may be designated as performing or non-performing. A TDR may be designated as performing if the loan has demonstrated sustained performance under the modified terms. The period of sustained performance may include the periods prior to modification if prior performance met or exceeded the modified terms. For non-performing restructured loans, the loan will remain on non-accrual status until the borrower demonstrates a sustained period of performance, generally six consecutive months of payments. The Bank had $403,000 and $727,000 in total performing restructured loans as of December 31, 2013 and 2012, respectively. Non-performing restructured loans were $7.7 million and $7.2 million at December 31, 2013 and 2012, respectively. All TDRs are included in the balance of impaired loans.

The following tables provide information on loans modified as TDRs during the year ended December 31, 2013 and 2012:

	Loans Modified as TDRs During the Year Ended December 31, 2013		
	Number of Contracts	**Pre-modification Outstanding Recorded Investment**	**Post-modification Outstanding Recorded Investment**
		(Dollars in thousands)	
Real Estate – Mini-Perm:			
Residential	—	$ —	$ —
Commercial	1	6,573	6,207
Real Estate – Construction:			
Residential	—	—	—
Commercial	—	—	—
Commercial & Industrial	—	—	—
Trade Finance	—	—	—
Total	1	$ 6,573	$ 6,207

	Loans Modified as TDRs During the Year Ended December 31, 2012		
	Number of Contracts	**Pre-modification Outstanding Recorded Investment**	**Post-modification Outstanding Recorded Investment**
		(Dollars in thousands)	
Real Estate – Mini-Perm:			
Residential	—	$ —	$ —
Commercial	2	14,302	7,876
Real Estate – Construction:			
Residential	—	—	—
Commercial	—	—	—
Commercial & Industrial	1	230	230
Trade Finance	—	—	—
Total	3	$ 14,532	$ 8,106

Modification of the term of a loan is individually evaluated based on the loan type and the circumstances of the borrower's financial difficulty in order to maximize the bank's recovery. Real estate mini-perm TDRs were primarily loans where we have modified the scheduled payments to interest only terms for a given period of time, normally one year. We expect to collect the balance of the loan as property cash flows and/or the guarantor's global cash flow improves to allow for the resumption of principal and interest payments. As of December 31, 2013 real estate mini-perm commercial TDRs modified with interest only terms totaled $6.2 million.

Subsequent to restructuring, a TDR that becomes delinquent, generally beyond 90 days for commercial and industrial and real estate mini-perm commercial loans, becomes non-accrual. There was one real estate mini-perm residential TDR with a recorded investment of $120,000, one real estate mini-perm commercial TDR with a recorded investment of $207,000, and one residential construction TDR with a recorded investment of $550,000 that subsequently defaulted during the year ended December 31, 2013. There was one real estate mini-perm residential TDR with a recorded investment of $171,000, three real estate mini-perm commercial TDRs with a combined investment of $752,000, and one commercial & industrial TDR with a recorded investment of $230,000 that subsequently defaulted during the year ended December 31, 2012.

All TDRs are included in the impaired loan valuation allowance process. All portfolio segments of TDRs are reviewed for necessary specific reserves in the same manner as impaired loans of the same portfolio segment which have not been identified as TDRs. The modification of the terms of each TDR is considered in the current impairment analysis of the respective TDR. For all portfolio segments of delinquent TDRs and when the restructured loan is less than the recorded investment in the loan, the deficiency is charged-off against the allowance for loan losses. If the loan is a performing TDR the deficiency is included in the specific allowance, as appropriate. As of December 31, 2013, the allowance for loan losses associated with TDRs was $0 for performing TDRs and $0 for non-performing TDRs.

Impaired loans and leases are those for which it is probable that we will not be able to collect all amounts due according to the contractual terms of the loan or lease agreement. The category of impaired loans and leases is not comparable with the category of non-accrual loans and leases. Management may choose to place a loan or lease on non-accrual status due to payment delinquency or uncertain collectability, while not classifying the loan or lease as impaired if it is probable that we will collect all amounts due in accordance with the original contractual terms of the loan or lease. Impaired loans totaled $14.4 million and $25.0 million at December 31, 2013 and 2012, respectively. The total allowance for loan and lease losses related to these loans was $0 and $2.3 million at December 31, 2013 and 2012, respectively. Interest income recognized on impaired loans during 2013, 2012 and 2011 was $105,000, $598,000 and $1.2 million, respectively. At December 31, 2013, the Bank had zero commitments to lend additional funds to debtors whose loans are impaired.

Impaired loans, disaggregated by loan class and excluding loans held for sale, as of December 31, 2013 and 2012 are set forth in the following tables:

	Unpaid Principal Balance	Recorded Investment with allowance	Recorded Investment without allowance	Total Recorded investment	Related Allowance	Average Recorded Investment	Interest Income Recognized
				(in thousands)			
2013							
Real estate - mini-perm:							
Residential	$ —	$ —	$ —	$ —	$ —	$ —	$ —
Commercial	3,153	—	2,457	2,457	—	2,668	105
Total R/E mini-perm	3,153	—	2,457	2,457	—	2,668	105
Real estate - construction:							
Residential	5,187	—	3,300	3,300	—	4,422	—
Commercial	—	—	—	—	—	—	—
Total R/E construction	5,187	—	3,300	3,300	—	4,422	—
Commercial	2,482	—	2,482	2,482	—	3,322	—
Trade Finance	—	—	—	—	—	—	—
Other loans	—	—	—	—	—	—	—
Total impaired loans	$ 10,822	$ —	$ 8,239	$ 8,239	$ —	$ 10,412	$ 105

	Unpaid Principal Balance	Recorded Investment with allowance	Recorded Investment without allowance	Total Recorded investment	Related Allowance	Average Recorded Investment	Interest Income Recognized
				(in thousands)			
2012							
Real estate - mini-perm:							
Residential	$ 727	$ —	$ 727	$ 727	$ —	$ 727	$ 20
Commercial	7,834	726	6,573	7,299	317	7,328	252
Total R/E mini-perm	8,561	726	7,300	8,026	317	8,055	272
Real estate - construction:							
Residential	5,543	5,543	—	5,543	180	5,807	—
Commercial	—	—	—	—	—	—	—
Total R/E construction	5,543	5,543	—	5,543	180	5,807	—
Commercial	18,788	6,592	4,867	11,459	1,834	22,302	343
Trade Finance	—	—	—	—	—	—	—
Other loans	—	—	—	—	—	—	—
Total impaired loans	$ 32,892	$ 12,861	$ 12,167	$ 25,028	$ 2,331	$ 36,164	$ 615

During 2013, loans with a recorded investment of $26.6 million were sold for a net gain of $514,000. One loan, with a recorded investment of $6.2 million remained as held for sale as of December 31, 2013. During 2012, loans with a recorded investment of $18.1 million were sold for a net gain of $290,000. Two loans, with a total recorded investment of $12.2 million, remained as loans held for sale at December 31, 2012.

The following table details activity in the allowance for credit losses by portfolio segment for the year ended December 31, 2013. Allocation of a portion of the allowance to one particular portfolio segment does not indicate that it is no longer available to absorb losses in other portfolio segments.

	Real estate - Mini-perm		Real estate - Construction		Commercial	Trade			
2013	**Residential**	**Commercial**	**Residential**	**Commercial**	**& Industrial**	**Finance**	**Other**	**Unallocated**	**Total**
	(In thousands)								
Balance at beginning of period	$ 2,062	$ 8,911	$ 1,107	$ 548	$ 5,069	$ 427	$ 4	$ 2,479	$ 20,607
Provision for credit losses	(1,742)	249	220	(196)	2,976	(23)	(1)	1,766	3,250
Loans and leases charged off	(138)	(1,529)	(2,438)	—	(4,147)	(11)	—	—	(8,264)
Recoveries	902	519	1,951	163	366	—	—	—	3,901
Net charge offs	764	(1,010)	(487)	163	(3,781)	(11)	—	—	(4,363)
Balance at end of period	$ 1,084	$ 8,150	$ 840	$ 515	$ 4,264	$ 393	$ 3	$ 4,245	$ 19,494
Period-end amount allocated to:									
Loans individually evaluated for impairment	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ —	$ —
Loans collectively evaluated for impairment	1,084	8,150	840	515	4,264	393	3	4,245	19,494
Total	$ 1,084	$ 8,150	$ 840	$ 515	$ 4,264	$ 393	$ 3	$ 2,479	$ 19,494

The Bank's recorded investment in loans as of December 31, 2013 related to each balance in the allowance for credit losses by portfolio segment and disaggregated on the basis of the Bank's impairment methodology was as follows:

	Real estate - Mini-perm		Real estate - Construction			Trade		
	Residential	**Commercial**	**Residential**	**Commercial**	**Commercial**	**Finance**	**Other**	**Total**
	(In thousands)							
Loans individually evaluated for impairment	$ —	$ 2,458	$ 3,300	$ —	$ 2,483	$ —	$ —	$ 8,241
Loan collectively evaluated for impairment	112,901	756,180	21,380	48,605	336,197	39,640	287	1,315,190
Ending balance	$ 112,901	$ 758,638	$ 24,680	$ 48,605	$ 338,680	$ 39,640	$ 287	$ 1,323,431

The following table details activity in the allowance for credit losses by portfolio segment for the year ended December 31, 2012. Allocation of a portion of the allowance to one particular portfolio segment does not indicate that is no longer available to absorb losses in other portfolio segments.

	Real estate - Mini-perm		Real estate - Construction		Commercial	Trade			
2012	**Residential**	**Commercial**	**Residential**	**Commercial**	**& Industrial**	**Finance**	**Other**	**Unallocated**	**Total**
	(In thousands)								
Balance at beginning of period	$ 1,640	$ 13,192	$ 1,199	$ 1,153	$ 3,156	$ 523	$ 7	$ 2,848	$ 23,718
Provision for credit losses	1,050	5,504	(94)	1,434	12,177	101	(3)	(369)	19,800
Loans and leases charged off	(927)	(9,845)	—	(2,184)	(10,328)	(197)	—	—	(23,481)
Recoveries	299	60	2	145	64	—	—	—	570
Net charge offs	(628)	(9,785)	2	(2,039)	(10,264)	(197)	—	—	(22,911)
Balance at end of period	$ 2,062	$ 8,911	$ 1,107	$ 548	$ 5,069	$ 427	$ 4	$ 2,479	$ 20,607
Period-end amount allocated to:									
Loans individually evaluated for impairment	$ —	$ 317	$ 180	$ —	$ 1,834	$ —	$ —	$ —	$ 2,331
Loans collectively evaluated for impairment	2,062	8,594	927	548	3,235	427	4	2,479	18,276
Total	$ 2,062	$ 8,911	$ 1,107	$ 548	$ 5,069	$ 427	$ 4	$ 2,479	$ 20,607

The Bank's recorded investment in loans as of December 31, 2012 related to each balance in the allowance for credit losses by portfolio segment and disaggregated on the basis of the Bank's impairment methodology was as follows:

	Real estate - Mini-perm		Real estate - Construction			Trade		
	Residential	**Commercial**	**Residential**	**Commercial**	**Commercial**	**Finance**	**Other**	**Total**
	(In thousands)							
Loans individually evaluated for impairment	$ 727	$ 7,299	$ 5,543	$ —	$ 11,459	$ —	$ —	$ 25,028
Loan collectively evaluated for impairment	58,794	605,827	30,804	38,063	313,294	47,413	330	1,094,525
Ending balance	$ 59,521	$ 613,126	$ 36,347	$ 38,063	$ 324,753	$ 47,413	$ 330	$ 1,119,553

As required by federal regulations, we classify our assets on a regular basis. In order to monitor the quality of our lending portfolio and quantify the risk therein, we maintain a loan grading system consisting of eight different categories (Grades 1-8). The grading system is used to determine, in part, the allowance for loan losses. The first four grades in the system are considered satisfactory, whereas the fifth grade is a transition grade known as "special mention". The other three grades (6-8) range from "substandard" to "doubtful" to a "loss" category. Loans graded as "loss" are charged-off in the period so rated. We use grades 6 and 7 of our loan grading system to identify potential problem assets for impairment analysis. In reviewing loans and evaluating the adequacy of the allowance, there are several risk characteristics considered. Those most relevant to the major portfolio segments includes vacancy and lease rates on commercial real estate, state of the general housing market, home prices, commercial real estate values and the impact of economic conditions and employment levels on the various businesses in our market area.

The following tables present weighted average risk grades and classified loans by class of loan as of December 31, 2013 and 2012. Classified loans include loans in risk grades 6 and 7, which correlate to substandard and doubtful for risk classification purposes.

2013	**Real Estate**		**Construction**		**Commercial**	**Trade**		**Total**
Grade:	**Residential**	**Commercial(1)**	**Residential**	**Commercial**	**& Industrial**	**Finance**	**Other**	**Loans**
(In thousands)								
Pass	$ 112,901	$ 753,304	$ 14,505	$ 48,605	$ 311,375	$ 37,090	$ 287	$ 1,278,067
Special Mention	—	2,877	—	—	19,970	—	—	22,847
Substandard	—	8,664	10,175	—	7,335	2,550	—	28,724
Doubtful	—	—	—	—	—	—	—	—
Total	$ 112,901	$ 764,845	$ 24,680	$ 48,605	$ 338,680	$ 39,640	$ 287	$ 1,329,638

(1) Real Estate – Commercial includes loans held for sale $6,207 with a Substandard rating.

2012	**Real Estate**		**Construction**		**Commercial**	**Trade**		**Total**
Grade:	**Residential**	**Commercial**	**Residential(2)**	**Commercial**	**& Industrial**	**Finance**	**Other**	**Loans**
(In thousands)								
Pass	$ 58,794	$ 607,489	$ 14,829	$ 38,063	$ 312,918	$ 47,412	$ 330	$ 1,079,835
Special Mention	—	—	—	—	—	—	—	—
Substandard	727	17,788	21,518	—	9,313	—	—	49,346
Doubtful	—	—	—	—	2,522	—	—	2,522
Total	$ 59,521	$ 625,277	$ 36,347	$ 38,063	$ 324,753	$ 47,412	$ 330	$ 1,131,703

(2) Real Estate – Commercial includes loans held for sale of $5,000 with a Pass rating and $7,150 with a Substandard rating.

(4) Bank, Premises, Furniture and Fixtures

As of December 31, 2013 and 2012, furniture and fixtures consists of the following:

	2013	**2012**
	(In thousands)	
Land and Building	$ 2,782	$ 2,782
Leasehold improvements	6,347	6,152
Furniture and fixtures	4,880	4,620
	14,009	13,554
Less accumulated depreciation and amortization	(9,804)	(9,171)
	$ 4,205	$ 4,383

Depreciation and amortization expense was $640,000, $650,000 and $739,000 for the years ended December 31, 2013, 2012 and 2011, respectively.

(5) Deposits

Time deposit accounts at December 31, 2013 mature as follows:

Year	**Maturities of time deposits**
	(In thousands)
2014	$ 547,162
2015	65,629
2016 & thereafter	85,033
	$ 697,824

At December 31, 2013 and 2012, approximately $35.2 million and $38.9 million, respectively, of the Bank's investment securities were pledged as collateral for certain public deposits. The aggregate amount of overdrafts that have been reclassified as loan balances was $31,000 and $24,000 at December 31, 2013 and 2012, respectively.

(6) Income Taxes

The income taxes expense (benefit) for the years ended December 31, 2013, 2012 and 2011 was as follows:

	2013	2012	2011
		(In thousands)	
Current income tax (benefit) expense:			
Federal	$ 5,597	$ 3,517	$ 1,755
State	1,699	(732)	200
	7,296	2,785	1,955
Deferred income tax (benefit) expense:			
Federal	3,828	(15,699)	(5,201)
State	1,166	(7,669)	(1,803)
	4,994	(23,368)	(7,004)
Income tax (benefit) expense:	$ 12,290	$ (20,583)	$ (5,049)

At December 31, 2013 and 2012, the current net income taxes receivables were $1.8 million and $542,000.

The components of the deferred tax assets and deferred tax liabilities as of December 31, 2013 and 2012 are as follows:

	2013	2012
	(in thousands)	
Deferred tax assets:		
Allowance for loan and lease losses	$ 8,522	$ 8,706
State taxes	626	62
Deferred compensation	371	251
Bank furniture and fixtures, net	1,375	1,376
Deferred stock units	1,379	1,379
Other than temporary impairment on securities	—	690
Non-qualified stock options	939	965
OREO	3,517	10,698
Net operating loss carryforward	1,083	1,657
Other	3,614	1,381
Accrued bonuses	1,569	—
AMT Credits	2,258	2,610
Gross deferred tax assets	25,253	29,775
Deferred tax liabilities:		
Unrealized gains on securities available-for-sale	(102)	(1,452)
Deferred loan costs	(736)	(327)
Discount accretion	(543)	(543)
FHLB stock	(400)	(400)
Low income housing tax credit	(72)	—
Other	(69)	(78)
Gross deferred liabilities	(1,922)	(2,800)
Valuation allowance	—	—
Net deferred tax assets	$ 23,331	$ 26,975

In assessing the realizability of deferred tax assets, management considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income during the periods in which those temporary differences become deductible. Management considers the projected future taxable income and tax planning strategies in making this assessment. Based upon the level of historical taxable income and projections for future taxable income over the periods in which the deferred tax assets are deductible, management believes it is more likely than not that the Bank will realize all benefits related to these deductible differences at December 31, 2013.

Pursuant to Sections 382 and 383 of the Internal Revenue Code, annual use of net operating loss and credit carryforwards may be limited in the event a cumulative change in ownership of more than 50 percentage points occurs within a three-year period. We determined that such an ownership change occurred as of June 21, 2010 as a result of stock issuances in 2010 and 2009. This ownership change resulted in estimated limitations on the utilization of tax attributes, including net operating loss carryforwards and tax credits. Although we fully expect to utilize all of the federal net operating loss carryforward prior to their expiration, the California net operating loss carryover has been significantly impacted by the IRC Sec. 382 limitation. We estimate that of approximately $83.5 million of the California net operating losses as of December 31, 2013 subject to $69.6 million are expected to expire in 2029 as they will be unutilized as a result of IRS Sec 382 limitation. This amounts to approximately $4.9 million of deferred tax assets which would not be realized. The remaining California net operating loss carryforward of the approximately $13.9 million at December 31, 2013, is subject to IRC Sec. 382 annual limitation amount of approximately $1.5 million.

As of December 31, 2013 and 2012, the Bank has federal net operating loss carryforwards of approximately $305,000, respectively, which, if unused, will begin to expire in 2030.

A reconciliation of the income tax expense (benefit) and the amount computed by applying the statutory federal income tax rate to the loss before income taxes is as follows for the years ended December 31, 2013, 2012 and 2011:

	2013		2012		2011	
	Amount	**Percentage**	**Amount**	**Percentage**	**Amount**	**Percentage**
			(In thousands)			
Statutory U.S. federal income tax	$ 11,021	35.0%	$ 1,151	35.0%	$ 2,515	35.0%
State taxes, net of federal benefit	1,862	5.9	(694)	(21.1)	519	7.2
Life insurance policies	(84)	(0.3)	(85)	(2.6)	(88)	(1.2)
Valuation allowance	—	—	(20,951)	(637.1)	(8,578)	(119.4)
Low income housing credits	(406)	(1.3)	—	—	—	—
Other	(103)	(0.3)	(4)	(0.1)	583	8.1
	$ 12,290	39.0%	$(20,583)	(625.9)%	$(5,049)	(70.3)%

The 2013 effective tax rate of 39.0% differs from the statutory rate primarily as a result of state taxes, income from bank owned life-insurance and low income housing tax credits. The 2012 effective tax rate was negative due to the reversal of the Bank's valuation on its deferred tax asset of $20.1 million. The 2011 net income tax benefit resulted from a provision for income taxes based on taxable earnings which was more than offset by a partial reversal of the Bank's deferred tax asset.

There were no unrecognized tax benefits for the years ended December 31, 2013 and 2012.

It is the policy of management to include any interest or penalties from income tax liabilities in the provision for income taxes. As of December 31, 2013 and 2012, the total amount of tax reserve, net of federal tax benefit, was $0 and $0, respectively, for uncertain tax positions. The Bank does not expect the amount of the unrecognized tax benefits to change significantly over the next 12 months.

