2017 Annual Report

PREFERRED BANK

California

New York

BRANCH LOCATIONS
www.preferredbank.com

- **Los Angeles Head Office**
  601 South Figueroa Street, 29th Floor
  Los Angeles, California 90017
  213.891.1188
- **San Gabriel Valley Regional Office**
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  Alhambra, California 91801
  626.282.9700
- **South Bay Regional Office**
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  Torrance, California 90503
  310.921.0100
- **Century City Regional Office**
  1801 Century Park East, Suite 100
  Los Angeles, California 90067
  310.286.2020
- **Irvine Regional Office**
  890 Roosevelt Avenue
  Irvine, California 92620
  949.262.9800
- **City of Industry Regional Office**
  17515 Colima Road
  City of Industry, California 91748
  626.935.1900
- **Arcadia Branch**
  1469 South Baldwin Avenue
  Arcadia, California 91007
  626.294.9800
- **Diamond Bar Branch**
  1373 South Diamond Bar Boulevard
  Diamond Bar, California 91765
  909.861.7200
- **Pico Rivera Branch**
  7004 Rosemead Boulevard
  Pico Rivera, California 90660
  562.641.2540
- **San Francisco Regional Office**
  600 California Street, Suite 550
  San Francisco, California 94108
  415.230.3288
- **San Francisco Richmond Office**
  5160 Geary Boulevard
  San Francisco, California 94108
  415.213.8880
- **San Fernando Valley Regional Office**
  18321 Ventura Boulevard Suite 100
  Tarzana, California 91356
  818.668.8800
- **Flushing New York Regional Office**
  41-60 Main Street
  Flushing, New York 11355
  718.886.1788

March 21, 2018

Dear Shareholders

2017 was another year of growth in profitability, total loans, total deposits and total assets. In addition, we also added fairly significantly to our back office staff in order to prepare us for further growth. Total shareholder return, including dividends was 13.6% for 2017, this coming off of a record year in which total shareholder return was 60.6% in 2016. Our three- and five-year total shareholder return is one of the best in the U.S.

With the late-2017 passing of the Tax Cut and Jobs Act in late 2017, we were required to write down part of our deferred tax asset ("DTA") in the fourth quarter of the year. This had the effect of reducing net income by $6.7 million for the quarter. While this is obviously a negative charge, we are very pleased with the passage of the Bill as it will significantly lower our effective tax rate in 2018 and beyond.

For 2017, Preferred Bank:

- Recorded net income of $43.4 million which is 19.3% higher than 2016, even after the DTA charges of $6.7 million in Q4 2017

- Increased loans by $398 million or 15.6% from 2016.

- Increased deposits by $499 million or 18.1% from 2016.

- Improved the efficiency ratio to 36.6%.

- Posted a best in class ROA of 1.43% and an ROE of 15.93% (Excluding deferred tax asset writedown).

With the lowered tax rate, the prospects for further earnings growth are significantly enhanced. We have already shared some of the tax savings with our employees who saw higher-than-normal pay increases for 2018. Our employees also benefit from the Bank's Bonus Plan which is highly correlated to the profitability of the Bank.

During the fourth quarter of 2017, we raised approximately $33.5 million in new capital through the at-the-market or ATM method. This helped to increase our tier 1 leverage ratio from 8.54% at September 30, 2017 to 9.52% as of December 31, 2017. Going forward, through the enhanced earnings power via the tax cut and anticipated interest rate increases, our capital should be sufficient for planned future growth.

Very Truly Yours,

Li Yu
Chairman and CEO

FEDERAL DEPOSIT INSURANCE CORPORATION

Washington, D.C. 20429

FORM 10-K

Mark One

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

For the fiscal year ended December 31, 2017

or

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

For the transition period from to .

PREFERRED BANK

(Exact name of registrant as specified in its charter)

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

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

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

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

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

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

None

(Title of class)

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

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

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

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

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

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

Large accelerated filed ☐ Accelerated filer ☒ Non-accelerated filer ☐ Smaller reporting company ☐
Emerging growth company ☐

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

The aggregate market value of the voting and non-voting common equity held by non-affiliates of the Registrant, computed by reference to the price at which the common equity was last sold as of the last business day of the Registrant's most recently completed second fiscal quarter (June 30, 2017) was $627,622,088.

Number of shares of common stock of the Registrant outstanding as of March 13, 2018, was 15,318,580.

The following documents are incorporated by reference herein:

Document Incorporated By Reference	**Part of Form 10-K Into Which Incorporated**
Definitive Proxy Statement for the Annual Meeting of Shareholders which will be filed within 120 days of the fiscal year ended December 31, 2017	Part III

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PART I

Forward-Looking Statements

Certain matters discussed in this Annual Report on Form 10-K ("Annual Report") may constitute forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended (the "Securities Act") and Seceeetion 21E of the Securities Exchange Act of 1934, as amended (the "Exchange Act"), and as such, may involve risks and uncertainties. We claim the protection of the safe harbor contained in the Private Securities Litigation Reform Act of 1995. These forward-looking statements relate to, among other things, the Bank's financial condition, results of operations, plans, objectives, expectations of the environment in which we operate and projections of future performance or business. Such statements can generally be identified by the use of forward-looking language, such as "is expected to," "will likely result," "anticipated," "projected", "estimate," "forecast," "intends to," or may include other similar words, phrases, or future or conditional verbs such as "aims", "believes," "plans," "continue," "remain," "may," "might," "will," "would," "should," "could," "can," or similar language. Forward-looking statements by us are based on estimates, beliefs, projections and assumptions of management and are not guarantees of future performance. Our actual results, performance, or achievements may differ significantly from the results, performance, or achievements expected or implied in such forward-looking statements. When considering these statements, you should not place undue reliance on these statements, as they are subject to certain risks and uncertainties, as well as any cautionary statements made within this Annual Report, and should also note that these statements are made as of the date of this Annual Report and based only on information known to us at that time.

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

- Regulatory decisions regarding the Bank, and impact of future regulatory and governmental agency decisions including Basel III capital standards
- Adequacy of allowance for loan and lease loss estimates in comparison to actual future losses
- Necessity of additional capital in the future, and possible unavailability of that capital on acceptable terms
- Economic and market conditions that may adversely affect the Bank and our industry
- Possible loss of members of senior management or other key employees upon whom the Bank heavily relies
- Natural disasters or recurring energy shortages
- Variations in interest rates which may negatively affect the Bank's financial performance
- Strong competition from other financial service entities
- Possibility that the Bank's underwriting practices may prove not to be effective
- Changes in the commercial and residential real estate markets
- A deterioration in the California real estate market could diminish the collateral value of our loans and increase charge-offs
- Adverse economic conditions in Asia which could negatively impact the Bank's business
- Geographic concentration of our operations
- The economic impact of Federal budgetary policies
- Failure to attract deposits, inhibiting growth

- Interruption or break in the communication, information, operating, and financial control systems upon which the Bank relies
- Changes in laws or the regulatory environment including regulatory reform initiatives and policies of the U.S. Department of Treasury, the Board of Governors of the Federal Reserve Board System, the Federal Deposit Insurance Corporation, and the Consumer Financial Protection Bureau
- Changes in accounting standards as may be required by the Financial Accounting Standards Board or other regulatory agencies and their impact on critical accounting policies and assumptions
- Potential changes in the U.S. government's monetary policies
- Risks associated with acquisitions
- Environmental liability with respect to properties to which the Bank takes title
- Negative publicity
- Possible security breaches in our online banking services
- The impact of tax reform legislation

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

ITEM 1. BUSINESS

References in this Annual Report to "we," "us," or "our," and the "Bank" mean Preferred Bank and its wholly-owned subsidiary, PB Investment and Consulting, Inc., or PB Consulting, which has no current operations.

General

We are one of the larger independent commercial banks in California focusing primarily on the diversified California market, with a historical niche in the Chinese-American market. We consider the Chinese-American market to encompass individuals born in the United States of Chinese ancestry, ethnic Chinese who have immigrated to the United States and ethnic Chinese who live abroad but conduct business in the United States. Although founded as a Bank that primarily serves the Chinese-American community, the majority of our current business activities come from the diverse mainstream markets of Southern and Northern California as well as Flushing, New York. We commenced operations in December 1991 as a California state-chartered bank in Los Angeles, California. Our deposits are insured by the Federal Deposit Insurance Corporation ("FDIC"). We are a member of the Federal Home Loan Bank ("FHLB") of San Francisco and of the FHLB of New York.

At December 31, 2017, our total assets were $3.77 billion, loans were $2.94 billion, deposits were $3.26 billion and shareholders' equity grew to $355.0 million. These balances all saw increases from assets of $3.22 billion, loans of $2.51 billion, deposits of $2.76 billion, and shareholders' equity of $298.1 million as of December 31, 2016. We had net earnings per share on a diluted basis of $2.96 for the year ended December 31, 2017 as compared to net earnings of $2.56 per share for the year ended December 31, 2016 and net earnings per share of $2.14 for the year ended December 31, 2015. Net interest income before provision for credit losses increased to $129.7 million for the year ended December 31, 2017, up from $104.2 million for the year ended December 31, 2016 and $83.8 million for the year ended December 31, 2015. We recorded a provision for credit losses of $5.5 million in 2017, which is down from the provision of $6.4 million recorded in 2016 and up from the provision of $1.8 million recorded in 2015.

We provide personalized deposit services as well as real estate finance, commercial loans and trade finance to small and mid-sized businesses and their owners, entrepreneurs, real estate developers and investors,

professionals and high net worth individuals. Traditionally, we have been more focused on businesses as opposed to retail customers and have a small relative number of customer relationships for whom we provide a high level of service and personal attention. During 2017, we created a home mortgage loan department and began originating home mortgage loans. As we were founded to serve the ethnic Chinese community, we believe we have benefited, and will continue to benefit, from the significant migration into California of ethnic Chinese from China and other areas of East Asia. While the majority of our business is not dependent on the Chinese-American market, it represents an important element of our operating strategy, especially for our branch network and deposit products and services.

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

We conduct operations from our main office in downtown Los Angeles, California and through twelve full-service branch banking offices in Los Angeles, Orange, and San Francisco Counties in California, as well as one location in Queens County in New York. We market our services and conduct our business primarily in the same markets as our branch office locations.

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

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

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

Our Traditional Banking Business

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

- *Real Estate Finance*—consisting of investors and developers within the real estate industry and of owner-occupied properties in Southern California. We have traditionally provided construction loans

and mini-permanent ("mini-perm") loans for residential, commercial, industrial and other income producing properties, although construction lending is no longer a focus for new business. A portion of our real estate loans are to borrowers who are also international trade finance customers. We do not typically market single-family residential mortgages but provide them as an accommodation to our business customers.

- *Middle Market Business*—consisting of manufacturing, service and distribution companies with annual sales of approximately $5 million to $100 million and with borrowing requirements of up to approximately $12 million. We offer a range of lending products to customers in this market, including working capital loans, equipment financing and commercial real estate loans. Additionally, we provide a full range of deposit products and related services including safe deposit boxes, account reconciliation, courier service and cash management services.
- *Trade Finance*—consisting of importers and exporters based in the U.S. requiring both borrowing and operational products. We offer a full range of products to international trade finance customers, including commercial and standby letters of credit, acceptance financing, documentary collections, foreign draft collections, international wires and foreign exchange.
- *High-wealth Banking*—consisting of wealthy individuals residing in the Pacific Rim area with residences, real estate investments or businesses in Southern California. We offer all of our banking products and services to this segment through our multi-lingual team of professionals knowledgeable in the business environment and financial affairs of Pacific Rim countries. We believe our language capabilities provide us with a competitive advantage.
- *Professionals*—consisting generally of physicians, accountants, attorneys, business managers and other professionals. We provide specialized personal banking services to customers in this segment including courier service, several types of specialized deposit accounts and personal and business loans as well as lines of credit.

We provide a fully operational internet banking website with bill pay services as well as mobile banking for phone and tablet applications for these customers.

Our Current Focus

Our current business focus is maintaining a high level of credit quality while continuing a similar level of growth achieved in the past few years. As the Bank gets larger in total assets, loans and deposits, maintaining the same growth pattern becomes more challenging. Traditionally the Bank has always placed a greater emphasis on gathering deposits rather than loans, knowing that the deposits are what drives a great deal of the franchise value of the Bank.

In addition, the Bank is also focused on loan portfolio diversification. In December of 2015, the FDIC released FIL 62-2015, Statement on Prudent Risk Management for CRE Lending. This was mostly a re-release of a similar interagency statement from 2006 which, among other things, set guidelines for CRE concentrations relative to total capital. In light of this, the Bank began to look at ways to reduce CRE concentrations and to diversify the loan portfolio. In June 2016, the Bank began issuing subordinated debt and eventually closed out the issuance in September 2016 at $100 million. As a result of the subordinated debt issuance, the Bank's total capital ratio significantly increased.

In mid-2016, we entered the residential mortgage market and hired a senior manager and staff to begin the process of establishing a residential mortgage origination department. This department began operations in the first quarter of 2017 and we expect this group to provide further diversification to our loan portfolio. We expect that nearly all loans originated will be held in the loan portfolio and that we will sell very few loans originated.

On September 25, 2017, the Bank was granted a Stock Permit (the "Stock Permit") from the California Department of Business Oversight ("DBO") authorizing it to sell, from time-to-time, up to $50 million in shares

of the Bank's common stock, by means of an "at the market offering" program (the "ATM Program"). The authorization to sell shares granted by the Stock Permit expires on March 26, 2018. During the fourth quarter of 2017, the Bank sold 541,975 shares through the ATM Program for the net proceeds of $32.8 million.

Our Market

We conduct operations from our main office in downtown Los Angeles, California and 12 full-size branch banking offices in Los Angeles, Orange, and San Francisco Counties in California, and one full-size branch in Queens County, New York, as of December 31, 2017. We market our services and conduct our business primarily in the same markets as our branch office locations.

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

- Deposit and cash management services to businesses and high net worth depositors with a high degree of personal service and responsiveness;
- An experienced, multi-lingual management team and staff who have an understanding of Asian markets and cultures who we believe can provide sophisticated credit solutions faster, more efficiently and with a higher degree of personal service than what is provided by our competition;
- Very responsive credit decisioning and execution which our clients value greatly and
- Loan products to customers requiring credit of a size in excess of what can be provided by our smaller competitors.

Our Lending Activities

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

- Real estate mortgage loans;
- Real estate construction loans;
- Commercial loans; and
- Trade finance.

We have also utilized our relationships within the banking industry to purchase and sell participations in loans that meet our underwriting criteria. As of December 31, 2017, we had a total of $327.9 million in purchased participation loans and $67.7 million in loan participations that we sold. Of the $327.9 million in purchased participations, $127.3 million are loans made to our own relationship customers, which we believe helps mitigate the risk of default. We manage our loan portfolio to provide for an adequate return, but also to provide for diversification of risk.

We have historically originated our loans from our banking offices in Los Angeles, Orange, and San Francisco counties. During 2015, the acquisition of United International Bank, or UIB, resulted in an additional office from which loans could be originated in the Northeast Tri-State Area. For mini-perm and construction loans, we have relied on referrals from existing clients who are real estate investors, owner/operators, and developers as well as internal business development efforts. For our commercial and trade finance lending, we have sought referrals from existing banking clients as well as referrals from professionals, such as certified public accountants, attorneys and business consultants.

At December 31, 2017, 82% of our loans carried interest rates that adjust with changes in the Prime Rate, 13% carried interest rates tied to the London Interbank Offered Rank ("LIBOR") or other indices and 5% carried a fixed rate or were tied to rates on certificates of deposit ("CDs"). Approximately 78% of our loan portfolio has an interest rate floor.

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

	At December 31, 2017
	(Dollars in thousands)
Real Estate Mini-Perm	
Portfolio size	$1,697,947
Number of loans	643
Average loan size	$ 2,641
Average LTV[1]	56%
Average DCR[2]	1.61x
Weighted average rate	5.43%
Average years since origination	2.3 years
Residential Mortgage	
Portfolio size	$ 71,354
Number of loans	143
Average loan size	$ 509
Average LTV[1]	59%
Weighted average rate	4.49%
Average years since origination	1.7 years
Real Estate Construction	
Portfolio size	$ 283,802
Number of loans	78
Average loan size	$ 3,638
Average LTV[1]	52%
Weighted average rate	5.68%
Average years since origination	1.6 years
Commercial Loans	
Portfolio size	$ 866,672
Number of loans	1,111
Average loan size	$ 780
Weighted average rate	4.70%
Average years since origination	2.8 years
Trade Finance	
Portfolio size	$ 21,310
Number of loans	77
Average loan size	$ 277
Weighted average rate	4.90%
Average years since origination	0.9 years

(1) Average loan-to-value at origination, or LTV, is calculated based upon a weighted average of outstanding principal loan balances (for mini-perm loans) or commitment (for construction loans) divided by the original value.

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

As of December 31, 2017, we had 456 loans with outstanding principal balances between $1 million to $5 million, 86 loans with outstanding principal balances between $5 million and $10 million, and 53 loans with outstanding principal balances over $10 million.

Real Estate Mortgage Loans

Our Real Estate Mortgage portfolio consists primarily of real estate mini-perm loans, as well as purchased residential mortgages. Real estate loans are secured by retail, industrial, office, special purpose, residential single- and residential multi-family properties and comprise 60% of our loan portfolio as of December 31, 2017.

We seek diversification in our loan portfolio by maintaining a broad base of borrowers and monitoring our exposure to various property types as well as geographic and industry concentrations. Total real estate loans were $1.77 billion at December 31, 2017 as compared to $1.55 billion as of December 31, 2016. Net recoveries of real estate loans accounted for (7.0%) of total net loan charge-offs during 2017. For 2016, net recoveries of real estate loans accounted for (28.4%) of total net loan charge-offs during the year. Loans secured by land totaled $10.9 million and $16.6 million at December 31, 2017 and 2016, respectively. There were no charge-offs or recoveries on land loans during 2017 or 2016.

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

Property Type	At December 31, 2017 Amount	At December 31, 2017 Percentage of Loans in Each Category in Total Loan Portfolio
	(Dollars in thousands)	
Commercial / Office	$ 266,508	9.06%
Retail	422,174	14.35
Industrial	190,471	6.48
Residential 1-4	362,276	12.32
Apartment 4+	151,677	5.16
Land	10,862	0.37
Special purpose	365,333	12.42
Total	$1,769,301	60.16%

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

At December 31, 2017						
Less than					More Than	Total Outstanding
1 Year	2 Years	3 Years	4 Years	5 Years	5 Years	Balance
			(In thousands)			
$302,540	$157,559	$265,029	$197,810	$375,247	$471,116	$1,769,301

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

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

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

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

- Maximum LTV of 50%-85%, depending on the property type. However, our practice is to lend at a maximum LTV of 65%.
- Minimum DCR of 1.1-1.25, depending on the property type.
- Requirements of personal guarantees from the principals of any closely-held entity.

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

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

In addition to real estate mini-perm loans, the Bank purchased a portfolio of home mortgage loans during the fourth quarter of 2015, and purchased two additional portfolios of home mortgage loans during 2016. The total home mortgage loan balance was $56.9 million at December 31, 2017 and was $87.1 million at December 31, 2016. The rate for these purchased loans adjusts with changes to either the 1-year Treasury rate or 1-year LIBOR. Total number of acquired home mortgage loans carried as of December 31, 2017 was 113 and average LTV for the acquired loans is approximately 63%. The number of acquired loans carried as of December 31, 2016 was 175, and average LTV for the loans was approximately 63%.

