

TRICO BANCSHARES /  
Form 10-Q  
August 09, 2016  
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**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**  
**WASHINGTON, D.C. 20549**

**FORM 10-Q**

x **Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934  
for the quarterly period ended: June 30, 2016**

.. **Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934  
for the transition period from \_\_\_\_\_ to \_\_\_\_\_.**

**Commission File Number: 000-10661**

**TriCo Bancshares**  
**(Exact Name of Registrant as Specified in Its Charter)**

**CALIFORNIA**  
**(State or Other Jurisdiction of**

**94-2792841**  
**(I.R.S. Employer**

**Incorporation or Organization)**

**Identification Number)**

**63 Constitution Drive**

**Chico, California 95973**

**(Address of Principal Executive Offices)(Zip Code)**

**(530) 898-0300**

**(Registrant's Telephone Number, Including Area Code)**

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

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

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

Large accelerated filer  Accelerated filer

Non-accelerated filer  Smaller reporting company

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

Indicate the number of shares outstanding for each of the issuer's classes of common stock, as of the latest practical date:

Common stock, no par value: 22,822,325 shares outstanding as of August 5, 2016

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TriCo Bancshares

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**FORWARD-LOOKING STATEMENTS**

This report on Form 10-Q contains forward-looking statements about TriCo Bancshares (the "Company" or "we") that are subject to the protection of the safe harbor provisions contained in the Private Securities Litigation Reform Act of 1995. These forward-looking statements are based on the current knowledge and belief of the Company's management ("Management") and include information concerning the Company's possible or assumed future financial condition and results of operations. When you see any of the words "believes", "expects", "anticipates", "estimates", or similar expressions, it may mean the Company is making forward-looking statements. A number of factors, some of which are beyond the Company's ability to predict or control, could cause future results to differ materially from those contemplated. The reader is directed to the Company's annual report on Form 10-K for the year ended December 31, 2015 and Part II, Item 1A of this report for further discussion of factors which could affect the Company's business and cause actual results to differ materially from those suggested by any forward-looking statement made in this report. Such Form 10-K and this report should be read in their entirety to put any forward-looking statements in context and to gain a more complete understanding of the risks and uncertainties involved in the Company's business. Any forward-looking statement may turn out to be wrong and cannot be guaranteed. The Company does not intend to update any forward-looking statement after the date of this report.

**Table of Contents****PART I FINANCIAL INFORMATION****Item 1. Financial Statements (unaudited)****TRICO BANCSHARES****CONDENSED CONSOLIDATED BALANCE SHEETS**

(In thousands, except share data; unaudited)

|  | At June 30,<br>2016               | At December 31,<br>2015 |
|--|-----------------------------------|-------------------------|
|  | (in thousands, except share data) |                         |
| <b>Assets:</b>                               |                                   |                         |
| Cash and due from banks                      | \$ 88,157                         | \$ 94,305               |
| Cash at Federal Reserve and other banks      | 128,629                           | 209,156                 |
| Cash and cash equivalents                    | 216,786                           | 303,461                 |
| <b>Investment securities:</b>                |                                   |                         |
| Available for sale                           | 529,017                           | 404,885                 |
| Held to maturity                             | 674,412                           | 726,530                 |
| Restricted equity securities                 | 16,956                            | 16,956                  |
| Loans held for sale                          | 2,904                             | 1,873                   |
| Loans  | 2,653,630                         | 2,522,937               |
| Allowance for loan losses                    | (35,509)                          | (36,011)                |
| Total loans, net                             | 2,618,121                         | 2,486,926               |
| Foreclosed assets, net                       | 3,842                             | 5,369                   |
| Premises and equipment, net                  | 51,728                            | 43,811                  |
| Cash value of life insurance                 | 94,572                            | 94,560                  |
| Accrued interest receivable                  | 11,602                            | 10,786                  |
| Goodwill                                     | 64,311                            | 63,462                  |
| Other intangible assets, net                 | 7,282                             | 5,894                   |
| Mortgage servicing rights                    | 6,720                             | 7,618                   |
| Other assets                                 | 54,239                            | 48,591                  |
| <b>Total assets</b>                          | <b>\$ 4,352,492</b>               | <b>\$ 4,220,722</b>     |
| <b>Liabilities and Shareholders' Equity:</b> |                                   |                         |
| <b>Liabilities:</b>                          |                                   |                         |
| <b>Deposits:</b>                             |                                   |                         |
| Noninterest-bearing demand                   | \$ 1,181,702                      | \$ 1,155,695            |
| Interest-bearing                             | 2,559,694                         | 2,475,571               |

|   |                     |                     |
|---|---------------------|---------------------|
| Total deposits  | 3,741,396           | 3,631,266           |
| Accrued interest payable  | 727                 | 774                 |
| Reserve for unfunded commitments  | 2,883               | 2,475               |
| Other liabilities   | 57,587              | 65,293              |
| Other borrowings  | 19,464              | 12,328              |
| Junior subordinated debt  | 56,567              | 56,470              |
| <b>Total liabilities</b>  | <b>3,878,624</b>    | <b>3,768,606</b>    |
| Commitments and contingencies (Note 18)   |                     |                     |
| Shareholders' equity:   |                     |                     |
| Common stock, no par value: 50,000,000 shares authorized; issued and outstanding: |                     |                     |
| 22,822,325 at June 30, 2016   | 249,860             |                     |
| 22,775,173 at December 31, 2015   |                     | 247,587             |
| Retained earnings   | 217,935             | 206,307             |
| Accumulated other comprehensive income, net of tax                                | 6,073               | (1,778)             |
| <b>Total shareholders' equity</b>   | <b>473,868</b>      | <b>452,116</b>      |
| <b>Total liabilities and shareholders' equity</b>                                 | <b>\$ 4,352,492</b> | <b>\$ 4,220,722</b> |

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

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

(In thousands, except per share data; unaudited)

|   | Three months ended<br>June 30, |               | Six months ended<br>June 30, |               |
|---|--------------------------------|---------------|------------------------------|---------------|
|   | 2016                           | 2015          | 2016                         | 2015          |
| <b>Interest and dividend income:</b>  |                                |               |                              |               |
| Loans, including fees   | \$ 34,338                      | \$ 32,019     | \$ 69,076                    | \$ 63,184     |
| <b>Investment securities:</b>   |                                |               |                              |               |
| Taxable   | 6,535                          | 6,403         | 13,080                       | 12,202        |
| Tax exempt  | 975                            | 324           | 1,872                        | 485           |
| Dividends   | 410                            | 977           | 785                          | 1,313         |
| Interest bearing cash at Federal Reserve and other banks                            | 332                            | 144           | 571                          | 408           |
| <b>Total interest and dividend income</b>   | <b>42,590</b>                  | <b>39,867</b> | <b>85,384</b>                | <b>77,592</b> |
| <b>Interest expense:</b>  |                                |               |                              |               |
| Deposits  | 881                            | 854           | 1,736                        | 1,753         |
| Other borrowings  | 3                              | 1             | 5                            | 2             |
| Junior subordinated debt  | 546                            | 491           | 1,081                        | 973           |
| <b>Total interest expense</b>   | <b>1,430</b>                   | <b>1,346</b>  | <b>2,822</b>                 | <b>2,728</b>  |
| <b>Net interest income</b>  | <b>41,160</b>                  | <b>38,521</b> | <b>82,562</b>                | <b>74,864</b> |
| <b>Benefit from reversal of provision for loan losses</b>                           | <b>(773)</b>                   | <b>(633)</b>  | <b>(564)</b>                 | <b>(436)</b>  |
| <b>Net interest income after benefit from reversal of provision for loan losses</b> | <b>41,933</b>                  | <b>39,154</b> | <b>83,126</b>                | <b>75,300</b> |
| <b>Noninterest income:</b>  |                                |               |                              |               |
| Service charges and fees  | 8,099                          | 8,848         | 15,404                       | 16,192        |
| Gain on sale of loans   | 889                            | 837           | 1,692                        | 1,459         |
| Commissions on sale of non-deposit investment products                              | 611                            | 784           | 1,143                        | 1,749         |
| Increase in cash value of life insurance  | 681                            | 675           | 1,377                        | 1,350         |
| Other   | 965                            | 936           | 1,419                        | 1,510         |
| <b>Total noninterest income</b>   | <b>11,245</b>                  | <b>12,080</b> | <b>21,035</b>                | <b>22,260</b> |

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|                                   |               |               |               |               |
|-----------------------------------|---------------|---------------|---------------|---------------|
| Noninterest expense:              |               |               |               |               |
| Salaries and related benefits     | 20,045        | 17,242        | 39,310        | 35,342        |
| Other                             | 18,222        | 15,194        | 32,708        | 29,376        |
| <b>Total noninterest expense</b>  | <b>38,267</b> | <b>32,436</b> | <b>72,018</b> | <b>64,718</b> |
| Income before income taxes        | 14,911        | 18,798        | 32,143        | 32,842        |
| <b>Provision for income taxes</b> | <b>5,506</b>  | <b>7,432</b>  | <b>12,064</b> | <b>13,140</b> |
| Net income                        | \$ 9,405      | \$ 11,366     | \$ 20,079     | \$ 19,702     |
| <b>Earnings per share:</b>        |               |               |               |               |
| Basic                             | \$ 0.41       | \$ 0.50       | \$ 0.88       | \$ 0.87       |
| Diluted                           | \$ 0.41       | \$ 0.49       | \$ 0.87       | \$ 0.86       |

See accompanying notes to unaudited condensed consolidated financial statements.

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

(In thousands; unaudited)

|  | Three months ended<br>June 30, |           | Six months ended<br>June 30, |           |
|--|--------------------------------|-----------|------------------------------|-----------|
|  | 2016                           | 2015      | 2016                         | 2015      |
| Net income   | \$ 9,405                       | \$ 11,366 | \$ 20,079                    | \$ 19,702 |
| Other comprehensive income, net of tax:  |                                |           |                              |           |
| Unrealized gains (losses) on available for sale securities arising during the period | 4,157                          | (2,754)   | 7,707                        | (2,745)   |
| Change in minimum pension liability  | 148                            | 111       | 148                          | 222       |
| Change in joint beneficiary agreement liability                                      | (4)                            |           | (4)                          |           |
| Other comprehensive income (loss)  | 4,301                          | (2,643)   | 7,851                        | (2,523)   |
| Comprehensive income   | \$ 13,706                      | \$ 8,723  | \$ 27,930                    | \$ 17,179 |

See accompanying notes to unaudited condensed consolidated financial statements.

**TRICO BANCSHARES****CONDENSED CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY**

(In thousands, except share and per share data; unaudited)

|                                     | Shares of<br>Common<br>Stock | Common<br>Stock | Retained<br>Earnings | Accumulated<br>Other<br>Comprehensive<br>Income (loss) | Total      |
|-------------------------------------|------------------------------|-----------------|----------------------|--|------------|
| Balance at December 31, 2014        | 22,714,964                   | \$ 244,318      | \$ 176,057           | \$ (2,203)   | \$ 418,172 |
| Net income                          |                              |                 | 19,702               |  | 19,702     |
| Other comprehensive loss            |                              |                 |                      | (2,523)  | (2,523)    |
| Stock option vesting                |                              | 419             |                      |  | 419        |
| RSU vesting                         |                              | 202             |                      |  | 202        |
| PSU vesting                         |                              | 77              |                      |  | 77         |
| Stock options exercised             | 64,000                       | 1,236           |                      |  | 1,236      |
| Tax effect of stock option exercise |                              | 30              |                      |  | 30         |
| Repurchase of common stock          | (29,441)                     | (317)           | (381)                |  | (698)      |
| Dividends paid (\$0.24 per share)   |                              |                 | (5,473)              |  | (5,473)    |



|                                     |            |            |            |            |            |
|-------------------------------------|------------|------------|------------|------------|------------|
| Balance at June 30, 2015            | 22,749,523 | \$ 245,965 | \$ 189,905 | \$ (4,726) | \$ 431,144 |
| Balance at December 31, 2015        | 22,775,173 | \$ 247,587 | \$ 206,307 | \$ (1,778) | \$ 452,116 |
| Net income                          |            |            | 20,079     |            | 20,079     |
| Other comprehensive income          |            |            |            | 7,851      | 7,851      |
| Stock option vesting                |            | 311        |            |            | 311        |
| RSU vesting                         |            | 261        |            |            | 261        |
| PSU vesting                         |            | 125        |            |            | 125        |
| Stock options exercised             | 127,200    | 2,814      |            |            | 2,814      |
| RSUs released                       | 16,948     |            |            |            |            |
| Tax effect of stock option exercise |            | (192)      |            |            | (192)      |
| Tax effect of RSU release           |            | 10         |            |            | 10         |
| Repurchase of common stock          | (96,996)   | (1,056)    | (1,610)    |            | (2,666)    |
| Dividends paid (\$0.30 per share)   |            |            | (6,841)    |            | (6,841)    |
| Balance at June 30, 2016            | 22,822,325 | \$ 249,860 | \$ 217,935 | \$ 6,073   | \$ 473,868 |

See accompanying notes to unaudited condensed consolidated financial statements.