The Bank files income tax returns in the U.S. federal jurisdiction and in the State of California. As a result of the 2009 and 2010 federal net operating loss carrybacks, the Bank's tax years from 2004 to 2010 were examined by the Internal Revenue Service (IRS). The IRS examination of the returns was finalized in April of 2012 resulting in the 2006, 2007, 2008 net assessment of approximately $449,000, including accrued interest of approximately $29,000, which was paid in February 2013. During 2010, the Bank was under audit by the California's Franchise Tax Board for the 2008 tax year and was assessed for an additional tax liability of $168,000 including interest of $14,000 in February 2011. The Bank is no longer subject to the U.S Federal and California tax examinations by tax authorities for the years before January 1, 2011 and January 1, 2010, respectively.

(7) Other Real Estate Owned

At December 31, 2013, OREO was comprised of 3 properties compared to 16 properties at December 31, 2012. During 2013, the Bank sold 13 OREO properties, at a net gain of $3.8 million. These gains are included in Loss (gain) on Sale of OREO and Related Expense in the Consolidated Statements of Operations and Comprehensive Income (Loss).

An analysis of the activity in the valuation allowance for other real estate losses for the years ended on December 31, 2013, 2012, and 2011 is as follows:

	2013	**2012**	**2011**
		(in thousands)	
Balance, beginning of the year	$ 22,036	$ 20,742	$ 18,235
Provision for losses	1,706	4,018	3,920
OREO disposal	(15,806)	(2,724)	(1,413)
Balance, end of the year	$ 7,936	$ 22,036	$ 20,742

The following table details the Bank's OREO properties by loan class as of December 31, 2013, and 2012, and 2011:

	2013		2012		2011	
	#	$	#	$	#	$
Loan class:	*(dollar amounts in thousands)*					
Real estate - Mini-perm						
Residential	2	$ 3,350	11	$ 15,127	10	$ 23,565
Commercial	1	2,252	3	7,829	3	8,316
Real estate - Construction						
Residential	—	—	1	3,051	1	5,461
Commercial	—	—	1	2,273	1	235
Commercial & Industrial	—	—	—	—	—	—
Trade Finance	—	—	—	—	—	—
Other	—	—	—	—	—	—
Total as of year end	3	$ 5,602	16	$ 28,280	15	$ 37,577

(8) Senior Debt and Other Borrowed Funds

On February 11, 2009, the Bank issued $26.0 million of unsecured senior debt in a pooled private placement transaction which carries the Federal Deposit Insurance Corporation's ("FDIC") guarantee under its Temporary Liquidity Guarantee Program. The issuance had a 3-year maturity and a fixed interest rate of 2.74% paid semiannually, and it matured on February 11, 2012. Under the Temporary Liquidity Guarantee Program, the FDIC provides a 100% guarantee of certain unsecured senior debt of eligible FDIC-insured institutions. As of December 31, 2013, the Bank has zero outstanding senior debt.

Advances from the Federal Home Loan Bank of San Francisco (FHLBSF) were $20.0 million and zero at December 31, 2013 and 2012, respectively. All advances are collateralized by commercial or residential real estate loans, FRC advances or by certain marketable investment securities (SBC). At December 31, 2013, approximately $188.5 million of the Bank's real estate loans was pledged as collateral.

The Bank had an approved short-term borrowings line available through the discount window at the Federal Reserve Bank of San Francisco (FRBSF) in the amount of $51.7 million. The Bank had no borrowing outstanding through the discount window outstanding as of December 31, 2013 or 2012.

(9) Commitments and Contingencies

Credit Extensions: As a financial institution, the Bank enters into a variety of financial transactions with its customers in the normal course of business. Many of these products do not necessarily entail present or future funded asset or liability positions, instead the nature of these is considered in the form of executor contracts.

Financial instrument transactions are subject to the Bank's normal credit standards, financial controls and risk-limiting, and monitoring procedures. Collateral requirements are determined on a case-by-case evaluation of each customer and product.

The Bank's exposure to credit risk under commitments to extend credit, standby letters of credit, and financial guarantees written is limited to the contractual amount of those instruments.

At December 31, 2013 and 2012, the Bank had commitments to fund loans of $354.5 million and $211.1 million, respectively. Other financial instruments with off-balance-sheet risk at December 31, 2013 and 2012 are as follows:

	2013	2012
	(In thousands)	
Commitments to extend credit	$ 354,463	$ 211,118
Commercial letters of credit	5,764	6,489
Standby letters of credit	12,057	6,309
Total	$ 372,284	$ 223,916

The Bank's exposure to credit losses in the event of non-performance by the other party to commitments to extend credit and standby letters of credit is represented by the contractual notional amount of those instruments. The Bank uses the same credit policies in making commitments and conditional obligations as it does for extending loan facilities to customers. The Bank evaluates each customer's credit-worthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by the Bank upon extension of credit, is based on management's credit evaluation of the counterparty.

Lease Commitments: The Bank is obligated under non-cancellable operating leases for the premises of its head office and certain branch offices. As of December 31, 2013, the future total minimum lease payments for the Bank's premises are as follows:

Year:	Total lease payment
	(In thousands)
2014	$ 1,935
2015	1,821
2016	1,693
2017	1,433
2018	1,199
Thereafter	1,278
	$ 9,359

Rental expense was $1.8 million, $1.3 million and $1.7 million for the years ended December 31, 2013, 2012 and 2011, respectively.

(10) Related Party Transactions

Loan and Commitments: The Bank has extended credit to certain directors and officers and companies in which they have an interest and certain shareholders which beneficially own more than 5% of the Bank's capital stock. In management's opinion, the loans to these related parties are made on substantially the same terms, including interest rates and collateral, as those made to nonrelated persons.

At December 31, 2013 and 2012, the aggregate loans (including commitments) to related parties were approximately $6.6 million (of which $0.8 million was outstanding) and $6.0 million (of which $0.8 million was outstanding), respectively. All related party loans were current at December 31, 2013 and 2012.

Changes in the outstanding loans to related parties are summarized as follows:

	2013	2012	2011
		(In thousands)	
Balance at beginning of year	$ 834	$ 2,092	$ 10,264
New loans	300	—	900
Net drawdowns (repayments)	(348)	(1,258)	(9,072)
Balance at end of year	$ 786	$ 834	$ 2,092

Deposits: The amount of deposits from related parties was $8.3 million and $2.7 million at December 31, 2013 and 2012, respectively.

(11) Restrictions on Cash Dividends, Regulatory Capital Requirements

The Bank has authorized 25,000,000 shares of preferred stock. The Board has the authority to issue the preferred stock in one or more series, and to fix the designations, rights, preferences, privileges, qualifications, and restrictions, including dividend rights, conversion rights, voting rights and terms of redemptions, liquidation preferences, and sinking fund terms, any or all of which may be greater than the rights of the common stock.

Under Section 1132 of the California Financial Code, funds available for cash dividend payments by a bank are restricted to the lesser of: (i) retained earnings or (ii) the bank's net income for its last three fiscal years (less any distributions to shareholders made during such period). Cash dividends may also be paid out of the greatest of: (i) retained earnings, (ii) net income for a bank's last preceding fiscal year, or (iii) net income of the Bank for its current fiscal year upon the prior approval of the Commissioner of Financial Institutions, State of California, without regard to retained earnings or net income for its prior three fiscal years.

As a result of a regulatory examination during 2013, the Memorandum of Understanding which the Bank entered into with the FDIC and CDBO on May 25, 2012 was terminated and the Bank entered into a new MOU with both the FDIC and the CDBO on October 1 2013, which among other things, restricts the payment of dividends without the prior approval of the FDIC and CDBO.

The Bank is subject to various regulatory capital requirements administered by the federal banking agencies. Failure to meet minimum capital requirements can initiate certain mandatory – and possibly additional discretionary – actions by regulators that, if undertaken, could have a direct effect on the Bank's financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Bank must meet specific capital guidelines that involve quantitative measures of the Bank's assets, liabilities, and certain off-balance-sheet items, as calculated under regulatory accounting policies. The Bank's capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings, and other factors.

The quantitative measures established by the regulation to ensure capital adequacy require the Bank to maintain amounts and ratios (set forth in the table below) of total and Tier 1 risk-based capital (as defined in the regulation) to risk-weighted assets (as defined) and of Tier 1 risk-based capital (as defined) to average assets (as defined). Management believes, as of December 31, 2013, that the Bank meets all capital adequacy requirements to which it is subject.

The Bank's actual capital and various regulatory required capital thresholds are presented in the following table:

	Actual		For capital adequacy purposes		To be well capitalized under prompt corrective action provision	
	Amount	**Ratio**	**Amount**	**Ratio**	**Amount**	**Ratio**
			(In thousands)			
As of December 31, 2013:						
Total risk-based capital	$ 225,373	15.03%	$119,959	≥ 8.00%	$ 149,949	≥ 10.00%
Tier 1 risk-based capital	206,617	13.78%	59,975	4.00%	89,964	6.00%
Leverage ratio	206,617	11.80%	59,975	4.00%	74,970	5.00%
As of December 31, 2012:						
Total risk-based capital	$ 196,466	14.98%	$104,921	≥ 8.00%	$ 131,152	≥ 10.00%
Tier 1 risk-based capital	180,021	13.73%	52,461	4.00%	78,691	6.00%
Leverage ratio	180,021	11.96%	52,461	4.00%	65,576	5.00%

(12) Share-Based Compensation

The Bank remunerates employees and directors through stock option compensation plans; the 1992 Stock Option Plan, Interim Stock Option Plan and the 2004 Equity Incentive Plan which are discussed below. Effective January 1, 2007, the Bank adopted FASB Accounting Standards Codification ("ASC") 718 "Compensation –Stock Compensation" ("ASC 718"). Share-based compensation expense for all share-based payment awards is based on the grant-date fair value estimated in accordance with the provisions of ASC 718. The Bank recognizes these compensation costs on a straight-line basis over the requisite service period for the entire award, which is the option vesting term of generally three to five years, for only those options expected to vest. The fair value of stock option awards was estimated using the Black-Scholes option pricing model with the grant-date assumptions and weighted-average fair value. When options are exercised, the Bank's policy is to issue new shares of stock. For the year ended December 31, 2013, 2012 and 2011, the Bank recognized share-based compensation expense of $2.5 million, $1.1 million and $1.1 million, respectively, resulting in the recognition of $403,000, $230,000 and $140,000 in related tax benefits, respectively.

The number of stock options and per stock option data has been adjusted to reflect the Bank's June 17, 2011 one-for-five reverse stock split.

1992 Stock Option Plan and Interim Stock Option Plan

The Bank's 1992 Stock Option Plan (the "1992 Plan") provides for granting of non-statutory stock options and incentive stock options to key full-time employees, officers, and the directors of the Bank. The number of shares authorized in this plan is 434,376 shares. The 1992 Stock Option Plan expired by its terms in 2003, and no shares are available for future grants. The options vest in installments of 20% each year and become fully vested after five years. Options under the 1992 Plan expire ten years after the grant date.

Because the 1992 Plan expired in 2003, the Bank did not issue any options under this Plan during 2013, 2012 or 2011.

In May 2003, April 2004 and June 2004, the Bank granted an additional 16,200, 9,600 and 25,000 stock options, respectively, to our employees and directors at exercise prices ranging from $53.45 to $95.05 per share under the Bank's Interim Stock Option Plan ("Interim Plan") which expired in 2004. Even though the terms of these stock options are consistent with the terms of the stock options granted under our 1992 Plan, these stock options are outside of the 1992 Plan because they were granted after the 1992 Plan's expiration. The Bank did not issue any options under the expired Interim Plan during 2013, 2012 and 2011.

The total intrinsic value of share options exercised during the year ended December 31, 2013, 2012 and 2011 was $0, $0, and $0, respectively, from the 1992 Plan and the Interim Plan. As of December 31, 2013, there was no compensation cost recognized that relates to options granted under the 1992 Plan and Interim Plan. The Bank did not recognize any tax benefits for the year ended December 31, 2013 under the 1992 Plan and the Interim Plan.

Under the 1992 Plan and the Interim Plan, the fair value of the options vested during the year ended December 31, 2013, 2012 and 2011 was $0, $0, and $0, respectively. No options were exercised during the same period.

The following is a summary of the transactions under the 1992 Plan and the Interim Plan for the years ended December 31, 2013:

	1992 Plan and Interim Plan		
	Number of Options	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life
Options outstanding as of December 31, 2010	52,160	82.56	
Granted	—	—	
Exercised	—	—	
Forfeited or expired	(750)	86.71	
Options outstanding as of December 31, 2011	51,410	$ 82.50	
Granted	—	—	
Exercised	—	—	
Forfeited or expired	(2,600)	84.89	
Options outstanding as of December 31, 2012	48,810	$ 82.37	
Granted	—	—	
Exercised	—	—	
Forfeited or expired	(17,580)	59.84	
Options outstanding as of December 31, 2013	31,230	$ 95.05	0.5 years
Options exercisable as of December 31, 2013	31,230	$ 95.05	0.5 years

As of December 31, 2013, the aggregate intrinsic value of options outstanding under the 1992 Plan and the Interim Plan was $0. As of December 31, 2013, stock options outstanding under the 1992 Plan and the Interim Plan were as follows:

	Options Outstanding			Options Exercisable		
Exercise Price Range	Number of Outstanding Options	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life	Number of Outstanding Options	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life
$25.00 - $49.99	—	$ —	—	—	$ —	—
$50.00 - $74.99	—	—	—	—	—	—
$75.00 - $99.99	31,230	95.05	0.5	31,230	95.05	0.5

2004 Equity Incentive Plan

The Bank’s 2004 Equity Incentive Plan (the “2004 Plan”) provides for granting of non-statutory stock options, incentive stock options and restricted share awards (RSA’s) to key full-time employees, officers, and the directors of the Bank. Stock options granted under the 2004 Plan have an exercise price equal to the fair value of the underlying common stock on the date of grant. Stock options granted under the 2004 Plan generally vest in installments between 20-33% each year, become fully vested after three to five years and expire between four to ten years from the date of grant.

Certain option and share awards provide for accelerated vesting if there is a change in control (as defined in the 2004 Plan). The number of shares authorized in this plan is 1,455,330 shares, as adjusted for the shares repurchased by the Company pursuant to the tender offer described below, whereby the shares repurchased were made available for future issuance under the 2004 Plan.

The total intrinsic value of share options exercised during the year ended December 31, 2013, 2012 and 2011 was $284,000, $23,000 and $0, respectively. As of December 31, 2013, the total compensation cost not yet recognized that relates to unvested options granted under the 2004 Plan was $2.6 million with a weighted-average recognition period of 1.5 years. The Bank recognized tax benefits of $115,000 and zero for the years ended December 31, 2013 and 2012 under the 2004 Plan.

For the years ended December 31, 2013, 2012 and 2011, the estimated weighted-average fair value per share of options granted under the 2004 Plan were as follows:

December 31,		
2013	**2012**	**2011**
$6.97	$4.12	$4.00

The estimated weighted-average fair value per share of options granted was estimated on the date of grant using the Black-Scholes option-pricing model with the following weighted-average assumptions:

	December 31,		
	2013	**2012**	**2011**
Weighted Average Assumptions:			
Expected Dividend Yield	0.00%	0.00%	0.00%
Expected Volatility	61.16%	70.54%	81.78%
Expected Term	3.6 Yrs.	3.0 Yrs.	3.0 Yrs.
Risk-Free Interest Rate	0.53%	0.31%	0.68%

Historically, expected volatility was determined based on the historical daily volatility of a set of California peer banks whose share volatility data are publicly available over a period equal to the expected term of the options granted, as a proxy for the Bank's historical daily volatility. Currently, the expected volatility is determined based on the historical daily volatility of the Bank's stock price over a period equal to the expected term of the options granted because there now exists enough historical daily trading price information of the common stock of Preferred Bank. The risk-free interest rate is based on the U.S. Treasury yield at the time of grant for a period equal to the expected term of the options granted. Dividend yield is computed over the four consecutive quarters preceding the date of grant.

The following information under the 2004 Plan is presented for the years ended December 31, 2013, 2012 and 2011:

The following is a summary of the transactions under the 2004 Plan for the years ended December 31, 2013, 2012 and 2011.

	December 31,		
	2013	**2012**	**2011**
	(In thousands)		
Grant Date Fair Value of Options Granted	$ 3,021	$ 1,303	$ 178
Fair Value of Options Vested	534	314	294
Total Intrinsic Value of Options Exercised	284	23	—
Cash Received from Options Exercised	309	43	—

2004 Plan

	Number of Options	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life
Options outstanding as of December 31, 2010	137,718	$ 40.40	
Granted	44,600	7.60	
Exercised	—	—	
Forfeited or expired	(10,488)	64.57	
Options outstanding as of December 31, 2011	171,830	$ 30.41	
Granted	327,500	8.91	
Exercised	(5,468)	7.95	
Forfeited or expired	(37,433)	9.97	
Options outstanding as of December 31, 2012	456,429	$ 16.93	
Granted	433,500	15.85	
Exercised	(34,795)	8.89	
Forfeited or expired	(96,212)	49.65	
Options outstanding as of December 31, 2013	758,922	$ 12.54	2.8 years
Options exercisable as of December 31, 2013	149,900	$ 8.57	1.7 years

As of December 31, 2013, the aggregate intrinsic value of options outstanding under the 2004 Plan was $5.4 million. As of December 31, 2013, stock options outstanding under the 2004 Plan were as follows:

	Options Outstanding			Options Exercisable		
Exercise Price Range	Number of Outstanding Options	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life	Number of Outstanding Options	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life
$0.00 - $24.99	758,772	$ 12.51	2.83	149,750	$ 8.45	1.69
$25.00 - $99.99	—	—	—	—	—	—
$100.00 - $124.99	—	—	—	—	—	—
$125.00 - $149.99	150	126.65	0.88	150	126.65	0.88

The following is a summary of the transactions for non-vested stock options under the 1992 Plan, the Interim Plan and the 2004 Plan for the year ended December 31, 2013:

	Number of Shares	Weighted Average Grant Date Fair Value
Non-Vested Options outstanding as of December 31, 2012	347,397	$ 4.12
Granted	433,500	$ 7.08
Forfeited or expired	(39,465)	$ 5.44
Vested	(132,410)	$ 5.19
Non-Vested Options outstanding as of December 31, 2013	609,022	$ 5.93

Restricted Stock Awards

The Bank's 2004 Plan provides for granting of RSA's to key full-time employees, officers, and the directors of the Bank. The Bank began granting RSAs in calendar year 2009. During the year ended December 31, 2013, the Bank granted 11,250 RSAs and recognized $1.3 million of compensation expense. The RSAs granted under the 2004 Plan have a one to three year vesting period and are to be distributed at the end of the vesting period. The total unrecognized compensation expense for outstanding RSAs was $1.7 million as of December 31, 2013, and will be recognized over 1.7 years.

The following is a summary of the transactions for non-vested RSAs under the 2004 Plan for the year ended December 31, 2013:

	Number of Shares	Weighted Average Grant Date Fair Value
Non-Vested RSAs as of December 31, 2010	207,400	$ 10.10
Granted	36,800	$ 7.49
Forfeited or expired	(4,150)	$ 7.58
Vested	(22,650)	$ 21.80
Non-Vested RSAs outstanding as of December 31, 2011	217,400	$ 8.49
Granted	8,600	$ 11.00
Forfeited or expired	(416)	$ 8.70
Vested	(91,917)	$ 8.46
Non-Vested RSAs outstanding as of December 31, 2012	133,667	$ 8.67
Granted	11,400	$ 19.40
Forfeited or expired	—	—
Vested	(95,667)	$ 9.06
Non-Vested RSAs outstanding as of December 31, 2013	49,400	$ 10.37

(13) Employee Benefit Plan

Effective January 1, 1994, the Bank began a 401k profit sharing plan for its eligible employees. Under the plan, the Bank matches 50% of a participant's contributions up to 6% of his/her salary subject to federal limitations on maximum contributions. Contributions made by the Bank for the years ended December 31, 2013, 2012 and 2011 totaled $210,000, $198,000 and $120,000, respectively.

(14) Bonus Plan

In April 1994, the Management Incentive Bonus Plan was approved. In December 2007 this Plan was amended and approved by the Board of Directors. The plan is administered by the Compensation Committee of the Board of Directors (the Committee). The Committee determines which employees may participate in the plan, the total amount of bonus payable to our employees each year, the amount of bonus to be carried over and paid in subsequent years and the allocation of the total amounts among our chairman, officers, and other employees. All awards are contingent upon the Bank attaining certain financial objectives with the exception of certain bonuses which may be awarded by the Compensation Committee irrespective of the certain financial targets as part of new employees' first year compensation. This is typically done as an alternative to a signing bonus. For the year ended December 31, 2012, the Bank did not meet its financial objectives required under the Plan. The Compensation Committee did, however, approve a discretionary bonus to certain officers in recognition for their efforts during 2012. For the year ended December 31, 2013, financial objectives required under the Plan were met. Total expense of the plan recorded by the Bank was $3.5 million, $1.5 million and $400,000 for 2013, 2012 and 2011, respectively. As of December 31, 2013 and 2012, the total bonus accrual included in the other liabilities amounted to $4.4 million and $1.5 million, respectively.