Real Estate Construction

Our construction loans are typically short-term loans of up to 18 months for the purpose of funding the costs of constructing a building. Construction loan net charge-offs as a percentage of total loan net charge-offs during 2017 and 2016 were not meaningful as there were net recoveries during each of these periods. We had 92 construction loans totaling $283.8 million as of December 31, 2017, and 71 construction loans totaling $233.4 million as of December 31, 2016. Outstanding construction loans by property type are summarized as follows:

	At December 31, 2017	
Property Type	**Amount**	**Percentage of Loans in Each Category in Total Loan Portfolio**
	(Dollars in thousands)	
Commercial / Office	$ 2,625	0.09%
Retail	22,748	0.77
Industrial	4,560	0.16
For sale attached residential	22,740	0.77
For sale detached residential	62,459	2.12
Apartment 4+	76,669	2.61
Land / Special Purpose	92,001	3.13
Total	$283,802	9.65%

Loan Origination: The origination process for construction loans is similar to our real estate mini-perm origination process described above under "—Real Estate Mortgage Loans—Loan Origination," but with one additional step. For construction loans, we require a third party review of the developer's proposed building costs for large scale projects, and for other building projects on a case-by-case basis.

Underwriting Standards: Our underwriting standards for construction loans are identical to those described above under "—Real Estate Mortgage Loans—Underwriting Standards." For the for-sale-housing projects, however, the DCR requirement is not applicable. In addition, we require that the construction loan applicant has proven experience in the type of project under consideration. Finally, notwithstanding the maximum 50-85% LTV discussed above under "—Real Estate Mortgage Loans—Underwriting Standards," we generally require a maximum 70% LTV for construction loans at origination.

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

Commercial Loans

We offer a variety of commercial loan products including lines of credit for working capital, term loans for capital expenditures and commercial and stand-by letters of credit. As a matter of practice, the Bank typically requires a deposit relationship with commercial borrowers. As of December 31, 2017, we had $866.7 million of commercial loans outstanding, which represented 29.4% of the overall loan portfolio, compared to $733.7 million outstanding as of December 31, 2016, which represented 28.8% of the overall portfolio as of that

time. This loan category has traditionally experienced lower loss rates, particularly when compared to the loss rates on construction and land loans. Currently, the Bank is working to grow this line of business primarily because of the additional deposit relationships as well as the risk diversity that this portfolio brings to our overall loan portfolio which is typically more concentrated in real estate-related loans. Lines of credit typically have a one to two year commitment and are secured by the borrower's assets. In cases of larger commitments, an updated borrowing base certificate from the borrower may be required to determine eligibility at the time of any given advance. Term loans seldom exceed 60 months, but in no case exceed the depreciable life of the tangible asset being financed.

Trade Finance Credits

Our trade finance portfolio totaled $21.3 million, or 0.7% of our total loan portfolio as of December 31, 2017, compared to $21.7 million, or 0.9%, as of December 31, 2016. Of this amount, virtually all loans were made to U.S.-based importers who are also our current borrowers or depositors. Trade finance loans are essentially commercial loans but are typically made to importers or exporters. This portfolio has, similar to commercial loans, performed relatively well. During both 2017 and 2016, there were no charge-offs or recoveries on trade finance loans. We also provide standby letters of credit and foreign exchange services to our clients. Our new trade finance credit relationships result from contacts and relationships with existing clients, certified public accountants and trade facilitators such as customs brokers. In many cases, the ability to generate new trade finance business is also a result of cultivated social contacts and extended family.

We offer the following services to importers:

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

We offer the following services to exporters:

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

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

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

- Cash flow is our primary underwriting criterion. We require a minimum 1.25:1 DCR for our commercial and trade finance loans. We also review trends in the borrower's sales levels, gross profit and expenses.
- We evaluate the borrower's financial statements to determine whether the given borrower's balance sheet provides for appropriate levels of equity and working capital.
- Since most of our borrowers are closely held companies, we require the principals to guarantee their company's debt. Our underwriting process, therefore, includes an evaluation of the guarantor's net worth, income and credit history. Where circumstances warrant, we may require guarantees be secured by collateral (generally real estate).
- Where there is a reliance on the accounts receivable and inventory of a company, we evaluate their condition, which may include third party onsite audits.

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

Loan Concentrations

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

As of both December 31, 2017 and 2016, the percentage of loans secured by real estate in our total loan portfolio was approximately 70%.

Our combined construction and real estate loans by type of collateral are as follows:

	At December 31, 2017	
Property Type	Amount	Percentage of Loans in Each Category in Total Loan Portfolio
	(Dollars in thousands)	
Commercial/Office	$ 269,133	9.15%
Retail[1]	444,922	15.13
Industrial	195,031	6.63
Residential 1-4	447,475	15.21
Apartment 4+	228,346	7.76
Land	10,862	0.37
Special purpose[2]	457,334	15.55
Total	$2,053,103	69.80%

(1) Includes shopping centers, strip malls or stand-alone properties which house retailers.

(2) Examples include hospitality and self-storage.

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

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

At December 31, 2017, the weighted average LTV of our construction and commercial real estate portfolio based on LTVs at the time of origination was 55%. Our practice is to require DCR's on commercial real estate loans of 1.1x to 1.25x, depending on the property type. We also underwrite our commercial real estate loans using a rate that is 1-2% greater than the proposed interest rate on the loan.

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

	At December 31, 2017					
(Dollars in thousands)	Inland Empire[1]	Southern California[2]	Other California	Tri State Area[3]	Other Areas	Total
Real estate mortgage—residential	$ 7,383	$ 212,138	$ 50,130	$ 92,161	$ 9,399	$ 371,211
Real estate mortgage—commercial	84,287	751,271	298,335	156,858	107,779	1,398,530
Construction Residential	—	55,929	12,837	16,433	—	85,199
Construction Commercial	18,647	93,319	40,288	38,018	8,331	198,603
Total Real Estate Loans	$110,317	$1,112,657	$401,590	$303,470	$125,509	$2,053,543

(1) Includes Riverside and San Bernardino counties.
(2) Includes Los Angeles, Orange and San Diego counties.
(3) Includes New York, New Jersey and Connecticut.

In addition, we have established certain concentration limits for our real estate lending activities by property type. Our other real estate loan limitations include out of area (California & the Tri State Area) lending at no more than 10% of our portfolio. At December 31, 2017, 6.1% of our real estate portfolio was secured by real estate located out of area. At December 31, 2017, the top 20 borrowing relationships of the Bank totaled $974.4 million in loans outstanding and comprised 33% of the total loan portfolio.

Except as described above, no individual or single group of related accounts is considered material in relation to our assets or deposits or in relation to our overall business. Approximately 70% of our loan portfolio at December 31, 2017 consisted of real estate secured loans. At December 31, 2017, we had 595 loans in excess of $1.0 million, totaling $2.60 billion. These loans comprise approximately 29% of our loan portfolio based on number of loans and 88% based on the total outstanding balance. Excluding consumer overdraft lines, our average loan size is $1.4 million.

Loan Maturities

In addition to measuring and monitoring concentrations in our loan portfolio, we also monitor the maturities and interest rate structure of our loan portfolio. The following table shows the amounts of loans outstanding as of December 31, 2017 which, based on remaining scheduled repayments of principal, were due in one year or less, more than one year through five years, and more than five years. The table also presents, for loans with maturities over one year, an analysis with respect to fixed interest rate loans and floating interest rate loans.

	At December 31, 2017				Rate Structure for Loans Maturing Over One Year	
	Maturity					
	One Year or Less	One through Five Years	Over Five Years	Total	Fixed Rate	Floating Rate
	(In thousands)					
Real estate mortgage	$302,540	$ 995,645	$471,116	$1,769,301	$19,516	$1,447,245
Real estate construction	235,590	44,787	3,425	283,802	—	48,212
Commercial	399,485	400,358	66,829	866,672	70,718	396,469
Trade finance	9,560	11,750	—	21,310	—	11,750
Consumer	—	—	—	—	—	—
Other	8	—	—	8	—	—
Total	$947,183	$1,452,540	$541,370	$2,941,093	$90,234	$1,903,676

The following table shows the amounts of loans outstanding as of December 31, 2016, which, based on remaining scheduled repayments of principal, were due in one year or less, more than one year through five years, and more than five years. Demand or other loans having no stated maturity and no stated schedule of repayments are reported as due in one year or less. The table also presents, for loans with maturities over one year, an analysis with respect to fixed interest rate loans and floating interest rate loans.

	At December 31, 2016				Rate Structure for Loans Maturing Over One Year	
	Maturity					
	One Year or Less	One through Five Years	Over Five Years	Total	Fixed Rate	Floating Rate
	(In thousands)					
Real estate mortgage	$248,360	$ 946,738	$355,080	$1,550,178	$ 44,778	$1,257,040
Real estate construction	171,172	62,222	—	233,394	—	62,222
Commercial	249,565	416,680	67,463	733,708	73,287	410,857
Trade finance	11,933	9,769	—	21,702	—	9,769
Consumer	2	—	4,401	4,403	—	4,401
Other	164	—	—	164	—	—
Total	$681,196	$1,435,409	$426,944	$2,543,549	$118,065	$1,744,289

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

Loan Authorizations

To ensure strength and diversity of the credit portfolio, the authorizations and approvals required to originate various loan types are detailed as follows:

- *Individual Authorities*. Our Chief Executive Officer, Chief Operating Officer and Chief Credit Officer have combined approval authority up to $12.0 million for loans secured by first deeds of trust and up to

$8.0 million for unsecured transactions. Loans in excess of these two limits are submitted to our Board of Directors Loan Committee for approval.

- *Board of Directors Loan Committee*. Our Board of Directors Loan Committee consists of five members of the Board of Directors and our Chief Executive Officer. It has approval authority up to our legal lending limit, which was approximately $120.1 million for real estate secured loans and $72.1 million for unsecured loans at December 31, 2017. The Board of Directors Loan Committee also reviews all loan commitments granted in excess of $1.0 million on a quarterly basis for the preceding quarter.

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

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

We believe that the current authority levels provide satisfactory management and a reasonable percentage of secondary review. Any conditions placed on loans in the approval process must be satisfied before our Chief Credit Officer will release loan documentation for execution.

Loan Grading and Loan Review

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

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

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

- Quarterly covenant tracking of commercial loans over $1 million;
- Semi-annual stress testing of real estate loans over $1.5 million;
- Semi-annual third party loan reviews;
- Bank regulatory examinations; and
- Monthly action plans submitted to the Chief Credit Officer by the responsible lending officers for each credit graded 5-8.

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

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

Purchased Loan Participations

As of December 31, 2017, we had a total of $327.9 million in purchased participation loans and $67.7 million in loan participations that we sold. Of the $327.9 million in purchased participations, $127.3 million are loans made to our own relationship customers, which we believe helps mitigate the risk of default. These loans include commercial real estate, construction and commercial loans. There were no charge-offs of loan participations during 2017. The Bank partially charged off one participation loan for $4.0 million during 2016. These loans are underwritten using the same standards as loans that the Bank originates directly.

Deposit Products and Other Sources of Funds

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

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

The following table shows the balance of each major category of deposits at December 31, 2017 and 2016:

	December 31, 2017		December 31, 2016	
	Amount	% of Total Deposits	Amount	% of Total Deposits
	(Dollars in thousands)			
Noninterest-Bearing deposits	$ 659,487	20.21%	$ 586,272	21.21%
Interest-Bearing Deposits:				
Interest-Bearing Demand	1,353,974	41.50%	1,019,058	36.87%
Savings	24,429	0.75%	34,067	1.23%
Time Certificates of $250,000 or more	621,648	19.05%	427,172	15.46%
Other Time Certificates	603,152	18.49%	697,155	25.23%
Total Deposits	$3,262,690	100.00%	$2,763,724	100.00%

Total deposits were $3.26 billion as of December 31, 2017, of which 20.2% were demand deposits, 42.3% were in savings and interest-bearing checking, 19.1% were in CD's greater than $250,000 and 18.5% were in other CD's. We closely monitor rates and terms of competing sources of funds and utilize those sources we believe to be the most cost effective, consistent with our asset and liability management policies.

Deposits and Related Services: We have historically relied primarily upon, and expect to continue to rely primarily upon, deposits to satisfy our needs for sources of funds. An important balance sheet component impacting our net interest margin is the composition and cost of our deposit base. We can improve our net interest margin to the extent that growth in deposits can be focused in the less volatile and somewhat more traditional core deposits, or total deposits excluding CDs greater than $250,000, which are commonly referred to as Jumbo CDs.

We provide a wide array of deposit products. We offer regular checking, savings, negotiable order of withdrawal ("NOW") and money market deposit accounts; fixed-rate, fixed maturity retail certificates of deposit ranging in terms from 14 days to two years; and individual retirement accounts and non-retail certificates of deposit consisting of Jumbo CDs. We attempt to price our deposit products in order to promote deposit growth

and satisfy our liquidity requirements. We provide remote deposit capture service or courier service to pick up non-cash deposits, and for those customers that use large amounts of cash, we arrange for armored car and vault service.

We provide a high level of personal service to our high net worth individual customers who have significant funds available to invest. We believe our Jumbo CDs are a stable source of funding because they are based primarily on service and personal relationships with senior Bank officers rather than the interest rate. Further evidence of this is the fact that our average Jumbo CD customer has been a customer of the Bank for over six years. Further, 9% of these Jumbo CDs are pledged as collateral for loans from us to the depositor or the depositor's affiliated business or family member. We monitor interest rates offered by our competitors and pay a rate we believe is competitive with the range of rates offered by such competitors.

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

At December 31, 2017, excluding government deposits, brokered deposits and deposits as direct collateral for loans, we had 136 depositors with deposits in excess of $3.0 million that totaled $1.8 billion, or 54.2% of our total deposits.

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

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

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

Other Borrowings: In the past we have also borrowed from the FHLB pursuant to an existing commitment based on the value of the collateral pledged (both loans and securities) in our portfolio. We had $6.4 million in outstanding FHLB advances at December 31, 2017. At December 31, 2017, approximately $591.3 million of the Bank's real estate loans was pledged as collateral with Federal Home Loan Bank and the remaining borrowing capacity was $305.1 million. In addition, we have pledged $134.3 million in securities at the Federal Reserve Bank Discount Window and may borrow against that as well.

Our Investment Activities

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

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

The total carrying value of investment securities (including both securities held-to-maturity and securities available-for-sale) amounted to $197.0 million and $210.2 million as of December 31, 2017 and 2016, respectively. Investment securities consist primarily of investment grade corporate notes, municipal bonds, collateralized mortgage obligations, U.S. government agency securities, and U.S. agency mortgage-backed securities. In addition, for bank liquidity purposes, we use overnight federal funds, which are temporary overnight sales of excess funds to correspondent banks.

As of both December 31, 2017 and 2016, the bank had two investment securities with total amortized cost of $8.8 million and $10.3 million, respectively, classified as "held-to-maturity." The remainder of our investment securities is classified as "available-for-sale" pursuant to Investments—Debt and Equity Securities Topic of the Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC"). Available-for-sale securities are reported at fair value, with unrealized gains and losses excluded from earnings and instead reported as a separate component of shareholders' equity. Held-to-maturity securities are securities for which we have both the intent and the ability to hold to maturity. These securities are carried at cost adjusted for amortization of premium and accretion of discount.

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

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

Our Competition

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

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

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

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

Mergers between financial institutions have placed additional pressure on banks to consolidate their operations, reduce expenses and increase revenues to remain competitive. The competitive environment is also

significantly impacted by federal and state legislation that make it easier for non-bank financial institutions to compete with us.

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

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

Foreign Operations

We have no foreign operations.

Segment Information

As discussed above, through our branch network, the Bank provides a broad range of financial services to individuals and companies located primarily in Southern California. Their services include demand, time and savings deposits and real estate, business and consumer lending. While our chief decision makers monitor the revenue streams of our various products and services, operations are managed and financial performance is evaluated on a company-wide basis. Accordingly, the Bank considers all of our operations to be aggregated in one reportable operating segment, which accounted for 100% of our revenue, net income and assets.

REGULATION AND SUPERVISION

The following discussion of statutes and regulations affecting banks is only a summary and does not purport to be complete nor does it address all applicable statutes and regulations. This discussion is qualified in its entirety by reference to such statutes and regulations referred to in this discussion. No assurance can be given that such statutes or regulations will not change in the future.

General

The Bank is extensively regulated under both federal and state laws. Regulation and supervision by the federal and state banking agencies is intended primarily for the protection of depositors, the Deposit Insurance Fund ("DIF") administered by the FDIC, borrowers and the stability of the U.S. banking system, and not for the benefit of the Bank's shareholders.

As a California state-chartered bank that is not a member of the Federal Reserve System, we are subject to supervision, periodic examination and regulation by the California Department of Business Oversight ("CDBO"), as the Bank's state regulator, and by the FDIC, as the Bank's primary federal regulator. The regulations of these agencies govern most aspects of our business, including the filing of periodic reports by us, and our activities relating to dividends, investments, loans, borrowings, capital requirements, certain check-clearing activities, branching, mergers and acquisitions, reserves against deposits, the timing of the availability of deposited funds, the nature and amount of and collateral for certain loans, and numerous other areas. The Bank is subject to significant regulation and restrictions by federal and state laws and regulatory agency regulations, policies and practices. The regulatory agencies have adopted guidelines to assist in identifying and addressing potential safety and soundness concerns before an institution's capital becomes impaired. The guidelines establish operational and managerial standards generally relating to: (1) internal controls, information systems, and internal audit systems; (2) loan documentation; (3) credit underwriting; (4) interest-rate exposure; (5) asset growth and asset quality; and (6) compensation, fees, and benefits. Further, the regulatory agencies have adopted safety and soundness guidelines for asset quality and for evaluating and monitoring earnings to ensure that earnings are sufficient for the maintenance of adequate capital and reserves. If, as a result of an examination, either the CDBO or the FDIC should determine that the financial condition, capital resources, asset quality, earnings prospects, management, liquidity, or other aspects of the Bank's operations are unsatisfactory or that the Bank or its management is violating or has violated any law or regulation, various remedies are available to the CDBO and the FDIC. These remedies include, but are not limited to, the power to (i) require affirmative action to correct any conditions resulting from any violation or unsafe and unsound practice; (ii) direct an increase in capital and the maintenance of higher specific minimum capital ratios, which may preclude the Bank from being deemed well capitalized and restrict its ability to accept certain brokered deposits; (iii) restrict the Bank's growth geographically, by products and services, or by mergers and acquisitions, including bidding in FDIC receiverships for failed banks; (iv) enter into informal nonpublic or formal public memoranda of understanding or written agreements and consent orders with the Bank to take corrective action; (v) issue an administrative cease and desist order that can be judicially enforced; (vi) enjoin unsafe or unsound practices; (vii) assess civil monetary penalties; and (viii) require prior approval of senior executive officers and director changes or remove officers and directors. Ultimately the FDIC could terminate the Bank's FDIC insurance and the CBDO could revoke the Bank's charter or take possession and close and liquidate the Bank.

Pursuant to the Federal Deposit Insurance Act ("FDI Act") and the California Financial Code, California state chartered commercial banks may generally engage in any activity permissible for national banks. Therefore, the Bank may form subsidiaries to engage in the many so-called "closely related to banking" or "nonbanking" activities commonly conducted by national banks in operating subsidiaries or in subsidiaries of bank holding companies. Further, California banks may conduct certain "financial" activities permitted under the Gramm-Leach-Bliley Act of 1999 in a "financial subsidiary" to the same extent as may a national bank, provided the bank is and remains "well-capitalized," "well-managed" and in satisfactory compliance with the Community Reinvestment Act (the "CRA"). Generally, a financial subsidiary is permitted to engage in activities that are

"financial in nature" or incidental thereto, even though they are not permissible for a national bank to conduct directly within the bank. The definition of "financial in nature" includes, among other items, underwriting, dealing in or making a market in securities, including, for example, distributing shares of mutual funds. The Bank presently has no non-banking or financial subsidiaries other than PB Consulting.