Table of Contents**TRICO BANCSHARES****CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**

(In thousands; unaudited)

|  | For the six months ended June 30, |               |
|--|-----------------------------------|---------------|
|  | 2016                              | 2015          |
| <b>Operating activities:</b>   |                                   |               |
| Net income   | \$ 20,079                         | \$ 19,702     |
| <b>Adjustments to reconcile net income to net cash provided by operating activities:</b> |                                   |               |
| Depreciation of premises and equipment, and amortization                                 | 3,245                             | 3,090         |
| Amortization of intangible assets  | 658                               | 578           |
| Benefit from reversal of provision for loan losses                                       | (564)                             | (436)         |
| Amortization of investment securities premium, net                                       | 2,334                             | 1,645         |
| Originations of loans for resale   | (58,952)                          | (55,669)      |
| Proceeds from sale of loans originated for resale  | 59,009                            | 55,656        |
| Gain on sale of loans  | (1,692)                           | (1,459)       |
| Change in market value of mortgage servicing rights                                      | 1,399                             | (15)          |
| Provision for losses on foreclosed assets  | 32                                | 241           |
| Gain on sale of foreclosed assets  | (149)                             | (426)         |
| Loss on disposal of fixed assets   | 39                                | 83            |
| Increase in cash value of life insurance   | (1,377)                           | (1,350)       |
| Life insurance proceeds in excess of cash value  | (238)                             |               |
| Equity compensation vesting expense  | 697                               | 698           |
| Tax effect of equity compensation exercise or release                                    | 182                               | (30)          |
| <b>Change in:</b>  |                                   |               |
| Reserve for unfunded commitments   | 408                               | (20)          |
| Interest receivable  | (816)                             | (789)         |
| Interest payable   | (47)                              | (181)         |
| Other assets and liabilities, net  | (629)                             | 4,249         |
| <b>Net cash from operating activities</b>  | <b>23,618</b>                     | <b>25,567</b> |
| <b>Investing activities:</b>   |                                   |               |
| Proceeds from maturities of securities available for sale                                | 26,359                            | 13,941        |
| Proceeds from maturities of securities held to maturity                                  | 50,963                            | 45,078        |
| Purchases of securities available for sale   | (155,444)                         | (220,383)     |
| Purchases of securities held to maturity   |                                   | (146,100)     |
| Loan origination and principal collections, net  | (135,638)                         | (112,372)     |
| Loans purchased  | (22,503)                          |               |
| Proceeds from sale of loans other than loans originated for sale                         | 27,049                            |               |
| Improvement of foreclosed assets   |                                   | (511)         |
| Proceeds from sale of other real estate owned  | 2,497                             | 1,033         |
| Proceeds from sale of premises and equipment   | 1                                 | 2             |
| Purchases of premises and equipment  | (9,053)                           | (1,293)       |

|   |            |            |
|---|------------|------------|
| Cash acquired in acquisition  | 156,316    |            |
| Net cash used by investing activities   | (59,453)   | (420,605)  |
| Financing activities:   |            |            |
| Net decrease in deposits  | (51,101)   | (38,741)   |
| Net change in other borrowings  | 7,136      | (2,541)    |
| Tax effect of equity compensation exercise or release   | (182)      | 30         |
| Repurchase of common stock  | (335)      | (31)       |
| Dividends paid  | (6,841)    | (5,473)    |
| Exercise of stock options   | 483        | 569        |
| Net cash used by financing activities   | (50,840)   | (46,187)   |
| Net change in cash and cash equivalents   | (86,675)   | (441,225)  |
| Cash and cash equivalents and beginning of year   | 303,461    | 610,728    |
| Cash and cash equivalents at end of period  | \$ 216,786 | \$ 169,503 |
| Supplemental disclosure of noncash activities:  |            |            |
| Unrealized gain (loss) on securities available for sale   | \$ 13,298  | \$ (4,737) |
| Loans transferred to foreclosed assets  | \$ 853     | \$ 1,649   |
| Market value of shares tendered in-lieu of cash to pay for exercise of options and/or related taxes | \$ 2,331   | \$ 667     |
| Supplemental disclosure of cash flow activity:  |            |            |
| Cash paid for interest expense  | \$ 2,869   | \$ 2,909   |
| Cash paid for income taxes  | \$ 12,540  | \$ 7,395   |
| Assets acquired in acquisition  | \$ 161,231 |            |
| Liabilities assumed in acquisition  | \$ 161,231 |            |

See accompanying notes to unaudited condensed consolidated financial statements.

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**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**Note 1 Summary of Significant Accounting Policies**

**Description of Business and Basis of Presentation**

TriCo Bancshares (the Company or we ) is a California corporation organized to act as a bank holding company for Tri Counties Bank (the Bank ). The Company and the Bank are headquartered in Chico, California. The Bank is a California-chartered bank that is engaged in the general commercial banking business in 26 California counties. Tri Counties Bank currently operates from 58 traditional branches and 10 in-store branches. The Company has five capital subsidiary business trusts (collectively, the Capital Trusts ) that issued trust preferred securities, including two organized by TriCo and three acquired with the acquisition of North Valley Bancorp. See Note 17 Junior Subordinated Debt.

The unaudited condensed financial statements of the Company have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission. Certain information and note disclosures normally included in annual financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted pursuant to those rules and regulations, although the Company believes that the disclosures made are adequate to make the information not misleading. In the opinion of the Company s management ( Management ), all adjustments, consisting solely of normal recurring adjustments, considered necessary for a fair presentation of results for the interim periods presented have been included. For financial reporting purposes, the Company s investments in the Capital Trusts of \$1,699,000 are accounted for under the equity method and, accordingly, are not consolidated and are included in other assets on the consolidated balance sheet. The subordinated debentures issued and guaranteed by the Company and held by the Capital Trusts are reflected as debt on the Company s consolidated balance sheet. These interim condensed consolidated financial statements should be read in conjunction with the financial statements and related notes contained in the Company s 2015 Annual Report on Form 10-K filed with the Securities and Exchange Commission on March 10, 2016.

**Use of Estimates in the Preparation of Financial Statements**

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 that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. The Company bases its estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions.

**Significant Group Concentration of Credit Risk**

The Company grants agribusiness, commercial, consumer, and residential loans to customers located throughout the northern San Joaquin Valley, the Sacramento Valley and northern mountain regions of California. The Company has a diversified loan portfolio within the business segments located in this geographical area. The Company currently classifies all its operation into one business segment that it denotes as community banking.

**Cash and Cash Equivalents**

For purposes of the consolidated statements of cash flows, cash and cash equivalents include cash on hand, amounts due from banks, and federal funds sold. Net cash flows are reported for loan and deposit transactions and other borrowings.

### **Investment Securities**

The Company classifies its debt and marketable equity securities into one of three categories: trading, available for sale or held to maturity. Trading securities are bought and held principally for the purpose of selling in the near term. Held to maturity securities are those securities which the Company has the ability and intent to hold until maturity. These securities are carried at cost adjusted for amortization of premium and accretion of discount, computed by the effective interest method over their contractual lives. All other securities not included in trading or held to maturity are classified as available for sale. Available for sale securities are recorded at fair value. Unrealized gains and losses, net of the related tax effect, on available for sale securities are reported as a separate component of other accumulated comprehensive income in shareholders' equity until realized. Premiums and discounts are amortized or accreted over the life of the related investment security as an adjustment to yield using the effective interest method. Dividend and interest income are recognized when earned. Realized gains and losses are derived from the amortized cost of the security sold. During the six months ended June 30, 2016 and throughout 2015, the Company did not have any securities classified as trading.

The Company assesses other-than-temporary impairment ( OTTI ) based on whether it intends to sell a security or if it is likely that the Company would be required to sell the security before recovery of the amortized cost basis of the investment, which may be maturity. For debt securities, if we intend to sell the security or it is more likely than not that we will be required to sell the security before recovering its cost basis, the entire impairment loss would be recognized in earnings as an OTTI. If we do not intend to sell the security and it is not likely that we will be required to sell the security but we do not expect to recover the entire amortized cost basis of the security, only the portion of the impairment loss representing credit losses would be recognized in earnings. The credit loss on a security is measured as the difference between the amortized cost basis and the present value of the cash flows expected to be collected. Projected cash flows are discounted by the original or current effective interest rate depending on the nature of the security being measured for potential OTTI. The remaining impairment related to all other factors, the difference between the present value of the cash flows expected to be collected and fair value, is recognized as a charge to other comprehensive income ( OCI ). Impairment losses related to all other factors are presented as separate categories within OCI. The accretion of the amount recorded in OCI increases the carrying value of the investment and does not affect earnings. If there is an indication of additional credit losses the security is re-evaluated according to the procedures described above. No OTTI losses were recognized during the six months ended June 30, 2016 and throughout 2015.

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### **Restricted Equity Securities**

Restricted equity securities represent the Company's investment in the stock of the Federal Home Loan Bank of San Francisco ( FHLB ) and are carried at par value, which reasonably approximates its fair value. While technically these are considered equity securities, there is no market for the FHLB stock. Therefore, the shares are considered as restricted investment securities. Management periodically evaluates FHLB stock for other-than-temporary impairment. Management's determination of whether these investments are impaired is based on its assessment of the ultimate recoverability of cost rather than by recognizing temporary declines in value. The determination of whether a decline affects the ultimate recoverability of cost is influenced by criteria such as (1) the significance of any decline in net assets of the FHLB as compared to the capital stock amount for the FHLB and the length of time this situation has persisted, (2) commitments by the FHLB to make payments required by law or regulation and the level of such payments in relation to the operating performance of the FHLB, (3) the impact of legislative and regulatory changes on institutions and, accordingly, the customer base of the FHLB, and (4) the liquidity position of the FHLB.

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

### **Loans Held for Sale**

Loans originated and intended for sale in the secondary market are carried at the lower of aggregate cost or fair value, as determined by aggregate outstanding commitments from investors of current investor yield requirements. Net unrealized losses are recognized through a valuation allowance by charges to noninterest income.

Mortgage loans held for sale are generally sold with the mortgage servicing rights retained by the Company. Gains or losses on the sale of loans that are held for sale are recognized at the time of the sale and determined by the difference between net sale proceeds and the net book value of the loans less the estimated fair value of any retained mortgage servicing rights.

### **Loans and Allowance for Loan Losses**

Loans originated by the Company, i.e., not purchased or acquired in a business combination, are referred to as originated loans. Originated loans that management has the intent and ability to hold for the foreseeable future or until maturity or payoff are reported at the principal amount outstanding, net of deferred loan fees and costs. Loan origination and commitment fees and certain direct loan origination costs are deferred, and the net amount is amortized as an adjustment of the related loan's yield over the actual life of the loan. Originated loans on which the accrual of interest has been discontinued are designated as nonaccrual loans.

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

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

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

Credit risk is inherent in the business of lending. As a result, the Company maintains an allowance for loan losses to absorb probable incurred losses inherent in the Company's originated loan portfolio. This is maintained through periodic charges to earnings. These charges are included in the Consolidated Statements of Income as provision for loan losses. All specifically identifiable and quantifiable losses are

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immediately charged off against the allowance. However, for a variety of reasons, not all losses are immediately known to the Company and, of those that are known, the full extent of the loss may not be quantifiable at that point in time. The balance of the Company's allowance for originated loan losses is meant to be an estimate of these probable incurred losses inherent in the portfolio.

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

The Company's method for assessing the appropriateness of the allowance for originated loan losses includes specific allowances for impaired originated loans, formula allowance factors for pools of credits, and allowances for changing environmental factors (e.g., interest rates, growth, economic conditions, etc.). Allowance factors for loan pools were based on historical loss experience by product type and prior risk rating.

During the three months ended September 30, 2015, the Company modified its methodology used to determine the allowance for home equity lines of credit that are about to exit their revolving period, or have recently entered into their amortization period and are now classified as home equity loans. This change in methodology increased the required allowance for such lines and loans by \$859,000, and \$459,000, respectively, and represents the increase in estimated incurred losses in these lines and loans as of September 30, 2015 due to higher required contractual principal and interest payments of such lines and loans.