(15) Deferred Compensation Arrangements

In 1996, the Bank implemented deferred compensation arrangements for the Bank's senior officers and directors. Pursuant to the Plan, each participant receives benefits for his/her deferred compensation upon his/her retirement or termination of service with the Bank prior to retirement. At December 31, 2013 and 2012, liabilities recorded for the deferred compensation plan totaled approximately $882,000 and $596,000, respectively.

In order to economically fund its obligation under the deferred compensation arrangements, the Bank purchased single-premium life insurance policies under which the executive officers and directors are the insured, while the Bank is the owner and beneficiary thereof. At December 31, 2013 and 2012, the cash surrender value of the policies totaled $8.3 million and $8.0 million, respectively. During 2013, 2012 and 2011, the income on the insurance policies was $331,000, $329,000 and $333,000, respectively.

(16) Litigation

From time to time, the Bank is a party to claims and legal proceedings arising in the ordinary course of business. There are no pending legal proceedings or, to the best of management's knowledge, threatened legal proceedings, to which the Bank is a party which may have a material adverse effect upon the Bank's financial condition, results of operations, or liquidity.

(17) Earnings per Share

The following table summarizes the basic and diluted earnings (loss) per share calculations for the periods indicated:

	2013	2012	2011
	(In thousands, except per share data)		
Basic earnings per share:			
Net income	$ 19,199	$ 23,872	$ 12,234
Less: income and dividends allocated to participating securities	(201)	(323)	(195)
Net income allocated to common shareholders-basic	$ 18,998	$ 23,549	$ 12,039
Basic weighted average common shares outstanding	13,116,563	13,050,559	12,995,525
Basic earnings per share	$ 1.45	$ 1.80	$ 0.93
Diluted earnings per share:			
Net income	$ 19,199	$ 23,872	$ 12,234
Less: income and dividends allocated to participating securities	(201)	(323)	(195)
Net income allocated to common shareholders-diluted	$ 18,998	$ 23,549	$ 12,039
Basic weighted average common shares outstanding	13,116,563	13,050,559	12,995,525
Effect of dilutive securities – stock options	247,607	196,829	—
Diluted weighted average shares outstanding	13,364,320	13,247,390	12,995,525
Diluted earnings per share	$ 1.42	$ 1.78	$ 0.93

Earnings (loss) per share (EPS) are computed on a basic and diluted basis. Basic EPS excludes dilution and is computed by dividing net income available to common shareholders by the weighted average number of common shares outstanding for the period. Diluted EPS reflects the potential dilution that could occur if stock options or other contracts to issue common stock were exercised or converted to common stock that would then share in our earnings, excluding common shares in treasury. At December 31, 2013, 2012 and 2011, there were 656,376, 477,947 and 223,240 shares, respectively, related to such awards which were excluded from the computation of diluted EPS due to their anti-dilutive effect.

(18) Quarterly Financial Data (Unaudited)

The following tables summarize the quarterly unaudited financial data for 2013 and 2012:

Quarterly Financial Data (Unaudited)

	Three months ended			
Year Ended December 31, 2013	**March 31**	**June 30**	**September 30**	**December 31**
	(In thousands, except per share data)			
Interest income	$ 16,489	$ 16,243	$ 18,480	$ 18,514
Interest expense	1,830	1,820	1,967	2,112
Interest income before provision for credit losses	14,659	14,423	16,513	16,402
Provision for credit losses	—	250	1,200	1,800
Noninterest income	858	718	213	214
Noninterest expense	8,841	7,218	7,789	5,413
Income tax expense	2,646	3,404	2,705	3,535
Net income	$ 4,030	$ 4,269	$ 5,032	$ 5,868
Earnings per share				
Basic	$ 0.30	$ 0.32	$ 0.38	$ 0.45
Diluted	$ 0.30	$ 0.32	$ 0.37	$ 0.43

	Three months ended			
Year Ended December 31, 2012	**March 31**	**June 30**	**September 30**	**December 31**
	(In thousands, except per share data)			
Interest income	$ 15,191	$ 15,147	$ 15,194	$ 16,010
Interest expense	2,197	1,922	1,857	1,806
Interest income before provision for credit losses	12,994	13,225	13,337	14,204
Provision for credit losses	1,800	14,500	1,200	2,300
Noninterest income	618	1,475	667	749
Noninterest expense	8,856	8,026	9,143	8,154
Income tax expense (benefit)	(18,783)	(2,217)	834	(416)
Net income (loss)	$ 21,739	$ (5,609)	$ 2,827	4,915
Earnings(loss) per share				
Basic	$ 1.64	$ (0.43)	$ 0.21	$ 0.37
Diluted	$ 1.62	$ (0.43)	$ 0.21	$ 0.37

(19) Regulatory Matters

As a result of a regulatory examination during 2013, the Memorandum of Understanding which the Bank entered into with the FDIC and CDBO on May 25, 2012 was terminated and the Bank entered into a new MOU with both the FDIC and the CDBO on October 1 2013. Among other things, the MOU requires the Bank to maintain a Tier 1 Leverage Ratio of 10%, improve its BSA compliance, maintain a minimum Tier 1 Leverage Ratio of 10%, and to refrain from declaring or paying cash dividends to its shareholders and establishing new branches and offices without the prior written approval of the FDIC and CDBO. As of December 31, 2013, the Tier 1 Leverage Ratio of the Bank was 11.80%, exceeding the level required by the MOU. In response to the examination findings, management has dedicated a significant amount of time and resources toward strengthening its BSA and compliance programs and complying with the MOU. The Board of Directors and management are committed to meeting all of the requirements of the MOU and seeing to its earliest possible termination.

The impacts on dividends and capital minimums are further discussed in Footnote 11 above.

(20) Fair Value of Financial Instruments

ASC Topic 825, *Financial Instruments*, requires that an entity disclose the fair value of all financial instruments, as defined, regardless of whether recognized in the financial statements of the reporting entity. For purposes of determining fair value, Financial Instruments Topic of FASB ASC provides that the fair value of a financial instrument is the amount at which the instrument could be exchanged in a current transaction between willing parties, other than in a forced or liquidation sale.

The following methods and assumptions were used to estimate the fair value of each class of financial instruments.

(a) Cash Due from Banks, Federal Funds Sold and Securities Purchased under Resale Agreements

For cash and short-term instruments whose original or purchased maturity is less than 90 days, the carrying amount was assumed to be a reasonable estimate of fair value.

(b) Securities available-for-sale

For securities available-for-sale, fair values were based on quoted market prices obtained from market quotes. If a quoted market price was not available, fair value was estimated using quoted market prices for similar securities or if no quotes on similar securities were available, a discounted cash flow analysis was used based on a market discount rate and adjusted for pre-payments and defaults.

(c) Federal Home Loan Bank Stock

The carrying amounts approximate fair value, as the stock may be sold back to the Federal Home Loan Bank at carrying value.

(d) Loans

Loans are not measured at fair value on a recurring basis. Therefore, the following valuation discussion relates to estimating the fair value disclosures under Financial Instruments Topic of FASB ASC. Fair values are estimated for portfolios of loans with similar financial characteristics. Loans are segregated by type and further segmented into fixed and adjustable rate interest terms. The fair value estimates do not take into consideration an exit price concept as contemplated in ASC Topic 820, Fair Value Measurements and Disclosures. As a result, the value of the loan portfolio in the event the loans have to be sold outside the parameters of normal operating activities may differ from the fair value disclosed. The fair value of performing fixed rate loans is estimated by discounting scheduled cash flows through the estimated maturity using estimated market prepayment speeds and discount rates that reflect the market rate of the loans. The fair value of performing adjustable rate loans is estimated by discounting scheduled cash flows through the next repricing date. As these loans reprice frequently at market rates and the credit risk is not considered to be greater than normal, the market value is typically close to the carrying amount of these loans.

Loans measured for impairment based on the fair value of the underlying collateral are considered recorded at fair value on a non-recurring basis. Impaired loans include all of the Bank’s non-accrual loans and certain restructured loans, all of which are reviewed individually for the amount of impairment, if any. The fair value of each loan's collateral is generally based on estimated market prices from an independently prepared appraisal, which is then adjusted for the cost related to liquidating such collateral; such valuation inputs result in a non-recurring fair value measurement that is categorized as a Level 2 measurement. When adjustments are made to an appraised value to reflect various factors such as the age of the appraisal or known changes in the market or the collateral or if an appraisal value is based on a discount cash flow rather than a market comparable, such valuation inputs are considered unobservable and the fair value measurement is categorized as a Level 3 measurement. In addition, unsecured impaired loans are measured at fair value based generally on unobservable inputs, such as the strength of a guarantor, discounted cash flow models and management's judgment; the fair value measurement of these loans is also categorized as a Level 3 measurement. Fair values were estimated for portfolios of loans with similar financial characteristics. Each loan category was further segmented into fixed and adjustable rate interest terms and by performing and non-performing categories.

(e) Loans held for sale

Loans held for sale are required to be measured based on the lower of cost or fair value. When there are loans held for sale on the balance sheet, the Bank obtains quotes or bids on all or part of these loans directly from the purchasing parties if possible. Otherwise, current appraisals are the basis for valuation.

(f) Other Real Estate Owned

Upon acquisition, real estate obtained in the settlement of loans is recorded at fair value on the basis of appraised value less estimated costs to sell at the date of acquisition. This is a level 2 measurement. Every 6-12 months, fair value adjustments are made to all real estate owned on an individual basis based on the current updated appraised value of the property. In addition, the Bank sometimes makes further adjustments to carrying value of a property based on conservative estimates considering factors such as slow property sales in the region or broker opinions. These are considered level 3 measurements.

(g) Accrued Interest Receivable and Accrued Interest Payable

The carrying amounts of accrued interest receivable and accrued interest payable approximate its fair value due to their short-term nature.

(g) Deposits

The fair value of demand deposits, saving accounts, and certain money market deposits were assumed to be the amount payable on demand at the reporting date. The fair value of fixed maturity certificates of deposit was estimated using the rates currently offered for deposits with similar remaining maturities.

(h) FHLB Borrowings and Senior Debt

The fair value of FHLB borrowings and Senior debt was based on rates currently offered for borrowings with similar remaining maturities.

(i) Commitment to Extend Credit and Letters of Credit

The majority of our commitments to extend credit carry market interest rates if converted to loans. Because these commitments are generally unassignable by either the borrower or us, they only have value to the borrower and us. The estimated fair value is not material. The fair value of letters of credit was based on fees currently charged for similar agreements or on the estimated cost to terminate them or otherwise settle the obligations with the counterparties at the reporting date.

The carrying amount and estimated fair value of assets and liabilities as of December 31, 2013 and 2012 is detailed on the table below.

	December 31, 2013				
	Carrying amount	Estimated fair value	Level 1	Level 2	Level 3
	(In thousands)				
Assets:					
Cash and cash equivalents	$ 246,615	$ 246,615	$ 246,615	$ —	$ —
Securities available-for-sale	142,670	142,670	4,840	137,830	—
Loans, net of allowance and net deferred loan fees	1,301,375	1,326,216	—	2,665	1,323,551
Loans held for sale	6,207	6,207	—	6,207	—
Accrued interest receivable	5,378	5,378	—	5,378	—
Federal Home Loan Bank stock	5,296	5,296	—	5,296	—
Customers' liabilities on acceptances	2,061	2,061	—	2,061	—
Liabilities:					
Demand deposits and savings:					
Noninterest-bearing	$ 338,530	$ 338,530	$ —	$ 338,530	$ —
Interest-bearing	492,960	441,829	—	441,829	—
Time deposits	697,824	699,329	—	699,329	—
FHLB borrowings and Senior Debt	20,000	20,000	—	20,000	—
Accrued interest payable	983	983	—	983	—
Bank's liabilities on acceptances outstanding	2,061	2,061	—	2,061	—
Off-balance sheet financial instruments:					
Commitments to extend credit and letters of credit	474	474	—	474	—

	December 31, 2012				
	Carrying amount	**Estimated fair value**	**Level 1**	**Level 2**	**Level 3**
	(In thousands)				
Assets:					
Cash and cash equivalents	$ 151,995	$ 151,995	$ 151,995	$ —	$ —
Securities held-to-maturity	979	982	—	982	—
Securities available-for-sale	210,742	210,742	4,973	204,221	1,548
Loans, net of allowance and net deferred loan fees	1,096,927	1,122,138	—	2,274	1,119,864
Loans held for sale	12,150	12,150	—	12,150	—
Accrued interest receivable	5,646	5,646	—	5,646	—
Federal Home Loan Bank stock	4,282	4,282	—	4,282	—
Customers' liabilities on acceptances	1,961	1,961	—	1,961	—
Liabilities:					
Demand deposits and savings:					
Noninterest-bearing	$ 446,734	$ 446,734	$ —	$ 446,734	$ —
Interest-bearing	346,862	357,769	—	346,862	—
Time deposits	563,931	565,376	—	563,931	—
FHLB borrowings and Senior Debt	968	968	—	968	—
Bank's liabilities on acceptances outstanding	1,961	1,961	—	1,691	—
Off-balance sheet financial instruments:					
Commitments to extend credit and letters of credit	169	169	—	169	—

The fair value estimates do not reflect any premium or discount that could result from offering the instruments for sale. Potential taxes and other expenses that would be incurred in an actual sale or settlement are not reflected in amounts disclosed. The fair value estimates are dependent upon subjective estimates of market conditions and perceived risks of financial instruments at a point in time and involve significant uncertainties resulting in variability in estimates with changes in assumptions.

The Bank adopted ASC Topic 820, *Fair Value Measurements and Disclosures,* or ASC 820, on January 1, 2008, and determined the fair values of its financial instruments based on the fair value hierarchy established in ASC 820. ASC 820 defines fair value, establishes a three-level fair value hierarchy based on the quality of inputs used to measure fair value and expands disclosures about fair value measurements.

The three-level categorizations to measure the fair value of assets and liabilities are as follows:

Level 1 - Quoted prices in active markets for identical assets or liabilities.

Level 2 - Observable prices in active markets for similar assets or liabilities; prices for identical or similar assets or liabilities in markets that are not active; directly observable market inputs for substantially the full term of the asset and liability; market inputs that are not directly observable but are derived from or corroborated by observable market data.

Level 3 - Unobservable inputs based on the Bank's own judgments about the assumptions that a market participant would use.

The Bank uses the following methodologies to measure the fair value of its financial assets on a recurring basis:

- Corporate notes – The Bank measures fair value of corporate notes by using quoted market prices for similar securities or dealer quotes, a level 2 measurement.

- Municipal securities – The Bank measures fair value of state and municipal securities by using quoted market prices for similar securities or dealer quotes, a level 2 measurement.

- U.S. Government Agencies – The Bank measures fair value of U.S. Government agency securities by using quoted market prices for similar securities or dealer quotes, a level 2 measurement.

- Mortgage-backed securities – The Bank measures fair value of mortgage-backed securities by using quoted market prices for similar securities or dealer quotes, a level 2 measurement.

- Collateralized mortgage obligations – The Bank measures fair value of collateralized mortgage obligations by using quoted market prices for similar securities or dealer quotes, a level 2 measurement.

- Collateralized debt obligations – The Bank uses a discounted cash flow analysis to determine the fair value of the four collateralized debt obligations which is level 3 measurement. The discount rate is determined by using a market interest rate for a similarly rated single issuer corporate security plus 100 basis points of illiquidity premium using loss rates determined by the financial health of the underlying issuer banks in each pool.

- Principal-only strip securities - The Bank measures fair value of principal-only strip securities by using quoted market prices for similar securities or dealer quotes, a level 2 measurement.

- Mutual funds (government bond funds) – The Bank measures fair value based on the quoted market price at the reporting date, a level 1 measurement.

The following table presents the Bank's hierarchy for its assets and liabilities measured at fair value on a recurring basis at December 31, 2013:

(In thousands)	Fair Value Measurements Using			
Assets	**Quoted Prices in Active Markets for Identical Assets (Level 1)**	**Significant Other Observable Inputs (Level 2)**	**Significant Unobservable Inputs (Level 3)**	**Balance at December 31, 2013**
Securities, available-for-sale:				
Mutual funds – government bond funds	$ 4,840	$ —	$ —	$ 4,840
Corporate notes	—	51,075	—	51,075
Principal-only strips	—	4,506	—	4,506
Mortgage-backed securities	—	51,342	—	51,342
Collateralized mortgage obligations	—	9,858	—	9,858
Municipal securities	—	21,049	—	21,049
Total	$ 4,840	$ 137,830	$ —	$ 142,670

The following table presents the Bank's hierarchy for its assets and liabilities measured at fair value on a recurring basis at December 31, 2012:

(In thousands)	Fair Value Measurements Using			
Assets	**Quoted Prices in Active Markets for Identical Assets (Level 1)**	**Significant Other Observable Inputs (Level 2)**	**Significant Unobservable Inputs (Level 3)**	**Balance at December 31, 2012**
Securities, available-for-sale:				
Mutual funds – government bond funds	$ 4,973	$ —	$ —	$ 4,973
Corporate notes	—	50,981	—	50,980
Principal-only strips	—	5,846	—	5,846
Mortgage-backed securities	—	96,924	—	96,924
Collateralized mortgage obligations	—	24,660	—	24,660
Municipal securities	—	25,811	—	25,812
Collateralized debt obligations	—	—	1,547	1,547
Total	$ 4,973	$ 204,222	$ 1,547	$ 210,742

There were no significant transfers in or out of Level 1 and Level 2 fair value measurements during the year ended December 31, 2013.

The following table presents the Bank's reconciliation and income statement classification of gains and losses for all assets measured at fair value on a recurring basis using significant unobservable inputs (Level 3) for year ended December 31, 2013:

	Fair Value Measurements Using Significant Unobservable Inputs(Level 3) (Dollars in thousands)				
	Beginning Balance as of December 31, 2012	**Sale of Securities**	**Realized Gains or Losses in Earnings (Expense)**	**Unrealized Gains or Losses in Other Comprehensive Income**	**Ending Balance as of December 31, 2013**
ASSETS:					
Securities, available-for-sale:					
Collateral debt obligations	$ 1,547	$ (1,540)	$ (7)	$ —	$ —

The following table presents the Bank's reconciliation and income statement classification of gains and losses for all assets measured at fair value on a recurring basis using significant unobservable inputs (Level 3) for year ended December 31, 2012:

	Fair Value Measurements Using Significant Unobservable Inputs(Level 3) (Dollars in thousands)				
	Beginning Balance as of December 31, 2011	**Purchases, Issuance and Settlements**	**Realized Gains or Losses in Earnings (Expense)**	**Unrealized Gains or Losses in Other Comprehensive Income**	**Ending Balance as of December 31, 2012**
ASSETS:					
Securities, available-for-sale:					
Collateral debt obligations	$ 1,224	$ —	$ (24)	$ 347	$ 1,547

Impaired loans – On a non-recurring basis, the Bank measures the fair value of impaired collateral dependent loans based on fair value of the collateral value which is derived from appraisals that take into consideration prices in observable transactions involving similar assets in similar locations in accordance with Receivables Topic of FASB ASC covering loan impairments. Collateral value determined based on recent independent appraisals are considered a level 2 measurement. Collateral values based on unobservable inputs that are supported by little or no market data and less current appraisals are considered a level 3 measurement.

Other real estate owned – Real estate acquired in the settlement of loans is initially recorded at fair value, less estimated costs to sell. The Bank records other real estate owned at fair value on a non-recurring basis. As from time to time, nonrecurring fair value adjustments to other real estate owned are recorded based on current appraisal value of the property, a Level 2 measurement, or management's judgment and estimation based on reported appraisal value, a Level 3 measurement.