From time to time, federal and state legislation is enacted and implemented by regulations which may have the effect of materially increasing the cost of doing business, limiting or expanding permissible activities, or affecting the competitive balance between banks and other financial services providers. Changes in federal or state banking laws or the regulations, policies or guidance of the federal or state banking agencies could have an adverse cost or competitive impact on the Bank's operations. We cannot predict whether or when potential legislation or new regulations will be enacted, and if enacted, the effect that new legislation or any implemented regulations and supervisory policies would have on our financial condition and results of operations. Such developments may further alter the structure, regulation, and competitive relationship among financial institutions, and may subject us to increased regulation, disclosure, and reporting requirements. Moreover, the bank regulatory agencies continue to be aggressive in responding to concerns and trends identified in examinations, and this has resulted in the increased issuance of enforcement actions to financial institutions requiring action to address credit quality, capital adequacy, liquidity and risk management, as well as other safety and soundness and compliance concerns. In addition, the outcome of any investigations initiated by federal or state authorities or the outcome of litigation may result in additional regulation, necessary changes in our operations and increased compliance costs.

Legislative and Regulatory Developments

The Dodd-Frank Act

The implementation and impact of legislation and regulations enacted since 2008 in response to the U.S. economic downturn and financial industry instability continued in 2017 as modest recovery has returned to many institutions in the banking sector. Many institutions have repaid and repurchased U.S. Treasury investments under the Troubled Asset Relief Program and the federal banking agencies continue to implement the remaining requirements in the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank") as well as promulgating other regulations and guidelines intended to assure the financial strength and safety and soundness of banks and the stability of the U.S. banking system. Certain provisions of the Dodd-Frank are effective and have been fully implemented, including the revisions in the deposit insurance assessment base for FDIC insurance and the permanent increase in coverage to $250,000; the permissibility of paying interest on business checking accounts; the removal of barriers to interstate branching and required disclosure and shareholder advisory votes on executive compensation. Implementation in 2014 of additional Dodd-Frank regulatory provisions included aspects of (i) the final new capital rules, and (ii) a final rule to implement the so called "Volcker Rule" restrictions on certain proprietary trading and investment activities. Legislation (the *Economic Growth, Regulatory Relief, and Consumer Protection Act*, S.2155, 115 Cong., 2 sess.) has been introduced in the U.S. Senate that would, among other things, eliminate the applicability or reduce the requirements of several provisions of Dodd-Frank to banks of our size. Unless and until any such or similar legislation is enacted, we cannot determine its effects on the Bank.

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

In the exercise of their supervisory and examination authority, the regulatory agencies have emphasized corporate governance, stress testing, enterprise risk management and other Board responsibilities; anti-money laundering compliance and enhanced high risk customer due diligence; vendor management; cyber security and fair lending and other consumer compliance obligations.

Capital Adequacy Requirements

Banks are subject to various regulatory capital requirements administered by state and federal banking agencies. New capital rules described below were effective on January 1, 2014, and are being phased in over various periods. The basic capital rule changes were fully effective on January 1, 2015, but many elements are being phased in over multiple future years. Capital adequacy guidelines and prompt corrective action regulations (See "Prompt Corrective Action Regulations" below) involve quantitative measures of assets, liabilities, and certain off-balance sheet items calculated under regulatory accounting practices. Capital amounts and classifications are also subject to qualitative judgments by regulators about components, risk weighting, and other factors. The risk-based capital guidelines for bank holding companies and banks require capital ratios that vary based on the perceived degree of risk associated with a banking organization's operations for both transactions reported on the balance sheet as assets, such as loans, and those recorded as off-balance sheet items, such as commitments, letters of credit and recourse arrangements. The risk-based capital ratio is determined by classifying assets and certain off-balance sheet financial instruments into weighted categories, with higher levels of capital being required for those categories perceived as representing greater risks and dividing its qualifying capital by its total risk-adjusted assets and off-balance sheet items. Banks engaged in significant trading activity may also be subject to the market risk capital guidelines and be required to incorporate additional market and interest rate risk components into their risk-based capital standards. To the extent that the new rules are not fully phased in, the prior capital rules continue to apply.

Under the risk-based capital guidelines in place prior to the effectiveness of the new capital rules, there were three fundamental capital ratios: a total risk-based capital ratio, a Tier 1 risk-based capital ratio and a Tier 1 leverage ratio. To be deemed "well capitalized" a bank must have a total risk-based capital ratio, a Tier 1 risk-based capital ratio and a Tier 1 leverage ratio of at least ten percent, six percent and five percent, respectively.

Prompt Corrective Action Regulations

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

The prompt corrective action standards were changed when the new capital rule ratios became effective. Under the new standards, in order to be considered well capitalized, the Bank is required to meet the new Common Equity Tier 1 ratio of 6.5%, an increased Tier 1 ratio of 8% (increased from 6%), a total capital ratio of 10% (unchanged) and a leverage ratio of 5% (unchanged).

The regulatory capital guidelines as well as the Bank's actual capitalization as of December 31, 2017, are as follows:

Tier 1 Leverage Ratio	
Preferred Bank	9.52%
Minimum requirement for "Well Capitalized" institution	5.00%
Common Equity Tier 1 Risk-Based Capital Ratio	
Preferred Bank	10.07%
Minimum requirement for "Well Capitalized" institution	6.50%
Tier 1 Risk-Based Capital Ratio	
Preferred Bank	10.07%
Minimum requirement for "Well Capitalized" institution	8.00%
Total Risk-Based Capital Ratio	
Preferred Bank	13.83%
Minimum requirement for "Well Capitalized" institution	10.00%

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

Capital Rules and Minimum Capital Returns

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

The following are among the new requirements that were phased in beginning January 1, 2015:

- An increase in the minimum Tier 1 capital ratio from 4.00% to 6.00% of risk-weighted assets;
- A new category and a required 4.50% of risk-weighted assets ratio is established for "Common Equity Tier 1" as a subset of Tier 1 capital limited to common equity;
- A minimum non-risk-based leverage ratio is set at 4.00%, eliminating a 3.00% exception for higher rated banks;
- Changes in the permitted composition of Tier 1 capital to exclude trust preferred securities, mortgage servicing rights and certain deferred tax assets and include unrealized gains and losses on available-for-sale debt and equity securities;
- The risk-weights of certain assets for purposes of calculating the risk-based capital ratios are changed for high volatility commercial real estate acquisition, development and construction loans, certain past due non-residential mortgage loans and certain mortgage-backed and other securities exposures;
- An additional "countercyclical capital buffer" is required for larger and more complex institutions; and
- A new additional capital conservation buffer of 2.5% of risk weighted assets over each of the required capital ratios will be phased in from 2016 to 2019 and must be met to avoid limitations on the ability of the Bank to pay dividends, repurchase shares or pay discretionary bonuses.

Including the capital conservation buffer of 2.5%, the new final capital rule would result in the following minimum ratios: (i) a Tier 1 capital ratio of 8.5%, (ii) a Common Equity Tier 1 capital ratio of 7.0%, and (iii) a

total capital ratio of 10.5%. The new capital conservation buffer requirement began to be phased in beginning in January 2016 at 0.625% of risk-weighted assets and increases each year until fully implemented in January 2019. The required capital conservation buffer for 2017 is 1.25%. At December 31, 2017 and 2016, the Bank's capital conservation buffer was 4.07% and 3.83%, respectively.

While the new final capital rule sets higher regulatory capital standards for the Bank, bank regulators may also continue their past policies of expecting banks to maintain additional capital beyond the new minimum requirements. The implementation of the new capital rules or more stringent requirements to maintain higher levels of capital beyond the aforementioned or to maintain higher levels of liquid assets could adversely impact the Bank's net income and return on equity, restrict the ability to pay dividends or executive bonuses and require the raising of additional capital.

Management believes that, as of December 31, 2017, the Bank would meet all applicable capital requirements under the new capital rules on a fully phased-in basis if such requirements were currently in effect (see "Legislative and Regulatory Developments" described above).

Final Volcker Rule

In December 2013, the federal bank regulatory agencies adopted final rules that implement a part of Dodd-Frank commonly referred to as the "Volcker Rule." Under these rules and subject to certain exceptions, banking entities, including the Bank, will be restricted from engaging in activities that are considered proprietary trading and from sponsoring or investing in certain entities, including hedge or private equity funds that are considered "covered funds." These rules became effective on April 1, 2014, although certain provisions are subject to delayed effectiveness under rules promulgated by the Federal Reserve. The Bank held no investment positions at December 31, 2017 which were subject to the final "Volcker Rule." Therefore, while these new rules may require us to conduct certain internal analysis and reporting, we believe that they will not require any material changes in our operations or business. The applicability of the Volker Rule to banks of our size may be eliminated if currently pending legislation is enacted into law (See, Legislation and Regulatory Developments—The Dodd-Frank Act").

Cybersecurity

The FRB and other bank regulatory agencies have adopted guidelines that address standards for developing and implementing administrative, technical and physical safeguards to protect the security, confidentiality, and integrity of customer information. These guidelines require each financial institution to create, implement, and maintain a comprehensive written information security program to control the identified risks, commensurate with the sensitivity of the information as well as the complexity and scope of the institution's activities. We have adopted a customer information security program to comply with these requirements.

Federal regulators have issued two related statements regarding cybersecurity. One statement indicates that financial institutions should design multiple layers of security controls to establish lines of defense and to ensure that their risk management processes also address the risk posed by compromised customer credentials, including security measures to reliably authenticate customers accessing Internet-based services of the financial institution. The other statement indicates that a financial institution's management is expected to maintain sufficient business continuity planning processes to ensure the rapid recovery, resumption and maintenance of the institution's operations after a cyber-attack involving destructive malware. A financial institution is also expected to develop appropriate processes to enable recovery of data and business operations and address rebuilding network capabilities and restoring data if the institution or its critical service providers fall victim to this type of cyber-attack. If we fail to observe the regulatory guidance, we could be subject to various regulatory sanctions, including financial penalties. For a further discussion of risks related to cybersecurity, see "Item 1A. Risk Factors" included in this Form 10-K.

Dividends and Other Transfers of Funds

The Bank is subject to various statutory and regulatory restrictions on its ability to pay dividends. In addition, the banking agencies have the authority to prohibit the Bank from paying dividends, depending upon the Bank's financial condition, if such payment would be deemed to constitute an unsafe or unsound practice.

The power of the Bank to declare cash dividends is subject to California law, which limits the amount available for cash dividends to the lesser of the Bank's retained earnings or net income for its last three fiscal years (less any distributions made to shareholders during that period). This restriction may only be exceeded with advance approval of the CDBO, which may approve declaration of an amount not exceeding the greatest of retained earnings of the Bank, the Bank's prior fiscal year net income, or the Bank's current fiscal year net income.

Deposit Insurance

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

Our FDIC insurance expense totaled $2.4 million for 2017. We are generally unable to control the amount of premiums that we are required to pay for FDIC insurance, which can be affected by the cost of bank failures to the FDIC among other factors. The FDIC will, at least semi-annually, update its income and loss projections for the DIF and, if necessary, propose rules to further increase assessment rates. Any future increases in FDIC insurance premiums may have a material and adverse effect on our earnings and could have a material adverse effect on the value of, or market for, our common stock.

Federal Home Loan Bank System

We are a member of the FHLB. Among other benefits, each of the 12 Federal Home Loan Banks serves as a reserve or central bank for its members within its assigned region. The FHLB makes available loans or advances to its members in compliance with the policies and procedures established by the Board of Directors of the individual FHLB. As an FHLB member, we are required to own a certain amount of restricted capital stock and maintain a certain amount of cash reserves in the FHLB. As of December 31, 2017, the Bank had $6.4 million of outstanding FHLB advances. At December 31, 2017, the Bank was in compliance with the FHLB's stock ownership and cash reserve requirements. As of December 31, 2017 and 2016, our investment in FHLB capital stock totaled $11.1 million and $9.3 million, respectively.

Securities Registration

The Bank's common stock is publicly held and listed on the NASDAQ Global Select Market ("NASDAQ"), and the Bank is subject to the periodic reporting information, proxy solicitation, insider trading, corporate governance and other requirements and restrictions of the Exchange Act as adopted by the FDIC and the regulations of the Securities and Exchange Commission (the "SEC") promulgated thereunder to the extent such regulations have been adopted by the FDIC as well as listing requirements of NASDAQ.

The Sarbanes-Oxley Act

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

Loans-to-One Borrower Limitations

With certain limited exceptions, the maximum amount of obligations, secured or unsecured, that any borrower (including certain related entities) may owe to a California state bank at any one time may not exceed 25% of the sum of the shareholders' equity, allowance for loan and lease losses, capital notes and debentures of the bank. Unsecured obligations may not exceed 15% of the sum of the shareholders' equity, allowance for loan and lease losses, capital notes and debentures of the bank. The Bank has established internal loan limits which are lower than the legal lending limits for a California state chartered bank. At December 31, 2017, the Bank's largest single lending relationship had a combined outstanding balance of $89.6 million, secured predominantly by commercial real estate properties in the Bank's primary lending area, and which is performing in accordance with the terms of the Bank's loans.

Extensions of Credit to Insiders and Transactions with Affiliates

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

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

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

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

Operations and Consumer Compliance

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

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

Dodd-Frank provided for the creation of the Consumer Finance Protection Bureau ("CFPB") as an independent entity within the Federal Reserve with broad rulemaking, supervisory and enforcement authority over consumer financial products and services, including deposit products, residential mortgages, home-equity loans and credit cards. The CFPB's functions include investigating consumer complaints, conducting market research, rulemaking, supervising and examining bank consumer transactions, and enforcing rules related to consumer financial products and services. CFPB regulations and guidance apply to all financial institutions and banks with $10 billion or more in assets. Accordingly, these financial institutions and banks are subject to examination by the CFPB. Banks with less than $10 billion in assets, including the Bank, will continue to be examined for compliance by their primary federal banking agency.

In 2014, the CFPB adopted revisions to Regulation Z, which implement the Truth in Lending Act, pursuant to Dodd-Frank, and apply to all consumer mortgages (except home equity lines of credit, timeshare plans, reverse mortgages, or temporary loans). The revisions mandate specific underwriting criteria for home loans in order for creditors to make a reasonable, good faith determination of a consumer's ability to repay and establish certain protections from liability under this requirement for "qualified mortgages" meeting certain standards. In particular, it will prevent banks from making "no doc" and "low doc" home loans, as the rules require that banks determine a consumer's ability to pay based in part on verified and documented information. Because we do not originate "no doc" or "low doc" loans, we do not believe this regulation will have a significant impact on our operations. However, because a substantial portion of the mortgage loans originated by the Bank do not meet the definition of a "qualified mortgage" under final regulations adopted by the CFPB, the Bank may be subject to additional disclosure obligations and extended time periods for the assertion of defenses by the borrower against enforcement in connection with such mortgage loans.

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

standards. State regulation of financial products and potential enforcement actions could also adversely affect the Bank's business, financial condition or results of operations.

Employees

As of December 31, 2017, the Bank had a total of 238 full-time equivalent employees. None of the employees are represented by a union or collective bargaining group. Management believes that employee relations are satisfactory.

Executive Officers of the Bank

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

Name	Age[(1)]	Position with Bank
Li Yu	77	Chairman of the Board and Chief Executive Officer
Wellington Chen	58	President and Chief Operating Officer
Edward J. Czajka	53	Executive Vice President and Chief Financial Officer
Nick Pi	57	Executive Vice President and Chief Credit Officer

(1) As of March 1, 2018.

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

Wellington Chen has been the President and Chief Operating Officer since August 2012. He joined the Bank in June 2011 as Chief Operating Officer. Prior to joining the Bank, Mr. Chen served over seven years as Executive Vice President and Director of Corporate Banking for EastWest Bank in Pasadena, California where he oversaw a significant portion of the loan and deposit production activities of the bank. Prior to joining East West Bank in December 2003, Mr. Chen was Senior Executive Vice President of Far East National Bank ("Far East") heading up their Commercial Bank Group, Consumer Banking Group, and Branch Channel. He also served on the Board of Directors of Far East. Mr. Chen's career with Far East began in 1986 and included a variety of branch and credit management positions. Prior to that, Mr. Chen spent three years with Security Pacific National Bank where he completed the management training program and served as an asset based lending auditor. Mr. Chen received his Bachelors of Science degree in Business Finance from University of Southern California and is a graduate of Pacific Coast Banking School at University of Washington.

Edward J. Czajka has been Senior Vice President and Chief Financial Officer since 2006 and was promoted to Executive Vice President in 2008. Before joining the Bank, Mr. Czajka was Chief Financial Officer of Presidio Bank, a San Francisco-based bank that was then in organization. Prior to this, Mr. Czajka was Executive Vice President and Chief Financial Officer of the former North Valley Bancorp, a publicly-traded multi-bank holding company located in Redding, California (now Tri Counties Bank). From 1994 through 2000, Mr. Czajka held the position of Vice President, Corporate Controller for the former Pacific Capital Bancorp in Santa Barbara, California (now Union Bank). Mr. Czajka graduated summa cum laude from Capella University with a BS in Business Administration and is a graduate of the Bank Administration Institute Graduate School of Banking at Vanderbilt University. He currently serves on the Board as Treasurer for Shane's Inspiration, a non-profit located in Los Angeles.

Nick Pi has been with the Bank since 2003 and has been our Executive Vice President Chief Credit Officer since June 2015. Before joining us, Mr. Pi was the Senior Vice President and Commercial Real Estate Lending Team Leader of Chinatrust Bank (U.S.A.) from 2000 to 2003. Prior to this, he held various corporate titles from Assistant Vice President to Senior Vice President at Chinatrust Bank (U.S.A.), mainly in the branch operation and lending fields from 1995 to 2000. His lending and credit experience also includes Grand Pacific Financing Corporation from 1989 to 1995, an affiliate of China Trust Group. Mr. Pi received a Bachelor of Arts degree in Business from National Taiwan University, Taiwan and a MBA degree from Emporia State University.

Available Information

The Bank also maintains an Internet website at *www.preferredbank.com.* The Bank makes its website content available for information purposes only. It should not be relied upon for investment purposes. None of the information on, or hyperlinked, from our website is incorporated into this Report.

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

ITEM 1A. RISK FACTORS

Risk Factors That May Affect Future Results

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

Risks Related to Our Business

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

A significant source of risk arises from the possibility that we could sustain losses because borrowers, guarantors and related parties may fail to perform in accordance with the terms of their loans. The underwriting and credit monitoring policies and procedures that we have adopted to address this risk may not prevent losses that could have an adverse effect on our business, financial condition, results of operations and cash flows. Losses may arise for a wide variety of reasons, many of which are beyond our ability to predict, influence or control. Some of these reasons could include an economic downturn in the State of California or in the Tri-State area, a reversal of the recent gains made in the California and New York real estate markets, changes in the interest rate environment, adverse economic conditions in Asia and natural disasters.

Like all financial institutions, we maintain an allowance for loan and lease losses to provide for loan and lease defaults and non-performance. Our allowance for loan and lease losses may not be adequate to cover actual loan and lease losses, and future provisions for loan and lease losses could materially and adversely affect our business, financial condition, results of operations and cash flows. Our allowance for loan and lease losses

reflects our best estimate of the losses incurred in the existing loan and lease portfolio at the relevant balance sheet date and is based on management's evaluation of the collectability of the loan and lease portfolio, which evaluation is based on historical loss experience and other significant factors. For the year ended December 31, 2017, we recorded a provision for loan and lease losses and net loan charge-offs of $5.5 million and $2.1 million, respectively, compared to a provision of $6.4 million and net loan charge-offs of $2.6 million for the year ended December 31, 2016.