Loans purchased or acquired in a business combination are referred to as acquired loans. Acquired loans are valued as of the acquisition date in accordance with Financial Accounting Standards Board Accounting Standards Codification ( FASB ASC ) Topic 805, *Business Combinations*. Loans acquired with evidence of credit deterioration since origination for which it is probable that all contractually required payments will not be collected are referred to as purchased credit impaired (PCI) loans. PCI loans are accounted for under FASB ASC Topic 310-30, *Loans and Debt Securities Acquired with Deteriorated Credit Quality*. Under FASB ASC Topic 805 and FASB ASC Topic 310-30, PCI loans are recorded at fair value at acquisition date, factoring in credit losses expected to be incurred over the life of the loan. Accordingly, an allowance for loan losses is not carried over or recorded as of the acquisition date. Fair value is defined as the present value of the future estimated principal and interest payments of the loan, with the discount rate used in the present value calculation representing the estimated effective yield of the loan. Default rates, loss severity, and prepayment speed assumptions are periodically reassessed and our estimate of future payments is adjusted accordingly. The difference between contractual future payments and estimated future payments is referred to as the nonaccretable difference. The difference between estimated future payments and the present value of the estimated future payments is referred to as the accretable yield. The accretable yield represents the amount that is expected to be recorded as interest income over the remaining life of the loan. If after acquisition, the Company determines that the estimated future cash flows of a PCI loan are expected to be more than originally estimated, an increase in the discount rate (effective yield) would be made such that the newly increased accretable yield would be recognized, on a level yield basis, over the remaining estimated life of the loan. If, thereafter, the Company determines that the estimated future cash flows of a PCI loan are expected to be less than previously estimated, an allowance for loan loss would be established through a provision for loan losses charged to expense to decrease the present value to



the required level. If the estimated cash flows improve after an allowance has been established for a loan, the allowance may be partially or fully reversed depending on the improvement in the estimated cash flows. Only after the allowance has been fully reversed may the discount rate be increased. PCI loans are put on nonaccrual status when cash flows cannot be reasonably estimated. PCI loans on nonaccrual status are accounted for using the cost recovery method or cash basis method of income recognition. The Company refers to PCI loans on nonaccrual status that are accounted for using the cash basis method of income recognition as PCI cash basis loans; and the Company refers to all other PCI loans as PCI other loans. PCI loans are charged off when evidence suggests cash flows are not recoverable. Foreclosed assets from PCI loans are recorded in foreclosed assets at fair value with the fair value at time of foreclosure representing cash flow from the loan. ASC 310-30 allows PCI loans with similar risk characteristics and acquisition time frame to be pooled and have their cash flows aggregated as if they were one loan. The Company elected to use the pooled method of ASC 310-30 for PCI other loans in the acquisition of certain assets and liabilities of Granite Community Bank, N.A. ( Granite ) during 2010 and Citizens Bank of Northern California ( Citizens ) during 2011.

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

Throughout these financial statements, and in particular in Note 4 and Note 5, when we refer to Loans or Allowance for loan losses we mean all categories of loans, including Originated, PNCI, PCI cash basis, and PCI - other. When we are not referring to all categories of loans, we will indicate which we are referring to Originated, PNCI, PCI cash basis, or PCI - other.

When referring to PNCI and PCI loans we use the terms nonaccretable difference, accretable yield, or purchase discount. Nonaccretable difference is the difference between undiscounted contractual cash flows due and undiscounted cash flows we expect to collect, or put another way, it is the undiscounted contractual cash flows we do not expect to collect. Accretable yield is the difference

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between undiscounted cash flows we expect to collect and the value at which we have recorded the loan on our financial statements. On the date of acquisition, all purchased loans are recorded on our consolidated financial statements at estimated fair value. Purchase discount is the difference between the estimated fair value of loans on the date of acquisition and the principal amount owed by the borrower, net of charge offs, on the date of acquisition. We may also refer to discounts to principal balance of loans owed, net of charge-offs. Discounts to principal balance of loans owed, net of charge-offs is the difference between principal balance of loans owed, net of charge-offs, and loans as recorded on our financial statements. Discounts to principal balance of loans owed, net of charge-offs arise from purchase discounts, and equal the purchase discount on the acquisition date.

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

**Foreclosed Assets**

Foreclosed assets include assets acquired through, or in lieu of, loan foreclosure. Foreclosed assets are held for sale and are initially recorded at fair value less estimated costs to sell at the date of foreclosure, establishing a new cost basis. Physical possession of residential real estate property collateralizing a consumer mortgage loan occurs when legal title is obtained upon completion of foreclosure or when the borrower conveys all interest in the property to satisfy the loan through completion of a deed in lieu of foreclosure or through a similar legal agreement. Any write-downs based on the asset's fair value less costs to sell at the date of acquisition are charged to the allowance for loan and lease losses. Any recoveries based on the asset's fair value less estimated costs to sell in excess of the recorded value of the loan at the date of acquisition are recorded to the allowance for loan and lease losses. These assets are subsequently accounted for at lower of cost or fair value less estimated costs to sell. If fair value declines subsequent to foreclosure, a valuation allowance is recorded through expense. Operating costs after acquisition are expensed. Revenue and expenses from operations and changes in the valuation allowance are included in other noninterest expense. Gain or loss on sale of foreclosed assets is included in noninterest income. Foreclosed assets that are not subject to a FDIC loss-share agreement are referred to as noncovered foreclosed assets.

Foreclosed assets acquired through FDIC-assisted acquisitions that are subject to a FDIC loss-share agreement, and all assets acquired via foreclosure of covered loans are referred to as covered foreclosed assets. Covered foreclosed assets are reported exclusive of expected reimbursement cash flows from the FDIC. Foreclosed covered loan collateral is transferred into covered foreclosed assets at the loan's carrying value, inclusive of the acquisition date fair value discount.

Covered foreclosed assets are initially recorded at estimated fair value less estimated costs to sell on the acquisition date based on similar market comparable valuations less estimated selling costs. Any subsequent valuation adjustments due to declines in fair value will be charged to noninterest expense, and will be mostly offset by noninterest income representing the corresponding increase to the FDIC indemnification asset for the offsetting loss reimbursement amount. Any recoveries of previous valuation adjustments will be credited to noninterest expense with a corresponding charge to noninterest income for the portion of the recovery that is due to the FDIC.

**Premises and Equipment**

Land is carried at cost. Land improvements, buildings and equipment, including those acquired under capital lease, are stated at cost less accumulated depreciation and amortization. Depreciation and amortization expenses are computed using the straight-line method over the estimated useful lives of the related assets or lease terms. Asset lives range from 3-10 years for furniture and equipment and 15-40 years for land improvements and buildings.

## **Goodwill and Other Intangible Assets**

Goodwill represents the excess of costs over fair value of net assets of businesses acquired. Goodwill and other intangible assets acquired in a purchase business combination and determined to have an indefinite useful life are not amortized, but instead tested for impairment at least annually. Intangible assets with estimable useful lives are amortized over their respective estimated useful lives to their estimated residual values, and reviewed for impairment.

The Company has an identifiable intangible asset consisting of core deposit intangibles (CDI). CDI are amortized over their respective estimated useful lives, and reviewed for impairment.

## **Impairment of Long-Lived Assets and Goodwill**

Long-lived assets, such as premises and equipment, and purchased intangibles subject to amortization, are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to estimated undiscounted future cash flows expected to be generated by the asset. If the carrying amount of an asset exceeds its estimated future cash flows, an impairment charge is recognized by the amount by which the carrying amount of the asset exceeds the fair value of the asset. Assets to be disposed of would be separately presented in the balance sheet and reported at the lower of the carrying amount or fair value less costs to sell, and are no longer depreciated. The assets and liabilities of a disposed group classified as held for sale would be presented separately in the appropriate asset and liability sections of the consolidated balance sheet.

As of December 31 of each year, goodwill is tested for impairment, and is tested for impairment more frequently if events and circumstances indicate that the asset might be impaired. An impairment loss is recognized to the extent that the carrying amount exceeds the asset's fair value. This determination is made at the reporting unit level. The Company may choose to first assess qualitative factors to determine whether the existence of events or circumstances leads to a determination that it is more likely than not that the fair value of a reporting unit is less than its carrying amount. If, after assessing the totality of events or circumstances, the Company determines it is not more likely than not that the fair value of a reporting unit is less than its carrying amount, then goodwill is deemed not to be impaired. However, if the Company concludes otherwise, or if the Company elected not to first assess qualitative factors, then the Company performs the first step of a two-step impairment test by calculating the fair value of the reporting unit and comparing the fair value with the carrying amount of the reporting unit.

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Second, if the carrying amount of the reporting unit exceeds its fair value, an impairment loss is recognized for any excess of the carrying amount of the reporting unit's goodwill over the implied fair value of that goodwill. The implied fair value of goodwill is determined by allocating the fair value of the reporting unit in a manner similar to a purchase price allocation. The residual fair value after this allocation is the implied fair value of the reporting unit goodwill. Currently, and historically, the Company is comprised of only one reporting unit that operates within the business segment it has identified as community banking. Goodwill was not impaired as of December 31, 2015 because the fair value of the reporting unit exceeded its carrying value.

**Mortgage Servicing Rights**

Mortgage servicing rights (MSR) represent the Company's right to a future stream of cash flows based upon the contractual servicing fee associated with servicing mortgage loans. Our MSR arise from residential and commercial mortgage loans that we originate and sell, but retain the right to service the loans. The net gain from the retention of the servicing right is included in gain on sale of loans in noninterest income when the loan is sold. Fair value is based on market prices for comparable mortgage servicing contracts, when available, or alternatively, is based on a valuation model that calculates the present value of estimated future net servicing income. The valuation model incorporates assumptions that market participants would use in estimating future net servicing income, such as the cost to service, the discount rate, the custodial earnings rate, an inflation rate, ancillary income, prepayment speeds and default rates and losses. Servicing fees are recorded in noninterest income when earned.

The Company accounts for MSR at fair value. The determination of fair value of our MSR requires management judgment because they are not actively traded. The determination of fair value for MSR requires valuation processes which combine the use of discounted cash flow models and extensive analysis of current market data to arrive at an estimate of fair value. The cash flow and prepayment assumptions used in our discounted cash flow model are based on empirical data drawn from the historical performance of our MSR, which we believe are consistent with assumptions used by market participants valuing similar MSR, and from data obtained on the performance of similar MSR. The key assumptions used in the valuation of MSR include mortgage prepayment speeds and the discount rate. These variables can, and generally will, change from quarter to quarter as market conditions and projected interest rates change. The key risks inherent with MSR are prepayment speed and changes in interest rates. The Company uses an independent third party to determine fair value of MSR.

**Indemnification Asset/Liability**

The Company accounts for amounts receivable or payable under its loss-share agreements entered into with the FDIC in connection with its purchase and assumption of certain assets and liabilities of Granite as indemnification assets in accordance with FASB ASC Topic 805, *Business Combinations*. FDIC indemnification assets are initially recorded at fair value, based on the discounted value of expected future cash flows under the loss-share agreements. The difference between the fair value and the undiscounted cash flows the Company expects to collect from or pay to the FDIC will be accreted into noninterest income over the life of the FDIC indemnification asset. FDIC indemnification assets are reviewed quarterly and adjusted for any changes in expected cash flows based on recent performance and expectations for future performance of the covered portfolios. These adjustments are measured on the same basis as the related covered loans and covered other real estate owned. Any increases in cash flow of the covered assets over those expected will reduce the FDIC indemnification asset and any decreases in cash flow of the covered assets under those expected will increase the FDIC indemnification asset. Increases and decreases to the FDIC indemnification asset are recorded as adjustments to noninterest income.

**Reserve for Unfunded Commitments**

The reserve for unfunded commitments is established through a provision for losses unfunded commitments charged to noninterest expense. The reserve for unfunded commitments is an amount that Management believes will be adequate to absorb probable losses inherent in existing commitments, including unused portions of revolving lines of credits and other loans, standby letters of credits, and unused deposit account overdraft privilege. The reserve for unfunded commitments is based on evaluations of the collectability, and prior loss experience of unfunded commitments. The evaluations take into consideration such factors as changes in the nature and size of the loan portfolio, overall loan portfolio quality, loan concentrations, specific problem loans and related unfunded commitments, and current economic conditions that may affect the borrower s or depositor s ability to pay.