The following table presents the Bank's hierarchy for its assets measured at estimated fair value on a nonrecurring basis through twelve months ended December 31, 2013, and the total losses resulting from these fair value adjustments for the twelve months ended December 31, 2013:

(In thousands)	Fair Value Measurements Using				
Assets	**Quoted Prices in Active Markets for Identical Assets (Level 1)**	**Significant Other Observable Inputs (Level 2)**	**Significant Unobservable Inputs (Level 3)**	**Balance at December 31, 2013**	**Year Ended December 31, 2013 Total Losses**
Impaired loans	$ —	$ —	$ 3,300	$ 3,300	$ (1,707)
Loans held for sale	—	—	6,207	6,207	(324)
Other real estate owned	—	—	—	—	—
Total Assets	$ —	$ —	$ 9,507	$ 9,507	$ (2,031)

The following table presents the Bank's hierarchy for its assets measured at estimated fair value on a nonrecurring basis through twelve months ended December 31, 2012, and the total losses resulting from these fair value adjustments for the year ended December 31, 2012:

(In thousands)	Fair Value Measurements Using				
Assets	**Quoted Prices in Active Markets for Identical Assets (Level 1)**	**Significant Other Observable Inputs (Level 2)**	**Significant Unobservable Inputs (Level 3)**	**Balance at December 31, 2012**	**Year Ended December 31, 2012 Total Losses**
Impaired loans	$ —	$ 2,274	$ 9,001	$ 11,275	$ (8,659)
Loans held for sale	—	12,150	—	12,150	(5,840)
Other real estate owned	—	21,816	6,464	28,280	(4,406)
Total Assets	$ —	$ 36,240	$ 15,465	$ 51,705	$ (18,905)

The following table represents quantitative information regarding the significant unobservable inputs used in significant Level 3 assets measured at fair value on a non-recurring basis at December 31, 2013 and 2012.

	At December 31, 2013 (Dollars In thousands)			
	Fair Value	**Valuation Technique**	**Unobservable Inputs**	**Range**
Assets:				
Impaired loans	3,300	Market comparables	Adjustments to appraisal value for Selling costs; Management judgment	6.0%

	At December 31, 2012 (Dollars In thousands)			
	Fair Value	**Valuation Technique**	**Unobservable Inputs**	**Range**
Assets:				
Impaired loans	9,001	Market comparables; Discounted cash flow	Adjustments to appraisal value for Selling costs; Management judgment	6.0%
OREO	6,464	Market comparables	Adjustments to appraisal value for selling costs*; Discount to reflect realizable value^; Management judgment	*4.0 – 6.0%; ^2.0 – 26.4%;

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Exchange Act, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

Dated: March 17, 2014

PREFERRED BANK
(Registrant)

By /s/ Li Yu
Li Yu
Chairman of the Board and Chief Executive Officer

Pursuant to the requirements of the Exchange Act, this report has been signed below by the following persons on behalf of the registrant in the capacities and on the dates indicated.

/s/ Li Yu Li Yu	Chairman of the Board and Chief Executive Officer (Principal executive officer)	March 17, 2014
/s/ Edward J. Czajka Edward J. Czajka	Executive Vice President and Chief Financial Officer (Principal financial and accounting officer)	March 17, 2014
/s/ J. Richard Belliston J. Richard Belliston	Director	March 17, 2014
/s/ William C. Y. Cheng William C.Y. Cheng	Director	March 17, 2014
/s/ Clark Hsu Clark Hsu	Director	March 17, 2014
/s/ Gary S. Nunnelly Gary S. Nunnelly	Director	March 17, 2014
/s/ Ching-Hsing Kao Ching-Hsing Kao	Director	March 17, 2014
/s/ Chih-Wei Wu Chih-Wei Wu	Director	March 17, 2014
/s/ Wayne Wu Wayne Wu	Director	March 17, 2014

INDEX TO EXHIBITS

Exhibit No.	Exhibit Description
3.1	Amended and Restated Articles of Incorporation(1)
3.2	Certificate of Determination of the Series A preferred Stock(4)
3.3	Amended and Restated Bylaws(1)
4.1	Common Stock Certificate(3)
10.1*	1992 Stock Option Plan(1)
10.2*	Management Incentive Bonus Plan(1)
10.3*	Deferred Compensation Plan(1)
10.4*	Stock Option Gain Deferred Compensation Plan(1)
10.5*	2004 Equity Incentive Plan(1)
10.6*	Form of Indemnification Agreement for directors and executive officers(1)
10.7*	Revised Bonus Plan(2)
10.8*	Deferred Compensation Plan-Deferred Stock Unit Agreement and Rabbi Trust
10.9*	Retention and Severance Agreement-Li Yu
12.1	Computation of Ratio of Earnings to Fixed Charges
31.1	Chief Executive Officer Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
31.2	Chief Financial Officer Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
32.1	Chief Executive Officer Certification Pursuant to 18 U.S.C. Section 1350, As Adopted Pursuant To Section 906 of the Sarbanes-Oxley Act of 2002
32.2	Chief Financial Officer Certification Pursuant to 18 U.S.C. Section 1350, As Adopted Pursuant To Section 906 of the Sarbanes-Oxley Act of 2002

(1) Incorporated by reference from Registrant's Registration Statement on Form 10 filed with the Federal Deposit Insurance Corporation on January 18, 2006.

(2) Incorporated by reference from Registrant's Registration Statement on Form 10 filed with the Federal Deposit Insurance Corporation on March 13, 2007.

(3) Incorporated by reference from Registrant's Registration Statement on Form 10 Amendment No. 1 filed with the Federal Deposit Insurance Corporation on February 2, 2006.

(4) Incorporated by reference from Current Report on Form 8-K filed with the Federal Deposit Insurance Corporation on June 10, 2010.

* Denotes management contract or compensatory plan or arrangement.

Exhibit 21.1

SUBSIDIARIES OF THE REGISTRANT

PB Investment and Consulting, Inc. (PBICI), a California corporation

Exhibit 31.1

CERTIFICATION PURSUANT TO RULE
13a-14(a) AND 15d-14(a),
AS ADOPTED PURSUANT TO
SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002

I, Li Yu, certify that:

1. I have reviewed this Annual Report on Form 10-K of Preferred Bank;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

   a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

   c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's Board of Directors (or persons performing the equivalent functions):

   a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

   b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: March 17, 2014

/s/ Li Yu

Li Yu
Chairman and Chief Executive Officer

Exhibit 31.2
CERTIFICATION PURSUANT TO RULE
13a-14(a) AND 15d-14(a),
AS ADOPTED PURSUANT TO
SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002

I, Edward J. Czajka, certify that:

1. I have reviewed this Annual Report on Form 10-K of Preferred Bank;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
   a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
   b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
   c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
   d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's Board of Directors (or persons performing the equivalent functions):
   a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
   b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: March 17, 2014

/s/ Edward J. Czajka
Edward J. Czajka
Executive Vice President and Chief Financial Officer

Exhibit 32.1

CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Annual Report of Preferred Bank (the “Bank”) on Form 10-K for the period ending December 31, 2013 as filed with the Federal Deposit Insurance Corporation on the date hereof (the “Report”), I, Li Yu, Chairman, President and Chief Executive Officer of the Bank, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

(1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 (15 U.S.C. 78m or 78o(d)); and

(2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Bank.

Date: March 17, 2014

/s/ Li Yu
Li Yu
Chairman and Chief Executive Officer

A signed original of this written statement required by Section 906, or other document authenticating acknowledging, or otherwise adopting the signature that appears in typed form within this version of this written statement required by Section 906, has been provided to the Bank and will be retained by the Bank and furnished to the Federal Deposit Insurance Corporation or its staff upon request.

Exhibit 32.2

CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Annual Report of Preferred Bank (the “Bank”) on Form 10-K for the period ending December 31, 2013 as filed with the Federal Deposit Insurance Corporation on the date hereof (the “Report”), I, Edward J. Czajka, Executive Vice President and Chief Financial Officer of the Bank, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

(1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 (15 U.S.C. 78m or 78o(d)); and

(2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Bank.

Date: March 17, 2014

/s/ Edward J. Czajka
Edward J. Czajka
Executive Vice President & Chief Financial Officer

A signed original of this written statement required by Section 906, or other document authenticating acknowledging, or otherwise adopting the signature that appears in typed form within this version of this written statement required by Section 906, has been provided to the Bank and will be retained by the Bank and furnished to the Federal Deposit Insurance Corporation or its staff upon request.

BYLAWS

OF

PREFERRED BANK

A CALIFORNIA BANKING CORPORATION

ARTICLE I

OFFICES

Section 1.1 PRINCIPAL EXECUTIVE OFFICE.

The principal executive office of the corporation shall be located at such place within the State of California as the board of directors shall from time to time determine.

Section 1.2 OTHER OFFICES.

Other offices may at any time be established by the board of directors, subject to the approval of the California State Banking Department, at any place or places where the corporation is qualified to do business.

ARTICLE II

MEETINGS OF SHAREHOLDERS

Section 2.1 PLACE OF MEETINGS.

All meetings of shareholders shall be held at the principal administrative office of the corporation or at any other place within the State of California which may be designated either by the board of directors or by the shareholders in accordance with these bylaws.

Section 2.2 ANNUAL MEETINGS.

The annual meeting shall be held each year at a date and time fixed in accordance with the bylaws. The board of directors by resolution shall designate the time, place and date (which shall be, in the case of the first annual meeting, not more than fifteen (15) months after the organization of the corporation and, in the case of all other annual meetings, no more than fifteen (15) months after the date of the last annual meeting) of the annual meeting of the shareholders for the election of directors and the transaction of any other proper business. If there is a failure to hold the annual meeting for a period of sixty (60) days after the date designated therefor or, if no date has been designated, for a period of fifteen (15) months after the organization of the corporation or after its last annual meeting, the superior court of the proper county may summarily order a meeting to be held upon the application of any shareholder after notice to the corporation giving it an opportunity to be heard. The shares represented at such meeting, either in person or by proxy, and entitled to vote thereat shall constitute a quorum for the purpose of such meeting, notwithstanding any provision of the articles or bylaws or in the California General Corporation Law.

Section 2.3 SPECIAL MEETINGS.

Special meetings of the shareholders, for the purpose of taking any action which is within the powers of the shareholders, may be called at any time by the chairman of the board, the chief executive officer, the president, the board of directors, or the holders of shares entitled to cast not less than ten percent (10%) of the votes at the meeting.

Section 2.4 NOTICE OF MEETINGS OF SHAREHOLDERS.

(a) Written notice of each meeting of shareholders, whether annual or special, shall be given to each shareholder entitled to vote thereat, either personally or by mail or other means of written communication, charges prepaid, addressed to such shareholder at the address of such shareholder appearing on the books of the corporation or given by such shareholder to the corporation for the purpose of notice. If any notice addressed to the shareholder at the address of such shareholder appearing on the books of the corporation is returned to the corporation by the United States Postal Service marked to indicate that the United States Postal Service is unable to deliver the notice to the shareholder at such address, all future notices shall be deemed to have been duly given without further mailing if the same shall be available for the shareholder upon written demand of the shareholder at the principal administrative office of the corporation for a period of one year from the date of the giving of the notice to all other shareholders. If no address appears on the books of the corporation or is given by the shareholder to the corporation for the purpose of notice, notice shall be deemed to have been given to such shareholder if sent by mail or other means of written communication addressed to the place where the principal administrative office of the corporation is located, or if published at least once in a newspaper of general circulation in the county in which the principal administrative office is located.

(b) All such notices shall be given not less than ten (10) days nor more than sixty (60) days before the meeting to each shareholder entitled to vote thereat. Any such notice shall be deemed to have been given at the time when delivered personally or deposited in the mail or sent by other means of written communication. An affidavit of mailing of any such notice in accordance with the foregoing provisions, executed by the secretary, assistant secretary or any transfer agent of the corporation, shall be prima facie evidence of the giving of the notice.

(c) All such notices shall state the place, date and hour of such meeting. In the case of a special meeting such notice shall also state the general nature of the business to be transacted at such meeting, and no other business may be transacted thereat. In the case of an annual meeting, such notice shall also state those matters which the board of directors at the time of the mailing of the notice intends to present for action by the shareholders.

(d) The notice of any meeting at which directors are to be elected shall include the names of nominees intended at the time of the notice to be presented by management for election.

(e) Upon request in writing that a special meeting of shareholders be called for any proper purpose, directed to the chairman of the board, chief executive officer, president, vice president or secretary by any person (other than the board) entitled to call a special meeting of shareholders, the officer forthwith shall cause notice to be given to the shareholders entitled to vote that a meeting will be held at a time requested by the person or persons calling the meeting, not less than thirty-five (35) nor more than sixty (60) days after receipt of the request.

Section 2.5 QUORUM.

The presence in person or by proxy of the holders of a majority of the shares entitled to vote at any meeting shall constitute a quorum for the transaction of business. The shareholders present at a duly called or held meeting at which a quorum is present may continue to transact business until adjournment, notwithstanding the withdrawal of enough shareholders to leave less than a quorum, if any action taken (other than adjournment) is approved by at least a majority of the shares required to constitute a quorum.

Section 2.6 ADJOURNED MEETINGS AND NOTICE THEREOF.

(a) Any shareholders' meeting, annual or special, whether or not a quorum is present, may be adjourned from time to time by vote of a majority of the shares, the holders of which are either present in person or by proxy thereat, but in the absence of a quorum, no other business may be transacted at any such meeting, except as provided in Section 2.5 of this Article II.

(b) When a shareholders' meeting is adjourned to another time or place, except as provided in this subsection (b), notice need not be given of the adjourned meeting if the time and place thereof are announced at the meeting at which the adjournment is taken. At the adjourned meeting the corporation may transact any business which might have been transacted at the original meeting. If the adjournment is for more than forty-five (45) days or if after the adjournment a new record date is fixed for the adjourned meeting, a notice of the adjourned meeting shall be given to each shareholder of record entitled to vote at the meeting.

Section 2.7 VOTING AND RECORD DATES.

(a) Voting Rights of Shares and Shareholders.

(1) Except as provided in Section 708 of the California General Corporation Law (election of directors) and except as may be otherwise provided in the articles of incorporation of this corporation, each outstanding share, regardless of class, shall be entitled to one vote on each matter submitted to a vote of shareholders.

(2) Any holder of shares entitled to vote on any matter may vote part of the shares in favor of the proposal and refrain from voting the remaining shares or vote them against the proposal, other than elections to office; but, if the shareholder fails to specify the number of shares such shareholder is voting affirmatively, it will be conclusively presumed that the shareholder's approving vote is with respect to all shares such shareholder is entitled to vote.

(b) Record Date Requirements.

(1) In order that the corporation may determine the shareholders entitled to notice of any meeting or to vote or entitled to receive payment of any dividend or other distribution or allotment of any rights or entitled to exercise any rights in respect of any other lawful action, the

board may fix, in advance, a record date, which shall not be more than sixty (60) nor less than ten (10) days prior to the date of such meeting nor more than sixty (60) days prior to any other action.

(2) If no record date is fixed:

(A) The record date for determining shareholders entitled to notice of or to vote at a meeting of shareholders shall be at the close of business on the business day preceding the day on which notice is given or, if notice is waived, at the close of business on the business day next preceding the day on which the meeting is held.

(B) The record date for determining shareholders entitled to give consent to corporate action in writing without a meeting, when no prior action by the board has been taken, shall be the day on which the first written consent is given.

(C) The record date for determining shareholders for any other purpose shall be at the close of business on the day on which the board adopts the resolution relating thereto, or the sixtieth (60th) day prior to the date of such other action, whichever is later.

(3) A determination of shareholders of record entitled to notice of or to vote at a meeting of shareholders shall apply to any adjournment of the meeting unless the board fixes a new record date for the adjourned meeting, but the board shall fix a new record date if the meeting is adjourned for more than forty-five (45) days from the date set for the original meeting.

(4) Shareholders as of the record date are entitled to notice and to vote or to receive the dividend, distribution or allotment of rights or to exercise the rights, as the case may be, notwithstanding any transfer of any shares on the books of the corporation after the record date, except as otherwise provided in the articles of incorporation of this corporation or by agreement or in the California General Corporation Law.

(c) Voting of Shares by Fiduciaries, Receivers, Pledgeholders and Minors.

(1) Subject to subdivision (3) of subsection (d) of this Section 2.7, shares held by an administrator, executor, guardian, conservator or custodian may be voted by such holder either in person or by proxy, without a transfer of such shares into the holder's name; and shares standing in

the name of a trustee may be voted by the trustee, either in person or by proxy, but no trustee shall be entitled to vote shares held by such trustee without a transfer of such shares into the trustee's name.

(2) Shares standing in the name of a receiver may be voted by such receiver; and shares held by or under the control of a receiver may be voted by such receiver without the transfer thereof into the receiver's name if authority to do so is contained in the order of the court by which such receiver was appointed.

(3) Subject to the provisions of Section 2.10 of this Article II and except where otherwise agreed in writing between the parties, a shareholder whose shares are pledged shall be entitled to vote such shares until the shares have been transferred into the name of the pledgee, and thereafter the pledgee shall be entitled to vote the shares so transferred.

(4) Shares standing in the name of a minor may be voted and the corporation may treat all rights incident thereto as exercisable by the minor, in person or by proxy, whether or not the corporation has notice, actual or constructive, of the nonage, unless a guardian of the minor's property has been appointed and written notice of such appointment given to the corporation.

(d) Voting of Shares by Other Corporations.

(1) Shares of this corporation standing in the name of another corporation, domestic or foreign, may be voted by such officer, agent or proxyholder as the bylaws of such other corporation may prescribe or, in the absence of such provision, as the board of such other corporation may determine or, in the absence of such determination, by the chairman of the board, president or any vice president of such other corporation, or by any other person authorized to do so by the chairman of the board, president or any vice president of such other corporation. Shares which are purported to be voted or any proxy purported to be executed in the name of a corporation (whether or not any title of the person signing is indicated) shall be presumed to be voted or the proxy executed in accordance with the provisions of this subdivision, unless the contrary is shown.

(2) Shares of this corporation owned by a subsidiary shall not be entitled to vote on any matter.

(3) Shares of this corporation held by this corporation in a fiduciary capacity, and any of its shares

held in a fiduciary capacity by its subsidiary, shall not be entitled to vote on any matter, except to the extent that the settlor or beneficial owner possesses and exercises a right to vote or to give the corporation binding instructions as to how to vote such shares.

(e) Voting of Shares Owned of Record by Two or More Persons.

(1) If shares stand of record in the names of two or more persons, whether fiduciaries, members of a partnership, joint tenants, tenants in common, husband and wife as community property, tenants by the entirety, voting trustees, persons entitled to vote under a shareholder voting agreement or otherwise, or if two or more persons (including proxyholders) have the same fiduciary relationship respecting the same shares, unless the secretary of the corporation is given written notice to the contrary and is furnished with a copy of the instrument or order appointing them or creating the relationship wherein it is so provided, their acts with respect to voting shall have the following effect:

(A) If only one votes, such act binds all;

(B) If more than one votes, the act of the majority so voting binds all;

(C) If more than one votes, but the vote is evenly split on any particular matter, each faction may vote the securities in question proportionately.

If the instrument so filed or the registration of the shares shows that any such tenancy is held in unequal interests, a majority or even split for the purpose of this section shall be a majority or even split in interest.

(f) Election of Directors; Cumulative Voting.

(1) Every shareholder complying with subdivision (2) of this subsection (f) of this Section 2.7 and entitled to vote at any election of directors may cumulate such shareholder's votes and give one candidate a number of votes equal to the number of directors to be elected multiplied by the number of votes to which the shareholder's shares are entitled, or distribute the shareholder's vote on the same principle among as many candidates as the shareholder thinks fit.

(2) No shareholder shall be entitled to cumulate votes (i.e., cast for any one or more candidates a

number of votes greater than the number of the shareholder's shares) unless such candidate's or candidates' names have been placed in nomination prior to the voting and the shareholder has given notice at the meeting prior to the voting of the shareholder's intention to cumulate the shareholder's votes. If any one shareholder has given such notice, all shareholders may cumulate their votes for candidates in nomination.

(3) In any election of directors, the candidates receiving the highest number of votes of the shares entitled to be voted for them, up to the number of directors to be elected, are elected.

(4) Elections for directors need not be by ballot unless a shareholder demands election by ballot at the meeting and before the voting begins.

Section 2.8 WAIVER OF NOTICE AND CONSENT OF ABSENTEES.

The transactions of any meeting of shareholders, either annual or special, however called and noticed and wherever held, are as valid as though had at a meeting duly held after regular call and notice, if a quorum is present either in person or by proxy, and if, either before or after the meeting, each of the persons entitled to vote, not present in person or by proxy, signs a written waiver of notice or a consent to the holding of the meeting, or an approval of the minutes thereof. All such waivers, consents and approvals shall be filed with the corporate records or made part of the minutes of the meeting. Attendance of a person at a meeting shall constitute a waiver of notice of such meeting, except when the person objects, at the beginning of the meeting, to the transaction of any business because the meeting is not lawfully called or convened and except that attendance at a meeting is not a waiver of any right to object to the consideration of matters required by law or these bylaws to be included in the notice but which was not so included, if such objection is expressly made at the meeting, provided, however, that any person making such objection at the beginning of the meeting or to the consideration of matters required to be but not included in the notice may orally withdraw such objection at the meeting or thereafter waive such objection by signing a written waiver thereof or a consent to the holding of the meeting or the consideration of the matter or an approval of the minutes of the meeting. Neither the business to be transacted at, nor the purpose of, any annual or special meeting of shareholders need be specified in any written waiver of notice, except that the general nature of a proposal to amend the articles of incorporation of the corporation and the proposals specified in subparagraphs (i) and (iii) through

(v) of subdivision (1) of subsection (c) of Section 2.9 of this Article II shall be so stated.