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

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

At December 31, 2017, our construction loans were $283.8 million, or 9.7% of our total loans held, and the average loan size of our construction loans was $3.6 million. The risks inherent in construction lending include, among other things, the possibility that contractors may fail to complete, or fail to complete on a timely basis, construction of the relevant properties; substantial cost overruns in excess of original estimates and financing; market deterioration during construction; and a lack of permanent take-out financing. Loans secured by these properties also involve additional risk because the properties have no operating histories. In these loans, funds are advanced upon the security of the project under construction, which is of uncertain value prior to completion of construction, and the estimated operating cash flow to be generated, by the completed project. The borrowers' ability to repay their obligations to us and the value of our security interest in the collateral will be materially adversely affected if the projects do not generate sufficient cash flow by being either sold or leased.

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

We will be subject to more stringent capital requirements. Pursuant to Dodd-Frank and the principles of the international Basel III standards, the federal banking agencies have adopted a new set of rules on minimum leverage and risk-based capital that will apply to both insured banks and their holding companies. These regulations were issued in July 2013, and are being phased in, for the Bank, over a period of five years, which began in 2015. Details of the new rules are discussed in the *Prompt Corrective Action Regulations* section earlier in this Annual Report.

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

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

Future regulatory requirements could adversely affect us.

Current and future legal and regulatory requirements, restrictions and regulations, including those imposed under Dodd-Frank, may adversely impact our profitability and may have a material and adverse effect on our business, financial condition, and results of operations, may require us to invest significant management attention and resources to evaluate and make any changes required by the legislation and accompanying rules and may make it more difficult for us to attract and retain qualified executive officers and employees. The implementation of certain final Dodd-Frank rules is delayed or phased over several years; therefore, as yet we cannot definitively assess what may be the short or longer term specific or aggregate effect of the full implementation of Dodd-Frank on us. In addition, in an Executive Order signed on February 3, 2017, the President of the United States directed the Secretary of the Treasury, in consultation with federal financial regulators, to assess the rules promulgated under Dodd-Frank since 2010 with a view to producing a plan to revise them as necessary. Finally, legislation has been introduced in the U.S. Senate that, if enacted, would eliminate the applicability of certain provisions of Dodd-Frank to banks of our size. We cannot predict the specific impact and long-term effects the Dodd-Frank Act, the regulations promulgated thereunder, or any revisions thereto will have on our financial performance, the markets in which we operate and the financial industry more generally.

Difficult economic and market conditions have adversely affected, and in the future could adversely affect, our industry and us.

Our operations and performance depend significantly on global, national and local economic conditions. During 2008-2010, dramatic declines in the housing market, with decreasing home prices and increasing delinquencies and foreclosures, negatively impacted the credit performance of mortgage and construction loans and resulted in significant write-downs of assets by many financial institutions. Although the national and local economies have improved dramatically, geopolitical, regulatory and other unforeseen events continue to have an impact on the economy and our markets. In particular, we may face the following risks in connection with these events:

- The process we use to estimate losses inherent in our credit exposure requires difficult, subjective and complex judgments, including forecasts of economic conditions and how these economic conditions might impair the ability of our borrowers to repay their loans. The level of uncertainty concerning economic conditions may adversely affect the accuracy of our estimates which may, in turn, impact the reliability of the process.
- Our banking operations are concentrated primarily in Southern California. Adverse economic conditions in this region in particular could impair borrowers' ability to service their loans, decrease the level and duration of deposits by customers, and erode the value of loan collateral. This could increase the amount of our non-performing assets and have an adverse effect on our efforts to collect our non-performing loans or otherwise liquidate our non-performing assets (including other real estate owned) on terms favorable to us, if at all, and could also cause a decline in demand for our products and services, or a lack of growth or a decrease in deposits, any of which may cause us to incur losses, adversely affect our capital, and hurt our business.

These and other global, national and local economic events and conditions could have a material adverse impact on demand for our products and services, our results of operations and our financial condition.

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

Our success depends heavily on the abilities and continued service of our executive officers, especially Li Yu, Chairman and Chief Executive Officer, and our President and Chief Operating Officer, Wellington Chen. Mr. Yu, who founded the Bank, and Mr. Chen, are both integral to implementing our business plan. We currently do not have an employment agreement or non-competition agreement with Messrs. Yu or Chen nor our other executives. Accordingly, members of our senior management team are not contractually prohibited from leaving

or joining one of our competitors. If we lose the services of any of our executive officers, especially Mr. Yu or Mr. Chen, our business, financial condition, results of operations and cash flows may be adversely affected. Furthermore, attracting suitable replacements may be difficult and may require significant management time and resources.

We also rely to a significant degree on the abilities and continued service of our private banking, loan origination, underwriting, administrative, marketing and technical personnel. Competition for qualified employees and personnel in the banking industry is intense and there are a limited number of qualified persons with knowledge of, and experience in, the California community banking industry. The process of recruiting personnel with the combination of skills and attributes required to carry out our strategies is often lengthy. If we fail to attract and retain qualified management personnel and the necessary deposit generation, loan origination, underwriting, administrative, finance, marketing and technical personnel, our business, financial condition, results of operations and cash flows may be materially adversely affected.

Our operations are concentrated geographically in California, particularly Southern California, and poor economic conditions in this area could adversely affect the demand for our products and our credit quality.

Our operations are located primarily in Southern California. Local economic conditions in Southern California can have a significant impact on the demand for our products and services, our loans and wealth management business, the ability of borrowers to pay interest on and repay the principal of these loans, and the value of the collateral securing these loans. Adverse changes in economic conditions in Southern California may negatively affect our business, results of operations or financial condition. Our loan portfolio, in particular, is concentrated in California in general. As of December 31, 2017, approximately 94% of the total dollar amount of our loans outstanding were secured by real estate located in California and the Tri-State Area, and approximately 60% are secured by real estate in Southern California. Declines in values in the California real estate market could have an adverse impact on our borrowers and on the value of the collateral securing many of our loans, which in turn could adversely affect our currently performing loans, leading to future delinquencies or defaults and increases in our provision for loan losses.

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

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

Recent mortgage regulations may adversely impact our business.

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

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

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

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

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

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

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

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

We also face competition from out-of-state financial intermediaries that have opened loan production offices or that solicit deposits in our market areas. In addition, we compete with other alternative lenders,

including finance companies, private equity and hedge funds, real estate investment funds, business development companies, and "marketplace" and peer-to-peer lenders. If we are unable to attract and retain banking customers, we may be unable to continue our loan growth and level of deposits, and our business, financial condition, results of operations and cash flows may be materially adversely affected.

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

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

A portion of the Bank's loan portfolio is secured by real estate and thus the Bank has a higher degree of risk from a downturn in real estate markets.

A decline in real estate markets could hurt the Bank's business because many of the Bank's loans are secured by real estate. Real estate values and real estate markets are generally affected by changes in national, regional or local economic conditions, fluctuations in interest rates and the availability of loans to potential purchasers, changes in tax laws and other governmental statutes, regulations and policies and acts of nature and national disasters, such as earthquakes which are particular to California. A significant portion of the Bank's real estate collateral is located in California. If real estate values decline, the value of real estate collateral securing the Bank's loans could be significantly reduced. The Bank's ability to recover on defaulted loans by foreclosing and selling the real estate collateral would then be diminished and the Bank would be more likely to suffer losses on defaulted loans. Furthermore, CRE and multifamily loans typically involve large balances to single borrowers or groups of related borrowers. Since payments on these loans are often dependent on the successful operation or management of the properties, as well as the business and financial condition of the borrower, repayment of such loans may be subject to adverse conditions in the real estate market, adverse economic conditions or changes in applicable government regulations. Borrowers' inability to repay such loans may have an adverse effect on the Bank's business.

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

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

Adverse economic conditions in Asia could impact our business adversely.

We believe that our Chinese-American customers maintain significant ties to many Asian countries and, therefore, could be affected by economic and other conditions in those countries. We cannot predict the behavior of the Asian economies. U.S. economic policies, the economic policies of countries in Asia, domestic unrest and/or military tensions, crises in leadership succession, currency devaluations, and an unfavorable global economic condition may among other things adversely impact the Asian economies. We generally do not loan to customers or take collateral located outside of Southern California. However, if Asian economic conditions should

deteriorate, we could experience an outflow of deposits by our Chinese-American customers. In addition, adverse economic conditions could prevent or delay these customers from meeting their obligations to us. This may adversely impact the recoverability of investments with or loans made to these customers. Adverse economic conditions may also negatively impact asset values and the profitability and liquidity of companies operating in Asia, which will also impact the Bank's liquidity.

At December 31, 2017, approximately $21.3 million, or 0.7%, of our loan portfolio consisted of loans made to finance international trade activities. Changes in monetary policy, including changes in interest rates, governmental regulation of international trade activities, currency valuation, price competition, competition from other financial institutions and general economic and political conditions could negatively impact the amount of goods imported to and exported from the United States, the ability of borrowers to repay loans made by us, and the number and extent of importers' and exporters' need for our trade finance products and services. It is possible that if the U.S. dollar weakens against other foreign currencies, the cost of imported goods will increase, which could have an adverse impact on some of our customers who import goods for resale in the United States. Such factors could have a material adverse effect on our business, financial condition, results of operations and cash flows.

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

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

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

Our average jumbo deposit customer has been a customer of the Bank for over six years which indicates that these are long-term customers who consistently renew their CDs with the Bank. At December 31, 2017, we held $621.6 million of Jumbo CDs, representing 19.1% of total deposits. These deposits are considered by the banking industry to be volatile and could be subject to withdrawal. Withdrawal of a material amount of such deposits would adversely impact our liquidity, profitability, business, financial condition, results of operations and cash flows.

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

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

We may be adversely affected by disruptions to our network and computer systems or to those of our service providers as a result of denial-of-service or other cyber attacks.

We may experience disruptions or failures in our computer systems and network infrastructure or in those of our third-party service providers as a result of denial-of-service or other cyber attacks. In recent years, federal and state regulators, including the FDIC, have made statements concerning cybersecurity risk management, preparedness and resiliency for financial institutions such as us. These statements range from issues with respect to client account protections to business continuity, and represent the regulators' expectations for financial institutions to have more robust cybersecurity risk management, preparedness and resiliency programs for themselves and their third-party service providers. A financial institution is also expected to develop processes to enable recovery of data and business operations and address rebuilding network capabilities and restoring data if the institution, or its critical third-party service providers, fall victim to this type of cyber attack. We have developed and continue to invest in, systems and processes that are designed to detect, prevent and minimize the impact of security breaches and cyber attacks. Due to the increasing sophistication of such attacks, we may not be able to prevent denial-of-service or other cyber attacks that could compromise our normal business operations or the normal business operations of our clients, or result in the unauthorized use of clients' confidential and proprietary information. The occurrence of any failure, interruption or security breach of network and computer systems resulting from denial-of-service or other cyber attacks could damage our reputation, result in a loss of client business, subject us to additional regulatory scrutiny, or expose us to civil litigation and possible financial liability, any of which could adversely affect our business, results of operations or financial condition.

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

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

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

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

We are subject to significant governmental supervision and regulation under federal and state laws, as well as supervision and examination by the FDIC, the CDBO, and the CFPB. Because our business is highly regulated, the laws, rules and regulations and supervisory guidance and policies applicable to us are subject to regular modification and change, which may have the effect of increasing or decreasing the cost of doing business, modifying permissible activities or enhancing the competitive position of other financial institutions. These laws are primarily intended for the protection of consumers, depositors and not for the protection of shareholders of bank holding companies or banks. Perennially, various laws, rules and regulations are proposed which, if adopted, could impact our operations by making compliance much more difficult or expensive, restricting our ability to originate or sell loans or further restricting the amount of interest or other charges or fees earned on loans or other products. We cannot assure you that laws, rules or regulations will not be adopted in the future that could make compliance much more difficult or expensive, restrict our ability to originate loans,

further limit or restrict the amount of commissions, interest or other charges earned on loans originated by us or otherwise adversely affect our business, financial condition, results of operations or cash flows, which could result in a decrease in the value of your shares.

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

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

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

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

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

Negative publicity could damage our reputation.

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

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

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

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

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

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

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

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

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

Changes in accounting standards or inaccurate estimates or assumptions in applying accounting policies could materially impact the Bank's financial statements.

From time to time, the FASB or the SEC may change the financial accounting and reporting standards that govern the preparation of the Bank's financial statements. In addition, the FASB, SEC, banking regulators and the Bank's independent registered public accounting firm may also amend or even reverse their previous interpretations or positions on how various standards should be applied. These changes may be difficult to predict and could impact how we prepare and report the Bank's financial statements. In some cases, we could be required to apply a new or revised standard retroactively, resulting in the Bank revising and republishing prior-period financial statements.

The impact of recent U.S. tax reform is uncertain.

The Tax Cuts and Jobs Act (the "Tax Reform Act") was enacted on December 22, 2017 and provides for significant changes, including to the taxation of business entities, allowable business expense deductions, limitations to mortgage interest, home equity interest and state and property tax deductions. Most changes are effective starting in 2018, and the overall impact of these changes on the Bank is uncertain due to, among other things, future guidance that may be issued by tax authorities and changes in interpretations and assumptions by the Bank. The short- and long-term impact of the Tax Reform Act on the economic conditions in the markets in which we operate, and in the United States as a whole, is also uncertain, and any unfavorable change in the general business environment in which we operate could adversely affect our business, results of operation or financial condition.

Risks Related to Our Common Stock

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

The stock market is subject to fluctuations in the share prices and trading volumes that affect the market prices of the shares of many companies. These broad market fluctuations could adversely affect the market price of our common stock. Among the factors that could affect our stock price are:

- Actual or anticipated quarterly fluctuations in our operating results and financial condition;
- Changes in revenue or earnings estimates or publication of research reports and recommendations by financial analysts;
- Failure to meet analysts' revenue or earnings estimates;
- Speculation in the press or investment community;
- Strategic actions by us or our competitors, such as acquisitions or restructurings;
- Actions by institutional shareholders;
- Fluctuations in the stock price and operating results of our competitors;

- General market conditions and, in particular, developments related to market conditions for the financial services industry;
- Proposed or adopted regulatory changes or developments;
- Anticipated or pending investigations, proceedings or litigation that involve or affect us;
- Domestic and international economic factors unrelated to our performance; or
- Other factors identified above in "Forward-Looking Statements."

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

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

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

The ability of the Bank to pay dividends to its shareholders is limited by applicable federal and California law and regulations. See "Business—Regulation and Supervision."

We may be subject to risks related to acquisitions.

Among the risks associated with expansion via acquisition are incorrectly assessing the quality of an acquired bank's assets, greater than anticipated costs associated with integrating acquired banks, resistance from customers or employees of acquired banks, and inability to generate a profit using assets acquired in the transaction. Additionally, new region-specific risks are introduced when a bank is acquired outside the Bank's current area of business. If we were to issue capital stock in connection with future transactions, the transactions and related stock issuances may have a dilutive effect on earnings per share and share ownership.

Failure to manage our growth may adversely affect our performance.

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

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

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

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

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

ITEM 1B. UNRESOLVED STAFF COMMENTS

N/A

ITEM 2. PROPERTIES

Our headquarters and main branch office are located at 601 S. Figueroa Street, 29th Floor, Los Angeles, California, 90017. This lease expires in August of 2020. In addition to this, we also maintain a leased office property in El Monte, California which houses a number of administrative departments.

At December 31, 2017, we maintained thirteen full-service branch offices in: Flushing, New York, and Alhambra, Arcadia, Century City, City of Industry, Diamond Bar, Los Angeles, Pico Rivera, San Francisco (two branches), Tarzana, Torrance, and Irvine, California all of which we lease, except the Irvine branch which we own.. We believe that no single lease is material to our operations. Leases for branch offices are generally 3 to 10 years in length and generally provide renewal terms of 3 to 5 additional years.

We believe that our existing facilities are adequate for our present purposes. We believe that, if necessary, we could secure alternative facilities on similar terms without adversely affecting our operations. Total lease expense was $3.0 million for the year ended December 31, 2017 and $2.9 million for the year ended December 31, 2016.

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

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

Location	Address	Current Lease Term Expiration Date	Square Footage
Los Angeles County			
Alhambra	325 E. Valley Blvd.	05/31/19	6,000
Arcadia	1469 S. Baldwin Avenue	03/01/19	2,600
Century City	1801 Century Park East, Suite 100	08/31/21	4,416
City of Industry	17515-A Colima Road	03/13/25	5,610
Diamond Bar	1373 S. Diamond Bar Blvd.	11/30/23	3,440
Los Angeles (Head Office & Branch)	601 S. Figueroa Street, 29th Floor	08/31/20	22,627
Pico Rivera	7004 Rosemead Blvd.	02/10/19	2,850
Torrance	21615 Hawthorne Boulevard, Suite 100	10/31/21	4,800
Tarzana	18321 Ventura Blvd, Suite 100	12/20/24	5,915
El Monte office	9350 Flair Dr., Suite 200	07/31/22	6,900
Orange County			
Irvine (Owned Branch Premises)	890 Roosevelt Avenue	N/A	4,960
Northern California			
San Francisco	600 California Street, Suite 550	12/31/22	3,679
San Francisco	5160 Geary Boulevard	12/31/20	2,400
New York State			
Flushing	41-60 Main Street	09/31/25	10,754

ITEM 3. LEGAL PROCEEDINGS

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

ITEM 4. MINE SAFETY DISCLOSURES

Not applicable.

PART II

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

Market Information

Our common stock is listed on the NASDAQ Global Select Market under the symbol "PFBC." Our common stock closed at $66.25 on March 13, 2018 and there were 15,318,580 outstanding shares of our common stock on that date.

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

	High	Low	Cash Dividends Declared
2016			
First Quarter	$32.73	$27.00	$0.15
Second Quarter	$33.43	$27.28	$0.15
Third Quarter	$35.93	$29.58	$0.15
Fourth Quarter	$52.75	$34.35	$0.18
2017			
First Quarter	$57.55	$49.28	$0.18
Second Quarter	$55.19	$47.82	$0.20
Third Quarter	$60.35	$50.18	$0.20
Fourth Quarter	$65.95	$57.65	$0.22

Holders

As of March 13, 2018, 15,318,580 shares of the Bank's common stock were held by 163 shareholders of record.

Dividends

Dividends depend upon our earnings, financial condition, results of operations, capital requirements, available investment opportunities, regulatory restrictions, contractual restrictions and other factors that our Board of Directors may deem relevant. Accordingly, there can be no assurance that any stock or cash dividends will be declared in the future, and if any are declared, what amount they will be.

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

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

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

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

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

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

On September 25, 2017, the Bank was granted a Stock Permit (the "Stock Permit") from the California Department of Business Oversight ("DBO") authorizing it to sell, from time-to-time, up to $50 million in shares of the Bank's common stock, by means of an "at the market offering" program (the "ATM Program"). During the fourth quarter of 2017, the Bank sold 541,975 shares through the ATM Program for the net proceeds of $32.8 million.

Recent Sales of Unregistered Securities

On October 3, 2017, we entered into an Equity Distribution Agreement with FBR Capital Markets & Co., Raymond James & Associates, Inc., and Sandler O'Neill & Partners, L.P. to sell shares of the Bank's common stock, no par value per share, having an aggregate offering price of up to $50,000,000, from time to time, through an "at the market offering" program (the "ATM Program"). During the quarter ended December 31, 2017, we sold 541,975 shares of common stock by means of the ATM Program for net proceeds of $32.8 million, which we used for general corporate purposes. These transactions were exempt from registration under the Securities Act, pursuant to Section 3(a)(2) thereof because the transaction involved securities issued by a bank.