### **Low Income Housing Tax Credits**

The Company accounts for low income housing tax credits and the related qualified affordable housing projects using the proportional amortization method. Under the proportional amortization method, the Company amortizes the initial cost of the investment in proportion to the tax credits and other tax benefits received and recognizes the net investment performance in the income statement as a component of income tax expense (benefit). Upon entering into a qualified affordable housing project, the Company records, in other liabilities, the entire amount that it has agreed to invest in the project, and an equal amount, in other assets, representing its investment in the project. As the Company disburses cash to satisfy its investment obligation, other liabilities are reduced. Over time, as the tax credits and other tax benefits of the project are realized by the Company, the investment recorded in other assets is reduced using the proportional amortization method.

### **Income Taxes**

The Company s accounting for income taxes is based on an asset and liability approach. The Company recognizes the amount of taxes payable or refundable for the current year, and deferred tax assets and liabilities for the future tax consequences that have been recognized in its financial statements or tax returns. The measurement of tax assets and liabilities is based on the provisions of enacted tax laws. A valuation allowance, if needed, reduces deferred tax assets to the expected amount most likely to be realized. Realization of deferred tax assets is dependent upon the generation of a sufficient level of future taxable income and recoverable taxes paid in prior years. Although realization is not assured, management believes it is more likely than not that all of the deferred tax assets will be realized. Interest and/or penalties related to income taxes are reported as a component of noninterest income.

### **Off-Balance Sheet Credit Related Financial Instruments**

In the ordinary course of business, the Company has entered into commitments to extend credit, including commitments under credit card arrangements, commercial letters of credit, and standby letters of credit. Such financial instruments are recorded when they are funded.

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**Table of Contents****Geographical Descriptions**

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

**Reclassifications**

Certain amounts reported in previous consolidated financial statements have been reclassified to conform to the presentation in this report. These reclassifications did not affect previously reported net income or total shareholders equity.

**Recent Accounting Pronouncements**

FASB issued Accounting Standard Update (ASU) No. 2016-9, *Compensation – Stock Compensation (Topic 718)*. ASU 2016-9, among other things, requires: (i) that all excess tax benefits and tax deficiencies (including tax benefits of dividends on share-based payment awards) should be recognized as income tax expense or benefit in the income statement, (ii) the tax effects of exercised or vested awards should be treated as discrete items in the reporting period in which they occur, (iii) an entity also should recognize excess tax benefits regardless of whether the benefit reduces taxes payable in the current period, (iv) excess tax benefits should be classified along with other income tax cash flows as an operating activity, (v) an entity can make an entity-wide accounting policy election to either estimate the number of awards that are expected to vest (current GAAP) or account for forfeitures when they occur, (vi) the threshold to qualify for equity classification permits withholding up to the maximum statutory tax rates in the applicable jurisdictions, and (vii) cash paid by an employer when directly withholding shares for tax withholding purposes should be classified as a financing activity. ASU 2016-9 will be effective for the Company on January 1, 2017 and is not expected to have a significant impact on the Company's consolidated financial statements.

FASB issued ASU No. 2016-13, *Financial Instruments – Credit Losses (Topic 326)*: ASU 2016-13 is the final guidance on the new current expected credit loss (CECL) model. ASU 2016-13, among other things, requires the incurred loss impairment methodology in current GAAP be replaced with a methodology that reflects expected credit losses and requires consideration of a broader range of reasonable and supportable information to estimate future credit loss estimates. As CECL encompasses all financial assets carried at amortized cost, the requirement that reserves be established based on an organization's reasonable and supportable estimate of expected credit losses extends to held to maturity (HTM) debt securities. ASU 2016-13 amends the accounting for credit losses on available-for-sale securities (AFS), whereby credit losses will be presented as an allowance as opposed to a write-down. In addition, CECL will modify the accounting for purchased loans with credit deterioration since origination, so that reserves are established at the date of acquisition for purchased loans. Lastly, ASU 2016-13 requires enhanced disclosures on the significant estimates and judgments used to estimate credit losses, as well as on the credit quality and underwriting standards of an organization's portfolio. These disclosures require organizations to present the currently required credit quality disclosures disaggregated by the year of origination or vintage. ASU 2016-13 allows for a modified retrospective approach with a cumulative effect adjustment to the balance sheet upon adoption (charge to retained earnings instead of the income statement). ASU 2016-13 will be effective for Company on January 1, 2020, and early adoption is permitted. The Company is currently evaluating the impact of adopting ASU 2016-13 on the Company's consolidated financial statements.

**Table of Contents****Note 2 - Business Combinations**

On March 18, 2016, the Bank completed its acquisition of three branch banking offices from Bank of America originally announced October 28, 2015. The acquired branches are located in Arcata, Eureka and Fortuna in Humboldt County on the North Coast of California, and have significant overlap when compared to the Company's then-existing Northern California customer base and branch locations. As a result, these branch acquisitions create potential cost savings and future growth potential. With the levels of capital at the time, the acquisitions fit well into the Company's growth strategy. Also on March 18, 2016, the electronic customer service and other data processing systems of the acquired branches were converted into Tri Counties Bank's systems, and the effect of revenue and expenses from the operations of the acquired branches are included in the results of the Company. The Bank paid \$3,204,000 for deposit relationships with balances of \$161,231,000 and loans with balances of \$289,000, and received cash of \$159,520,000 from Bank of America.

The assets acquired and liabilities assumed in the acquisition of these branches were accounted for in accordance with ASC 805 Business Combinations, using the acquisition method of accounting and were recorded at their estimated fair values on the March 18, 2016 acquisition date, and the results of operations of the acquired branches are included in the Company's consolidated statements of income since that date. The excess of the fair value of consideration transferred over total identifiable net assets was recorded as goodwill. The goodwill arising from the acquisition consists largely of the synergies and economies of scale expected from combining the operations of the Company and the acquired branches. \$849,000 of the goodwill is deductible for income tax purposes as the acquisition was accounted for as a purchase of assets and assumption of liabilities for tax purposes.

The following table discloses the calculation of the fair value of consideration transferred, the total identifiable net assets acquired and the resulting goodwill relating to the acquisition of three branch banking offices and certain deposits from Bank of America on March 18, 2016:

| (in thousands)                                       | March 18, 2016 |
|--|----------------|
| <b>Fair value of consideration transferred:</b>      |                |
| Cash consideration                                   | \$ 3,204       |
| <b>Total fair value of consideration transferred</b> | <b>3,204</b>   |
| <b>Asset acquired:</b>                               |                |
| Cash and cash equivalents                            | 159,520        |
| Loans  | 289            |
| Premises and equipment                               | 1,590          |
| Core deposit intangible                              | 2,046          |
| Other assets   | 141            |
| <b>Total assets acquired</b>                         | <b>163,586</b> |
| <b>Liabilities assumed:</b>                          |                |
| Deposits   | 161,231        |
| <b>Total liabilities assumed</b>                     | <b>161,231</b> |

|                           |    |       |
|---------------------------|----|-------|
| Total net assets acquired |    | 2,355 |
| Goodwill recognized       | \$ | 849   |

A summary of the cash paid and estimated fair value adjustments resulting in the goodwill recorded in the acquisition of three branch banking offices and certain deposits from Bank of America on March 18, 2016 are presented below:

|                                | March 18, 2016 |         |
|--------------------------------|----------------|---------|
| (in thousands)                 |                |         |
| Cash paid                      | \$             | 3,204   |
| Cost basis net assets acquired |                |         |
| Fair value adjustments:        |                |         |
| Loans                          |                |         |
| Premises and Equipment         |                | (309)   |
| Core deposit intangible        |                | (2,046) |
| Goodwill                       | \$             | 849     |

As part of the acquisition of three branch banking offices from Bank of America, the Company performed a valuation of premises and equipment acquired. This valuation resulted in a \$309,000 increase in the net book value of the land and buildings acquired, and was based on current appraisals of such land and buildings.



The Company recognized a core deposit intangible of \$2,046,000 related to the acquisition of the core deposits. The recorded core deposit intangibles represented approximately 1.50% of the core deposits acquired and will be amortized over their estimated useful lives of 7 years.

A valuation of the time deposits acquired was also performed as of the acquisition date. Time deposits were split into similar pools based on size, type of time deposits, and maturity. A discounted cash flow analysis was performed on the pools based on current market rates currently paid on similar time deposits. The valuation resulted in no material fair value discount or premium, and none was recorded.

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

The amortized cost and estimated fair values of investments in debt and equity securities are summarized in the following tables:

|  | June 30, 2016     |                              |                               | Estimated<br>Fair<br>Value |
|--|-------------------|------------------------------|-------------------------------|----------------------------|
|  | Amortized<br>Cost | Gross<br>Unrealized<br>Gains | Gross<br>Unrealized<br>Losses |                            |
| (in thousands)   |                   |                              |                               |                            |
| <b><u>Securities Available for Sale</u></b>              |                   |                              |                               |                            |
| Obligations of U.S. government corporations and agencies | \$ 398,811        | \$ 10,175                    |                               | \$ 408,986                 |
| Obligations of states and political subdivisions         | 111,763           | 5,221                        |                               | 116,984                    |
| Marketable equity securities                             | 3,000             | 47                           |                               | 3,047                      |
| <b>Total securities available for sale</b>               | <b>\$ 513,574</b> | <b>\$ 15,443</b>             |                               | <b>\$ 529,017</b>          |

|  |                   |                  |  |                   |
|--|-------------------|------------------|--|-------------------|
| <b><u>Securities Held to Maturity</u></b>                |                   |                  |  |                   |
| Obligations of U.S. government corporations and agencies | \$ 659,867        | \$ 24,532        |  | \$ 684,399        |
| Obligations of states and political subdivisions         | 14,545            | 655              |  | 15,200            |
| <b>Total securities held to maturity</b>                 | <b>\$ 674,412</b> | <b>\$ 25,187</b> |  | <b>\$ 699,599</b> |

|  | December 31, 2015 |                              |                               | Estimated<br>Fair<br>Value |
|--|-------------------|------------------------------|-------------------------------|----------------------------|
|  | Amortized<br>Cost | Gross<br>Unrealized<br>Gains | Gross<br>Unrealized<br>Losses |                            |
| (in thousands)   |                   |                              |                               |                            |
| <b><u>Securities Available for Sale</u></b>              |                   |                              |                               |                            |
| Obligations of U.S. government corporations and agencies | \$ 312,917        | \$ 2,761                     | \$ (1,996)                    | \$ 313,682                 |
| Obligations of states and political subdivisions         | 86,823            | 1,428                        | (33)                          | 88,218                     |
| Marketable equity securities                             | 3,000             |                              | (15)                          | 2,985                      |
| <b>Total securities available for sale</b>               | <b>\$ 402,740</b> | <b>\$ 4,189</b>              | <b>\$ (2,044)</b>             | <b>\$ 404,885</b>          |

|  |                   |                 |                   |                   |
|--|-------------------|-----------------|-------------------|-------------------|
| <b><u>Securities Held to Maturity</u></b>                |                   |                 |                   |                   |
| Obligations of U.S. government corporations and agencies | \$ 711,994        | \$ 8,394        | \$ (2,882)        | \$ 717,506        |
| Obligations of states and political subdivisions         | 14,536            | 277             | (110)             | 14,703            |
| <b>Total securities held to maturity</b>                 | <b>\$ 726,530</b> | <b>\$ 8,671</b> | <b>\$ (2,992)</b> | <b>\$ 732,209</b> |

No investment securities were sold during the six months ended June 30, 2016 or the six months ended June 30, 2015. Investment securities with an aggregate carrying value of \$277,023,000 and \$297,547,000 at June 30, 2016 and December 31, 2015, respectively, were pledged as collateral for specific borrowings, lines of credit and local agency deposits.