Section 2.9 ACTION WITHOUT A MEETING.

(a) Directors may be elected without a meeting by a consent in writing, setting forth the action so taken, signed by all of the persons who would be entitled to vote for the election of directors, provided that a director may be elected at any time to fill a vacancy not filled by the directors by the written consent of persons holding a majority of the outstanding shares entitled to vote for the election of directors.

(b) Any other action which, under any provision of the California General Corporation Law may be taken at any annual or special meeting of the shareholders, may be taken without a meeting, and without prior notice except as hereinafter set forth, if a consent in writing, setting forth the action so taken, is signed by the holders of outstanding shares having not less than the minimum number of votes that would be necessary to authorize or take such action at a meeting at which all shares entitled to vote thereon were present and voted.

(c) Unless the consents of all shareholders entitled to vote have been solicited in writing:

(1) Notice of any shareholder approval without a meeting, by less than unanimous written consent, of (i) a contract or other transaction between the corporation and one or more of its directors or any corporation, firm or association in which one or more of its directors has a material financial interest or is also a director, (ii) indemnification of an agent of the corporation as authorized by the articles of incorporation of the corporation, (iii) a reorganization of the corporation as defined in Section 181 of the California General Corporation Law, (iv) an election to wind up and dissolve the corporation, or (v) the distribution of shares, obligations or securities of any other corporation or assets other than money which is not in accordance with the liquidation rights of preferred shares if the corporation is in the process of winding up, shall be given at least ten (10) days before the consummation of the action authorized by such approval; and

(2) Prompt notice shall be given of the taking of any other corporate action, including the filling of a vacancy on the board of directors, approved by shareholders without a meeting, by less than unanimous written consent, to those shareholders entitled to vote who have not consented in

writing. Such notices shall be given in the manner and shall be deemed to have been given as provided in Section 2.4 of this Article II.

(d) Any shareholder giving a written consent, or the shareholder's proxyholders, or a transferee of the shares or a personal representative of the shareholder or their respective proxyholders, may revoke the consent by a writing received by the corporation prior to the time that written consents of the number of shares required to authorize the proposed action have been filed with the secretary of the corporation, but may not do so thereafter. Such revocation is effective upon its receipt by the secretary of the corporation.

Section 2.10 PROXIES.

(a) Every person entitled to vote shares or execute consents may authorize another person or persons to act by proxy with respect to such vote or consent. Any proxy purporting to be executed in accordance with the provisions of this Section 2.10 shall be presumptively valid.

(b) No proxy shall be valid after the expiration of eleven (11) months from the date thereof unless otherwise provided in the proxy. Every proxy continues in full force and effect until revoked by the person executing it prior to the vote pursuant thereto, except as otherwise provided in this Section 2.10. Such revocation may be effected by a writing delivered to the corporation stating that the proxy is revoked or by a subsequent proxy executed by, or by attendance at a meeting and voting in person by, the person executing the proxy. The dates contained on the forms of proxy presumptively determine the order of execution, regardless of the postmark dates on the envelopes in which they are mailed.

(c) A proxy is not revoked by the death or incapacity of the maker unless, before the vote is counted, written notice of such death or incapacity is received by the corporation.

(d) Except when other provision shall have been made by written agreement between the parties, the recordholder of shares that such person holds as pledgee or otherwise as security or which belong to another shall issue to the pledgor or to the owner of such shares, upon demand therefor and payment of necessary expenses thereof, a proxy to vote or take other action thereon.

(e) A proxy which states that it is irrevocable is irrevocable for the period specified therein (notwithstanding subsection (c) of this Section 2.10) when it is held by any of the following or any other entity as specified in the California General Corporation Law or a nominee of any of such persons:

(1) A pledgee;

(2) A person who has purchased or agreed to purchase or holds an option to purchase the shares of a person who has sold a portion of such person's shares in the corporation to the maker of the proxy;

(3) A creditor or creditors of the corporation or the shareholder who extended or continued credit to the corporation or the shareholder in consideration of the proxy if the proxy states that it was given in consideration of such extension or continuation of credit and the name of the person extending or continuing credit;

(4) A person who has contracted to perform services as an employee of the corporation, if a proxy is required by the contract of employment and if the proxy states that it was given in consideration of such contract of employment, the name of the employee and the period of employment contract for; or

(5) A person designated by or under an agreement under Section 706 of the California General Corporation Law.

Notwithstanding the period of irrevocability specified, the proxy becomes revocable when the pledge is redeemed, the option or agreement to purchase is terminated, the seller no longer owns any shares of the corporation or dies, the debt of the corporation or the shareholder is paid, the period of employment provided for in the contract of employment has terminated or the agreement under Section 706 of the California General Corporation Law has terminated. In addition to the foregoing subdivisions (1) through (5), a proxy may be made irrevocable (notwithstanding subsection (c) of this Section 2.10) if it is given to secure the performance of a duty or to protect a title, either legal or equitable, until the happening of events which, by its terms, discharge the obligations secured by it.

(f) A proxy may be revoked, notwithstanding a provision making it irrevocable, by a purchaser of shares without knowledge of the existence of the provision, unless the existence of the proxy and its irrevocability appears on the certificate representing such shares.

Section 2.11 INSPECTORS OF ELECTION.

(a) In advance of any meeting of shareholders, the board of directors may appoint any persons as inspectors of election to act at such meeting or any adjournment thereof. If inspectors of election are not so appointed, or if any person so appointed fails to appear or refuses to act, the chairman of any such meeting may, and on the request of any shareholder or his proxy shall, make such appointment at the meeting. The number of inspectors shall be either one or three. If appointed at a meeting on the request of one or more shareholders or proxies, the majority of shares represented in person or by proxy shall determine whether one or three inspectors are to be appointed.

(b) The inspectors of election shall determine the number of shares outstanding and the voting power of each, the shares represented at the meeting, the existence of a quorum and the authenticity, validity and effect of proxies, receive votes, ballots or consents, hear and determine all challenges and questions in any way arising in connection with the right to vote, count and tabulate all votes or consents, determine when the polls shall close, determine the result and do such acts as may be proper to conduct the election or vote with fairness to all shareholders.

(c) The inspectors of election shall perform their duties impartially, in good faith, to the best of their ability and as expeditiously as is practical. If there are three inspectors of election, the decision, act or certificate of a majority is effective in all respects as the decision, act or certificate of all. Any report or certificate made by the inspectors of election is prima facie evidence of the facts stated therein.

Section 2.12 NOMINATIONS.

Nominations for election of members of the board of directors may be made by the board of directors or by any shareholder of any outstanding class of capital stock of the corporation entitled to vote for the election of directors. Notice of intention to make any nomination shall be made in writing and shall be delivered or mailed to the chairman of the board of the corporation or the secretary of the corporation, not less than twenty-one days (or ten days following the giving of notice of the meeting to shareholders, whichever is latest) nor more than sixty days prior to any meeting of shareholders called for the election of directors; provided, however, that if less than twenty-one days notice of the meeting is given to the shareholders, such notice of intention to nominate shall be mailed or delivered to the chairman of the board of the corporation or the secretary of the corporation, not later than the close of business on the tenth day following the date on which the notice of meeting was mailed. Such notification shall contain the following information to the extent known to the notifying shareholder: 1) the name and address of each proposed nominee; 2) the principal occupation of each proposed nominee; 3) the number of shares of capital stock of the corporation owned by each proposed nominee; 4) the name and residence address of the notifying shareholder[s]; and 5) the number of shares of capital stock of the corporation owned by the notifying shareholder. Nominations not made in accordance herewith shall be disregarded by the chairman of the meeting, and upon his instructions, the inspectors of election shall disregard all votes cast for such nominee.

The first paragraph of this Article II, Section 2.12, shall be set forth in any notice of shareholders' meetings, at which meeting the election of directors is to be considered. Such notice must be given to the shareholders at least ten days prior to the date nominations must be received.

ARTICLE III

DIRECTORS

Section 3.1 POWERS.

Subject to the California General Corporation Law and any limitations in the articles of incorporation of this corporation relating to action requiring shareholder authorization or approval, the business and affairs of the corporation shall be managed and all corporate powers shall be exercised by or under the direction of the board of directors.

Section 3.2 NUMBER AND QUALIFICATION OF DIRECTORS.

The number of directors of the corporation shall not be less than six (6) nor more than eleven (11) until changed by a bylaw amending this Section 3.2 duly adopted by the vote or written consent of holders of a majority of the outstanding shares entitled to vote. The exact number of directors shall be fixed from time to time, within the limits specified in this Section 3.2, by a bylaw or amendment thereof or by a resolution duly adopted by a vote of a majority of the shares entitled to vote represented at a duly held meeting at which a quorum is present, by the written consent of the holders of a majority of the outstanding shares entitled to vote, or by the board of directors.

Section 3.3 ELECTION AND TERM OF OFFICE.

The directors shall be elected at each annual meeting of shareholders, but if any such annual meeting is not held or the directors are not elected at any annual meeting, the directors may be elected at any special meeting of shareholders held for that purpose or by written consent in accordance with Section 2.9 of Article II. Each director, including a director elected to fill a vacancy, shall hold office until the expiration of the term for which elected and until his successor has been elected and qualified, subject to the California General Corporation Law and the provisions of these bylaws with respect to vacancies on the board.

Section 3.4 DIRECTOR'S OATH.

Each director upon taking office shall make an oath or affirmation as required by Section 682 of the California Financial Code, and each such oath, subscribed by the director and certified by the officer before whom it is taken, shall be immediately filed with the California Superintendent of Banks.

Section 3.5 RESIGNATION AND REMOVAL OF DIRECTORS.

Any director may resign effective upon giving written notice to the chairman of the board, the president, the secretary or the board of directors of the corporation, unless the notice specifies a later time for the effectiveness of such resignation. If the resignation is effective at a future time a successor may be elected to take office when the resignation becomes effective. The board of directors may declare vacant the office of a director who has been declared of unsound mind by an order of court or convicted of a felony. Any or all of the directors may be removed without cause if such removal is approved by the affirmative vote of a majority of the outstanding shares entitled to vote provided that no director may be removed (unless the entire board is removed) when the votes cast against removal (or, if such action is taken by written consent, the shares held by persons not consenting in writing to such removal) would be sufficient to elect such director if voted cumulatively at an election at which the same total number of votes were cast (or, if such action is taken by written consent, all shares entitled to vote were voted) and the entire number of directors authorized at the time of the director's most recent election were then being elected. No reduction of the authorized number of directors shall have the effect of removing any director prior to the expiration of his term of office.

Section 3.6 VACANCIES.

A vacancy or vacancies on the board of directors shall exist on the death, resignation or removal of any director, or if the board declares vacant the office of a director if he is declared of unsound mind by an order of court or is convicted of a felony, or if the authorized number of directors is increased, or if the shareholders fail to elect the full authorized number of directors to be voted for at any shareholders' meeting at which an election of directors is held. Vacancies on the board of directors (except vacancies created by the removal of a director) may be filled by a majority of the directors then in office, whether or not less than a quorum, or by a sole remaining director. The shareholders may elect a director at any time to fill any vacancy not filled by the directors or which occurs by reason of the removal of a director. Any such election by written consent of shareholders shall require the consent of a majority of the outstanding shares entitled to vote. If the resignation of a director states that it is to be effective at a future time, a successor may be elected to take office when the resignation becomes effective.

Section 3.7 PLACE OF MEETINGS.

Regular and special meetings of the board of directors may be held at any place within the State of California which has been designated in the notice of the meeting, or, if not stated in the notice or there is no notice, designated by resolution or by written consent of all of the members of the board of directors. If the place of a regular or special meeting is not designated in the notice or fixed by a resolution of the board or consented to in writing by all members of the board of directors, it shall be held at the corporation's principal administrative office.

Section 3.8 ORGANIZATION MEETINGS.

The board of directors shall hold a regular meeting not less than once each calendar quarter. The board of directors shall hold the regular meetings at such times and places as are fixed by the board of directors. Call and notice of regular meetings of the board of directors shall not be required.

Section 3.9 SPECIAL MEETINGS.

Special meetings of the board of directors for any purpose or purposes may be called at any time by the chairman of the board, the chief executive officer, the president, the secretary, or any two directors. Notice of the time and place of special meetings shall be delivered personally to each director or by telephone, facsimile or telegraph or sent to the director by mail. In case notice is given by mail or telegram, it shall be sent, charges prepaid, addressed to the director at his address appearing on the corporate records or if it is not on these records or is not readily ascertainable, at the place where the meetings of the directors are regularly held. If notice is delivered personally, by facsimile or given by telephone or telegraph, it shall be given or delivered to the telegraph office at least twenty-four (24) hours before the meeting. If notice is mailed it shall be deposited in the United States mail at least four (4) days before the meeting. Such mailing, faxing, telegraphing or delivery, personally or by telephone, as provided in this Section 3.9, shall be due, legal and personal notice to such director. A notice or waiver of notice need not specify the purpose of any regular or special meeting of the board of directors.

Section 3.10 QUORUM.

A majority of the authorized number of directors shall constitute a quorum of the board of directors for the transaction of business. Every act or decision done or made by a majority of the directors present at a meeting duly held at which a quorum is present is the act of the board of directors, subject to the provisions of Section 310 (Transactions with Interested Directors) and subdivision (e) of Section 317 (Indemnification of Corporate Agents) of the California General Corporation Law. A meeting at which a quorum is initially present may continue to transact business notwithstanding the withdrawal of directors, provided that any action taken is approved by at least a majority of the required quorum for such meeting.

Section 3.11 WAIVER OF NOTICE OR CONSENT.

The transactions of any meeting of the board of directors, however called and noticed or wherever held, shall be as valid as though had at a meeting duly held after regular call and notice, if a quorum is present and if, either before or after the meeting, each of the directors not present or who though present, has prior to the meeting or at its commencement, protested the lack of proper notice to him, signs a written waiver of notice, or a consent to holding the meeting, or an approval of the minutes of the meeting. All such waivers, consents and approvals shall be filed with the corporate records or made a part of the minutes of the meeting. A notice or waiver of notice need not specify the purpose of any regular or special meeting of the board of directors. Notice of a meeting need not be given to any director who signs a waiver of notice, whether before or after the meeting, or who attends the meeting without protesting, prior to or at its commencement, the lack of notice to such director.

Section 3.12 ADJOURNMENT.

A majority of the directors present, whether or not a quorum is present, may adjourn any meeting to another time and place. If the meeting is adjourned for more than twenty-four (24) hours, notice of the adjournment to another time or place shall be given prior to the time of the adjourned meeting to the directors who were not present at the time of the adjournment.

Section 3.13 MEETINGS BY CONFERENCE TELEPHONE.

Members of the board of directors may participate in a meeting through use of conference telephone or similar communications equipment, so long as all members participating in such meeting can hear one another. Participation by directors in a meeting in the manner provided in this Section 3.13 constitutes presence in person at such meeting.

Section 3.14 ACTION WITHOUT A MEETING.

Any action required or permitted to be taken by the board of directors may be taken without a meeting, if all members of the board of directors shall individually or collectively consent in writing to such action. Such written consent or consents shall be filed with the minutes of the proceedings of the board of directors. Such action by written consent shall have the same force and effect as a unanimous vote of such directors.

Section 3.15 FEES AND COMPENSATION.

Directors and members of the committees may receive such compensation, if any, for their services, and such reimbursement for expenses, as may be fixed or determined by resolution of the board of directors.

Section 3.16 COMMITTEES.

The board of directors may, by resolution adopted by a majority of the authorized number of directors, designate one or more committees, each consisting of two or more directors, to serve at the pleasure of the board of directors. The board of directors may designate one or more directors as alternate members of any committee, who may replace any absent member at any meeting of the committee. The board of directors may delegate to any such committee, to the extent provided in such resolution, any of the board of directors' powers and authority in the management of the corporation's business and affairs, except such powers and authority that conflict with the California General Corporation Law or the corporation's articles of incorporation.

The board of directors may prescribe appropriate rules, not inconsistent with these bylaws, by which proceedings of any such committee shall be conducted. The provisions of these bylaws relating to the calling of meetings of the board of directors, notice of meetings of the board of directors and waiver of such notice, adjournments of meetings of the board of directors, written consents to board of directors meetings and approval of minutes, action by the board of directors by consent in writing without a meeting, the place of holding such meetings, meetings by conference telephone or similar communications equipment, the quorum for such meetings, the vote required at such meetings and the withdrawal of directors after commencement of a meeting shall apply to committees of the board of directors and action by such committees. In addition, any member of the committee designated by the board of directors as the chairman or as secretary of the committee or any two members of a committee may call meetings of the committee. Regular meetings of any committee may be held without notice if the time and place of such meetings are fixed by the board of directors or the committee.

Section 3.17 INDEMNIFICATION OF AGENTS.

The board of directors may authorize the corporation to indemnify an agent, as herein defined, to the fullest extent permitted under law, including but not limited to the California General Corporation Law.

For the purposes of this section: (1) "agent" means any person who is or was a director, officer, employee or other agent of the corporation, or is or was serving at the request of this corporation as a director, officer, employee or agent of another foreign or domestic corporation, partnership, joint venture, trust or other enterprise, or was a director, officer, employee or agent of a foreign or domestic corporation which was a predecessor corporation of the corporation or of another enterprise at the request of such predecessor corporation; (2) "proceeding" means any threatened, pending or completed action or proceeding; and (3) "expenses" includes, without limitation, attorneys' fees and any expenses of establishing a right to indemnification.

ARTICLE IV

OFFICERS

Section 4.1 OFFICERS.

The officers of the corporation shall be a chairman of the board or a president, or both, a chief executive officer, a secretary and a chief financial officer. The corporation may also have, at the discretion of the board of directors, one or more vice-chairmen, one or more vice presidents, one or more assistant secretaries, a cashier, one or more assistant cashiers and such other officers as may be appointed in accordance with the provisions of Section 4.3 of this Article IV. Any two or more offices may be held by the same person; provided that in the execution of written instruments and in the performance of any executive or administrative duties on behalf of the corporation, such officer may only act in one capacity when joint execution or action by two officers is required.

Section 4.2 ELECTIONS.

The officers of the corporation, except such officers as may be appointed in accordance with the provisions of Section 4.3 or Section 4.5 of this Article IV, shall be chosen by the board of directors, and each shall hold his office until he shall resign or be removed or is otherwise disqualified to serve, or until his successor is chosen and qualified.

Section 4.3 OTHER OFFICERS.

The board of directors may appoint, and may empower the chairman of the board or the chief executive officer or both of them to appoint, such other officers as the business of the corporation may require, each of whom shall hold office for such period, have such authority and perform such duties as are provided in the bylaws or as the board of directors may from time to time determine.

Section 4.4 REMOVAL AND RESIGNATION.

Any officer may be removed with or without cause either by the board of directors or, except for an officer chosen by the board, by any officer upon whom the power of removal may be conferred by the board (subject, in each case, to the rights, if any, of an officer under any contract of employment). Any officer may resign at any time upon written notice to the corporation (without prejudice however, to the rights, if any, of the corporation under any contract to which the officer is a party). Any such resignation shall take effect upon receipt of such notice or at any such later time as agreed to by the board of directors. If the resignation is effective at a future time, a successor may be elected to take office when the resignation becomes effective. Unless a resignation specifies otherwise, its acceptance by the corporation shall not be necessary to make it effective.

Section 4.5 VACANCIES.

A vacancy in any office because of death, resignation, removal, disqualification or any other cause shall be filled in the manner prescribed in the bylaws for regular appointments to such office.

Section 4.6 CHAIRMAN OF THE BOARD.

The board of directors may, in its discretion, elect a chairman of the board who, unless otherwise determined by the board of directors, shall preside at all meetings of the board of directors at which he is present and shall exercise and perform any other powers and duties assigned to him by the board of directors or prescribed by the bylaws. If the office of president is vacant, the chairman of the board shall exercise the duties of the president, and when so acting, shall have all the powers of, and be subject to all the restrictions on, the president. The chairman of the board shall preside as chairman at all meetings of the shareholders unless otherwise determined by the board of directors.

Section 4.7 VICE-CHAIRMAN OF THE BOARD.