Issuer's Purchases of Equity Securities

The following table summarizes purchases made by the Bank of its common stock for each calendar month in the fourth quarter of 2017:

	Total Number of Shares Purchased	Average Price Paid Per Share
	(in thousands)	
January:		
Employee transactions[(1)]	52	$52.34
March:		
Employee transactions[(1)]	22	$51.68
Total:		
Employee transactions[(1)]	74	$52.23

(1) Includes restricted shares withheld (under the terms of grants under employee stock incentive plans) to offset tax withholding obligations that occur upon vesting and release of restricted shares. The Bank may receive shares delivered or attested to pay the exercise price and/or to satisfy tax withholding obligations by employees who exercise stock options granted under employee stock incentive plans, which are commonly referred to as stock swap exercises.

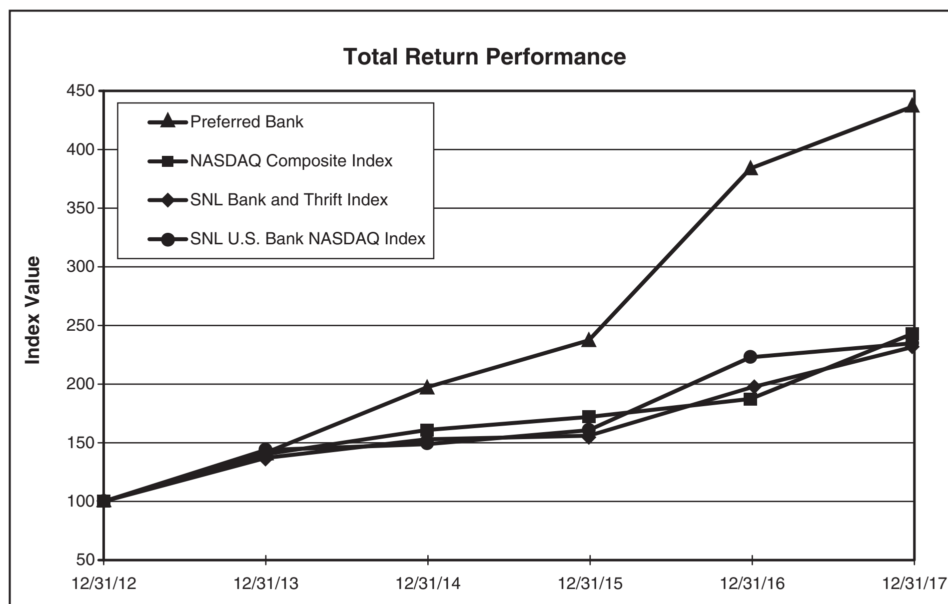
Securities Authorized for Issuance Under Equity Compensation Plans.

The following table provides information as of December 31, 2017, regarding equity compensation plans under which equity securities of the Bank were authorized for issuance.

Plan Category	Number of securities to be issued upon exercise of outstanding options (a)	Weighted average exercise price of outstanding options (b)	Number of securities available for future issuance under equity compensation plans excluding securities reflected in column (a) (c)
Equity incentive plans approved by security holders	73,300	$15.79	2,166,705
Equity incentive plans not approved by security holders	—	—	—
	73,300		2,166,705

Stock Performance Graph

The following graph shows a comparison of shareholder return on the Bank's common stock based on the market price of the common stock assuming the reinvestment of dividends, for the period beginning December 31, 2012 assuming an investment of $100 in each as of December 31, 2012. The Bank is not included in these indices. Total shareholder return for the Bank, as well as for the indices, is based on the cumulative amount of dividends for a given period (assuming dividend reinvestment) and the difference between the share price at the beginning and at the end of the period. This graph is historical only and may not be indicative of possible future performance of the common stock.



Index	*Period Ending* 12/31/12	12/31/13	12/31/14	12/31/15	12/31/16	12/31/17
Preferred Bank	100.00	141.20	197.24	237.23	383.82	436.49
NASDAQ Composite	100.00	140.12	160.78	171.97	187.22	242.71
SNL Bank and Thrift	100.00	136.92	152.85	155.94	196.86	231.49
SNL NASDAQ U.S. Bank	100.00	143.73	148.86	160.70	222.81	234.58

ITEM 6. SELECTED FINANCIAL DATA

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

Our financial condition data as of December 31, 2017 and 2016 and our statement of operations data for the years ended December 31, 2017, 2016 and 2015 have been derived from our audited historical financial statements included elsewhere in this Form 10-K.

	At or for the Year Ended December 31,				
	2017	2016	2015	2014	2013
	(Dollars in thousands, except per share data)				
Financial Condition Data:					
Total assets	$ 3,769,859	$ 3,221,598	$ 2,598,846	$ 2,054,154	$ 1,768,959
Total deposits	3,262,690	2,763,724	2,286,559	1,776,259	1,529,314
Investment securities held-to-maturity	8,780	10,337	5,830	7,815	—
Investment securities available-for-sale, at fair value	188,203	199,833	169,502	150,539	142,670
Loans and leases, gross[(1)]	2,941,093	2,543,549	2,059,392	1,604,149	1,323,431
Cash and cash equivalents	555,322	403,830	309,175	240,194	246,615
Other real estate owned[(2)]	4,112	4,112	4,112	8,811	5,602
Subordinated debt issuance, net	98,963	98,839	—	—	—
Shareholders' equity	355,034	298,065	264,145	235,026	206,916
Statement of Operations Data:					
Interest income	$ 157,600	$ 122,913	$ 94,702	$ 80,327	$ 69,726
Interest expense	27,896	18,734	10,856	9,340	7,729
Net interest income	129,704	104,179	83,846	70,987	61,997
Provision for credit losses	5,500	6,400	1,800	3,350	3,250
Net interest income after provision for loan and lease losses	124,204	97,779	82,046	67,637	58,747
Noninterest income	5,824	5,459	3,892	3,621	2,003
Noninterest expense	49,548	43,538	35,710	30,411	29,261
Income before provision for income taxes	80,480	59,700	50,228	40,847	31,489
Provision (benefit) for income taxes	37,086	23,331	20,485	16,255	12,290
Net income	$ 43,394	$ 36,369	$ 29,743	$ 24,592	$ 19,199
Income allocated to participating securities	(361)	(428)	(410)	(270)	(201)
Dividends allocated to participating securities	(138)	(119)	(126)	(30)	—
Net income available to common shareholders	$ 42,895	$ 35,822	$ 29,207	$ 24,292	$ 18,998

	At or for the Year Ended December 31,				
	2017	2016	2015	2014	2013
	(Dollars in thousands, except per share data)				
Share Data:					
Net income per share, basic[3]	$ 2.97	$ 2.58	$ 2.17	$ 1.83	$ 1.45
Net income per share, diluted[3][10]	$ 2.96	$ 2.56	$ 2.14	$ 1.78	$ 1.42
Book value per share[4]	$ 23.48	$ 20.94	$ 19.02	$ 17.40	$ 15.58
Cash dividends declared per common share	$ 0.80	$ 0.63	$ 0.51	$ 0.20	$ —
Shares outstanding at period end	15,122,313	14,232,907	13,884,942	13,503,458	13,280,653
Weighted average number of shares outstanding, basic[3]	14,438,964	13,883,497	13,484,216	13,290,258	13,116,563
Weighted average number of shares outstanding, diluted[3]	14,492,671	13,987,257	13,677,892	13,620,027	13,364,320
Selected Other Balance Sheet Data[5]:					
Average assets	$ 3,509,775	$ 2,872,707	$ 2,200,557	$ 1,880,019	$ 1,633,710
Average earning assets	3,431,985	2,815,545	2,154,355	1,836,375	1,578,570
Average shareholders' equity	314,731	284,734	251,949	223,198	196,981
Selected Financial Ratios[5]:					
Return on average assets	1.24%	1.27%	1.35%	1.31%	1.18%
Return on average shareholders' Equity[5]	13.79	12.77	11.81	11.02	9.75
Shareholders' equity to assets[6]	9.42	9.25	10.16	11.44	11.70
Net interest margin[7]	3.80	3.72	3.92	3.89	3.95
Efficiency ratio[8]	36.56	39.71	40.70	40.76	45.72
Selected Asset Quality Ratios:					
Non-performing loans to total loans and leases[9]	0.22%	0.30%	0.10%	0.53%	1.06%
Non-performing assets to total assets[10]	0.28	0.37	0.23	0.85	1.11
Allowance for loans and lease losses to total loans and leases	1.02	1.04	1.10	1.43	1.47
Allowance for loans and lease losses to non-performing loans	461.32	346.22	1,140.29	268.19	138.80
Net charge-offs (recoveries) to average loans and leases	0.08	0.11	0.12	(0.01)	0.36

(1) Excludes loans held for sale of $440 as of December 31, 2017, zero as of December 31, 2016, zero as of December 31, 2015, zero as of December 31, 2014, $6,207 as of December 31, 2013.

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

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

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

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

(6) For a discussion of the components of the capital ratios, see “Management’s Discussion and Analysis of Financial Condition and Results of Operations—Capital Resources.”
(7) Net interest margin is net interest income expressed as a percentage of average total interest-earning assets.
(8) The efficiency ratio is the ratio of noninterest expense divided by the sum of net interest income before the provision for credit losses plus noninterest income.
(9) Non-performing loans consist of loans on non-accrual and loans past due 90 days or more and restructured debt.
(10) Non-performing assets consist of non-performing loans and other real estate owned.

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

Our discussion and analysis of earnings and related financial data are presented herein to assist investors in understanding the financial condition of the Bank at December 31, 2017 and 2016, and the results of operations for the years ended December 31, 2017, 2016 and 2015. This discussion should be read in conjunction with the consolidated financial statements and related footnotes of our Company presented elsewhere herein.

Overview

We experienced fairly significant growth in loans, deposits and net income in the past three years. The national economy is improving and the local economy has continued to gain strength. We consider the real estate market in Southern California, the Bay Area and the Tri-State Area to be strong; however, there are still some pockets of weakness in some outlying areas of Southern California. During 2017, the Bank posted a high level of net income due to growth in loans, a reduction in the provision for loan losses and strong management of the Bank's non-interest expenses.

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

For the year ended December 31, 2017, the Bank recorded net income of $43.4 million as compared to net income of $36.4 million for the year ended December 31, 2016. At December 31, 2017, the Bank recorded an all-time high asset balance at $3.77 billion. Loans grew by $397.5 million, or 15.6%, and deposits grew by $499.0 million, or 18.1%. See "Results of Operations."

For the year ended December 31, 2016, the Bank recorded net income of $36.4 million as compared to net income of $29.7 million for the year ended December 31, 2015. At December 31, 2016, total assets were $3.22 billion. During 2017, loans grew by $484.2 million, or 23.5%, and deposits grew by $477.2 million, or 20.9%. See "Results of Operations."

On June 13, 2016, the Bank completed a private placement of $62.5 million in principal amount of fixed-to-floating rate subordinated notes to certain qualified investors. On July 8, 2016, and September 30, 2016, the Bank issued additional debt under the same terms of $10.0 million and $27.5 million respectively, bringing the total debt issuance to $100.0 million. The proceeds from the placement of the notes are to be used for general corporate purposes, capital management, and to support future growth. The subordinated notes have a maturity date of June 15, 2026 and bear interest, payable semiannually, at the rate of 6.0% per annum until June 15, 2021. On that date, the interest rate will be adjusted to float at a rate equal to the three-month LIBOR rate plus 467.3 basis points (4.673%) until maturity. The notes include a right of prepayment, on or after June 15, 2021 and, in certain limited circumstances, before that date. The indebtedness evidenced by the subordinated notes, including principal and interest, is unsecured and subordinate and junior in right to payment to general and secured creditors and depositors of the Bank. The subordinated notes have been structured to qualify as Tier 2 capital for regulatory purposes. The subordinated debt issuance is further discussed in "Notes to Consolidated Financial Statements, Note 9—Long-Term Debt."

On September 25, 2017, the Bank was granted a Stock Permit (the "Stock Permit") from the California Department of Business Oversight ("DBO") authorizing it to sell, from time-to-time, up to $50 million in shares of the Bank's common stock, by means of an "at the market offering" program (the "ATM Program"). During the fourth quarter of 2017, the Bank sold 541,975 shares through the ATM Program for the net proceeds of $32.8 million.

Critical Accounting Policies

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

Allowance for Loan and Lease Losses

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

We evaluate our allowance for loan and lease losses quarterly. We believe that the allowance for loan and lease losses is a "critical accounting estimate" because it is based upon management's assessment of various factors affecting the collectability of the loans and leases, including current economic conditions, past credit experience, delinquency status, the value of the underlying collateral, if any, and a continuing review of the portfolio of loans and leases. On a recurring basis, the Bank measures the fair value of impaired collateral dependent loans based on fair value of the collateral value which is derived from appraisals that take into consideration prices in observable transactions involving similar assets in similar locations in accordance with Receivables Topic of FASB ASC 310-10 covering loan impairments.

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

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

Investment Securities

The classification and accounting for investment securities are discussed in detail in Note 1 of the Consolidated Financial Statements presented elsewhere herein. Under Investments—Debt and Equity Securities Topic of FASB ASC, investment securities must be classified as held-to-maturity, available-for-sale, or trading. The appropriate classification is based partially on our ability to hold the securities to maturity and largely on management's intentions with respect to either holding or selling the securities. The classification of investment securities is significant since it directly impacts the accounting for unrealized gains and losses on securities. Unrealized gains and losses on trading securities flow directly through earnings during the periods in which they arise, whereas unrealized gains and losses on available-for-sale securities are recorded as a separate component of shareholders' equity (accumulated other comprehensive income or loss) and do not affect earnings until

realized. The fair values of our investment securities are generally determined by an independent pricing service and are considered to be level 2 or 3 categories as defined by Fair Value Measurements and Disclosures Topic of FASB ASC. The fair values of investment securities are generally determined by reference to market prices obtained from an independent external pricing service. In obtaining such valuation information from third parties, we have evaluated the methodologies used to develop the resulting fair values. The procedures include, but are not limited to, initial and on-going review of third-party pricing methodologies, review of pricing trends, and monitoring of trading volumes. We ensure whether prices received from independent brokers represent a reasonable estimate of fair value through the use of external cash flow model developed based on spreads, and when available, market indices. As a result of this analysis, if we determine there is a more appropriate fair value based upon the available market data, the price received from the third party may be adjusted accordingly. Management reviews the fair value of investment securities on a monthly basis for reasonableness. In addition, management has a separate fixed income broker/dealer review the fair values received from the pricing service on a quarterly basis as an additional control over the process of determining fair values. On a quarterly basis, management thoroughly assesses the fair values of impaired investment securities by looking at other data regarding the fair values such as: recent trading levels of the same or similarly rated securities, reviewing assumptions used in discounted cash flow analyses for reasonableness and other information such as general market conditions.

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

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

We re-examine the financial resources, intent and the overall ability of the Bank to hold the securities until their fair values recover. Management does not believe that there are any investment securities, other than those identified in the current and previous periods, which are deemed to be “other-than-temporarily” impaired as of

December 31, 2017. Investment securities are discussed in more detail in "Notes to Consolidated Financial Statements, Note 3—Securities Available-for-Sale and Held-to-Maturity" presented elsewhere in this Report.

Income Taxes

We accounted for income taxes under the asset and liability method, which requires the recognition of deferred tax assets and liabilities for the expected future tax consequences of events that have been included in the financial statements. Under this method, deferred tax assets and liabilities are determined based on the differences between the financial statements and tax basis of assets and liabilities using enacted tax rates in effect for the year in which the differences are expected to reverse. The effect of a change in tax rates on deferred tax rates on deferred tax assets and liabilities is recognized in income in the period that includes the enacted date. Income taxes are discussed in more detail in "Notes to Consolidated Financial Statements, Note 1—Summary of Significant Accounting Policies" and "Note 7—Income Taxes."

On December 22, 2017, President Trump signed the Tax Cuts and Jobs Act into legislation, substantially amending the Internal Revenue Code. Under FASB ASC 740, the effects of changes in tax rates and laws are recognized in the period in which the new legislation is enacted. As a result of this new legislation, the Company incurred a one-time increase in tax expense of $6.0 million from the re-measurement of deferred tax assets and liabilities resulting from the legislation's decrease in the corporate Federal income tax rate from 35% to 21%.

Results of Operations

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

	Year Ended December 31,		
	2017	2016	2015
	(Dollars in thousands, except per share data)		
Net income	$43,394	$36,369	$29,743
Net income per share, basic	$ 2.97	$ 2.58	$ 2.17
Net income per share, diluted	$ 2.96	$ 2.56	$ 2.14
Return on average assets	1.24%	1.27%	1.35%
Return on average shareholders' equity	13.79%	12.77%	11.81%
Dividend payout ratio	26.93%	23.43%	21.54%
Equity to assets ratio	9.42%	9.25%	10.16%

Year Ended December 31, 2017 Compared to Year Ended December 31, 2016

	Year Ended December 31,		
	2017	**2016**	**Increase (Decrease)**
	(Dollars in thousands, except per share data)		
Statement of Operations Data:			
Interest income	$157,600	$122,913	$34,687
Interest expense	27,896	18,734	9,162
Net interest income	129,704	104,179	25,525
Provision for credit losses	5,500	6,400	(900)
Net interest income after provision for loan and lease losses	124,204	97,779	26,425
Noninterest income	5,824	5,459	365
Noninterest expense	49,548	43,538	6,010
Income before income taxes	80,480	59,700	20,780
Income tax expense	37,086	23,331	13,755
Net income	$ 43,394	$ 36,369	$ 7,025
Income allocated to participating securities	(361)	(428)	67
Dividends allocated to participating securities	(138)	(119)	(19)
Net income available to common shareholders-basic	$ 42,895	$ 35,822	$ 7,073
Net income per share, basic	$ 2.97	$ 2.58	$ 0.39
Net income per share, diluted	$ 2.96	$ 2.56	$ 0.40

Net income increased from 2016 to 2017, primarily as a result of increased net interest income between the years. The $25.5 million, or 24.5%, increase in net interest income was due primarily to growth of the loan portfolio. Our overall cost of funds in 2017 increased 17 basis points from 0.92% during 2016 to 1.09% for 2017, while average yields on earning assets increased by 23 basis points to 4.62% from 4.39%. The increase in cost of funds is primarily due to interest expense for the subordinated debt issued during 2016. The yield on earning assets saw an increase primarily due to the 29 basis point increase in average interest rates on loans during the year, increasing from 5.00% to 5.29%. Additionally, the yield on other earning assets increased 44 basis points from 0.85% to 1.29%.

Income tax expense increased $7.0 million during the year ended December 31, 2017 and were impacted by $6.0 million in additional income tax expense resulting from the change in Federal income tax rates, which increased our effective tax rate by 7.5% during the year ended December 31, 2017.

As of December 31, 2017, 82% of our loan portfolio was tied to the Prime Rate, which has the potential to re-price daily, and 13% was tied to the London Interbank Offered Rate, or LIBOR, or other indices, which re-price periodically. Approximately 78% of our loan portfolio had a floor interest rate at various levels, which provides us with some protection in the current environment with the Prime Rate at a level below the floor interest rate. Approximately 3% of our loan portfolio had interest rate ceilings at various rates limiting the amount of interest rate increases that can be passed on to the borrower. Our weighted average maturity of certificates of deposit at December 31, 2017 was 6.4 months. Since the majority of our loans re-price more rapidly than the interest rates on our deposits, a rising interest rate environment should be beneficial to the amount of net interest income we will realize during that period.