The amortized cost and estimated fair value of debt securities at June 30, 2016 by contractual maturity are shown below. Actual maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties. At June 30, 2016, obligations of U.S. government corporations and agencies with a cost basis totaling \$1,058,678,000 consist almost entirely of mortgage-backed securities whose contractual maturity, or principal repayment, will follow the repayment of the underlying mortgages. For purposes of the following table, the entire outstanding balance of these mortgage-backed securities issued by U.S. government corporations and agencies is categorized based on final maturity date. At June 30, 2016, the Company estimates the average remaining life of these mortgage-backed securities issued by U.S. government corporations and agencies to be approximately 3.9 years. Average remaining life is defined as the time span after which the principal balance has been reduced by half.

| Investment Securities                  | Available for Sale |                      | Held to Maturity  |                      |
|--|--------------------|----------------------|-------------------|----------------------|
|  | Amortized Cost     | Estimated Fair Value | Amortized Cost    | Estimated Fair Value |
| (In thousands)                         |                    |                      |                   |                      |
| Due in one year                        | \$ 1               | \$ 1                 |                   |                      |
| Due after one year through five years  | 12,246             | 12,748               | \$ 1,161          | \$ 1,201             |
| Due after five years through ten years | 16,676             | 17,557               | 845               | 936                  |
| Due after ten years                    | 484,651            | 498,711              | 672,406           | 697,462              |
| <b>Totals</b>                          | <b>\$ 513,574</b>  | <b>\$ 529,017</b>    | <b>\$ 674,412</b> | <b>\$ 699,599</b>    |

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Gross unrealized losses on investment securities and the fair value of the related securities, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position, were as follows:

| June 30, 2016 | Less than 12 months |                 | 12 months or more |                 | Total      |                 |
|---------------|---------------------|-----------------|-------------------|-----------------|------------|-----------------|
|               | Fair Value          | Unrealized Loss | Fair Value        | Unrealized Loss | Fair Value | Unrealized Loss |

**Securities Available for Sale:**

Obligations of U.S. government corporations and agencies

Obligations of states and political subdivisions

Marketable equity securities

**Total securities available-for-sale**

**Securities Held to Maturity:**

Obligations of U.S. government corporations and agencies

Obligations of states and political subdivisions

**Total securities held-to-maturity**

| December 31, 2015 | Less than 12 months |                 | 12 months or more |                 | Total      |                 |
|-------------------|---------------------|-----------------|-------------------|-----------------|------------|-----------------|
|                   | Fair Value          | Unrealized Loss | Fair Value        | Unrealized Loss | Fair Value | Unrealized Loss |

**Securities Available for Sale:**

Obligations of U.S. government corporations and agencies

Obligations of states and political subdivisions

Marketable equity securities

**Total securities available-for-sale**

**Securities Held to Maturity:**

Obligations of U.S. government corporations and agencies

Obligations of states and political subdivisions

|  |            |            |          |         |            |            |
|--|------------|------------|----------|---------|------------|------------|
|  | \$ 193,306 | \$ (1,996) |          |         | \$ 193,306 | \$ (1,996) |
|  | 6,469      | (33)       |          |         | 6,469      | (33)       |
|  | 2,985      | (15)       |          |         | 2,985      | (15)       |
|  | \$ 202,760 | \$ (2,044) |          |         | \$ 202,760 | \$ (2,044) |
|  | \$ 198,481 | \$ (2,882) |          |         | \$ 198,481 | \$ (2,882) |
|  | 497        | (11)       | \$ 1,121 | \$ (99) | 1,618      | (110)      |

|                                   |            |            |          |         |            |            |
|-----------------------------------|------------|------------|----------|---------|------------|------------|
| Total securities held-to-maturity | \$ 198,978 | \$ (2,893) | \$ 1,121 | \$ (99) | \$ 200,099 | \$ (2,992) |
|-----------------------------------|------------|------------|----------|---------|------------|------------|

Obligations of U.S. government corporations and agencies: Unrealized losses on investments in obligations of U.S. government corporations and agencies are caused by interest rate increases. The contractual cash flows of these securities are guaranteed by U.S. Government Sponsored Entities (principally Fannie Mae and Freddie Mac). It is expected that the securities would not be settled at a price less than the amortized cost of the investment. Because the decline in fair value is attributable to changes in interest rates and not credit quality, and because the Company does not intend to sell and more likely than not will not be required to sell, these investments are not considered other-than-temporarily impaired. At June 30, 2016, no debt securities representing obligations of U.S. government corporations and agencies had unrealized losses.

Obligations of states and political subdivisions: The unrealized losses on investments in obligations of states and political subdivisions were caused by increases in required yields by investors in these types of securities. It is expected that the securities would not be settled at a price less than the amortized cost of the investment. Because the decline in fair value is attributable to changes in interest rates and not credit quality, and because the Company does not intend to sell and more likely than not will not be required to sell, these investments are not considered other-than-temporarily impaired. At June 30, 2016, no debt securities representing obligations of states and political subdivisions had unrealized losses.

Marketable equity securities: At June 30, 2016, no marketable equity securities had unrealized losses.

**Table of Contents****Note 4 Loans**

A summary of loan balances follows (in thousands):

|   | June 30, 2016       |                   |                     |                   |                     |
|---|---------------------|-------------------|---------------------|-------------------|---------------------|
|   | Originated          | PNCI              | PCI -<br>Cash basis | PCI -<br>Other    | Total               |
| <b>Mortgage loans on real estate:</b>                                   |                     |                   |                     |                   |                     |
| Residential 1-4 family  | \$ 221,460          | \$ 95,121         |                     | \$ 1,625          | \$ 318,206          |
| Commercial  | 1,297,858           | 281,018           |                     | 15,942            | 1,594,818           |
| <b>Total mortgage loan on real estate</b>                               | <b>1,519,318</b>    | <b>376,139</b>    |                     | <b>17,567</b>     | <b>1,913,024</b>    |
| <b>Consumer:</b>  |                     |                   |                     |                   |                     |
| Home equity lines of credit   | 273,849             | 26,579            | 4,092               | 2,158             | 306,678             |
| Home equity loans   | 36,517              | 3,854             | 124                 | 1,507             | 42,002              |
| Other   | 29,623              | 2,748             |                     | 63                | 32,434              |
| <b>Total consumer loans</b>   | <b>339,989</b>      | <b>33,181</b>     | <b>4,216</b>        | <b>3,728</b>      | <b>381,114</b>      |
| Commercial  | 189,494             | 16,062            |                     | 4,284             | 209,840             |
| <b>Construction:</b>  |                     |                   |                     |                   |                     |
| Residential   | 48,608              | 13,174            |                     | 549               | 62,331              |
| Commercial  | 78,200              | 9,121             |                     |                   | 87,321              |
| <b>Total construction</b>   | <b>126,808</b>      | <b>22,295</b>     |                     | <b>549</b>        | <b>149,652</b>      |
| <b>Total loans, net of deferred loan fees and discounts</b>             | <b>\$ 2,175,609</b> | <b>\$ 447,677</b> | <b>\$ 4,216</b>     | <b>\$ 26,128</b>  | <b>\$ 2,653,630</b> |
| <b>Total principal balance of loans owed, net of charge-offs</b>        |                     |                   |                     |                   |                     |
|   | \$ 2,181,868        | \$ 459,359        | \$ 11,025           | \$ 30,949         | \$ 2,683,201        |
| Unamortized net deferred loan fees                                      | (6,259)             |                   |                     |                   | (6,259)             |
| Discounts to principal balance of loans owed, net of charge-offs        |                     | (11,682)          | (6,809)             | (4,821)           | (23,312)            |
| <b>Total loans, net of unamortized deferred loan fees and discounts</b> | <b>\$ 2,175,609</b> | <b>\$ 447,677</b> | <b>\$ 4,216</b>     | <b>\$ 26,128</b>  | <b>\$ 2,653,630</b> |
| Noncovered loans  | \$ 2,175,609        | \$ 447,677        | \$ 4,216            | \$ 21,884         | \$ 2,649,386        |
| Covered loans   |                     |                   |                     | 4,244             | 4,244               |
| <b>Total loans, net of unamortized deferred loan fees and discounts</b> | <b>\$ 2,175,609</b> | <b>\$ 447,677</b> | <b>\$ 4,216</b>     | <b>\$ 26,128</b>  | <b>\$ 2,653,630</b> |
| <b>Allowance for loan losses</b>  | <b>\$ (30,362)</b>  | <b>\$ (2,339)</b> | <b>\$ (16)</b>      | <b>\$ (2,792)</b> | <b>\$ (35,509)</b>  |



**Table of Contents****Note 4 Loans (continued)**

A summary of loan balances follows (in thousands):

|   | December 31, 2015   |                   |                     |                  | Total               |
|---|---------------------|-------------------|---------------------|------------------|---------------------|
|   | Originated          | PNCI              | PCI -<br>Cash basis | PCI -<br>Other   |                     |
| <b>Mortgage loans on real estate:</b>                                   |                     |                   |                     |                  |                     |
| Residential 1-4 family  | \$ 207,585          | \$ 104,535        |                     | \$ 2,145         | \$ 314,265          |
| Commercial  | 1,163,643           | 310,864           |                     | 23,060           | 1,497,567           |
| <b>Total mortgage loan on real estate</b>                               | <b>1,371,228</b>    | <b>415,399</b>    |                     | <b>25,205</b>    | <b>1,811,832</b>    |
| <b>Consumer:</b>  |                     |                   |                     |                  |                     |
| Home equity lines of credit   | 285,419             | 29,335            | \$ 4,954            | 2,784            | 322,492             |
| Home equity loans   | 34,717              | 4,018             | 124                 | 1,503            | 40,362              |
| Other   | 28,998              | 3,367             |                     | 64               | 32,429              |
| <b>Total consumer loans</b>   | <b>349,134</b>      | <b>36,720</b>     | <b>5,078</b>        | <b>4,351</b>     | <b>395,283</b>      |
| Commercial  | 170,320             | 19,744            | 1                   | 4,848            | 194,913             |
| <b>Construction:</b>  |                     |                   |                     |                  |                     |
| Residential   | 31,778              | 13,636            |                     | 721              | 46,135              |
| Commercial  | 66,285              | 8,489             |                     |                  | 74,774              |
| <b>Total construction</b>   | <b>98,063</b>       | <b>22,125</b>     |                     | <b>721</b>       | <b>120,909</b>      |
| <b>Total loans, net of deferred loan fees and discounts</b>             | <b>\$ 1,988,745</b> | <b>\$ 493,988</b> | <b>\$ 5,079</b>     | <b>\$ 35,125</b> | <b>\$ 2,522,937</b> |
| <b>Total principal balance of loans owed, net of charge-offs</b>        |                     |                   |                     |                  |                     |
|   | \$ 1,995,296        | \$ 507,935        | \$ 12,686           | \$ 39,693        | \$ 2,555,610        |
| Unamortized net deferred loan fees                                      | (6,551)             |                   |                     |                  | (6,551)             |
| Discounts to principal balance of loans owed, net of charge-offs        |                     | (13,947)          | (7,607)             | (4,568)          | (26,122)            |
| <b>Total loans, net of unamortized deferred loan fees and discounts</b> | <b>\$ 1,988,745</b> | <b>\$ 493,988</b> | <b>\$ 5,079</b>     | <b>\$ 35,125</b> | <b>\$ 2,522,937</b> |
| Noncovered loans  | \$ 1,988,745        | \$ 493,988        | \$ 5,079            | \$ 29,890        | \$ 2,517,702        |
| Covered loans   |                     |                   |                     | 5,235            | 5,235               |
| <b>Total loans, net of unamortized deferred loan fees and discounts</b> | <b>\$ 1,988,745</b> | <b>\$ 493,988</b> | <b>\$ 5,079</b>     | <b>\$ 35,125</b> | <b>\$ 2,522,937</b> |



|                           |             |            |          |            |             |
|---------------------------|-------------|------------|----------|------------|-------------|
| Allowance for loan losses | \$ (31,271) | \$ (1,848) | \$ (121) | \$ (2,771) | \$ (36,011) |
|---------------------------|-------------|------------|----------|------------|-------------|

The following is a summary of the change in accretable yield for PCI other loans during the periods indicated (in thousands):

|   | Three months ended June 30, |           | Six months ended June 30, |           |
|---|-----------------------------|-----------|---------------------------|-----------|
|   | 2016                        | 2015      | 2016                      | 2015      |
| <b>Change in accretable yield:</b>                  |                             |           |                           |           |
| Balance at beginning of period                      | \$ 11,980                   | \$ 13,402 | \$ 13,255                 | \$ 14,159 |
| Accretion to interest income                        | (1,016)                     | (1,375)   | (2,107)                   | (2,930)   |
| Reclassification (to) from nonaccretable difference | 811                         | 920       | 627                       | 1,718     |
| Balance at end of period                            | \$ 11,775                   | \$ 12,947 | \$ 11,775                 | \$ 12,947 |

**Table of Contents****Note 5 Allowance for Loan Losses**

The following tables summarize the activity in the allowance for loan losses, and ending balance of loans, net of unearned fees for the periods indicated.