The board of directors may, in its discretion, elect one vice-chairman of the board or more than one vice-chairmen of the board. Unless otherwise determined by the board of directors, the vice-chairman of the board shall preside as chairman, or if there are vice-chairmen of the board, the vice chairmen of the board shall jointly preside as co-chairmen, at all meetings of the board of directors or meetings of the shareholders from which the chairman of the board is absent. The vice-chairman, or vice-chairmen, of the board shall exercise and perform any other powers and duties assigned to the vice-chairman of the board by the board of directors or prescribed by the bylaws. If the office of chairman of the board is vacant, the vice-chairman of the board shall exercise, or if there are vice-chairmen, the vice-chairmen of the board shall jointly exercise, the duties of the chairman of the board, and when so acting, shall have all the powers of, and be subject to the restrictions on, the chairman of the board.

Section 4.8 CHIEF EXECUTIVE OFFICER.

Subject to any supervisory powers, if any, that the board of directors or the bylaws have given to the chairman of the board, if there be such an officer, or to the president, the chief executive officer shall be the corporation's general manager. Subject to the control of the board of directors, the chief executive officer shall direct the total operation of the corporation and shall have responsibility for the attainment of goals, plans and directives established by the board of directors. The chief executive officer shall be a member of the board of directors. Unless otherwise determined by the board of directors, and in the absence of the chairman of the board and the vice-chairman, or vice-chairmen, of the board, the chief executive officer shall preside as chairman at all meetings of the board of directors and of the shareholders. The chief executive officer shall have the general powers and duties of management usually vested in the office of chief executive officer and shall have any other powers and duties prescribed by the board of directors or the bylaws.

Section 4.9 PRESIDENT.

Subject to the supervisory powers, if any, that the bylaws or the board of directors have given to the chairman of the board, if there be such an officer, or to the chief executive officer, the president shall be the corporation's chief operating officer and shall have general supervision, direction and control of the business, affairs and officers of the corporation. Unless otherwise determined by the board of directors, and in the absence of the chairman of the board, the vice-chairman, or vice-chairmen, of the board and the chief executive officer, the president shall preside as chairman at all meetings of the board of directors and of the shareholders. The president shall have the general powers and duties of management usually vested in the office of president; shall have any other powers and duties prescribed by the bylaws or the board of directors; and shall be primarily responsible for carrying out all orders and resolutions of the board of directors.

Section 4.10 VICE PRESIDENTS.

In the absence or disability of the president, the vice presidents in order of their rank as fixed by the board of directors, or if not ranked, the vice president designated by the board of directors, or if there has been no such designation, the vice president designated by the chief executive officer or president, shall perform all duties of the president, and when so acting, shall have all the powers of, and be subject to all the restrictions on, the president. Each vice president shall have any of the powers and perform any other duties that from time to time the board of directors, the bylaws or the chief executive officer may prescribe for him.

Section 4.11 SECRETARY.

The secretary shall keep or cause to be kept a book of minutes of all meetings and actions by written consent of all directors, shareholders and committees of the board of directors. The minutes of each meeting shall state the time and place that it was held and such other information as shall be necessary to determine whether the meeting was held in accordance with the law and these bylaws and the actions taken thereat. The secretary shall keep or cause to be kept at the corporation's principal executive office, or at the office of its transfer agent or registrar, a record of the shareholders of the corporation, giving the names and addresses of all shareholders and the number and class of shares held by each. The secretary shall give, or cause to be given, notice of all meetings of shareholders, directors and committees required to be given under these bylaws or by law, shall keep or cause the keeping of the corporate seal in safe custody and shall have any other powers and perform any other duties that are prescribed by the board of directors or the bylaws or the chief executive officer. If the secretary refuses or fails to give notice of any meeting lawfully called, any other officer of the corporation may give notice of such meeting. The assistant secretary, or if there be more than one, any assistant secretary, may perform any or all of the duties and exercise any or all of the powers of the secretary unless prohibited from doing so by the board of directors, the chief executive officer or the secretary, and shall have such other powers and perform any other duties as are prescribed for him by the board of directors or the chief executive officer.

Section 4.12 CHIEF FINANCIAL OFFICER.

The chief financial officer, who shall also be deemed to be the treasurer, when a treasurer may be required, shall keep and maintain, or cause to be kept and maintained, adequate and correct books and records of account. The chief financial officer shall cause all money and other valuables in the name and to the credit of the corporation to be deposited at the depositories designated by the board of directors or any person authorized by the board of directors to designate such depositories. He shall render to the chief executive officer and board of directors when requested by either of them, an account of all his transactions as chief financial officer and of the financial condition of the corporation, and shall have any other powers and perform any other duties prescribed by the board of directors, the bylaws or the chief executive officer.

Section 4.13 CASHIER.

The cashier may also be the chief financial officer and may also be an assistant secretary. In the absence or disability of the chief financial officer, the cashier shall perform all the duties of the chief financial officer, and when so acting, shall have all the powers of, and be subject to all the restrictions on, the chief financial officer. He shall have the general powers and duties of management usually vested in the office of cashier, when there also is an office of chief financial officer, and shall have any other powers and duties prescribed by the bylaws or the board of directors. The assistant cashier, or if there be more than one, any assistant cashier, may perform any or all of the duties and exercise any or all of the powers of the cashier unless prohibited from doing so by the board of directors, the chief executive officer or the cashier, and shall have such other powers and perform any other duties as are prescribed for him by the board of directors, the chief executive officer or the cashier.

ARTICLE V

MISCELLANEOUS

Section 5.1 RECORD DATE.

The board of directors may fix a time in the future as a record date for the determination of the shareholders entitled to notice of any meeting of shareholders or to vote or entitled to receive payment of any dividend or distribution or allotment of any rights or entitled to exercise any rights in respect of any other lawful action. The record date so fixed shall be not more than sixty (60) days nor less than ten (10) days prior to the date of such meeting, nor more than sixty (60) days prior to any other action for the purposes of which it is fixed. When a record date is so fixed, only shareholders of record on that date are entitled to notice of and to vote at any such meeting, to receive a dividend, distribution, or allotment of rights, or to exercise the rights, as the case may be, notwithstanding any transfer of any shares on the books of the corporation after the record date, except as otherwise provided in the articles of incorporation or bylaws of this corporation.

Section 5.2 INSPECTION OF CORPORATE RECORDS.

The accounting books and records and record of shareholders, and minutes of proceedings of the shareholders and the board and committees of the board of directors of this corporation shall be open to inspection upon the written demand on the corporation of any shareholder or holder of a voting trust certificate at any time during usual business hours, for a purpose reasonably related to such holder's interests as a shareholder or as the holder of such voting trust certificate. Such inspection by a shareholder or holder of a voting trust certificate may be made in person or by agent or attorney, and the right of inspection includes the right to copy and make extracts.

A shareholder or shareholders holding at least five percent (5%) in the aggregate of the outstanding voting shares of the corporation or who hold at least one percent (1%) of such voting shares and have filed a Form F-6 with the Federal Deposit Insurance Corporation relating to the election of directors of the corporation shall have (in person, or by agent or attorney) the absolute right to inspect and copy the record of shareholders' names and addresses and shareholdings during usual business hours upon five (5) business days' prior written demand upon the corporation or to obtain from the transfer agent for the corporation, upon written demand and upon the tender of its usual charges, a list of the shareholders' names and addresses, who are entitled to vote for the election of directors, and their shareholdings, as of the most recent record date of which it has been compiled or as of a date specified by the shareholder subsequent to the date of demand. The list shall be made available on or before the later of five (5) business days after the demand is received or the date specified therein as the date as of which the list is to be compiled.

Every director shall have the absolute right at any reasonable time to inspect and copy all books, records and documents of every kind and to inspect the physical properties of this corporation and any subsidiary of this corporation. Such inspection by a director may be made in person or by agent or attorney and the right of inspection includes the right to copy and make extracts.

Section 5.3 CHECKS, DRAFTS, ETC.

All checks, drafts or other orders for payment of money, notes or other evidences of indebtedness, issued in the name of or payable to the corporation, shall be signed or endorsed by such person or persons and in such manner as, from time to time, shall be determined by resolution of the board of directors. The board of directors may authorize one or more officers of the corporation to designate the person or persons authorized to sign such documents and the manner in which such documents shall be signed.

Section 5.4 ANNUAL AND OTHER REPORTS.

(a) The board of directors of the corporation shall cause an annual report to be sent to the shareholders not later than one hundred twenty (120) days after the close of the fiscal year and at least fifteen (15) days prior to the annual meeting of shareholders to be held during the next fiscal year. Such report shall contain a balance sheet as of the end of such fiscal year and an income statement and statement of changes in financial position for such fiscal year, accompanied by any report thereon of independent accountants or, if there is no such report, the certificate of an authorized officer of the corporation that such statements were prepared without audit from the books and records of the corporation as required by Section 1501 of the California General Corporation Law.

(b) If no annual report for the last fiscal year has been sent to shareholders, the corporation shall, upon the written request of any shareholder made more than one hundred twenty (120) days after the close of such fiscal year, deliver or mail to the person making the request within thirty (30) days thereafter the financial statements required by subdivision (a) of Section 1501 of the California General Corporation Law for such year. A shareholder or shareholders holding at least five percent (5%) of the outstanding shares of any class of the corporation may make a written request to the corporation for an income statement of the corporation for the three-month, six-month or nine-month period of the current fiscal year ended more than thirty (30) days prior to the date of the request and a balance sheet of the corporation as of the end of such period and, in addition, if no annual report for the last fiscal year has been sent to shareholders, the statements referred to in subdivision (a) of Section 1501 of the California General Corporation Law for the last fiscal year. The statements shall be delivered or mailed to the person making the request within thirty (30) days thereafter. A copy of such statements shall be kept on file in the principal administrative office of the corporation for twelve (12) months and they shall be exhibited at all reasonable times to any shareholder demanding an examination of them or a copy shall be mailed to such shareholder.

(c) The corporation shall, upon the written request of any shareholder, mail to the shareholder a copy of the last annual, semi-annual or quarterly income statement which it has prepared and a balance sheet as of the end of the period.

(d) The quarterly income statements and balance sheets referred to in subsection (c) of this Section 5.4 shall be accompanied by the report thereon, if any, of any independent accountants engaged by the corporation or the certificate of an authorized officer of the corporation that such financial statements were prepared without audit from the books and records of the corporation.

(e) Unless otherwise determined by the board of directors or the chief executive officer, the chief financial officer and the cashier are each authorized officers of the corporation to execute the certificate that the annual report and quarterly income statements and balance sheets referred to in this section were prepared without audit from the books and records of the corporation.

Any report, including financial statements as required by Section 1501 of the California General Corporation Law, sent to the shareholders shall be given personally or by mail or other means of written communication, charges prepaid, addressed to such shareholder at the address of such shareholder appearing on the books of the corporation or given by such shareholder, to the corporation for the purpose of notice or set forth in the written request of the shareholder as provided in this section. If any report addressed to the shareholder at the address of such shareholder appearing on the books of the corporation is returned to the corporation by the United States Postal Service marked to indicate that the United States Postal Service is unable to deliver the report to the shareholder at such address, all future reports shall be deemed to have been duly given without further mailing if the same shall be available for the shareholder upon written demand of the shareholder at the principal administrative office of the corporation for a period of one year from the date of the giving of the report to all other shareholders. If no address appears on the books of the corporation or is given by the shareholder to the corporation for the purpose of notice or is set forth in the written request of the shareholder as provided in this section, such report shall be deemed to have been given to such shareholder, if sent by mail or other means or written communication addressed to the place where the principal administrative office of the corporation is located, or if published at least once in a newspaper of general circulation in the county in which the principal administrative office is located. Any such report shall be deemed to have been given at the time when delivered personally or deposited in the mail or sent by other means of written communication. An affidavit of mailing of any such report in accordance with the foregoing provisions, executed by the secretary, assistant secretary or any transfer agent of the corporation, shall be prima facie of the giving of the report.

Section 5.5 CONTRACTS, ETC.: HOW EXECUTED.

The board of directors, except as the bylaws or articles of incorporation otherwise provide, may authorize any officer or officers and/or agent or agents to enter into any contract or execute any instrument in the name of and/or on behalf of the corporation, and such authority may be general or confined to specific instances.

Section 5.6 CERTIFICATE FOR SHARES.

(a) Every holder of shares in the corporation shall be entitled to have a certificate signed in the name of the corporation by the chairman or a vice chairman of the board or the president or a vice president and by the chief financial officer or an assistant treasurer or the secretary or any assistant secretary, certifying the number of shares and the class or series of shares owned by the shareholder. Any or all of the signatures on the certificate may be facsimile. In case any officer, transfer agent or registrar who has signed or whose facsimile signature has been placed upon a certificate shall have ceased to be such officer, transfer agent or registrar before such certificate is issued, it may be issued by the corporation with the same effect as if such person were such officer, transfer agent or registrar at the date of issue.

(b) Any such certificate shall also contain such legend or other statement as may be required by Section 418 of the California General Corporation Law, the Corporate Securities Law of 1968, and any agreement between the corporation and the issuee thereof, and may contain such legend or other statement as may be required by any other applicable law or regulation or agreement.

(c) Certificates for shares may not be issued prior to full payment thereof.

(d) No new certificate for shares shall be issued in place of any certificate theretofore issued unless the latter is surrendered and cancelled at the same time; provided, however, that a new certificate may be issued without the surrender and cancellation of the old certificate if the certificate theretofore issued is alleged to have been lost, stolen or destroyed. In case of any such allegedly lost, stolen or destroyed certificate, the corporation may require the owner thereof or the legal representative of such owner to give the corporation a bond (or other adequate security) sufficient to indemnify it against any claim that may be made against it (including any expense or liability) on account of the alleged loss, theft or destruction of any such certificate or the issuance of such new certificate.

Section 5.7 REPRESENTATION OF SHARES OF OTHER CORPORATIONS.

Unless the board of directors shall otherwise determine, the chairman of the board, any vice chairman, the president, the chief executive officer, and the secretary of this corporation are each authorized to vote, represent and exercise on behalf of this corporation all rights incident to any and all shares of any other corporation or corporations standing in the name of this corporation. The authority herein granted to such officers to vote or represent on behalf of this corporation any and all shares held by this corporation in any other corporation or corporations may be exercised either by such officers in person or by any person authorized so to do by proxy or power of attorney or other document duly executed by any such officer.

Section 5.8 INSPECTION OF BYLAWS.

The corporation shall keep in its principal executive office in California, the original or a copy of the bylaws as amended to date, which shall be open to inspection by the shareholders at all reasonable times during office hours.

Section 5.9 SEAL.

The corporation may have a common seal.

Section 5.10 CONSTRUCTION AND DEFINITIONS.

Unless the context otherwise requires, the general provisions, rules of construction and definitions contained in the California General Corporation Law shall govern the construction of these bylaws. Without limiting the generality of the foregoing, the masculine gender includes the feminine and neuter, the singular number includes the plural and the plural number includes the singular, and the term "person" includes a corporation as well as a natural person.

ARTICLE VI

AMENDMENTS

Section 6.1 POWER OF SHAREHOLDERS.

New bylaws may be adopted or these bylaws may be amended or repealed by the affirmative vote of a majority of the outstanding shares entitled to vote or by the written assent of shareholders entitled to vote such shares, except as otherwise provided by law or by the articles of incorporation of this corporation.

Section 6.2 POWER OF DIRECTORS.

Subject to the right of shareholders as provided in Section 1 of this Article VI to adopt, amend or repeal bylaws, bylaws other than a bylaw or amendment thereof changing the authorized number of directors may be adopted, amended or repealed by the board of directors.

CERTIFICATE OF SECRETARY

I, the undersigned, do hereby certify:

(1) That I am the duly elected and acting secretary of Preferred Bank, a California corporation; and

(2) That the foregoing bylaws, comprising twenty-nine (29) pages, constitute the bylaws of such corporation as duly adopted by action of the Board of Directors of the corporation duly taken on October 8, 1991.

IN WITNESS WHEREOF, I have hereunto subscribed my name and affixed the seal of such corporation this 8th day of October, 1991.

Li Yu, Secretary

AMENDED AND RESTATED BYLAWS

OF

PREFERRED BANK

A CALIFORNIA BANKING CORPORATION

ARTICLE I

OFFICES

Section 1.1 PRINCIPAL EXECUTIVE OFFICE.

The principal executive office of the corporation shall be located at such place within the State of California as the Board of Directors shall from time to time determine.

Section 1.2 OTHER OFFICES.

Other offices may at any time be established by the Board of Directors, subject to the approval of the California Department of Financial Institutions, at any place or places where the corporation is qualified to do business.

ARTICLE II

MEETINGS OF SHAREHOLDERS

Section 2.1 PLACE OF MEETINGS.

All meetings of shareholders shall be held at the principal administrative office of the corporation or at any other place within the State of California which may be designated by the Board of Directors in accordance with these Amended and Restated Bylaws.

Section 2.2 ANNUAL MEETINGS.

The annual meeting of the shareholders shall be held each year at a date and time fixed in accordance with these Amended and Restated Bylaws. The Board of Directors by resolution shall designate the time, place and date (which shall be no more than fifteen (15) months after the date of the last annual meeting) of the annual meeting of the shareholders for the election of directors and the transaction of any other proper business.

Section 2.3 SPECIAL MEETINGS.

Special meetings of the shareholders, for the purpose of taking any action which is within the powers of the shareholders, may be called at any time by the Chairman of the Board, the Chief Executive Officer, the President, the Board of Directors, or the holders of shares entitled to cast not less than ten percent (10%) of the votes at the meeting.

Section 2.4 NOTICE OF MEETINGS OF SHAREHOLDERS.

(a) Written notice of each meeting of shareholders, whether annual or special, shall be given to each shareholder entitled to vote thereat, either personally or by mail, or if the corporation shall have outstanding shares held of record by 500 or more persons (determined as provided in Section 605 of the California Corporations Code) on the record date for the shareholders' meeting notice may be sent by third class mail, or other means of written communication, charges prepaid, addressed to such shareholder at the address of such shareholder appearing on the books of the corporation or given by such shareholder to the corporation for the purpose of notice.

(b) If any notice addressed to the shareholder at the address of such shareholder appearing on the books of the corporation is returned to the corporation by the United States Postal Service marked to indicate that the United States Postal Service is unable to deliver the notice to the shareholder at such address, all future notices shall be deemed to have been duly given without further mailing if the same shall be available for the shareholder upon written demand of the shareholder at the principal administrative office of the corporation for a period of one year from the date of the giving of the notice to all other shareholders. If no address appears on the books of the corporation or is given by the shareholder to the corporation for the purpose of notice, notice shall be deemed to have been given to such shareholder if sent by mail or other means of written communication addressed to the place where the principal administrative office of the corporation is located, or if published at least once in a newspaper of general circulation in the county in which the principal administrative office is located.

(c) All such notices shall be given not less than ten (10) days (or, if sent by third class mail, (30) days) nor more than sixty (60) days before the meeting to each shareholder entitled to vote thereat. Any such notice shall be deemed to have been given at the time when delivered personally or deposited in the mail or sent by other means of written communication. An affidavit of mailing of any such notice in accordance with the foregoing provisions, executed by the Secretary, Assistant Secretary or any transfer agent of the corporation, shall be prima facie evidence of the giving of the notice.

(d) All such notices shall state the place, date and hour of such meeting. In the case of a special meeting, such notice shall also state the general nature of the business to be transacted at such meeting, and no other business may be transacted thereat. In the case of an annual meeting, such notice shall also state those matters which the board of directors at the time of the mailing of the notice intends to present for action by the shareholders, but, subject to the provisions of Section 601(f) of the California Corporations Code, any proper matter may be presented at the meeting for such action.

(e) The notice of any meeting at which directors are to be elected shall include the names of nominees intended at the time of the notice to be presented by management for election.

(f) Upon request in writing that a special meeting of shareholders be called for any proper purpose, directed to the Chairman of the Board of Directors, Chief Executive Officer, President, Vice President or Secretary by any person (other than the Board of Directors) entitled to call a special meeting of shareholders, the officer forthwith shall cause notice to be given to the shareholders entitled to vote that a meeting will be held at a time requested by the person or persons calling the meeting, not less than thirty-five (35) nor more than sixty (60) days after receipt of the request.

Section 2.5 QUORUM; ACTION AT MEETINGS.

(a) The presence at any meeting, in person or by proxy, of the holders of a majority of the shares entitled to vote at such meeting shall constitute a quorum for the transaction of business at a meeting of the shareholders.