Year Ended December 31, 2016 Compared to Year Ended December 31, 2015

	Year Ended December 31,		
	2016	2015	Increase (Decrease)
	(Dollars in thousands, except per share data)		
Statement of Operations Data:			
Interest income	$122,913	$94,702	$28,211
Interest expense	18,734	10,856	7,878
Net interest income	104,179	83,846	20,333
Provision for credit losses	6,400	1,800	4,600
Net interest income after provision for loan and lease losses	97,779	82,046	15,733
Noninterest income	5,459	3,892	1,567
Noninterest expense	43,538	35,710	7,828
Income before income taxes	59,700	50,228	9,472
Income tax expense	23,331	20,485	2,846
Net income	$ 36,369	$29,743	$ 6,626
Income allocated to participating securities	(428)	(410)	(18)
Dividends allocated to participating securities	(119)	(126)	7
Net income available to common shareholders-basic	$ 35,822	$29,207	$ 6,615
Net income per share, basic	$ 2.58	$ 2.17	$ 0.41
Net income per share, diluted	$ 2.56	$ 2.14	$ 0.42

Net income increased from 2015 to 2016, primarily as a result of increased net interest income between the years. The $28.2 million, or 29.8%, increase in net interest income was due primarily to growth of the loan portfolio. Our overall cost of funds in 2016 increased 17 basis points from 0.75% during 2015 to 0.92% for 2016, while average yields on earning assets decreased by 3 basis points to 4.39% from 4.42%. The increase in cost of funds is primarily due interest expense for the subordinated debt issued during 2016. Yield on earning assets saw a slight decrease primarily due to slightly decreased average interest rates on loans during the year, decreasing from 5.09% to 5.00%. Additionally, during the first quarter of 2016, we noted errors in the accrual of interest on several loans which had been charged off as early as 2011. The amount involved was deemed to be immaterial and this event was confirmed to be isolated. The total cumulative amount involved was $805,000, and this amount was recorded in the first quarter of 2016 as a reduction of loan interest income. Separately, interest income of $253,000 was collected from the payoff of a loan previously on nonaccrual status. The two items in combination negatively impacted the net interest margin for 2016 by approximately 2 basis points.

As of December 31, 2016, 80% of our loan portfolio was tied to the Prime Rate, which has the potential to re-price daily, and 13% was tied to the London Interbank Offered Rate, or LIBOR, or other indices, which re-price periodically. Approximately 78% of our loan portfolio had a floor interest rate at various levels, which provides us with some protection in the current environment with the Prime Rate at a level below the floor interest rate. Approximately 3% of our loan portfolio had interest rate ceilings at various rates limiting the amount of interest rate increases that can be passed on to the borrower. Our weighted average maturity of certificates of deposit at December 31, 2016 was 8.2 months. Since the majority of our loans re-price more rapidly than the interest rates on our deposits, a rising interest rate environment should be beneficial to the amount of net interest income we will realize during that period.

Net Interest Income and Net Interest Margin

Year ended December 31, 2017 compared to 2016

Net interest income before the provision for credit losses for the year ended December 31, 2017 increased $25.5 million, or 24.5%, to $129.7 million from $104.2 million for the year ended December 31, 2016. This increase was due to an increase of $34.7 million in interest income, offset by a $9.2 million increase in interest expense. Total increase in interest income is primarily due to the higher average loan balance of $2.73 billion in 2017, an increase from $2.28 billion average loan balance in 2016, coupled with an increase in average loan yields from 5.00% to 5.29% between the periods.

The average yield on our interest-earning assets increased by 23 basis points to 4.62% in the year ended December 31, 2017 from 4.39% in the year ended December 31, 2016. Yield on earning assets saw an increase primarily due to overall higher market interest rates during the year.

The cost of average interest-bearing liabilities increased by 17 basis points to 1.09% in the year ended December 31, 2017 from 0.92% in the year ended December 31, 2016. This increase was primarily caused by the 8 basis point increase in both the cost of deposits from 0.80% to 0.88% and FHLB borrowings from 0.98% to 1.07% during the year.

Year ended December 31, 2016 compared to 2015

Net interest income before the provision for credit losses for the year ended December 31, 2016 increased $20.3 million, or 24.3%, to $104.2 million from $83.8 million for the year ended December 31, 2015. This increase was due to an increase of $28.2 million in interest income, offset by a $7.9 million increase in interest expense. Total increase in interest income is primarily due to the higher average loan balance of $2.28 billion in 2016, an increase from $1.73 billion average balance in 2015, offset by a decrease in the average loan yield from 5.09% to 5.00% between the periods.

The average yield on our interest-earning assets decreased by 3 basis points to 4.39% in the year ended December 31, 2016 from 4.42% in the year ended December 31, 2015. Yield on earning assets saw a slight decrease primarily due to the lower interest rates on loans during the year.

The cost of average interest-bearing liabilities increased by 17 basis points to 0.92% in the year ended December 31, 2016 from 0.75% in the year ended December 31, 2015. This increase was primarily caused by interest expense for the subordinated debt issued during 2016, which carried an interest rate of 6.16% for the year.

	Year Ended December 31, 2017			Year Ended December 31, 2016			Year Ended December 31, 2015		
	Average Balance	Interest Income or Expense	Average Yield or Cost	Average Balance	Interest Income or Expense	Average Yield or Cost	Average Balance	Interest Income or Expense	Average Yield or Cost
	(Dollars in thousands)								
ASSETS									
Interest-earning assets:									
Loans and leases[1][2]	$2,733,369	$144,678	5.29%	$2,282,074	$114,148	5.00%	$1,731,871	$88,235	5.09%
Investment securities[3]	204,004	7,250	3.55%	190,475	6,571	3.45%	169,129	5,568	3.29%
Federal funds sold	84,308	1,130	1.34%	62,333	473	0.76%	34,293	163	0.48%
Other earning assets	410,304	5,293	1.29%	280,663	2,380	0.85%	219,062	1,338	0.61%
Total interest-earning assets	$3,431,985	$158,351	4.62%	$2,815,545	$123,572	4.39%	$2,154,355	$95,304	4.42%
Deferred loan fees, net	(2,745)			(2815)			(2,180)		
Allowance for loan and lease losses	(27,781)			(23,920)			(23,635)		
Noninterest-earning assets:									
Cash and due from banks	13,286			5,544			5,663		
Other assets	95,030			78,353			66,354		
Total assets	$3,509,775			$2,872,707			$2,200,557		
LIABILITIES AND SHAREHOLDERS' EQUITY									
Interest-bearing liabilities:									
Deposits									
Interest-bearing demand	$ 402,302	$ 2,951	0.73%	$ 286,323	$ 1,667	0.58%	$ 177,220	$ 994	0.56%
Money market	794,767	4,950	0.62%	594,438	3,063	0.52%	438,583	2,166	0.49%
Savings	28,926	72	0.25%	30,573	76	0.25%	22,719	59	0.26%
Time certificates of deposit	1,222,879	13,633	1.11%	1,050,690	10,855	1.03%	796,344	7,455	0.94%
Total interest-bearing deposits	2,448,874	21,606	0.88%	1,962,024	15,661	0.80%	1,434,866	10,674	0.74%
Short-term borrowings	1	—	0.00%	1	—	0.00%	1	—	0.00%
Subordinated debt issuance	98,897	6,123	6.19%	45,704	2,814	6.16%	—	—	0.00%
Long-term debt (FHLB and Senior debt)	15,720	167	1.06%	26,452	259	0.98%	20,876	182	0.87%
Total interest-bearing liabilities	2,563,492	27,896	1.09%	2,034,181	18,734	0.92%	1,455,742	10,856	0.75%
Noninterest-bearing liabilities:									
Demand deposits	590,036			526,344			474,856		
Other liabilities	41,516			27,448			18,008		
Total liabilities	3,195,044			2,587,973			1,948,608		
Shareholders' equity	314,731			284,734			251,949		
Total liabilities and shareholders' equity	$3,509,775			$2,872,707			$2,200,557		
Net interest income		$130,455			$104,838			$84,448	
Net interest spread			3.53%			3.47%			3.68%
Net interest margin			3.80%			3.72%			3.92%

(1) Includes average non-accrual loans and leases.

(2) Net loan and lease fee income of $3.3 million, $2.5 million and $1.5 million for the year ended December 31, 2017, 2016 and 2015, respectively, are included in the yield computations.

(3) Yields on securities have been adjusted to a tax-equivalent basis.

In addition to the distribution, yields and costs of our assets and liabilities, our net income is also affected by changes in the volume of and rates on our assets and liabilities. The following table shows the change in interest income and interest expense and the amount of change attributable to variances in volume, rates and the combination of volume and rates based on the relative changes of volume and rates.

	Year Ended December 31,					
	2017 vs. 2016			2016 vs. 2015		
	Net Change	Rate	Volume	Net Change	Rate	Volume
	(In thousands)					
Interest income:						
Loans and leases	$30,530	$6,941	$23,589	$25,913	$(1,636)	$27,549
Investment securities[(1)]	679	204	475	1,002	275	727
Federal funds sold	657	450	207	310	131	179
Other earning assets	2,913	1,543	1,370	1,043	605	438
Total interest income	34,779	9,138	25,641	28,268	(625)	28,893
Interest expense:						
Interest-bearing demand	1,284	502	782	674	40	634
Money market	1,887	722	1,165	896	97	799
Savings	(4)	—	(4)	17	(3)	20
Time certificates of deposit	2,778	1,006	1,772	3,400	884	2,516
Short-term borrowings	—	—	—	—	—	—
Subordinated debt	3,309	16	3,293	2,814	—	2,814
Long-term debt	(92)	21	(113)	77	428	(351)
Total interest expense	9,162	2,267	6,895	7,878	1,446	6,432
Net interest income	$25,617	$6,871	$18,746	$20,390	$(2,071)	$22,461

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

Provision for Credit Losses

In response to the credit risk inherent in our lending business, we maintain allowances for loan losses through charges to earnings.

The provision for credit losses decreased by $900,000 during 2017 to $5.5 million from $6.4 million for 2016. Net loans and lease charge-offs decreased $523,000 to a net charge-off of $2.1 million during 2017 from net charge-offs of $2.6 million during 2016. The provision decreased between 2016 and 2017 as a result of consistent credit quality relative to the increase in loan portfolio size. In calculating the need for allowance levels based on historical losses, the Bank uses a weighted 4-year historical loss measurement period. Also, the Bank utilizes qualitative factors used in calculating allowance levels, such as the mix of the loan portfolio, concentration levels and trends, local and national economic conditions, changes in capabilities and experience of lending management and staff and other external factors including industry conditions, competition and regulatory requirements. Non-performing loans decreased from $7.6 million as of December 31, 2016 to $6.5 million as of December 31, 2017, due primarily to the charge-off of one commercial loan totaling $1.3 million, offset by the one additional commercial loan totaling $0.2 million being placed on nonaccrual status during the third quarter of 2017. The ratio of allowance for loan and lease losses to total loans decreased slightly from 1.04% of total loans at December 31, 2016 to 1.02% at December 31, 2017. Management believes that through the application of the allowance methodology's quantitative and qualitative components, the provision and overall level of allowance is adequate for probable losses estimated to be incurred in the portfolio as of December 31, 2017.

The provision for credit losses for 2016 increased by $4.6 million to $6.4 million from $1.8 million for 2015. The Bank's net loans and lease charge-offs increased to a net charge-off of $2.6 million during 2016 from

net charge-offs of $2.1 million during 2015. The provision increased between 2015 and 2016 due to continued increase in the size of the loan portfolio. In calculating the need for allowance levels based on historical losses, the Bank uses a weighted 4-year historical loss measurement period. Also, the Bank utilizes qualitative factors used in calculating allowance levels, such as the mix of the loan portfolio, concentration levels and trends, local and national economic conditions, changes in capabilities and experience of lending management and staff and other external factors including industry conditions, competition and regulatory requirements. Non-performing loans increased from $2.0 million as of December 31, 2015 to $7.6 million as of December 31, 2016, due to one commercial loan and one international loan placed on nonaccrual status during the fourth quarter of 2016. The ratio of allowance for loan and lease losses to total loans decreased slightly from 1.10% of total loans at December 31, 2015 to 1.04% at December 31, 2016. Management believes that through the application of the allowance methodology's quantitative and qualitative components, the provision and overall level of allowance is adequate for probable losses estimated to be incurred in the portfolio as of December 31, 2016.

Additionally, a separate reserve is maintained related to off-balance sheet items such as commitments to extend credits, or letters of credit. See the "Contractual Obligations" section below for further discussion of off-balance sheet items.

Noninterest Income

We earn noninterest income primarily through fees related to:

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

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

	Year Ended December 31,		
	2017	2016	2015
	(In thousands)		
Fees and service charges on deposit accounts	$1,269	$1,212	$1,178
Letter of credit fee income	2,635	2,371	1,630
BOLI income	351	346	339
Net gain on sale or call of investment securities	4	169	—
Other income	1,565	1,361	745
Total noninterest income	$5,824	$5,459	$3,892

Total noninterest income increased by $365,000 or 7%, to $5.8 million during 2017 from $5.5 million during 2016. The increase was primarily due to a $264,000 or 11% increase in letter of credit fee income, and was aided by a $204,000 or 15% increase in other income between 2016 and 2017 due, in part, to loan settlements received. Offsetting these increases was a $165,000 or 97% decrease in net gain on sale or call of investment securities due to limited activity during 2017.

Total noninterest income increased by $1.6 million or 40%, to $5.5 million during 2016 from $3.9 million during 2015. The increase was primarily due to a $741,000 or 45% increase in letter of credit fee income, and was aided by a $616,000 or 83% increase in other income between 2015 and 2016 consisting mostly of fees for services to loan customers.

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

Noninterest Expense

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

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

	Year Ended December 31,		
	2017	**2016**	**2015**
		(In thousands)	
Salaries and employee benefits	$30,041	$25,813	$20,960
Net occupancy expense	4,942	4,830	3,681
Business development and promotion expense	883	845	593
Professional services	4,390	5,297	4,906
Office supplies and equipment expense	1,340	1,422	1,119
OREO related expense, net	563	825	(480)
Other	7,389	4,506	4,931
Total noninterest expense	49,548	43,538	35,710

Total noninterest expense increased by $6.0 million, or 14%, to $49.5 million during 2017 from $43.5 million during 2016. The main driver of the increase was salaries and benefits expense, which increased $4.2 million over 2016 levels due to the hiring of additional administrative and support staff to support the Bank's future growth. Other noninterest expense increase by $2.9 million or 64% to $7.4 million in 2017 from $4.5 million in 2016. The increase in other expense is primary attributable to a $2.1 million increase in our loan settlement reserve and a $1.2 million increase in FDIC assessment premiums. Offsetting these increases in noninterest expenses were a decrease of $907,000 in professional services as a result of decreased legal fees from the prior period and a $262,000 decrease in OREO related expenses as a result of decreased REO activity between periods.

Total noninterest expense increased by $7.8 million, or 22%, to $43.5 million during 2016 from $35.7 million during 2015. The main driver of the increase was salaries and benefits expense, which increased $4.9 million over 2015 levels due to the addition of business development staff, additional loan production staff, and staff for the New York branch acquired in the acquisition of UIB in November 2015. Net occupancy expense increased by $1.1 million, or 31%, primarily due to the lease for the New York branch. Professional fees increased by $391,000 to $5.3 million during 2016 from $4.9 million in 2015 due primarily to increased legal fees comparing the periods. OREO related expense totaled $825,000 in 2016, up from a net gain of $480,000 in 2015. This consists of appraisal costs and legal fees related to the OREO property, and no sales during the year compared to one sale with gain in 2015. Other noninterest expenses were $4.5 million in 2016, a decrease of $425,000 from the $4.9 million in 2015 due mainly to expenses related to the acquisition of UIB which increased this expense amount in 2015.

Provision for Income Taxes

We accounted for income taxes under the asset and liability method, which requires the recognition of deferred tax assets and liabilities for the expected future tax consequences of events that have been included in

the financial statements. Under this method, deferred tax assets and liabilities are determined based on the differences between the financial statements and tax basis of assets and liabilities using enacted tax rates in effect for the year in which the differences are expected to reverse. The effect of a change in tax rates on deferred tax rates on deferred tax assets and liabilities is recognized in income in the period that includes the enacted date.

We record net tax assets to the extent we believe these assets will more likely than not be realized. In making such determination, we consider all available positive and negative evidence, including scheduled reversals of deferred tax liabilities, projected future taxable income, tax planning strategies and recent financial operations. We have assessed the likelihood that our deferred tax asset would be recovered from taxable income and determined that recovery was more likely than not based upon the totality of the evidence, both positive and negative.

We recorded a provision of $37.1 million for income taxes related to the pre-tax income for the year ended December 31, 2017 at an effective tax rate of 46.1%. On December 22, 2017, President Trump signed the Tax Cuts and Jobs Act into legislation, substantially amending the Internal Revenue Code. Under FASB ASC 740, the effects of changes in tax rates and laws are recognized in the period in which the new legislation is enacted. As a result of this new legislation, the Company incurred a one-time increase in tax expense of $6.0 million from the re-measurement of deferred tax assets and liabilities resulting from the legislation’s decrease in the corporate Federal income tax rate from 35% to 21%. The $6.0 million in additional income tax expense from the change in Federal income tax rates increased our effective tax rate by 7.5% during the year ended December 31, 2017. Our effective tax rate excluding the impact of the change in Federal income tax rates was 38.6%.

In 2016, we recorded a provision for income taxes of $23.3 million at an effective tax rate of 39.1%. In 2015, we recorded a provision for income taxes of $20.5 million at an effective tax rate of 40.8%. As of December 31, 2017 we had federal and state net operating loss (“NOL”) carryforwards of $1.6 million and $23.2 million, respectively.

As of result of the UIB acquisition the Bank now files in the federal, California and New York jurisdictions.

Pursuant to Sections 382 and 383 of the Internal Revenue Code (“IRC”), annual use of NOL and credit carryforwards may be limited in the event a cumulative change in ownership of more than 50 percent points occurs within a three-year period. We determined that such an ownership change occurred as of June 21, 2010 as a result of stock issuances in 2010 and 2009. This ownership change resulted in estimated limitations on the utilization of tax attributes, including NOL carryforwards and tax credits. Although we fully expect to utilize all of the federal NOL carryforward prior to their expiration, the California NOL carryover has been significantly impacted by the IRC Sec. 382 limitation. We estimate that of approximately $79.0 million of the California NOL as of December 31, 2017, $55.8 million are expected to expire in 2029 and $3.2 million are expected to expire in 2030 as they will be unutilized as a result of IRS Sec 382 limitation. This amounts to approximately $5.1 million of deferred tax assets which would not be realized. The remaining California NOL carryforward of the approximately $19.9 million at December 31, 2017, is subject to IRC Sec. 382 annual limitation amount of approximately $1.5 million. Additionally, the Bank has $5.2 million of Federal excess realized built in losses and $6.1 million of California excess built in losses as of December 31, 2017 which are also subject to IRC Sec. 382 annual limitation amount of approximately $1.5 million. As a result of the UIB acquisition, the Bank has an additional $1.6 million of federal NOLs and $3.3 million of New York NOLs that are subject to Section 382 limitation of $0.6 million remaining as of December 31, 2017. Management fully expects to use the acquired NOL carryforwards before their expiration beginning in 2025 for New York NOLs and 2033 for federal NOLs.

Financial Condition

For the period between December 31, 2016 and December 31, 2017, our assets, loans and deposits grew at the rate of 17.0%, 15.6% and 18.1%, respectively. Our total assets at December 31, 2017 were $3.77 billion compared to $3.22 billion at December 31, 2016. Our earning assets at December 31, 2017 totaled $3.70 billion

compared to $3.16 billion at December 31, 2016. Total deposits at December 31, 2017 and December 31, 2016 were $3.26 billion and $2.76 billion, respectively.