| (in thousands)      | Allowance for Loan Losses Three Months Ended June 30, 2016 |           |             |          |          |         |              |          |        |           |
|---------------------|--|-----------|-------------|----------|----------|---------|--------------|----------|--------|-----------|
|                     | RE Mortgage  |           | Home Equity |          | Auto     | Other   | Construction |          |        | Total     |
|                     | Resid.   | Comm.     | Lines       | Loans    | Indirect | Consum. | C&I          | Resid.   | Comm.  |           |
| Beginning balance   | \$ 2,765   | \$ 11,895 | \$ 9,907    | \$ 3,111 |          | \$ 687  | \$ 6,139     | \$ 1,066 | \$ 818 | \$ 36,388 |
| Charge-offs         | (125)  |           | (114)       | (93)     |          | (233)   | (76)         |          |        | (641)     |
| Recoveries          | 225  | 65        | 60          | 23       |          | 101     | 61           |          |        | 535       |
| (Benefit) provision | (173)  | 400       | (651)       | (20)     |          | 141     | (859)        | 255      | 134    | (773)     |
| Ending balance      | \$ 2,692   | \$ 12,360 | \$ 9,202    | \$ 3,021 |          | \$ 696  | \$ 5,265     | \$ 1,321 | \$ 952 | \$ 35,509 |

| (in thousands)      | Allowance for Loan Losses Six Months Ended June 30, 2016 |           |             |          |          |         |              |          |        |           |
|---------------------|--|-----------|-------------|----------|----------|---------|--------------|----------|--------|-----------|
|                     | RE Mortgage  |           | Home Equity |          | Auto     | Other   | Construction |          |        | Total     |
|                     | Resid.   | Comm.     | Lines       | Loans    | Indirect | Consum. | C&I          | Resid.   | Comm.  |           |
| Beginning balance   | \$ 2,507   | \$ 11,443 | \$ 11,253   | \$ 3,138 |          | \$ 688  | \$ 5,271     | \$ 899   | \$ 812 | \$ 36,011 |
| Charge-offs         | (162)  | (793)     | (328)       | (93)     |          | (440)   | (114)        |          |        | (1,930)   |
| Recoveries          | 227  | 882       | 341         | 72       |          | 231     | 238          |          | 1      | 1,992     |
| (Benefit) provision | 120  | 828       | (2,064)     | (96)     |          | 217     | (130)        | 422      | 139    | (564)     |
| Ending balance      | \$ 2,692   | \$ 12,360 | \$ 9,202    | \$ 3,021 |          | \$ 696  | \$ 5,265     | \$ 1,321 | \$ 952 | \$ 35,509 |

|                                   |        |        |        |        |  |       |        |  |  |          |
|-----------------------------------|--------|--------|--------|--------|--|-------|--------|--|--|----------|
| Ending balance:                   |        |        |        |        |  |       |        |  |  |          |
| Individ. evaluated for impairment | \$ 474 | \$ 253 | \$ 506 | \$ 203 |  | \$ 87 | \$ 647 |  |  | \$ 2,170 |

|                             |          |           |          |          |  |        |          |          |        |           |
|-----------------------------|----------|-----------|----------|----------|--|--------|----------|----------|--------|-----------|
| Loans pooled for evaluation | \$ 2,008 | \$ 10,648 | \$ 8,680 | \$ 2,818 |  | \$ 609 | \$ 3,545 | \$ 1,271 | \$ 952 | \$ 30,531 |
|                             | \$ 210   | \$ 1,459  | \$ 16    |          |  |        | \$ 1,073 | \$ 50    |        | \$ 2,808  |

Loans  
acquired  
with  
deteriorated  
credit  
quality

| (in<br>thousands)  | Loans, net of unearned fees As of June 30, 2016 |              |             |           |          |           |              |           |           |              |
|--------------------|---|--------------|-------------|-----------|----------|-----------|--------------|-----------|-----------|--------------|
|                    | RE Mortgage                                     |              | Home Equity |           | Auto     | Other     | Construction |           |           | Total        |
|                    | Resid.  | Comm.        | Lines       | Loans     | Indirect | Consum.   | C&I          | Resid.    | Comm.     |              |
| Ending<br>balance: |   |              |             |           |          |           |              |           |           |              |
| Total loans        | \$ 318,206                                      | \$ 1,594,818 | \$ 306,678  | \$ 42,002 |          | \$ 32,434 | \$ 209,840   | \$ 62,331 | \$ 87,321 | \$ 2,653,630 |

|  |          |           |          |          |  |        |          |       |  |           |
|--|----------|-----------|----------|----------|--|--------|----------|-------|--|-----------|
| Individ.<br>evaluated<br>for<br>impairment | \$ 6,629 | \$ 12,152 | \$ 4,984 | \$ 1,944 |  | \$ 277 | \$ 1,930 | \$ 11 |  | \$ 27,927 |
|--|----------|-----------|----------|----------|--|--------|----------|-------|--|-----------|

|                                   |            |              |            |           |  |           |            |           |           |              |
|-----------------------------------|------------|--------------|------------|-----------|--|-----------|------------|-----------|-----------|--------------|
| Loans<br>pooled for<br>evaluation | \$ 309,952 | \$ 1,566,724 | \$ 295,444 | \$ 38,427 |  | \$ 32,094 | \$ 203,626 | \$ 61,771 | \$ 87,321 | \$ 2,595,359 |
|-----------------------------------|------------|--------------|------------|-----------|--|-----------|------------|-----------|-----------|--------------|

|  |          |           |          |          |  |       |          |        |  |           |
|--|----------|-----------|----------|----------|--|-------|----------|--------|--|-----------|
| Loans<br>acquired<br>with<br>deteriorated<br>credit<br>quality | \$ 1,625 | \$ 15,942 | \$ 6,250 | \$ 1,631 |  | \$ 63 | \$ 4,284 | \$ 549 |  | \$ 30,344 |
|--|----------|-----------|----------|----------|--|-------|----------|--------|--|-----------|

| (in<br>thousands)       | Allowance for Loan Losses - Year Ended December 31, 2015 |           |             |          |          |         |              |          |        |           |
|-------------------------|--|-----------|-------------|----------|----------|---------|--------------|----------|--------|-----------|
|                         | RE Mortgage  |           | Home Equity |          | Auto     | Other   | Construction |          |        | Total     |
|                         | Resid.   | Comm.     | Lines       | Loans    | Indirect | Consum. | C&I          | Resid.   | Comm.  |           |
| Beginning<br>balance    | \$ 3,086   | \$ 9,227  | \$ 15,676   | \$ 1,797 | \$ 9     | \$ 719  | \$ 4,226     | \$ 1,434 | \$ 411 | \$ 36,585 |
| Charge-offs             | (224)  |           | (694)       | (242)    | (4)      | (972)   | (680)        |          |        | (2,816)   |
| Recoveries<br>(Benefit) | 204  | 243       | 666         | 252      | 42       | 500     | 677          | 1,728    | 140    | 4,452     |
| provision               | (559)  | 1,973     | (4,395)     | 1,331    | (47)     | 441     | 1,048        | (2,263)  | 261    | (2,210)   |
| Ending<br>balance       | \$ 2,507   | \$ 11,443 | \$ 11,253   | \$ 3,138 |          | \$ 688  | \$ 5,271     | \$ 899   | \$ 812 | \$ 36,011 |
| Ending<br>balance:      |  |           |             |          |          |         |              |          |        |           |
| Individ.<br>evaluated   | \$ 335   | \$ 395    | \$ 605      | \$ 294   |          | \$ 74   | \$ 1,187     |          |        | \$ 2,890  |

for  
impairment

|                                   |    |       |    |       |    |        |    |       |  |    |     |    |       |    |     |    |     |    |        |
|-----------------------------------|----|-------|----|-------|----|--------|----|-------|--|----|-----|----|-------|----|-----|----|-----|----|--------|
| Loans<br>pooled for<br>evaluation | \$ | 2,112 | \$ | 9,596 | \$ | 10,423 | \$ | 2,844 |  | \$ | 614 | \$ | 2,983 | \$ | 844 | \$ | 812 | \$ | 30,228 |
|-----------------------------------|----|-------|----|-------|----|--------|----|-------|--|----|-----|----|-------|----|-----|----|-----|----|--------|

|  |    |    |    |       |    |     |  |  |  |    |       |    |    |  |  |  |  |    |       |
|--|----|----|----|-------|----|-----|--|--|--|----|-------|----|----|--|--|--|--|----|-------|
| Loans<br>acquired<br>with<br>deteriorated<br>credit<br>quality | \$ | 60 | \$ | 1,452 | \$ | 225 |  |  |  | \$ | 1,101 | \$ | 55 |  |  |  |  | \$ | 2,893 |
|--|----|----|----|-------|----|-----|--|--|--|----|-------|----|----|--|--|--|--|----|-------|

**Table of Contents****Note 5 Allowance for Loan Losses (continued)**

| (in thousands)                                  | RE Mortgage |              | Loans, net of unearned fees |           |           |              | As of December 31, 2015 |           | Total        |
|---|-------------|--------------|-----------------------------|-----------|-----------|--------------|-------------------------|-----------|--------------|
|   | Resid.      | Comm.        | Home Equity                 | Auto      | Other     | Construction | C&I                     |           |              |
| Ending balance:                                 | Lines       | Loans        | Indirect                    | Consum.   | C&I       | Resid.       | Comm.                   |           |              |
| Total loans                                     | \$ 314,265  | \$ 1,497,567 | \$ 322,492                  | \$ 40,362 | \$ 32,429 | \$ 194,913   | \$ 46,135               | \$ 74,774 | \$ 2,522,937 |
| Individ. evaluated for impairment               | \$ 6,767    | \$ 32,407    | \$ 5,747                    | \$ 1,731  | \$ 288    | \$ 2,671     | \$ 4                    | \$ 490    | \$ 50,105    |
| Loans pooled for evaluation                     | \$ 305,353  | \$ 1,442,100 | \$ 309,007                  | \$ 37,004 | \$ 32,077 | \$ 187,393   | \$ 45,410               | \$ 74,284 | \$ 2,432,628 |
| Loans acquired with deteriorated credit quality | \$ 2,145    | \$ 23,060    | \$ 7,738                    | \$ 1,627  | \$ 64     | \$ 4,849     | \$ 721                  |           | \$ 40,204    |

| (in thousands)                 | RE Mortgage |           | Allowance for Loan Losses |          |        |              | Three Months Ended June 30, 2015 |        | Total     |           |
|--------------------------------|-------------|-----------|---------------------------|----------|--------|--------------|----------------------------------|--------|-----------|-----------|
|                                | Resid.      | Comm.     | Home Equity               | Auto     | Other  | Construction | C&I                              |        |           |           |
| Beginning balance              | Lines       | Loans     | Indirect                  | Consum.  | C&I    | Resid.       | Comm.                            |        |           |           |
| Beginning balance              | \$ 2,765    | \$ 10,451 | \$ 15,233                 | \$ 1,980 | \$ 6   | \$ 644       | \$ 3,976                         | \$ 750 | \$ 250    | \$ 36,055 |
| Charge-offs                    | (128)       |           | (84)                      | (117)    | (4)    | (176)        | (5)                              |        |           | (514)     |
| Recoveries (Benefit) provision |             | 53        | 230                       | 6        | 16     | 107          | 121                              |        | 14        | 547       |
| Ending balance                 | 198         | (363)     | (1,386)                   | 259      | (18)   | 130          | 310                              | 92     | 145       | (633)     |
| Ending balance                 | \$ 2,835    | \$ 10,141 | \$ 13,993                 | \$ 2,128 | \$ 705 | \$ 4,402     | \$ 842                           | \$ 409 | \$ 35,455 |           |

| (in thousands)                 | RE Mortgage |           | Allowance for Loan Losses |          |        |              | Six Months Ended June 30, 2015 |        | Total     |           |
|--------------------------------|-------------|-----------|---------------------------|----------|--------|--------------|--------------------------------|--------|-----------|-----------|
|                                | Resid.      | Comm.     | Home Equity               | Auto     | Other  | Construction | C&I                            |        |           |           |
| Beginning balance              | Lines       | Loans     | Indirect                  | Consum.  | C&I    | Resid.       | Comm.                          |        |           |           |
| Beginning balance              | \$ 2,765    | \$ 10,451 | \$ 15,233                 | \$ 1,980 | \$ 6   | \$ 644       | \$ 3,976                       | \$ 750 | \$ 250    | \$ 36,055 |
| Charge-offs                    | (128)       |           | (84)                      | (117)    | (4)    | (176)        | (5)                            |        |           | (514)     |
| Recoveries (Benefit) provision |             | 53        | 230                       | 6        | 16     | 107          | 121                            |        | 14        | 547       |
| Ending balance                 | 198         | (363)     | (1,386)                   | 259      | (18)   | 130          | 310                            | 92     | 145       | (633)     |
| Ending balance                 | \$ 2,835    | \$ 10,141 | \$ 13,993                 | \$ 2,128 | \$ 705 | \$ 4,402     | \$ 842                         | \$ 409 | \$ 35,455 |           |