(b) Except as provided in subdivision (c) of this section, the affirmative vote of a majority of the shares represented, in person or by proxy, and voting at a duly held meeting at which a quorum is present (which shares voting affirmatively also constitute at least a majority of the required quorum) shall be the act of the shareholders, unless the vote of a greater number is required by law or the Amended and Restated Articles of Incorporation.

(c) Shareholders present at a valid meeting at which a quorum is initially present may continue to do business until adjournment, notwithstanding the withdrawal of enough shareholders to leave less than a quorum, if any action taken (other than adjournment or as otherwise provided in the Amended and Restated Articles of Incorporation or these Amended and Restated Bylaws) is approved by at least a majority of the shares required to constitute a quorum.

Section 2.6 ADJOURNED MEETINGS AND NOTICE THEREOF.

(a) Any annual or special shareholders' meeting may be adjourned from time to time, even though a quorum is not present, by the affirmative vote of the holders of a majority of the shares present at the meeting, either in person or by proxy, provided that in the absence of a quorum, no other business may be transacted at any such meeting, except as provided in Section 2.5 of this Article II.

(b) When a shareholders' meeting is adjourned to another time or place, except as provided in this subsection (b), notice need not be given of the adjourned meeting if the time and place thereof are announced at the meeting at which the adjournment is taken. At the adjourned meeting the corporation may transact any business which might have been transacted at the original meeting. If the adjournment is for more than forty-five (45) days or if after the adjournment a new record date is fixed for the adjourned meeting, a notice of the adjourned meeting shall be given to each shareholder of record entitled to vote at the meeting.

Section 2.7 VOTING RIGHTS OF SHARES AND SHAREHOLDERS.

(a) Except as may be otherwise provided in the Amended and Restated Articles of Incorporation, each outstanding share, regardless of class, shall be entitled to one vote on each matter submitted to a vote of shareholders.

(b) Any holder of shares entitled to vote on any matter may vote part of the shares in favor of the proposal and refrain from voting the remaining shares or vote them against the proposal, other than elections to office; but, if the shareholder fails to specify the number of shares such shareholder is voting affirmatively, it will be conclusively presumed that the shareholder's approving vote is with respect to all shares such shareholder is entitled to vote.

Section 2.8 RECORD DATE.

(a) In order that the corporation may determine the shareholders entitled to notice of, or to vote at, any meeting, or entitled to receive payment of any dividend or other distribution or allotment of any rights or entitled to exercise any rights in respect of any other lawful action, the Board of Directors may fix, in advance, a record date, which shall not be more than sixty (60) nor less than ten (10) days prior to the date of such meeting nor more than sixty (60) days prior to any other action.

(b) If no record date is fixed:

(i) The record date for determining shareholders entitled to notice of, or to vote at, a meeting of shareholders shall be at the close of business on the business day preceding the day on which notice is given or, if notice is waived, at the close of business on the business day next preceding the day on which the meeting is held.

(ii) The record date for determining shareholders for any other purpose shall be at the close of business on the day on which the Board of Directors adopts the resolution relating thereto, or the sixtieth (60th) day prior to the date of such other action, whichever is later.

(c) A determination of shareholders of record entitled to notice of, or to vote at, a meeting of shareholders shall apply to any adjournment of the meeting unless the Board of Directors fixes a new record date for the adjourned meeting, but the Board of Directors shall fix a new record date if the meeting is adjourned for more than forty-five (45) days from the date set for the original meeting.

(d) Only shareholders of record at the close of business on the record date are entitled to notice of, and to vote at, at meeting of shareholders, or to receive a dividend, distribution or allotment of rights or to exercise the rights, as the case may be, notwithstanding any transfer of any shares on the books of the corporation after the record date.

Section 2.9 ELECTION OF DIRECTORS.

(a) Shareholders shall not be permitted to cumulate their votes for the election of directors.

(b) Voting may be by voice or ballot, provided that any election of directors must be by ballot upon the demand of any shareholder made at the meeting and before the voting begins.

(c) In any election of directors, the candidates receiving the highest number of votes of the shares entitled to be voted for them up to the number of directors of each class to be elected by such shares are elected as directors. If, at any meeting of shareholders, due to a vacancy or vacancies or otherwise, directors of more than one class of the Board of Directors are to be elected, each class of directors to be elected at the meeting shall be elected in a separate election.

Section 2.10 ACTION WITHOUT A MEETING.

Except as may be otherwise provided in the Amended and Restated Articles of Incorporation, no action by written consent of shareholders without a meeting shall be permitted and no such action by written consent shall be valid as approval of any matter by the shareholders.

Section 2.11 WAIVER OF NOTICE AND CONSENT OF ABSENTEES.

(a) The transactions of any meeting of shareholders, either annual or special, however called and noticed, and wherever held, are as valid as though they had taken place at a meeting duly held after regular call and notice, if a quorum is present either in person or by proxy, and if, either before or after the meeting, each of the persons entitled to vote, not present in person or by proxy, signs a written waiver of notice or a consent to the holding of the meeting or an approval of the minutes thereof.

(b) All such waivers, consents and approvals shall be filed with the corporate records or made a part of the minutes of the meeting. Attendance of a person at a meeting shall constitute a waiver of notice of, and presence at, such meeting, except when the person objects, at the beginning of the meeting, to the transaction of any business because the meeting is not lawfully called or convened and except that attendance at a meeting is not a waiver of any right to object to the consideration of matters required by Section 2.4 of these Amended and Restated Bylaws or Section 601(f) of the California Corporations Code to be included in the notice but not so included, if such objection is expressly made at the meeting; *provided, however,* that any person making such objection at the beginning of the meeting or to the consideration of matters required to be but not included in the notice may orally withdraw such objection at the meeting or thereafter waive such objection by signing a written waiver thereof or a consent to the holding of the meeting or the consideration of the matter or an approval of the minutes of the meeting.

(c) Neither the business to be transacted at, nor the purpose of, any regular or special meeting of shareholders need be specified in any written waiver of notice, consent to the holding of the meeting or approval of the minutes thereof, except as provided in Section 601(f) of the California Corporations Code.

Section 2.12 PROXIES.

(a) Every person entitled to vote shares may authorize another person or persons to act by proxy with respect to such vote. Any proxy purporting to be executed in accordance with the provisions of this Section 2.12 shall be presumptively valid.

(b) No proxy shall be valid after the expiration of eleven (11) months from the date thereof unless otherwise provided in the proxy. Every proxy continues in full force and effect until revoked by the person executing it prior to the vote pursuant thereto, except as otherwise provided in Section 705 of the California Corporations Code. Such revocation may be effected by (i) a writing delivered to the corporation stating that the proxy is revoked, (ii) by a subsequent proxy executed by the person executing the proxy, or (iii) by attendance at a meeting and voting in person by the person executing the proxy. The dates contained on the forms of proxy presumptively determine the order of execution, regardless of the postmark dates on the envelopes in which they are mailed.

(c) A proxy is not revoked by the death or incapacity of the maker unless, before the vote is counted, written notice of such death or incapacity is received by the corporation.

(d) A proxy which states that it is irrevocable for the period specified therein shall be subject to the provisions of subdivisions (e) and (f) of Section 705 of the California Corporations Code.

Section 2.13 INSPECTORS OF ELECTION.

(a) In advance of any meeting of shareholders, the Board of Directors may appoint any persons as inspectors of election to act at such meeting or any adjournment thereof. If inspectors of election are not so appointed, or if any person so appointed fails to appear or refuses to act, the Chairman of any such meeting may, and on the request of any shareholder or his proxy shall, appoint inspectors of election at the meeting. The number of inspectors shall be either one or three. If appointed at a meeting on the request of one or more shareholders or proxies, the majority of shares represented in person or by proxy shall determine whether one or three inspectors are to be appointed.

(b) The inspectors of election shall (i) determine the number of shares outstanding and the voting power of each, the shares represented at the meeting, the existence of a quorum and the authenticity, validity and effect of proxies, (ii) receive votes or ballots, (iii) hear and determine all challenges and questions in any way arising in connection with the right to vote, (iv) count and tabulate all votes, determine when the polls shall close, (v) determine the result and (vi) do such acts as may be proper to conduct the election or vote with fairness to all shareholders.

(c) The inspectors of election shall perform their duties impartially, in good faith, to the best of their ability and as expeditiously as is practical. If there are three inspectors of election, the decision, act or certificate of a majority is effective in all respects as the decision, act or certificate of all. Any report or certificate made by the inspectors of election is prima facie evidence of the facts stated therein.

Section 2.14 ADVANCE NOTICE OF SHAREHOLDER NOMINEES FOR DIRECTOR AND OTHER SHAREHOLDER PROPOSALS.

(a) <u>Annual Meeting of Shareholders</u>.

(i) Nominations of individuals for election to the Board of Directors and the proposal of other business to be considered by the shareholders may be made at an annual meeting of shareholders (1) pursuant to the corporation's notice of meeting, (2) by or at the direction of the Board of Directors or (3) by any shareholder of the corporation who was a shareholder of record both at the time of giving of notice by the shareholder as provided for in this Section 2.14(a) and at the time of the annual meeting, who is entitled to vote at the meeting and who has complied with this Section 2.14(a).

(ii) For nominations or other business to be properly brought before an annual meeting by a shareholder pursuant to clause (3) of paragraph (a)(i) of this Section 2.14(a), the shareholder must have given timely notice thereof in writing to the Secretary of the corporation and such other business must otherwise be a proper matter for action by the shareholders. To be timely, a shareholder's notice shall set forth all information required under this Section 2.14(a) and shall be delivered to the Secretary at the principal executive office of the corporation not earlier than the 90th day and not later than 5:00 p.m., Pacific Time, on the 60th day prior to the first anniversary of the date of mailing of the notice for the preceding year's annual meeting; *provided*, *however*, that in the event that the date of the mailing of the notice for the annual meeting is advanced or delayed by more than 30 days from the first anniversary of the date of mailing of the notice for the preceding year's annual meeting, notice by the shareholder to be timely must be so delivered not earlier than the 90th day prior to the date of mailing of the notice for such annual meeting and not later than 5:00 p.m., Pacific Time, on the later of the 60th day prior to the date of mailing of the notice for such annual meeting or the tenth day following the day on which public announcement of the date of mailing of the notice for such meeting is first made. The public announcement of a postponement or adjournment of an annual meeting shall not commence a new time period for the giving of a shareholder's notice as described above.

(iii) Such shareholder's notice shall set forth (1) as to each person whom the shareholder proposes to nominate for election or re-election as a director, (A) the name, age, business address and residence address of each such person; (B) the principal occupation or employment of each such person; (C) the class and number of shares of capital stock of the corporation beneficially owned by each such person; and (D) any other information relating to such person that is required to be disclosed in solicitations of proxies for election of directors, or is otherwise required, in each case pursuant to Regulation 14A under the Securities Exchange Act of 1934, as amended (including without limitation such persons' written consent to being named in the proxy statement as a nominee and to serving as a director if elected); and (2) as to the shareholder giving the notice, (A) the name and address, as they appear on the corporation's books, of such shareholder and (B) the class and number of shares of capital stock of the corporation beneficially owned by such shareholder.

(iv) Such shareholder's notice, as to any other business that the shareholder proposes to bring before the meeting, shall set forth with particularity (1) the name and address of the shareholder submitting such proposal and all persons acting in concert with such shareholder; (2) the name and address of the persons identified in clause (1), as they appear on the corporation's books (if they so appear); (3) the class and number of shares of capital stock of the corporation beneficially owned by the persons identified in clause (1); (4) a description of the proposal containing all material information relating thereto, including, without limitation, the reasons for submitting such proposal; and (v) such other information as the Board of Directors reasonably determines is necessary or appropriate to enable the Board of Directors and shareholders of the corporation to consider such proposal.

(b) Special Meeting of Shareholders. Only such business shall be conducted at a special meeting of shareholders as shall have been brought before the meeting pursuant to the corporation's notice of meeting. Nominations of individuals for election to the Board of Directors may be made at a special meeting of shareholders at which directors are to be elected (i) pursuant to the corporation's notice of meeting, (ii) by or at the direction of the Board of Directors or (iii) provided that the Board of Directors has determined that directors shall be elected at such special meeting, by any shareholder of the corporation who is a shareholder of record both at the time of giving of notice provided for in this Section 2.14 and at the time of the special meeting, who is entitled to vote at the meeting and who complied with the notice procedures set forth in this Section 2.14(b). In the event the corporation calls a special meeting of shareholders for the purpose of electing one or more individuals to the Board of Directors, any such shareholder may nominate an individual or individuals (as the case may be) for election as a director as specified in the corporation's notice of meeting, if the shareholder's notice required by paragraph (ii) of Section 2.14(a) shall be delivered to the Secretary at the principal executive office of the corporation not earlier than the 90th day prior to such special meeting and not later than 5:00 p.m., Pacific Time, on the later of the 60th day prior to such special meeting or the tenth day following the day on which public announcement is first made of the date of the special meeting and of the nominees proposed by the Board of Directors to be elected at such meeting. The public announcement of a postponement or adjournment of a special meeting shall not commence a new time period for the giving of a shareholder's notice as described above.

(c) General.

(i) Upon written request by the Secretary or the Board of Directors or any committee thereof, any shareholder proposing a nominee for election as a director or any proposal for other business at a meeting of shareholders shall provide, within five business days of delivery of such request (or such other period as may be specified in such request), written verification, satisfactory, in the discretion of the Board of Directors or any committee thereof or any authorized officer of the corporation, to demonstrate the accuracy of any information submitted by the shareholder pursuant to this Section 2.14. If a shareholder fails to provide such written verification within such period, the information as to which written verification was requested may be deemed not to have been provided in accordance with this Section 2.14.

(ii) Only such individuals who are nominated in accordance with this Section 2.14 shall be eligible for election by shareholders as directors, and only such business shall be conducted at a meeting of shareholders as shall have been brought before the meeting in accordance with this Section 2.14. The Chairman of the meeting shall have the power to determine whether a nomination or any other business proposed to be brought before the meeting was made or proposed, as the case may be, in accordance with this Section 2.14 and, if any proposed nomination or business is not in compliance with this Section 2.14, to declare that such defective nomination or proposal be disregarded.

(iii) For purposes of this Section 2.14, (1) the "date of mailing of the notice" shall mean the date of the proxy statement for the solicitation of proxies for election of directors and (2) "public announcement" shall mean disclosure (A) in a press release reported by the Dow Jones News Service, Associated Press, Business Wire, PR Newswire or comparable news service or (B) in a document publicly filed by the corporation with the Securities and Exchange Commission pursuant to the Exchange Act.

(iv) Notwithstanding the foregoing provisions of this Section 2.14, a shareholder shall also comply with all applicable requirements of state law and of the Exchange Act and the rules and regulations thereunder with respect to the matters set forth in this Section 2.14. Nothing in this Section 2.14 shall be deemed to affect any right of a shareholder to request inclusion of a proposal in, nor the right of the corporation to omit a proposal from, the corporation's proxy statement pursuant to Rule 14a-8 (or any successor provision) under the Exchange Act.

(v) A copy of this Section 2.14 shall be set forth in a notice to shareholders of any annual or special meeting of the shareholders.

ARTICLE III

DIRECTORS

Section 3.1 POWERS.

Subject to any provisions of the California Corporations Code, of the Amended and Restated Articles of Incorporation and of these Amended and Restated Bylaws limiting the powers of the Board of Directors or reserving powers to the shareholders, the Board of Directors shall, directly or by delegation, manage the business and affairs of the corporation and exercise all corporate powers permitted by law. The Board of Directors may organize and operate any committees deemed necessary and desirable by the Board of Directors.

Section 3.2 NUMBER AND QUALIFICATION OF DIRECTORS.

(a) The number of directors of the corporation shall not be less than eight (8) nor more than eleven (11). The exact number of directors shall be eight (8) until changed, within the limits specified above, by a resolution duly adopted by the Board of Directors or by the shareholders of the corporation.

(b) The maximum or minimum authorized number of directors may only be changed by an amendment of this section approved by the vote of a majority of the outstanding shares entitled to vote; *provided, however*, that an amendment reducing the minimum number to a number less than five (5) shall not be adopted if the votes cast against its adoption at a meeting exceed 16-2/3% of such outstanding shares; *provided further*, however, that in no case shall the stated maximum authorized number of directors exceed two times the stated minimum number of authorized directors minus one.

(c) No reduction of the authorized number of directors shall have the effect of removing any director before his or her term of office expires.

Section 3.3 CLASSIFICATION OF DIRECTORS.

(a) Upon the effectiveness of Article IX of the corporation's Amended and Restated Articles of Incorporation, the Board of Directors shall be classified into two classes, as nearly equal in numbers as the then total number of directors constituting the entire Board of Directors permits, the members of each class to serve for a term of two years.

(b) Upon the effectiveness of Article IX of the corporation's Amended and Restated Articles of Incorporation, the election of directors by the shareholders shall not be by cumulative voting.

(c) At the first annual meeting of shareholders held after the effectiveness of Article IX of the corporation's Amended and Restated Articles of Incorporation, directors of the first class shall be elected to hold office for a term expiring at the next succeeding annual meeting of shareholders and directors of the second class shall be elected to hold office for a term expiring at the second succeeding annual meeting of shareholders. At each subsequent annual meeting of shareholders, the successor to the class of directors whose term shall then expire shall be elected to hold office for a term expiring at the second succeeding annual meeting of shareholders.

(d) If at any time this corporation ceases to be a listed corporation as defined in Section 301.5 of the California Corporations Code, at each succeeding annual meeting of shareholders where the existing term of a class of directors is expiring, the directors of each such class shall then be elected for a term expiring in one year until all directors are elected for one year terms. The election of all directors at the annual meeting of shareholders for a term of one year shall continue until the corporation once again qualifies as a listed corporation within the meaning of Section 301.5 of the California Corporations Code, and the foregoing provisions of Article IX of the corporation's Amended and Restated Articles of Incorporation can be reinstated.

Section 3.4 ELECTION AND TERM OF OFFICE.

Except as provided in Section 3.7 of these Amended and Restated Bylaws, each director, including a director elected to fill a vacancy, shall hold office until the expiration of the term for which elected and until his successor has been elected and qualified.

Section 3.5 DIRECTOR'S OATH.

Each director upon taking office shall make an oath or affirmation as required by Section 682 of the California Financial Code, and each such oath, subscribed by the director and certified by the officer before whom it is taken, shall be immediately filed with the California Superintendent of Banks.

Section 3.6 RESIGNATION.

Any director may resign effective upon giving written notice to the Chairman of the Board of Directors, the President, the Secretary or the Board of directors of the corporation, unless the notice specifies a later time for the effectiveness of such resignation. If the resignation is effective at a future time a successor may be elected to take office when the resignation becomes effective.

Section 3.7 REMOVAL OF DIRECTORS.

(a) A director may be removed from office by the Board of Directors if he or she is declared of unsound mind by an order of court or convicted of a felony.

(b) Any or all of the directors may be removed without cause if such removal is approved by the affirmative vote of a majority of the outstanding shares entitled to vote; *provided*, *however*, that a director may not be removed if the votes cast against removal of the director would be sufficient to elect the director if voted cumulatively (without regard to whether shares may otherwise be voted cumulatively) at an election at which the same total number of votes were cast and either the number of directors elected at the most recent annual meeting of shareholders, or if greater, the number of directors for whom removal is being sought, were then being elected.

Section 3.8 VACANCIES.

(a) A vacancy or vacancies on the Board of Directors shall exist on the death, resignation, or removal of any director, or if the authorized number of directors is increased or the shareholders fail to elect the full authorized number of directors.

(b) Except for a vacancy created by the removal of a director, vacancies on the Board of Directors may be filled by a majority of the remaining directors although less than a quorum, or by a sole remaining director, and each director elected in this manner shall hold office until his or her successor is elected at an annual or special shareholders' meeting. A vacancy created by the removal of a director shall be filled only by shareholders.

(c) The shareholders may elect a director at any time to fill any vacancy not filled by the directors.

Section 3.9 PLACE OF MEETINGS.

(a) Regular and special meetings of the Board of Directors may be held at any place within the State of California which has been designated in the notice of the meeting, or, if not stated in the notice or there is no notice, designated by a resolution or by written consent of all of the members of the Board of Directors.

(b) If the place of a regular or special meeting is not designated in the notice or fixed by a resolution of the board or consented to in writing by all members of the Board of Directors, it shall be held at the corporation's principal administrative office.

Section 3.10 ORGANIZATION MEETINGS.

The Board of Directors shall hold a regular meeting not less than once each calendar quarter. The Board of Directors shall hold the regular meetings at such times and places as are fixed by the Board of Directors. Call and notice of regular meetings of the Board of Directors shall not be required.

Section 3.11 SPECIAL MEETINGS.