Loans and Leases

The largest component of our assets and largest source of interest income is our loan portfolio. The following table sets forth the amount of our loans and leases outstanding at the end of each of the periods indicated, and the percentages the overall loan segment represented. The Bank had no foreign loans. The Bank had two energy-related loans totaling $14.0 million and $14.2 million as of December 31, 2017 and 2016, respectively.

	December 31,									
	2017		2016		2015		2014		2013	
	(in thousands)									
Loans and leases (by portfolio and class):										
Real Estate Mortgage:										
Real Estate—Residential	$ 370,771	12.6%	$ 334,794	13.2%	$ 259,862	12.6%	$ 145,276	9.1%	$ 105,144	7.9%
Real Estate—Commercial	1,398,530	47.6	1,215,384	47.8	1,027,179	49.8	805,683	50.2	766,395	57.9
Total Real Estate Mortgage	$1,769,301		$1,550,178		$1,287,041		$ 950,959		$ 871,539	
Real Estate—Construction:										
R/E Construction—Residential	85,199	2.9	104,960	4.1	88,755	4.3	48,892	3.1	24,997	1.9
R/E Construction—Commercial	198,603	6.8	128,434	5.0	42,649	2.1	77,593	4.8	48,288	3.7
Total Real Estate—Construction	$ 283,802		$ 233,394		$ 131,404		$ 126,485		$ 73,285	
Commercial & Industrial	866,672	29.4	733,708	28.8	596,787	29.0	495,827	30.9	338,680	25.6
Trade Finance	21,310	0.7	21,702	0.9	38,225	1.9	30,498	1.9	39,640	3.0
Consumer & Other	8	0.0	4,567	0.2	5,935	0.3	380	0.0	287	0.0
Total gross loans and leases	$2,941,093	100.0%	$2,543,549	100.0%	$2,059,392	100.0%	$1,604,149	100.0%	$1,323,431	100.0%
Less: allowance for loan and lease losses	(29,921)		(26,478)		(22,658)		(22,974)		(19,494)	
Deferred loan and lease fees, net	(3,099)		(1,682)		(3,012)		(2,100)		(2,562)	
Total loans excluding loans held for sale	$2,908,073		$2,515,389		$2,033,722		$1,579,075		$1,301,375	
Loans held for sale	440		—		—		—		6,207	
Total net loans and leases	$2,908,513		$2,515,389		$2,033,722		$1,579,075		$1,307,582	

Total gross loans at December 31, 2017, net of loans held for sale, were $2.94 billion, up 15.6% from $2.54 billion as of December 31, 2016. Total gross loans at December 31, 2016, net of loans held for sale, were $2.54 billion, up from the $2.06 billion as of December 31, 2015. As we continued to grow our lending staff and target strong portfolio growth, loan balances in most portfolios increased from December 31, 2016 to December 31, 2017, with the exception of trade finance loans, which are primarily working capital revolving and term loans for business operations, and residential real estate construction loans which also declined. Management's focus from a lending perspective is on commercial and industrial loans and prime-owner-occupied, income-producing commercial real estate and multi-family real estate. Management continually evaluates the mix of loan types in the loan portfolio in order to minimize risk and maximize returns within the portfolio.

Our real estate loan portfolio increased in 2017 by $219.1 million or 14.1% to $1.77 billion at December 31, 2017 from $1.55 billion at December 31, 2016. The overall increasing trend is due to management's focus from a lending perspective on prime owner-occupied, income-producing commercial real estate as well as commercial & industrial loans as seen in the results of the loan portfolio changes from December 31, 2016. Residential real estate loans increased by $36.0 million, or 10.7%, and commercial real estate loans grew by $183.1 million or 15.1%. Retail-purpose grew during 2017, with an increase of $93.2 million, or 28.3%, with most of that coming during the early part of the year, land loans decreased by $5.7 million, or 34.5%, and special

purpose loans increased $98.1 million, or 36.7%. Further detail regarding the real estate portfolio by property type is provided in the table below.

The following table provides information about our real estate mortgage portfolio by property type:

	At December 31, 2017		At December 31, 2016	
Property Type	Amount	Percentage of Loans in Each Category in Total Loan Portfolio	Amount	Percentage of Loans in Each Category in Total Loan Portfolio
	(Dollars in thousands)		(Dollars in thousands)	
Commercial/Office	$ 266,508	9.06%	$ 243,886	9.59%
Retail	422,174	14.35	329,023	12.94
Industrial	190,471	6.48	207,137	8.14
Residential 1-4	362,276	12.32	320,020	12.58
Apartment 4+	151,677	5.16	166,262	6.54
Land	10,862	0.37	16,575	0.65
Special purpose	365,333	12.42	267,275	10.51
Total	$1,769,301	60.16%	$1,550,178	60.95%

As of December 31, 2017, loans held for sale, consisting of one single-family residential loan, totaled $440,000. There were no loans held for sale at December 31, 2016.

Total commercial loan commitments (including undisbursed amounts) at December 31, 2017 increased $140.6 million or 13.0% to $1.22 billion from $1.08 billion at December 31, 2016 partly due to the rising rate of credit utilization, which increased to 70.8% as of December 31, 2017 from 67.7% at December 31, 2016.

Other loans, examples of which include installment/consumer debt leases receivable, are relatively insignificant.

Non-Performing Assets

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

A TDR is a debt restructuring in which a bank, for economic or legal reasons specifically related to a borrower’s financial condition, grants a concession to the borrower that it would not otherwise consider. At December 31, 2017, there were three loans totaling $5.9 million classified as non-performing TDRs, all of which were on nonaccrual status. At December 31, 2016, there were three loans totaling $6.0 million classified as TDRs, all of which were on nonaccrual status.

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

	Year Ended December 31,				
	2017	2016	2015	2014	2013
	(Dollars in thousands)				
Non-accrual loans and leases*	$ 6,486	$ 7,648	$1,987	$ 8,116	$14,044
Accruing loans and leases past due 90 days or more	—	—	—	450	—
Total non-performing loans (NPLs)	6,486	7,648	1,987	8,566	14,044
OREO	4,112	4,112	4,112	8,811	5,602
Total non-performing assets (NPAs)	$10,598	$11,760	$6,099	$17,377	$19,646
Selected ratios:					
NPLs to total gross loans and leases held for investment	0.22%	0.30%	0.10%	0.53%	1.06%
NPAs to total assets	0.28%	0.37%	0.23%	0.85%	1.11%

* Non-accrual Troubled Debt Restructurings (TDRs) that are included in non-accrual loans are as follows: 2017—$5,864; 2016—$5,988; 2015—$0; 2014—$0; 2013—$7,665. TDRs that are performing according to their revised terms are not reflected as non-performing loans (NPLs).

Non-accrual loans decreased by $1.2 million, from $7.6 million as of December 31, 2016 to $6.5 million as of December 31, 2017. The decrease was primarily due to the charge-off of one commercial loan totaling $1.3 million, offset by the one additional commercial loan totaling $0.2 million being placed on nonaccrual status during the third quarter of 2017.

The amount of interest income that would have been recorded on impaired loans that were non-accrual loans and leases had the loans and leases been current totaled $697,000, $540,000, and $193,000, for 2017, 2016, and 2015, respectively. When an asset is placed on non-accrual status, previously accrued but unpaid interest is reversed against current income. Subsequent collections of cash are applied as principal reductions when received, except when the ultimate collectability of principal is probable, in which case interest payments are credited to income. See Note 3 of the Consolidated Financial Statements for further details regarding non-accrual and past due loans by loan class.

As of both December 31, 2017 and December 31, 2016, we had one OREO property for $4.1 million. There were no sales of OREO property during 2017 and 2016. During 2015, the Bank sold one OREO property at a net gain of $325,000. The following table summarizes the Bank's OREO as of the periods presented.

Foreclosed assets (OREO) as of December 31, 2017 and 2016 were as follows:

	2017		2016	
Loan Class	#	$	#	$
(Dollars in thousands)				
Real Estate Mortgage:				
Residential	—	$ —	—	$ —
Commercial	1	4,112	1	4,112
Real Estate Construction:				
Residential	—	—	—	—
Commercial	—	—	—	—
Commercial & Industrial	—	—	—	—
Total as of December 31	1	$4,112	1	$4,112

OREO is initially stated at fair value of the property based on appraisal, less estimated selling cost. Any cost in excess of the fair value at the time of acquisition is accounted for as a loan charge-off and deducted from the

allowance for loan and lease losses. A valuation allowance is established for any subsequent declines in value through a charge to earnings. Operating expenses of such properties, net of related income, and gains and losses on their disposition are included in other operating income or expense, as appropriate.

Impaired Loans and Leases

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

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

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

We had $7.6 million, $8.8 million and $2.0 million of impaired loans or leases at December 31, 2017, 2016, and 2015, respectively. The $1.2 million decrease in impaired loans during 2017 was primarily the result of charge-offs of two loans considered impaired at December 31, 2016, offset by management's determination that two additional loans are considered impaired at December 31, 2017. The increase from December 31, 2015 to December 31, 2016 is the result management's determination during the year that two loans within one borrowing relationship are considered impaired. The total allowance for loan and lease losses related to impaired loans and leases was $2.0 million, $1.7 million, and $398,000 at December 31, 2017, 2016 and 2015, respectively. Interest income recognized on such loans and leases during 2017, 2016 and 2015 was $164,000, 320,000, and zero, respectively. The average recorded investment on impaired loans and leases including loans held for sale during 2017, 2016 and 2015 was $8.2 million, $8.0 million and $2.3 million, respectively.

Allowance for Loan and Lease Losses

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

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

Specifically, our allowance methodology contains four elements: (a) amounts based on specific evaluations of impaired loans; (b) amounts of estimated losses on loans classified as 'special mention' and 'substandard' that are not already included in impaired loan analysis; (c) amounts of estimated losses on loans not adversely

classified which we refer to as ‘pass’ based on historical loss rates by loan type; and (d) amounts for estimated losses on loans rated as pass based on economic and other factors that indicate probable losses were incurred but were not captured through the other elements of our allowance process.

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

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

Finally, in order to ensure our allowance methodology is incorporating recent trends and economic conditions, we apply environmental and general economic factors to our allowance methodology including: credit concentrations; delinquency trends; national and local economic and business conditions; the quality of lending management and staff; lending policies and procedures; loss and recovery trends; nature and volume of the portfolio; changes in the value of underlying collateral for collateral dependent loans; the quality of loan reviews; and other external factors including competition, legal, and regulatory factors.

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

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

Allowance for Loan and Lease Loss History

	Year Ended December 31,				
	2017	2016	2015	2014	2013
	(Dollars in thousands)				
Allowance for loan and lease losses:					
Balance at beginning of period	$ 26,478	$ 22,658	$ 22,974	$ 19,494	$ 20,607
Actual charge-offs:					
Commercial	2,274	4,323	1,475	436	4,147
Trade finance	—	—	—	—	11
Real estate construction	—	—	—	—	2,438
Real estate mortgage	—	—	1,793	4,243	1,668
Other	—	—	—	—	—
Total charge-offs	2,274	4,323	3,268	4,679	8,264
Less recoveries:					
Commercial	55	985	131	3	366
Trade finance	—	—	—	—	—
Real estate construction	17	26	20	134	2,114
Real estate mortgage	145	732	1,001	4,672	1,421
Other	—	—	—	—	—
Total recoveries	217	1,743	1,152	4,809	3,901
Net loans charged-off	2,057	2,580	2,116	(130)	4,363
Provision for credit losses	5,500	6,400	1,800	3,350	3,250
Balance at end of period	$ 29,921	$ 26,478	$ 22,658	$ 22,974	$ 19,494
Total gross loans and leases at end of period	2,941,093	2,543,549	2,059,392	1,604,149	1,323,431
Average total loans and leases *	2,733,369	2,282,074	1,731,871	1,438,122	1,217,383
Non-performing loans and leases	6,486	7,648	1,987	8,566	14,044
Selected ratios:					
Net charge-offs (recoveries) to average loans and leases	0.08%	0.11%	0.12%	(0.01%)	0.36%
Provision for loan losses to average loans and leases	0.20%	0.28%	0.10%	0.23%	0.27%
Allowance for loan and lease losses to loans and leases at end of period	1.02%	1.04%	1.10%	1.43%	1.47%
Allowance for loan and lease losses to non-performing loans and leases	461.28%	346.22%	1,140.29%	268.19%	138.80%

* Includes average loans held for sale balance of $4 for the year ended December 31, 2017, zero for the years ended December 31, 2016 and December 31, 2015, $3,409 for the year ended December 31, 2014, and $12,495 for the year ended December 31, 2013.

The coverage ratio for the allowance for loan and lease losses to non-performing loans increased to 461.28% at December 31, 2017 from 346.22%. The increase in this coverage ratio was due to the $3.4 million increase in the allowance for loans losses, coupled with the $1.2 million decrease in non-performing loans between periods. Net charge-offs to average loans were 0.08% for the year ended December 31, 2017 compared to 0.11% for the year ended December 31, 2016. See “Critical Accounting Policies,” and “Notes to Consolidated Financial Statements, Note 5.”

In determining our allowance for loan and lease losses, management has considered the credit risk in the various loan and lease categories in our portfolio. As such, the establishment of the allowance for loan and lease losses is based upon our historical net loan and lease loss experience and the other factors discussed above.

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

	At December 31,									
	2017		2016		2015		2014		2013	
	Allocation of the Allowance	Percent of Loans in Each Category in Total Loans	Allocation of the Allowance	Percent of Loans in Each Category in Total Loans	Allocation of the Allowance	Percent of Loans in Each Category in Total Loans	Allocation of the Allowance	Percent of Loans in Each Category in Total Loans	Allocation of the Allowance	Percent of Loans in Each Category in Total Loans
	(Dollars in thousands)									
Real estate mortgage	$15,494	60.2%	$13,578	60.9%	$13,660	62.5%	$11,375	59.3%	$ 9,234	65.9%
Real estate construction	1,902	9.7	1,967	9.2	1,404	6.4	2,846	7.9	1,355	5.5
Commercial	11,590	29.4	10,412	28.8	6,993	29.0	6,621	30.9	4,264	25.6
Trade finance	558	0.7	177	0.9	385	1.9	408	1.9	393	3.0
Consumer & Other	—	0.0	67	0.2	4	0.3	6	0.0	3	0.0
Unallocated	377	0.0	277	0.0	212	0.0	1,718	0.0	4,245	0.0
Total	$29,921	100%	$26,478	100%	$22,658	100%	$22,974	100%	$19,494	100%

Allowance for Losses Related to Undisbursed Loan and Lease Commitments

We maintain a reserve for undisbursed loan and lease commitments. Management estimates the amount of probable incurred losses by applying the loss factors used in our allowance for loan and lease loss methodology to our estimate of the expected usage of undisbursed commitments for each loan and lease type. Provisions for allowance for undisbursed loan and lease commitments are recorded in other expense. The allowance for undisbursed loan and lease commitments totaled $400,000 and $280,000 at December 31, 2017 and 2016, respectively.

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

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

The Bank performs regular impairment analysis on its investment securities portfolio, following FASB standards which provide guidance on: identifying whether a market for an asset or liability is distressed or inactive, determining whether an entity has the intent and ability to hold a security to its anticipated recovery and whether an investment is other-than-temporarily impaired. If it is determined that the impairment is other than temporary for equity securities, the impairment loss is recognized in earnings equal to the difference between the

investment's cost and its fair value. If it is determined that the impairment is other-than-temporary for debt securities, the Bank will recognize the credit component of an other-than-temporary impairment in earnings and the non-credit component in other comprehensive income when the Bank does not intend to sell the security and it is more likely than not that the Bank will not be required to sell the security prior to recovery. The new cost basis is not changed for subsequent recoveries in fair value.

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

Our portfolio of investment securities consists primarily of investment grade corporate notes, U.S. Agency mortgage-backed securities ("MBS"), municipal bonds, collateralized mortgage obligations ("CMOs") and U.S. Government agency securities, and small business administration ("SBA") securities. We have generally categorized our entire securities portfolio as available-for-sale securities. We invest in securities to generate interest income and to maintain a liquid source of funding for our lending and other operations, including withdrawals of deposits. We do not engage in active trading in our investment securities portfolio. While management has the intent and ability to hold all securities until maturity, we have realized and from time to time and again may realize gains from sales of selected securities primarily in response to changes in interest rates. The Bank owns two mortgage-backed securities considered held-to-maturity as of December 31, 2017 with a carrying value of $8.8 million. At December 31, 2017, investment securities classified as available-for-sale with a carrying value of $52.4 million were pledged to secure public deposits.

The carrying value of our held-to-maturity investment securities was $8.8 million at December 31, 2017 and $10.3 million at December 31, 2016. The carrying value of our available-for-sale investment securities at December 31, 2017 totaled $188.2 million compared to $199.8 million at December 31, 2016. The $11.6 million decrease in investment securities available-for-sale during 2017 was primarily due to maturities and principal reductions totaling $23.9 million, offset by $8.3 million in purchases of corporate notes and agency mortgage-backed securities during 2017.

The carrying value of our portfolio of available-for-sale investment securities at December 31, 2017, 2016, and 2015 was as follows:

	Estimated Fair Value At December 31,		
	2017	2016	2015
	(In thousands)		
Mutual funds	$ 4,727	$ 4,772	$ 5,201
Asset-backed securities	4,297	4,388	5,151
Corporate notes	99,622	99,276	66,490
U.S. Agency mortgage-backed securities	26,462	30,889	39,878
Collateralized mortgage obligations	3,745	5,595	10,074
Municipal securities	46,390	50,800	37,080
U.S. Agency principal-only strip securities	1,653	2,200	2,726
SBA Securities	1,307	1,913	2,902
Total securities available-for-sale	$188,203	$199,833	$169,502

The following table shows the maturities of available-for-sale investment securities at December 31, 2017, and the weighted average yields of such securities. The table does not consider the impact of prepayments on the maturities:

	At December 31, 2017									
	Within One Year		After One Year but within Five Years		After Five Years but within Ten Years		After Ten Years		Total	
	Amount	Yield	Amount	Yield	Amount	Yield	Amount	Yield	Amount	Yield
	(Dollars in thousands)									
Asset-backed securities	—	— %	—	— %	—	— %	4,297	2.25%	4,297	2.25%
Corporate notes	—	—	34,450	4.15	62,407	3.99	2,765	3.01	99,622	4.02
U.S. Agency principal-only strips	—	—	—	—	—	—	1,653	0.92	1,653	0.92
U. S. Agency mortgage-backed securities	—	—	296	3.81	8,163	2.17	18,003	2.17	26,462	2.19
Municipal securities	—	—	—	—	1,496	5.88	44,894	4.55	46,390	4.59
Collateralized mortgage obligations	110	4.48	—	—	103	2.81	3,532	2.21	3,745	2.29
SBA securities	147	3.20	77	2.88	1,083	3.19	—	—	1,307	3.17
Mutual Fund	—	—	—	—	—	—	4,727	1.96	4,727	1.96
Total securities available-for-sale	$257	3.74%	$34,823	4.15%	$73,252	3.81%	$79,871	3.50%	$188,203	3.74%

The Bank performs a regular impairment analysis on its investment securities portfolio and management has analyzed all investment securities which have an amortized cost that exceeds fair value as of December 31, 2017.