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|   |             |              |             |           |          |           |            |              |           |              |
|---|-------------|--------------|-------------|-----------|----------|-----------|------------|--------------|-----------|--------------|
| Beginning balance                               | \$ 3,086    | \$ 9,227     | \$ 15,676   | \$ 1,797  | \$ 9     | \$ 719    | \$ 4,226   | \$ 1,434     | \$ 411    | \$ 36,585    |
| Charge-offs                                     | (209)       |              | (425)       | (128)     | (4)      | (444)     | (539)      |              |           | (1,749)      |
| Recoveries                                      | 1           | 149          | 349         | 9         | 36       | 259       | 208        | 11           | 33        | 1,055        |
| (Benefit) provision                             | (43)        | 765          | (1,607)     | 450       | (41)     | 171       | 507        | (603)        | (35)      | (436)        |
| Ending balance                                  | \$ 2,835    | \$ 10,141    | \$ 13,993   | \$ 2,128  |          | \$ 705    | \$ 4,402   | \$ 842       | \$ 409    | \$ 35,455    |
| Ending balance:                                 |             |              |             |           |          |           |            |              |           |              |
| Individ. evaluated for impairment               | \$ 857      | \$ 418       | \$ 1,779    | \$ 387    |          | \$ 128    | \$ 676     |              |           | \$ 4,245     |
| Loans pooled for evaluation                     | \$ 1,884    | \$ 8,390     | \$ 11,798   | \$ 1,741  |          | \$ 577    | \$ 2,536   | \$ 653       | \$ 409    | \$ 27,988    |
| Loans acquired with deteriorated credit quality | \$ 94       | \$ 1,333     | \$ 416      |           |          |           | \$ 1,190   | \$ 189       |           | \$ 3,222     |
| Loans, net of unearned fees As of June 30, 2015 |             |              |             |           |          |           |            |              |           |              |
|   | RE Mortgage |              | Home Equity |           | Auto     | Other     |            | Construction |           |              |
| (in thousands)                                  | Resid.      | Comm.        | Lines       | Loans     | Indirect | Consum.   | C&I        | Resid.       | Comm.     | Total        |
| Ending balance:                                 |             |              |             |           |          |           |            |              |           |              |
| Total loans                                     | \$ 291,488  | \$ 1,395,079 | \$ 344,115  | \$ 34,572 |          | \$ 33,101 | \$ 195,791 | \$ 41,958    | \$ 57,658 | \$ 2,393,762 |
| Individ. evaluated for impairment               | \$ 7,467    | \$ 47,118    | \$ 6,135    | \$ 1,438  |          | \$ 403    | \$ 2,048   | \$ 328       | \$ 88     | \$ 65,025    |
| Loans pooled for evaluation                     | \$ 280,147  | \$ 1,320,440 | \$ 329,788  | \$ 32,372 |          | \$ 32,631 | \$ 188,642 | \$ 40,907    | \$ 57,570 | \$ 2,282,497 |
| Loans acquired with deteriorated credit         | \$ 3,874    | \$ 27,521    | \$ 8,192    | \$ 762    |          | \$ 67     | \$ 5,101   | \$ 723       |           | \$ 46,240    |

quality

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**Table of Contents****Note 5 Allowance for Loan Losses (continued)**

As part of the on-going monitoring of the credit quality of the Company's loan portfolio, management tracks certain credit quality indicators including, but not limited to, trends relating to (i) the level of criticized and classified loans, (ii) net charge-offs, (iii) non-performing loans, and (iv) delinquency within the portfolio.

The Company utilizes a risk grading system to assign a risk grade to each of its loans. Loans are graded on a scale ranging from Pass to Loss. A description of the general characteristics of the risk grades is as follows:

*Pass* This grade represents loans ranging from acceptable to very little or no credit risk. These loans typically meet most if not all policy standards in regard to: loan amount as a percentage of collateral value, debt service coverage, profitability, leverage, and working capital.

*Special Mention* This grade represents Other Assets Especially Mentioned in accordance with regulatory guidelines and includes loans that display some potential weaknesses which, if left unaddressed, may result in deterioration of the repayment prospects for the asset or may inadequately protect the Company's position in the future. These loans warrant more than normal supervision and attention.

*Substandard* This grade represents Substandard loans in accordance with regulatory guidelines. Loans within this rating typically exhibit weaknesses that are well defined to the point that repayment is jeopardized. Loss potential is, however, not necessarily evident. The underlying collateral supporting the credit appears to have sufficient value to protect the Company from loss of principal and accrued interest, or the loan has been written down to the point where this is true. There is a definite need for a well defined workout/rehabilitation program.

*Doubtful* This grade represents Doubtful loans in accordance with regulatory guidelines. An asset classified as Doubtful has all the weaknesses inherent in a loan classified Substandard with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently existing facts, conditions and values, highly questionable and improbable. Pending factors include proposed merger, acquisition, or liquidation procedures, capital injection, perfecting liens on additional collateral, and financing plans.

*Loss* This grade represents Loss loans in accordance with regulatory guidelines. A loan classified as Loss is considered uncollectible and of such little value that its continuance as a bankable asset is not warranted. This classification does not mean that the loan has absolutely no recovery or salvage value, but rather that it is not practical or desirable to defer writing off the loan, even though some recovery may be affected in the future. The portion of the loan that is graded loss should be charged off no later than the end of the quarter in which the loss is identified.

The following tables present ending loan balances by loan category and risk grade for the periods indicated:



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| (in thousands)          | RE Mortgage       |                     | Credit Quality Indicators As of June 30, 2016 |                  |                  |                   | Construction     |                  | Total               |
|-------------------------|-------------------|---------------------|---|------------------|------------------|-------------------|------------------|------------------|---------------------|
|                         | Resid.            | Comm.               | Home Equity Lines                             | Loans Indirec    | Auto Consum.     | Other C&I         | Resid.           | Comm.            |                     |
| Originated loans:       |                   |                     |   |                  |                  |                   |                  |                  |                     |
| Pass                    | \$ 214,128        | \$ 1,271,457        | \$ 265,496                                    | \$ 32,662        | \$ 29,100        | \$ 182,447        | \$ 48,608        | \$ 78,200        | \$ 2,122,098        |
| Special mention         | 2,117             | 12,509              | 2,335   | 1,060            |                  | 357               | 4,049            |                  | 22,427              |
| Substandard             | 5,215             | 13,892              | 6,018   | 2,795            |                  | 166               | 2,998            |                  | 31,084              |
| <b>Total originated</b> | <b>\$ 221,460</b> | <b>\$ 1,297,858</b> | <b>\$ 273,849</b>                             | <b>\$ 36,517</b> | <b>\$ 29,623</b> | <b>\$ 189,494</b> | <b>\$ 48,608</b> | <b>\$ 78,200</b> | <b>\$ 2,175,609</b> |
| PNCI loans:             |                   |                     |   |                  |                  |                   |                  |                  |                     |
| Pass                    | \$ 93,348         | \$ 261,862          | \$ 25,075                                     | \$ 3,691         | \$ 2,573         | \$ 15,995         | \$ 13,174        | \$ 9,121         | \$ 424,839          |
| Special mention         | 540               | 8,107               | 410   | 74               | 57               | 8                 |                  |                  | 9,196               |
| Substandard             | 1,233             | 11,049              | 1,094   | 89               | 118              | 59                |                  |                  | 13,642              |
| <b>Total PNCI</b>       | <b>\$ 95,121</b>  | <b>\$ 281,018</b>   | <b>\$ 26,579</b>                              | <b>\$ 3,854</b>  | <b>\$ 2,748</b>  | <b>\$ 16,062</b>  | <b>\$ 13,174</b> | <b>\$ 9,121</b>  | <b>\$ 447,677</b>   |
| PCI loans               | \$ 1,625          | \$ 15,942           | \$ 6,250                                      | \$ 1,631         | \$ 63            | \$ 4,284          | \$ 549           |                  | \$ 30,344           |
| <b>Total loans</b>      | <b>\$ 318,206</b> | <b>\$ 1,594,818</b> | <b>\$ 306,678</b>                             | <b>\$ 42,002</b> | <b>\$ 32,434</b> | <b>\$ 209,840</b> | <b>\$ 62,331</b> | <b>\$ 87,321</b> | <b>\$ 2,653,630</b> |

| (in thousands)          | RE Mortgage       |                     | Credit Quality Indicators As of December 31, 2015 |                  |                  |                   | Construction     |                  | Total               |
|-------------------------|-------------------|---------------------|---|------------------|------------------|-------------------|------------------|------------------|---------------------|
|                         | Resid.            | Comm.               | Home Equity Lines                                 | Loans Indirec    | Auto Consum.     | Other C&I         | Resid.           | Comm.            |                     |
| Originated loans:       |                   |                     |   |                  |                  |                   |                  |                  |                     |
| Pass                    | \$ 199,837        | \$ 1,118,868        | \$ 275,251  | \$ 31,427        | \$ 28,339        | \$ 166,559        | \$ 31,440        | \$ 66,285        | \$ 1,918,006        |
| Special mention         | 2,018             | 10,321              | 2,494   | 1,027            |                  | 415               | 1,037            | 334              | 17,646              |
| Substandard             | 5,730             | 34,454              | 7,674   | 2,263            |                  | 244               | 2,724            | 4                | 53,093              |
| <b>Total originated</b> | <b>\$ 207,585</b> | <b>\$ 1,163,643</b> | <b>\$ 285,419</b>                                 | <b>\$ 34,717</b> | <b>\$ 28,998</b> | <b>\$ 170,320</b> | <b>\$ 31,778</b> | <b>\$ 66,285</b> | <b>\$ 1,988,745</b> |
| PNCI loans:             |                   |                     |   |                  |                  |                   |                  |                  |                     |
| Pass                    | \$ 102,895        | \$ 293,935          | \$ 27,378   | \$ 3,789         | \$ 3,164         | \$ 19,666         | \$ 13,636        | \$ 8,489         | \$ 472,952          |
| Special mention         | 600               | 10,795              | 445   | 80               | 74               |                   |                  |                  | 11,994              |
| Substandard             | 1,040             | 6,134               | 1,512   | 149              | 129              | 78                |                  |                  | 9,042               |
| <b>Total PNCI</b>       | <b>\$ 104,535</b> | <b>\$ 310,864</b>   | <b>\$ 29,335</b>                                  | <b>\$ 4,018</b>  | <b>\$ 3,367</b>  | <b>\$ 19,744</b>  | <b>\$ 13,636</b> | <b>\$ 8,489</b>  | <b>\$ 493,988</b>   |
| PCI loans               | \$ 2,145          | \$ 23,060           | \$ 7,738  | \$ 1,627         | \$ 64            | \$ 4,849          | \$ 721           |                  | \$ 40,204           |

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|             |            |              |            |           |           |            |           |           |              |
|-------------|------------|--------------|------------|-----------|-----------|------------|-----------|-----------|--------------|
| Total loans | \$ 314,265 | \$ 1,497,567 | \$ 322,492 | \$ 40,362 | \$ 32,429 | \$ 194,913 | \$ 46,135 | \$ 74,774 | \$ 2,522,937 |
|-------------|------------|--------------|------------|-----------|-----------|------------|-----------|-----------|--------------|

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**Table of Contents****Note 5 Allowance for Loan Losses (continued)**

Consumer loans, whether unsecured or secured by real estate, automobiles, or other personal property, are susceptible to three primary risks; non-payment due to income loss, over-extension of credit and, when the borrower is unable to pay, shortfall in collateral value. Typically non-payment is due to loss of job and will follow general economic trends in the marketplace driven primarily by rises in the unemployment rate. Loss of collateral value can be due to market demand shifts, damage to collateral itself or a combination of the two.

Problem consumer loans are generally identified by payment history of the borrower (delinquency). The Bank manages its consumer loan portfolios by monitoring delinquency and contacting borrowers to encourage repayment, suggest modifications if appropriate, and, when continued scheduled payments become unrealistic, initiate repossession or foreclosure through appropriate channels. Collateral values may be determined by appraisals obtained through Bank approved, licensed appraisers, qualified independent third parties, public value information (blue book values for autos), sales invoices, or other appropriate means. Appropriate valuations are obtained at initiation of the credit and periodically (every 3-12 months depending on collateral type) once repayment is questionable and the loan has been classified.

Commercial real estate loans generally fall into two categories, owner-occupied and non-owner occupied. Loans secured by owner occupied real estate are primarily susceptible to changes in the business conditions of the related business. This may be driven by, among other things, industry changes, geographic business changes, changes in the individual fortunes of the business owner, and general economic conditions and changes in business cycles. These same risks apply to commercial loans whether secured by equipment or other personal property or unsecured. Losses on loans secured by owner occupied real estate, equipment, or other personal property generally are dictated by the value of underlying collateral at the time of default and liquidation of the collateral. When default is driven by issues related specifically to the business owner, collateral values tend to provide better repayment support and may result in little or no loss. Alternatively, when default is driven by more general economic conditions, underlying collateral generally has devalued more and results in larger losses due to default. Loans secured by non-owner occupied real estate are primarily susceptible to risks associated with swings in occupancy or vacancy and related shifts in lease rates, rental rates or room rates. Most often these shifts are a result of changes in general economic or market conditions or overbuilding and resultant over-supply. Losses are dependent on value of underlying collateral at the time of default. Values are generally driven by these same factors and influenced by interest rates and required rates of return as well as changes in occupancy costs.