(a) Special meetings of the Board of Directors for any purpose or purposes may be called at any time by the Chairman of the Board of Directors, the Chief Executive Officer, the President, the Secretary, or any two directors.

(b) Special meetings of the Board shall be held upon four days' notice by mail or 48 hours' notice delivered personally or by telephone, including a voice messaging system or other system or technology designed to record and communicate messages, telegraph, facsimile, electronic mail or other electronic means. Notice by mail shall be deemed to have been given at the time a written notice is deposited in the United States Mails, postage prepaid. Any other written notice, including facsimile, telegram or electronic mail message, shall he deemed to have been given at the time it is personally delivered to the recipient or is delivered to a common carrier for transmission, or actually transmitted by the person giving the notice by electronic means, to the recipient. Oral notice shall be deemed to have been given at the time it is communicated, in person or by telephone, including a voice messaging system or other system or technology designed to record or communicate messages, or wireless, to the recipient, including the recipient's designated voice mailbox or address on such system, or to a person at the office of the recipient who the person giving the notice has reason to believe will promptly communicate it to the recipient.

Section 3.12 QUORUM; ACTION AT MEETINGS.

(a) A majority of the authorized number of directors shall constitute a quorum of the Board of Directors for the transaction of business, except to adjourn a meeting under this Section 3.12 of these Amended and Restated Bylaws.

(b) Every act or decision done or made by a majority of the directors present at a meeting duly held at which a quorum is present is the act of the Board of Directors, unless the vote of a greater number is required by law, the Amended and Restated Articles of Incorporation or these Amended and Restated Bylaws, and subject to the provisions of Section 310 (Transactions with Interested Directors) and subdivision (e) of Section 317 (Indemnification of Corporate Agents) of the California Corporations Code.

(c) A meeting at which a quorum is initially present may continue to transact business notwithstanding the withdrawal of directors, provided that any action taken is approved by at least a majority of the required quorum for such meeting.

Section 3.13 CONTENTS OF NOTICE AND WAIVER OF NOTICE.

(a) Neither the business to be transacted at, nor the purpose of, any regular or special Board of Directors meeting need be specified in the notice or waiver of notice of the meeting.

(b) Notice of a meeting need not be given to any director who signs a waiver of notice or a consent to holding the meeting or an approval of the minutes thereof, either before or after the meeting, or who attends the meeting without protesting, prior thereto or at its commencement, the lack of notice to said director. All such waivers, consents and approvals shall be filed with the corporate records or made a part of the minutes of the meeting.

Section 3.14 ADJOURNMENT.

A majority of the directors present, whether or not a quorum is present, may adjourn any meeting to another time and place. If the meeting is adjourned for more than twenty-four (24) hours, notice of the adjournment to another time or place shall be given prior to the time of the adjourned meeting to the directors who were not present at the time of the adjournment.

Section 3.15 MEETINGS BY CONFERENCE TELEPHONE.

(a) Members of the Board of Directors may participate in a meeting through use of conference telephone or similar communications equipment, so long as all members participating in such meeting can hear one another.

(b) Members of the Board of Directness may participate in a meeting through the use of electronic video screen communication or other communications equipment, other than conference telephone if all of the provisions of Section 307(a)(6) of the California Corporations Code are followed.

(c) Participation by directors in a meeting in the manner provided in this Section 3.15 constitutes presence in person at such meeting.

Section 3.16 ACTION WITHOUT A MEETING.

Any action required or permitted to be taken by the Board of Directors may be taken without a meeting, if all members of the Board of Directors shall individually or collectively consent in writing to such action. Such written consent or consents shall be filed with the minutes of the proceedings of the Board of Directors. Such action by written consent shall have the same force and effect as a unanimous vote of such directors.

Section 3.17 FEES AND COMPENSATION.

Directors and members of the committees may receive such compensation, if any, for their services, and such reimbursement for expenses, as may be fixed or determined by resolution of the Board of Directors.

Section 3.18 COMMITTEES.

(a) The Board of Directors may, by resolution adopted by a majority of the authorized number of directors, designate one or more committees, each consisting of two or more directors, to serve at the pleasure of the Board of Directors. The Board of Directors may designate one or more directors as alternate members of any committee, who may replace any absent member at any meeting of the committee. The Board of Directors may delegate to any such committee, to the extent provided in such resolution, any of the Board of Directors' powers and authority in the management of the corporation's business and affairs, except such powers and authority that conflict with the California Corporations Code or the corporation's Amended and Restated Articles of Incorporation.

(b) The Board of Directors may prescribe appropriate rules, not inconsistent with these Amended and Restated Bylaws, by which proceedings of any such committee shall be conducted. The provisions of Amended and Restated Bylaws relating to the calling of meetings of the Board of Directors, notice of meetings of the Board of Directors and waiver of such notice, adjournments of meetings of the Board of Directors, written consents to Board of Directors meetings and approval of minutes, action by the Board of Directors by consent in writing without a meeting, the place of holding such meetings, meetings by conference telephone or similar communications equipment, the quorum for such meetings, the vote required at such meetings and the withdrawal of directors after commencement of a meeting shall apply to committees of the Board of Directors and action by such committees. In addition, any member of the committee designated by the Board of Directors as the Chairman or as Secretary of the committee or any two members of a committee may call meetings of the committee. Regular meetings of any committee may be held without notice if the time and place of such meetings are fixed by the Board of Directors or the committee.

ARTICLE IV

OFFICERS

Section 4.1 OFFICERS.

(a) The officers of the corporation shall be a Chairman of the Board or a President, or both, a Chief Executive Officer, a Secretary and a Chief Financial Officer.

(b) The corporation may also have, at the discretion of the Board of Directors, one or more Vice-Chairmen, one or more Vice Presidents, one or more Assistant Secretaries, a Cashier, one or more Assistant Cashiers and such other officers as may be appointed in accordance with the provisions of Section 4.3 of this Article IV. Any two or more offices may be held by the same person; *provided, however*, that in the execution of written instruments and in the performance of any executive or administrative duties on behalf of the corporation, such officer may only act in one capacity when joint execution or action by two officers is required.

Section 4.2 ELECTIONS.

The officers of the corporation, except such officers as may be appointed in accordance with the provisions of Section 4.3 or Section 4.5 of this Article IV, shall be chosen by the Board of Directors and serve at the pleasure of the Board of Directors, and each shall hold his office until he shall resign or be removed or is otherwise disqualified to serve, or until his successor is chosen and qualified.

Section 4.3 OTHER OFFICERS.

The Board of Directors may appoint, and may empower the Chairman of the Board or the Chief Executive Officer or both of them to appoint, such other officers as the business of the corporation may require, each of whom shall hold office for such period, have such authority and perform such duties as are provided in the bylaws or as the Board of Directors may from time to time determine.

Section 4.4 REMOVAL AND RESIGNATION.

(a) Any officer may be removed with or without cause either by the Board of Directors or, except for an officer chosen by the Board of Directors, by any officer upon whom the power of removal may be conferred by the board (subject, in each case, to the rights, if any, of an officer under any contract of employment).

(b) Any officer may resign at any time upon written notice to the corporation (without prejudice however, to the rights, if any, of the corporation under any contract to which the officer is a party). Any such resignation shall take effect upon receipt of such notice or at any such later time as agreed to by the Board of Directors. If the resignation is effective at a future time, a successor may be elected to take office when the resignation becomes effective. Unless a resignation specifies otherwise, its acceptance by the corporation shall not be necessary to make it effective.

Section 4.5 VACANCIES.

A vacancy in any office because of death, resignation, removal, disqualification or any other cause shall be filled in the manner prescribed in these Amended and Restated Bylaws for regular appointments to such office.

Section 4.6 CHAIRMAN OF THE BOARD.

The Board of Directors may, in its discretion, elect a Chairman of the Board who, unless otherwise determined by the Board of Directors, shall preside at all meetings of the Board of Directors at which he is present and shall exercise and perform any other powers and duties assigned to him by the Board of Directors or prescribed by these Amended and Restated Bylaws. If the office of President is vacant, the Chairman of the Board shall exercise the duties of the President, and when so acting, shall have all the powers of, and be subject to all the restrictions on, the President. The Chairman of the Board shall preside as chairman at all meetings of the shareholders unless otherwise determined by the Board of Directors.

Section 4.7 VICE-CHAIRMAN OF THE BOARD.

The Board of Directors may, in its discretion, elect one Vice-Chairman of the Board or more than one Vice-Chairmen of the Board. Unless otherwise determined by the Board of Directors, the Vice-Chairman of the Board shall preside as Chairman, or if there are Vice-Chairmen of the Board, the Vice Chairmen of the Board shall jointly preside as co-chairmen, at all meetings of the Board of Directors or meetings of the shareholders from which the Chairman of the Board is absent. The Vice-Chairman, or Vice-Chairmen, of the Board shall exercise and perform any other powers and duties assigned to the Vice-Chairman of the Board by the Board of Directors or prescribed by these Amended and Restated Bylaws. If the office of Chairman of the Board is vacant, the Vice-Chairman of the Board shall exercise, or if there are Vice-Chairmen, the Vice-Chairmen of the Board shall jointly exercise, the duties of the Chairman of the Board, and when so acting, shall have all the powers of, and be subject to the restrictions on, the Chairman of the Board.

Section 4.8 CHIEF EXECUTIVE OFFICER.

Subject to any supervisory powers, if any, that the Board of Directors or these Amended and Restated Bylaws have given to the Chairman of the Board, if there be such an officer, or to the President, the Chief Executive Officer shall be the corporation's general manager. Subject to the control of the Board of Directors, the Chief Executive Officer shall direct the total operation of the corporation and shall have responsibility for the attainment of goals, plans and directives established by the Board of Directors. The Chief Executive Officer shall be a member of the Board of Directors. Unless otherwise determined by the Board of Directors, and in the absence of the Chairman of the Board and the Vice-Chairman, or Vice-Chairmen, of the Board, the Chief Executive Officer shall preside as Chairman at all meetings of the Board of Directors and of the shareholders. The Chief Executive Officer shall have the general powers and duties of management usually vested in the office of Chief Executive Officer and shall have any other powers and duties prescribed by the Board of Directors or these Amended and Restated Bylaws.

Section 4.9 PRESIDENT.

Subject to the supervisory powers, if any, that these Amended and Restated Bylaws or the Board of Directors have given to the Chairman of the Board, if there be such an officer, or to the Chief Executive Officer, the President shall be the corporation's chief operating officer and shall have general supervision, direction and control of the business, affairs and officers of the corporation. Unless otherwise determined by the Board of Directors, and in the absence of the Chairman of the Board, the Vice-Chairman, or Vice-Chairmen, of the Board and the Chief Executive Officer, the President shall preside as chairman at all meetings of the Board of Directors and of the shareholders. The President shall have the general powers and duties of management usually vested in the office of President; shall have any other powers and duties prescribed by these Amended and Restated Bylaws or the Board of Directors; and shall be primarily responsible for carrying out all orders and resolutions of the Board of Directors.

Section 4.10 VICE PRESIDENTS.

In the absence or disability of the President, the Vice Presidents in order of their rank as fixed by the Board of Directors, or if not ranked, the Vice President designated by the Board of Directors, or if there has been no such designation, the Vice President designated by the Chief Executive Officer or President, shall perform all duties of the President, and when so acting, shall have all the powers of, and be subject to all the restrictions on, the President. Each Vice President shall have any of the powers and perform any other duties that from time to time the Board of Directors, these Amended and Restated Bylaws or the Chief Executive Officer may prescribe for him.

Section 4.11 SECRETARY; ASSISTANT SECRETARY.

The Secretary shall keep or cause to be kept a book of minutes of all meetings and actions by written consent of all directors, shareholders and committees of the Board of Directors. The minutes of each meeting shall state the time and place that it was held and such other information as shall be necessary to determine whether the meeting was held in accordance with the law and these Amended and Restated Bylaws and the actions taken thereat. The Secretary shall keep or cause to be kept at the corporation's principal executive office, or at the office of its transfer agent or registrar, a record of the shareholders of the corporation, giving the names and addresses of all shareholders and the number and class of shares held by each. The Secretary shall give, or cause to be given, notice of all meetings of shareholders, directors and committees required to be given under these Amended or Restated Bylaws or by law, shall keep or cause the keeping of the corporate seal in safe custody and shall have any other powers and perform any other duties that are prescribed by the Board of Directors or these Amended or Restated Bylaws or the Chief Executive Officer. If the Secretary refuses or fails to give notice of any meeting lawfully called, any other officer of the corporation may give notice of such meeting. The Assistant Secretary, or if there be more than one, any Assistant Secretary, may perform any or all of the duties and exercise any or all of the powers of the Secretary unless prohibited from doing so by the Board of Directors, the chief executive officer or the Secretary, and shall have such other powers and perform any other duties as are prescribed for him by the Board of Directors or the chief executive officer.

Section 4.12 CHIEF FINANCIAL OFFICER.

The Chief Financial Officer, who shall also be deemed to be the treasurer, when a treasurer may be required, shall keep and maintain, or cause to be kept and maintained, adequate and correct books and records of account. The Chief Financial Officer shall cause all money and other valuables in the name and to the credit of the corporation to be deposited at the depositories designated by the Board of Directors or any person authorized by the Board of Directors to designate such depositories. He shall render to the chief executive officer and Board of Directors when requested by either of them, an account of all his transactions as Chief Financial Officer and of the financial condition of the corporation, and shall have any other powers and perform any other duties prescribed by the Board of Directors, the bylaws or the chief executive officer.

ARTICLE V

MISCELLANEOUS

Section 5.1 INSPECTION OF CORPORATE RECORDS.

(a) Books and records of account and minutes of the proceedings of the shareholders, Board of Directors, and committees of the Board of Directors shall be kept available at the principal office for inspection by the shareholders to the extent required by Section 1601 of the California Corporations Code.

(b) Every director shall have the absolute right at any reasonable time to inspect and copy all books, records and documents of every kind and to inspect the physical properties of the corporation and its subsidiary corporations, domestic or foreign. Such inspection by a director may be made in person or by agent or attorney and includes the right to copy and make extracts.

Section 5.2 CHECKS, DRAFTS, ETC.

All checks, drafts or other orders for payment of money, notes or other evidences of indebtedness, issued in the name of or payable to the corporation, shall be signed or endorsed by such person or persons and in such manner as, from time to time, shall be determined by resolution of the Board of Directors. The Board of Directors may authorize one or more officers of the corporation to designate the person or persons authorized to sign such documents and the manner in which such documents shall be signed.

Section 5.3 ANNUAL AND OTHER REPORTS TO SHAREHOLDERS.

(a) The Board of Directors shall cause to be sent to the shareholders such annual or other periodic reports as the Board of Directors considers appropriate or as otherwise required by law.

(b) If no annual report for the last fiscal year has been sent to shareholders, the corporation shall, upon the written request of any shareholder made more than 120 days after the close of such fiscal year, deliver or mail to the person making the request within 30 days thereafter the financial statements referred to in Section 1501(a) for such year.

Section 5.4 CORPORATE CONTRACTS, ETC.: HOW EXECUTED.

The Board of Directors, except as these Amended and Restated Bylaws or the Amended and Restated Articles of Incorporation otherwise provide, may authorize any officer or officers and/or agent or agents to enter into any contract or execute any instrument in the name of and/or on behalf of the corporation, and such authority may be general or confined to specific instances.

Section 5.5 CERTIFICATE FOR SHARES.

The shares of the corporation shall be represented by certificates, unless and until the Board of Directors of the corporation adopts a resolution permitting some or all of any class or series of stock to be uncertificated. Any such resolution shall not apply to shares represented by a certificate until the certificate is surrendered to the corporation. Notwithstanding the adoption of any resolution providing for uncertificated shares, every holder of stock of the corporation represented by certificates and, upon request, every holder of uncertificated shares, shall be entitled to have a certificate for shares of stock of the corporation executed by (a) the Chairman or Vice-Chairman of the Board, the President or any Executive Vice President, and (b) the Chief Financial Officer, the Secretary or an Assistant Secretary, certifying the number of shares owned by such stockholder in the corporation.

Section 5.6 LOST CERTIFICATES.

No new certificate for shares shall be issued in place of any certificate theretofore issued unless the latter is surrendered and cancelled at the same time; *provided*, *however,* that, a new certificate may be issued without the surrender and cancellation of the old certificate if the certificate theretofore issued is alleged to have been lost, stolen or destroyed. In case of any such allegedly lost, stolen or destroyed certificate, the corporation may require the owner thereof or the legal representative of such owner to give the corporation a bond (or other adequate security) sufficient to indemnify it against any claim that may be made against it (including any expense or liability) on account of the alleged loss, theft or destruction of any such certificate or the issuance of such new certificate.

Section 5.7 REPRESENTATION OF SHARES OF OTHER CORPORATIONS.

Unless the Board of Directors shall otherwise determine, the Chairman of the Board, any Vice Chairman, the President, the Chief Executive Officer, and the Secretary of this corporation are each authorized to vote, represent and exercise on behalf of this corporation all rights incident to any and all shares of any other corporation or corporations standing in the name of this corporation. The authority herein granted to such officers to vote or represent on behalf of this corporation any and all shares held by this corporation in any other corporation or corporations may be exercised either by such officers in person or by any person authorized so to do by proxy or power of attorney or other document duly executed by any such officer.

Section 5.8 CONSTRUCTION AND DEFINITIONS.

Unless the context otherwise requires, the general provisions, rules of construction and definitions contained in the California Corporations Code shall govern the construction of these Amended and Restated Bylaws. Without limiting the generality of the foregoing, the masculine gender includes the feminine and neuter, the singular number includes the plural and the plural number includes the singular, and the term “person” includes a corporation as well as a natural person.

Section 5.9 FISCAL YEAR.

The fiscal year of this corporation shall begin on the first day of January and end on the 31st day of December of each year.

Section 5.10 INDEMNIFICATION OF CORPORATE AGENTS.

The corporation shall have power to indemnify each of its agents to the fullest extent permissible by the California Corporations Code. Without limiting the generality of the foregoing sentence, the corporation:

(a) is authorized to provide indemnification of agents in excess of that expressly permitted by Section 317 of the California Corporations Code for those agents of the corporation for breach of duty to the corporation and its shareholders, *provided*, *however*, that the corporation is not authorized to provide indemnification of any agent for any acts or omissions or transactions from which a director may not be relieved of liability as set forth in the exception to Section 204(a)(10) of the California Corporations Code or as to circumstances in which indemnity is expressly prohibited by Section 317 of the California Corporations Code;

(b) shall advance the expenses reasonably expected to be incurred by such agent in defending any such proceeding upon receipt of the undertaking required by subdivision (f) of Section 317 of the California Corporations Code; and

(c) shall have power to purchase and maintain insurance on behalf of any agent of the corporation against any liability asserted against or incurred by the agent in such capacity or arising out of the agent's status as such, whether or not the corporation would have the power to indemnify the agent against such liability under the provisions of section 317 of the California Corporations Code.

The term "agent" used in this section 5.10 shall have the same meaning as such term in section 317 of the California Corporations Code.

ARTICLE VI

AMENDMENTS

Section 6.1 POWER TO AMEND.

(a) Except as otherwise provided in the Amended and Restated Articles of Incorporation or the California Corporations Code, these Amended and Restated Bylaws or any of them may be amended or repealed, in any respect, and new bylaws may be adopted, at any time, either (i) by the affirmative vote of the holders of a majority of the outstanding shares entitled to vote or (ii) by the affirmative vote of a majority of the directors present at a meeting of the Board of Directors, in each case, in accordance with the terms of these Amended and Restated Bylaws.

(b) Except as otherwise provided in the Amended and Restated Articles of Incorporation, any bylaw adopted by the Board of Directors may be amended or repealed by the affirmative vote of a majority of the outstanding shares entitled to vote.

Section 6.2 AMENDMENT AFFECTING ELECTION OF DIRECTORS.

If any bylaw regulating an impending election of directors is adopted, amended, or repealed by the Board of Directors, there shall be set forth in the notice of the next meeting of shareholders for the election of directors the bylaw so adopted, amended, or repealed, together with a concise statement of the changes made.

CERTIFICATE OF SECRETARY

I, the undersigned, do hereby certify:

(a) That I am the duly elected and acting secretary of Preferred Bank, a California banking corporation; and

(b) That the foregoing Amended and Restated Bylaws, comprising twenty (20) pages, constitute the bylaws of such corporation as duly adopted by action of the Board of Directors of the corporation duly taken on November 21, 2007.

IN WITNESS WHEREOF, I have hereunto subscribed my name and affixed the seal of such corporation this 26th day of November, 2007.

/s/ Li Yu
Name: Li Yu
Title: Secretary