Construction loans, whether owner occupied or non-owner occupied commercial real estate loans or residential development loans, are not only susceptible to the related risks described above but the added risks of construction itself including cost over-runs, mismanagement of the project, or lack of demand or market changes experienced at time of completion. Again, losses are primarily related to underlying collateral value and changes therein as described above.

Problem C&I loans are generally identified by periodic review of financial information which may include financial statements, tax returns, rent rolls and payment history of the borrower (delinquency). Based on this information the Bank may decide to take any of several courses of action including demand for repayment, additional collateral or guarantors, and, when repayment becomes unlikely through borrower's income and cash flow, repossession or foreclosure of the underlying collateral.

Collateral values may be determined by appraisals obtained through Bank approved, licensed appraisers, qualified independent third parties, public value information (blue book values for autos), sales invoices, or other appropriate means. Appropriate valuations are obtained at initiation of the credit and periodically (every 3-12 months depending on collateral type) once repayment is questionable and the loan has been classified.

Once a loan becomes delinquent and repayment becomes questionable, a Bank collection officer will address collateral shortfalls with the borrower and attempt to obtain additional collateral. If this is not forthcoming and payment in full is unlikely, the Bank will estimate its probable loss, using a recent valuation as appropriate to the underlying collateral less estimated costs of sale, and charge the loan down to the estimated net realizable amount. Depending on the length of time until ultimate collection, the Bank may revalue the underlying collateral and take additional charge-offs as warranted. Revaluations may occur as often as every 3-12 months depending on the underlying collateral and volatility of values. Final charge-offs or recoveries are taken when collateral is liquidated and actual loss is known. Unpaid balances on loans after or during collection and liquidation may also be pursued through lawsuit and attachment of wages or judgment liens on borrower's other assets.

The following table shows the ending balance of current, past due, and nonaccrual originated loans by loan category as of the date indicated:

| Analysis of Past Due and Nonaccrual Originated Loans As of June 30, 2016 |             |              |             |           |         |              |            |           |           |              |
|--|-------------|--------------|-------------|-----------|---------|--------------|------------|-----------|-----------|--------------|
|  | RE Mortgage |              | Home Equity | Auto      | Other   | Construction |            |           |           |              |
| (in thousands)   | Resid.      | Comm.        | Lines       | Loans     | Indirec | Consum.      | C&I        | Resid.    | Comm.     | Total        |
| Originated loan balance:   |             |              |             |           |         |              |            |           |           |              |
| Past due:  |             |              |             |           |         |              |            |           |           |              |
| 30-59 Days   | \$ 46       | \$ 1,948     | \$ 1,326    | \$ 272    | \$      | \$ 47        | \$ 611     |           | \$ 397    | \$ 4,647     |
| 60-89 Days   | 70          | 298          | 250         | 110       |         | 9            | 415        |           |           | 1,152        |
| > 90 Days  | 344         | 364          | 219         | 482       |         | 9            | 295        |           |           | 1,713        |
| Total past due   | \$ 460      | \$ 2,610     | \$ 1,795    | \$ 864    | \$      | \$ 65        | \$ 1,321   |           | \$ 397    | \$ 7,512     |
| Current  | 221,000     | 1,295,248    | 272,054     | 35,653    |         | 29,558       | 188,173    | \$ 48,608 | 77,803    | 2,168,097    |
| Total orig. loans  | \$ 221,460  | \$ 1,297,858 | \$ 273,849  | \$ 36,517 |         | \$ 29,623    | \$ 189,494 | \$ 48,608 | \$ 78,200 | \$ 2,175,609 |
| > 90 Days and still accruing   |             |              |             |           |         |              |            |           |           |              |
| Nonaccrual loans   | \$ 2,375    | \$ 2,961     | \$ 2,826    | \$ 1,396  | \$      | \$ 9         | \$ 444     | \$ 11     |           | \$ 10,022    |

**Table of Contents****Note 5 Allowance for Loan Losses (continued)**

The following table shows the ending balance of current, past due, and nonaccrual PNCI loans by loan category as of the date indicated:

| (in thousands)               | Analysis of Past Due and Nonaccrual PNCI Loans |            |                      |                        |                  |           | As of June 30, 2016    |          | Total      |
|------------------------------|--|------------|----------------------|------------------------|------------------|-----------|------------------------|----------|------------|
|                              | RE Mortgage<br>Resid.                          | Comm.      | Home Equity<br>Lines | Auto<br>Loans Indirect | Other<br>Consum. | C&I       | Construction<br>Resid. | Comm.    |            |
| PNCI loan balance:           |  |            |                      |                        |                  |           |                        |          |            |
| Past due:                    |  |            |                      |                        |                  |           |                        |          |            |
| 30-59 Days                   |  |            | \$ 48                | \$ 20                  | \$ 21            |           |                        |          | \$ 89      |
| 60-89 Days                   | \$ 29  | \$ 744     | 11                   | 33                     |                  |           |                        |          | 817        |
| > 90 Days                    | 287  | 80         |                      |                        | 8                |           |                        |          | 375        |
| Total past due               | \$ 316   | \$ 824     | \$ 59                | \$ 53                  | \$ 29            |           |                        |          | \$ 1,281   |
| Current                      | 94,805   | 280,194    | 26,520               | 3,801                  | 2,719            | \$ 16,062 | \$ 13,174              | \$ 9,121 | 446,396    |
| Total PNCI loans             | \$ 95,121                                      | \$ 281,018 | \$ 26,579            | \$ 3,854               | \$ 2,748         | \$ 16,062 | \$ 13,174              | \$ 9,121 | \$ 447,677 |
| > 90 Days and still accruing |  |            |                      |                        |                  |           |                        |          |            |
| Nonaccrual loans             | \$ 532   | \$ 2,667   | \$ 512               | \$ 70                  | \$ 8             |           |                        |          | \$ 3,789   |

The following table shows the ending balance of current, past due, and nonaccrual originated loans by loan category as of the date indicated:

| (in thousands)           | Analysis of Past Due and Nonaccrual Originated Loans |        |                      |                        |                  |          | As of December 31, 2015 |       | Total    |
|--------------------------|--|--------|----------------------|------------------------|------------------|----------|-------------------------|-------|----------|
|                          | RE Mortgage<br>Resid.                                | Comm.  | Home Equity<br>Lines | Auto<br>Loans Indirect | Other<br>Consum. | C&I      | Construction<br>Resid.  | Comm. |          |
| Originated loan balance: |  |        |                      |                        |                  |          |                         |       |          |
| Past due:                |  |        |                      |                        |                  |          |                         |       |          |
| 30-59 Days               | \$ 791   | \$ 200 | \$ 1,033             | \$ 402                 | \$ 12            | \$ 2,197 |                         |       | \$ 4,635 |
| 60-89 Days               |  | 491    | 324                  | 341                    | 40               |          |                         |       | 1,196    |
| > 90 Days                | 271  | 3,425  | 520                  | 82                     | 19               | 24       |                         |       | 4,341    |

|                |         |           |         |        |        |         |           |           |           |
|----------------|---------|-----------|---------|--------|--------|---------|-----------|-----------|-----------|
| Total past due | 1,062   | 4,116     | 1,877   | 825    | 71     | 2,221   |           |           | 10,172    |
| Current        | 206,523 | 1,159,527 | 283,542 | 33,892 | 28,927 | 168,099 | \$ 31,778 | \$ 66,285 | 1,978,573 |

|                   |            |              |            |           |           |            |           |           |              |
|-------------------|------------|--------------|------------|-----------|-----------|------------|-----------|-----------|--------------|
| Total orig. loans | \$ 207,585 | \$ 1,163,643 | \$ 285,419 | \$ 34,717 | \$ 28,998 | \$ 170,320 | \$ 31,778 | \$ 66,285 | \$ 1,988,745 |
|-------------------|------------|--------------|------------|-----------|-----------|------------|-----------|-----------|--------------|

> 90 Days and still accruing

|                  |          |           |          |          |       |        |       |  |           |
|------------------|----------|-----------|----------|----------|-------|--------|-------|--|-----------|
| Nonaccrual loans | \$ 3,045 | \$ 14,196 | \$ 3,379 | \$ 1,195 | \$ 21 | \$ 976 | \$ 12 |  | \$ 22,824 |
|------------------|----------|-----------|----------|----------|-------|--------|-------|--|-----------|

The following table shows the ending balance of current, past due, and nonaccrual PNCI loans by loan category as of the date indicated:

| Analysis of Past Due and Nonaccrual PNCI Loans As of December 31, 2015 |             |            |             |          |          |          |              |           |          |
|--|-------------|------------|-------------|----------|----------|----------|--------------|-----------|----------|
| (in thousands)   | RE Mortgage |            | Home Equity | Auto     |          | Other    | Construction |           | Total    |
|  | Resid.      | Comm.      | Lines       | Loans    | Indirect | Consum.  | C&I          | Resid.    | Comm.    |
| PNCI loan balance:   |             |            |             |          |          |          |              |           |          |
| Past due:  |             |            |             |          |          |          |              |           |          |
| 30-59 Days   | \$ 3,106    | \$ 4,037   | \$ 92       | \$ 23    |          | \$ 1     |              |           | \$ 7,259 |
| 60-89 Days   |             |            |             |          |          | \$ 13    |              |           | 13       |
| > 90 Days  | 58          | 748        | 275         | 71       |          | 10       |              | \$ 490    | 1,652    |
| Total past due   | 3,164       | 4,785      | 367         | 94       |          | 23       | 1            | 490       | 8,924    |
| Current  | 101,371     | 306,079    | 28,968      | 3,924    |          | 3,344    | 19,743       | \$ 13,636 | 7,999    |
| Total PNCI loans   | \$ 104,535  | \$ 310,864 | \$ 29,335   | \$ 4,018 |          | \$ 3,367 | \$ 19,744    | \$ 13,636 | \$ 8,489 |
| > 90 Days and still accruing   |             |            |             |          |          |          |              |           |          |
| Nonaccrual loans   | \$ 348      | \$ 3,742   | \$ 676      | \$ 109   |          | \$ 33    |              | \$ 490    | \$ 5,398 |

**Table of Contents****Note 5 Allowance for Loan Losses (continued)**

Impaired originated loans are those where management has concluded that it is probable that the borrower will be unable to pay all amounts due under the contractual terms. The following tables show the recorded investment (financial statement balance), unpaid principal balance, average recorded investment, and interest income recognized for impaired Originated and PNCI loans, segregated by those with no related allowance recorded and those with an allowance recorded for the periods indicated.

| (in thousands)                      | Impaired Originated Loans |           |                      |               |                   | As of, or for the Six Months Ended, June 30, 2016 |        |                        |       | Total     |
|-------------------------------------|---------------------------|-----------|----------------------|---------------|-------------------|---|--------|------------------------|-------|-----------|
|                                     | RE Mortgage<br>Resid.     | Comm.     | Home Equity<br>Lines | Auto<br>Loans | Other<br>Indirect | Other<br>Consum.                                  | C&I    | Construction<br>Resid. | Comm. |           |
| With no related allowance recorded: |                           |           |                      |               |                   |   |        |                        |       |           |
| Recorded investment                 | \$ 3,223                  | \$ 7,927  | \$ 2,861             | \$ 1,217      |                   | \$ 9  | \$ 321 | \$ 11                  |       | \$ 15,569 |
| Unpaid principal                    | \$ 4,706                  | \$ 8,428  | \$ 5,267             | \$ 1,871      | \$ 7              | \$ 13   | \$ 356 | \$ 16                  |       | \$ 20,664 |
| Average recorded Investment         | \$ 3,554                  | \$ 17,518 | \$ 2,912             | \$ 1,082      | \$ 1              | \$ 13   | \$ 448 | \$ 8                   |       | \$ 25,536 |
| Interest income Recognized          | \$ 43                     | \$ 156    | \$ 12                | \$ 8          |                   |   | \$ 8   |                        |       | \$ 227    |
| With an allowance recorded:         |                           |           |                      |               |                   |   |        |                        |       |           |
| Recorded investment                 | \$                        |           |                      |               |                   |   |        |                        |       |           |