As of December 31, 2017 the Bank owned 5 corporate securities where the amortized cost exceeded fair value for greater than 12 months. The total amortized cost of these securities was $18.9 million and their fair value was $18.7 million. Management performed an analysis on all of the issuers of these securities which focused on the recent financial results of the companies, capital ratios, debt ratings, and long-term prospects of the issuers and deemed all 5 corporate securities to be temporarily impaired. Management has concluded that the market value decline is a result of the interest rate environment and not credit impairment, and that the fair value of these securities will recover as the macroeconomic environment improves. The intent of the Bank is to hold these securities until a recovery in value, and management has determined that it is not more likely than not that the Bank will be required to sell the securities prior to recovery of the amortized cost basis.

The Bank owns 42 available-for-sale mortgage-backed securities, 4 of which were in an unrealized loss position for longer than 12 months as of December 31, 2017. The total amortized cost of these securities was $8.9 million and the total fair value was $8.7 million. Based on factors including the Bank's intent to hold the securities until a recovery in value and the determination that it is not more likely than not that the Bank will be required to sell the securities prior to recovery of amortized cost basis, management determined that the securities were not other-than-temporarily impaired as of December 31, 2017.

As of December 31, 2017, the Bank owned one asset-backed security ("ABS") where the amortized cost exceeded fair value for greater than 12 months. The total amortized cost of this security was $2.5 million and the total fair value was $2.4 million. Management determined that the ABS was not other-than-temporarily impaired as of December 31, 2017. This determination was made based on several factors such as debt rating of the securities, amount of credit protection, the Bank's intent and ability to hold the security until a recovery in value and the determination that it is not more likely than not that the Bank will be required to sell the security prior to recovery of amortized cost basis.

The Bank owns 80 available-for-sale municipal securities, 33 of which were in an unrealized loss position for longer than 12 months as of December 31, 2017. The total amortized cost of these securities was $20.4 million and the total fair value was $20.1 million. Based on factors including the Bank's intent to hold the securities until a recovery in value and the determination that it is not more likely than not that the Bank will be required to sell the securities prior to recovery of amortized cost basis, management determined that the securities were not other-than-temporarily impaired as of December 31, 2017.

The Bank owns one mutual fund investment, which was in an unrealized loss position for longer than 12 months as of December 31, 2017. The amortized cost of this investment was $5.0 million and the fair value was $4.7 million. This mutual fund invests primarily in short to intermediate maturity U.S. government obligations (i.e. Treasury bonds, notes, and bills and other bonds and obligations guaranteed by the U.S. government) and its decline in value was primarily due to interest rate movements and not any credit related event. Based on this factor and including the Bank's intent to hold the security until a recovery in value and the determination that it is not more likely than not that the Bank will be required to sell the security prior to recovery of amortized cost basis, management determined that the security was not other-than-temporarily impaired as of December 31, 2017.

As of December 31, 2017, the Bank owned one collateralized mortgage obligation ("CMO") where the amortized cost exceeded fair value for greater than 12 months. The total amortized cost of this security was $2.2 million and the total fair value was $2.2 million. Management determined that the CMO were not other-than-temporarily impaired as of December 31, 2017. This determination was made based on several factors such as debt rating of the security, amount of credit protection, the Bank's intent and ability to hold the security until a recovery in value and the determination that it is not more likely than not that the Bank will be required to sell the security prior to recovery of amortized cost basis.

As of December 31, 2017, the Bank owned one U.S. Agency principal-only strip where the amortized cost exceeded fair value for greater than 12 months. The total amortized cost of this security was $1.8 million and the total fair value was $1.7 million. Based on factors including the Bank's intent to hold the security until a recovery in value and the determination that it is not more likely than not that the Bank will be required to sell the security prior to recovery of amortized cost basis, management determined that the security was not other-than-temporarily impaired as of December 31, 2017.

At December 31, 2017, there were a total of 11 and 46 investment securities that were in an unrealized loss position for less than 12 months and for 12 months or greater, respectively. Temporary impairments related to corporate notes, mortgage-backed securities, and municipal securities are primarily attributable to declining market prices caused by lack of trading liquidity in these instruments and in the case of corporate notes, resulted from increases in credit spreads between U.S. Treasuries and corporate bonds subsequent to the date that these securities were purchased. None of the securities in the Bank's investment portfolio rely on an insurance wrap as a credit enhancement. Management believes that it is not probable that the Bank will not receive all amounts due under the contractual terms of these securities. If economic conditions worsen, or if the financial condition of specific issuers within these portfolios deteriorates, then the Bank could record "other-than-temporary" impairment ("OTTI") charges in 2018 on specific investments within these portfolios.

In accordance with Section 939A of the Dodd-Frank Wall Street Reform and Consumer Protection Act, the Bank performs a thorough annual review of each of the investment securities in its portfolio (other than US Government and Agency securities) to determine, among other things, the current financial status of the issuer as well as the issuer's ability to repay the debt. This analysis is performed in addition to the quarterly review that is performed on all investment securities which are in an unrealized loss position.

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

Deposits

Total deposits were $3.26 billion at December 31, 2017 compared to $2.76 billion at December 31, 2016. Noninterest-bearing demand deposits increased $73.2 million or 12.5%. This increase was due to a continued focus on business customers and commercial and industrial loan relationships as the Bank typically requires businesses to have their primary operating accounts at the Bank. The ratio of noninterest-bearing deposits to total deposits was 20.2% at December 31, 2017 and 21.2% at December 31, 2016. Interest-bearing deposits are comprised of interest-bearing demand deposits, money market accounts, regular savings accounts, time deposits of under $250,000 and time deposits of $250,000 or more. Interest-bearing demand and savings deposits increased by $325.3 million or 30.9%, and time deposits increased $100.5 million or 8.9%. The increase in demand and interest-bearing demand deposits is a direct result of management's desire to grow this segment of the deposit base as these deposits are typically related to long-term customer relationships and also carry the lowest interest costs.

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

	Year Ended December 31,					
	2017		2016		2015	
	Average Balance	Average Rate	Average Balance	Average Rate	Average Balance	Average Rate
	(Dollars in thousands)					
Noninterest-bearing deposits	$ 590,036	0.00%	$ 526,344	0.00%	$ 474,856	0.00%
Interest-bearing demand	402,302	0.73	286,323	0.58	177,220	0.56
Money market	794,767	0.62	594,438	0.52	438,583	0.49
Savings	28,926	0.25	30,573	0.25	22,719	0.26
Time certificates of deposit	1,222,879	1.11	1,050,690	1.03	796,344	0.94
Total	$3,038,910	0.71%	$2,488,368	0.63%	$1,909,722	0.56%

Average total deposits increased by $550.5 million in 2017. The increase in average total deposits for 2017 was primarily driven by increases of $172.2 million in average time certificates of deposit, $200.3 million in average money market accounts, $116.0 million in average interest-bearing demand, and $63.7 million in average noninterest-bearing demand between the years.

Although we have increased both demand deposits and money market accounts significantly, over the past three years, the largest single component of our deposits continues to be time certificates of deposit. We market and receive time certificates of deposit from our existing and new high net worth customers, especially from the Chinese communities within our branch network. While we do not attempt to be a market leader in offered interest rates, we attempt to offer competitive rates on these time certificates of deposit within a range offered by other competing banks.

The following table shows the maturities of time certificates of deposit over $250,000 at December 31, 2017 and 2016:

	At December 31,	
	2017	2016
	(In thousands)	
Three months or less	$218,128	$140,865
Over three months through six months	132,465	108,503
Over six months through twelve months	233,131	146,031
Over twelve months	37,924	31,773
Total	$621,648	$427,172

Capital Resources

Current risk-based regulatory capital standards generally require banks to maintain a ratio of "core" or "Tier 1" capital (consisting principally of common equity) to risk-weighted assets of at least 6%, a ratio of only common equity Tier 1 capital to risk-weighted assets of at least 4.5%, a ratio of Tier 1 capital to adjusted total assets (leverage ratio) of at least 4% and a ratio of total capital (which includes Tier 1 capital plus certain forms of subordinated debt, a portion of the allowance for loan and lease losses and preferred stock) to risk-weighted assets of at least 8%. Risk-weighted assets are calculated by multiplying the balance in each category of assets by a risk factor, which ranges from zero for cash assets and certain government obligations to 100% for some types of loans, and adding the products together.

Our goal is to exceed the minimum regulatory capital requirements for well capitalized institutions. At December 31, 2017 and 2016, our capital ratios were above the minimum requirements for well capitalized institutions. On a quarterly basis, we perform a stress test on our capital to determine our level of capital in various economic circumstances looking out twenty-four months into the future.

	At December 31, 2017	At December 31, 2016
Leverage Ratio		
Preferred Bank	9.52%	9.43%
Minimum requirement for "Well Capitalized" institution	5.00%	5.00%
Common Equity Tier 1 Risk-Based Capital Ratio		
Preferred Bank	10.07%	9.83%
Minimum requirement for "Well Capitalized" institution	6.50%	6.50%
Tier 1 Risk-Based Capital Ratio		
Preferred Bank	10.07%	9.83%
Minimum requirement for "Well Capitalized" institution	8.00%	8.00%
Total Risk-Based Capital Ratio		
Preferred Bank	13.83%	14.09%
Minimum requirement for "Well Capitalized" institution	10.00%	10.00%

The final rules implementing Basel Committee on Banking Supervision's capital guidelines for U.S. banks ("Basel III rules") became effective for the Bank on January 1, 2015 with full compliance with all of the requirements being phased in over a multi-year schedule, and fully phased in by January 1, 2019. Under the Basel III rules, the Bank must hold a capital conversation buffer above the adequately capitalized risk-based capital ratios. The capital conservation buffer is being phased in from 0.0% for 2015 to 2.50% by 2019. The required capital conservation buffer for 2017 is 1. 25%. The Bank's capital conservation buffer was 4.07% as of December 31, 2017. Management believes that as of December 31, 2017 the Bank meets all capital adequacy requirements to which it is subject.

On October 3, 2017, the Bank entered into an Equity Distribution Agreement (the "Distribution Agreement") with FBR Capital Markets & Co., Raymond James & Associates, Inc., and Sandler O'Neill & Partners, L.P., (collectively, the "Distribution Agents") to sell shares of the Bank's common stock, no par value per share (the "ATM Shares"), having an aggregate offering price of up to $50,000,000, from time to time, through an "at the market offering" program (the "ATM Program").

The sales may be made in negotiated transactions or transactions that are deemed to be "at the market offerings" as defined in Rule 415 under the Securities Act of 1933, as amended (the "Securities Act"). Subject to the terms and conditions of the Distribution Agreement, upon its acceptance of written instructions from the Bank, the Distribution Agent designated by the Bank to sell ATM Shares will use its commercially reasonable efforts to sell on the Banks's behalf all of the designated ATM Shares requested to be sold by us. The Bank may also sell ATM Shares under the Distribution Agreement to each of the Distribution Agents, as principals for their

respective accounts, at a price per share agreed upon at the time of sale. Actual sales will depend on a variety of factors to be determined by the Bank from time to time. The Bank has no obligation to sell any of the ATM Shares under the Distribution Agreement, and may at any time suspend sales of the ATM Shares under the Distribution Agreement.

The Bank will pay the Distribution Agents commissions for their services in acting as agent in the sale of ATM Shares, and the Company has agreed to advance $90,000 to the Distribution Agents for their out-of-pocket legal fees incurred in connection with the ATM Program. The Distribution Agents will be entitled to compensation at a commission rate equal to 2.0% of the gross proceeds from the sale of ATM Shares pursuant to the Distribution Agreement; provided, however, that the compensation payable to each Distribution Agent upon the sale of ATM Shares pursuant to the Distribution Agreement will be reduced by $30,000 in a manner such that no compensation will be paid to a Distribution Agent until the amount of the commission earned by such Distribution Agent exceeds $30,000.

The Distribution Agreement contains representations and warranties and covenants that are customary for transactions of this type. In addition, the Bank has agreed to indemnify the Distribution Agents against certain liabilities on customary terms, subject to limitations on such arrangements imposed by applicable law and regulation. In the ordinary course of its business, the Distribution Agents and/or their affiliates have engaged and may engage in commercial and investment banking transactions, financial advisory and other transactions with the Bank. The Distribution Agents have received, or may receive, customary compensation and expenses in connection with such other transactions.

During the fourth quarter of 2017, we commenced sales of common stock through the ATM Program. The details of the shares of common stock sold through the ATM Program during the fourth quarter of 2017 are as follows:

Month	Number of Shares Sold	Weighted Average Price	Net Proceeds
(in thousands, except share and per share amounts)			
October 2017	286,203	$61.07	$17,160
November 2017	103,285	$62.94	6,370
December 2017	152,487	$62.36	9,319
Total	541,975	$61.79	$32,849

As of December 31, 2017, the remaining dollar value of common stock we had available to sell under the ATM Program was $16.5 million. The actual number of shares of our common stock, if any, that may be sold under the ATM Program in the future will depend upon the sale price for such shares.

Contractual Obligations and Off-Balance Sheet Arrangements

The following table presents our contractual cash obligations, excluding deposits and unrecognized tax benefits, as of December 31, 2017:

Contractual Obligations[1]	Amount of Commitment Expiring per Period				
	Total Amounts Committed	Less Than 1 year	1-3 Years	3-5 Years	After 5 Years
	(In thousands)				
Operating lease obligations	$ 16,642	$3,358	$5,903	$3,911	$ 3,470
Data processing service agreements	6,867	1,371	1,985	2,001	1,510
FHLB advances	6,334	5,000	1,334	—	—
Subordinated debt	100,000	—	—	—	100,000
Total	$129,843	$9,729	$9,222	$5,912	$104,980

(1) Contractual obligations do not include interest.

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

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

The following table presents these off-balance sheet arrangements at December 31, 2017:

	Amount of off-balance sheet Expiring per Period				
Off-balance sheet arrangements	**Total Amounts Committed**	**Less Than 1 year**	**1-3 Years**	**3-5 Years**	**After 5 Years**
			(In thousands)		
Commitments to extend credit	$828,218	$438,817	$278,549	$101,467	$ 9,385
Commercial letters of credit	5,328	5,328	—	—	—
Standby letter of credit	138,920	87,626	18,280	3,975	29,039
Total	$972,466	$531,771	$296,829	$105,442	$38,424

Liquidity

Based on our existing business plan, we believe that our level of liquid assets is sufficient to meet our current and presently anticipated funding needs for at least the next twelve months. We rely on deposits as the principal source of funds and, therefore, must be in a position to service depositors' needs as they arise. We attempt to maintain a loan-to-deposit ratio below approximately 95%. Our loan-to-deposit ratio was 90.1% at December 31, 2017 compared to 92.0% at December 31, 2016.

Borrowings from the FHLB are another source of funding for our loan and investment activities. At December 31, 2017, we had $6.4 million of outstanding FLHB borrowings, and we could additionally borrow up to $305.1 million with collateral of specifically identified loans and securities. In addition, we have pledged securities with a fair value of $134.3 million at the Federal Reserve Discount Window which we may borrow from on an overnight basis. We have one uncommitted fed funds line with a financial institution for $25.0 million. As an additional condition of borrowing from the FHLB, we are required to purchase FHLB stock. For the year ended December 31, 2017, the Bank was required to maintain the minimum stock requirement of $11.1 million of FHLB stock based on the volume of "membership assets" as defined by the FHLB. At December 31, 2017, the Bank held $11.1 million in FHLB stock. For the years ended December 31, 2017 and 2016, dividends from the FHLB totaled $0.9 million and $1.0 million, respectively, representing an average yield of 8.52% and 11.87%, respectively.

We also attempt to maintain a liquidity ratio (liquid assets, including cash and due from banks, federal funds sold and investment securities not pledged as collateral expressed as a percentage of total deposits) above approximately 18%. Our liquidity ratios were 32% at December 31, 2017 and 22% at December 31, 2016. We believe that in the event the level of liquid assets (our primary liquidity) does not meet our liquidity needs, other available sources of liquid assets (our secondary liquidity), including the sales of securities under agreements to repurchase, sales of unpledged investment securities or loans, utilizing the discount window borrowings from the Federal Reserve Bank as well as borrowing from the FHLB could be employed to meet those funding needs. We have a Contingency Funding Plan which is reviewed annually by the Board of Directors which sets forth actions to be taken in the event that our liquidity ratios fall below Board-established guidelines. We also perform

quarterly liquidity stress tests to review various adverse scenarios. Although we believe that our funding resources will be more than adequate to meet our obligations, we cannot be certain of this adequacy if economic deterioration or other negative events occur that could impair our ability to meet our funding obligations.

Quantitative and Qualitative Disclosures about Market Risk

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

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

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

Market Value of Portfolio Equity

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

The following table presents forecasted changes in net portfolio value using a base market rate and the estimated change to the base scenario given an immediate and sustained upward movement in interest rates of 100, 200, 300 and 400 basis points and an immediate and sustained downward movement in interest rates of 100 and 300 basis points at December 31, 2017.

Market Value of Portfolio Equity

Interest Rate Scenario	Market Value	Percentage Change from Base	Percentage of Total Assets	Percentage of Portfolio Equity Book Value
		(Dollars in thousands)		
Up 400 basis points	$768,468	33.85%	20.82%	216.45%
Up 300 basis points	$728,383	26.87%	19.64%	205.16%
Up 200 basis points	$683,044	18.97%	18.33%	192.39%
Up 100 basis points	$631,964	10.08%	16.89%	178.00%
Base	$574,108	— %	15.27%	161.71%
Down 100 basis points	$517,407	(9.88%)	13.64%	145.73%
Down 300 basis points	$431,552	(24.83%)	11.18%	121.55%

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

Net Interest Income

In order to measure interest rate risk at December 31, 2017, we used a simulation model to project changes in net interest income that result from forecasted changes in interest rates. This analysis calculates the difference between net interest income forecasted using a rising and a falling interest rate scenario and a net interest income forecast using a base market interest rate derived from the current treasury yield curve. The income simulation model includes various assumptions regarding the re-pricing relationships for each of our products. Many of our assets are floating rate loans, which are assumed to re-price immediately, and to the same extent as the change in market rates according to their contracted index. Some loans and investment vehicles include the opportunity of prepayment (embedded options), and accordingly the simulation model uses national indexes to estimate these prepayments and reinvest their proceeds at current yields. Non-term deposit products reprice more slowly, usually changing less than the change in market rates and at management discretion.

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

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

Sensitivity of Net Interest Income December 31, 2017

Interest Rate Scenario	Adjusted Net Interest Income	Percentage Change from Base	Net Interest Margin Percent	Net Interest Margin Change
	(Dollars in thousands)			
Up 400 basis points	$236,208	63.56%	6.20%	2.39
Up 300 basis points	$213,457	47.81%	5.61%	1.80
Up 200 basis points	$190,526	31.93%	5.02%	1.20
Up 100 basis points	$167,460	15.96%	4.42%	0.60
Base	$144,412	— %	3.82%	—
Down 100 basis points	$130,210	(9.83)%	3.44%	(0.37)
Down 300 basis points	$127,667	(11.60)%	3.38%	(0.44)

Inflation

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

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES OF MARKET RISKS

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

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

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

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

None.

ITEM 9A. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

As of December 31, 2017, we carried out an evaluation, under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures and internal controls over financial reporting pursuant to SEC rules, as such rules are adopted by the FDIC. Based upon that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were effective as of December 31, 2017. We believe that the financial statements in this Annual Report on Form 10-K fairly present, in all material respects, our financial position, results of operations and cash flows for the periods presented in conformity with U.S. generally accepted accounting principles.

Management's Report on Internal Control over Financial Reporting

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

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

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

Management under the supervision and with the participation of the Bank's principal executive officer and principal financial officer assessed the effectiveness of the Bank's internal control over financial reporting as of December 31, 2017. Management based this assessment on criteria for effective internal control over financial reporting described in *Internal Control-Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission. Management's assessment included an evaluation of the design of the Bank's internal control over financial reporting and testing of the operational effectiveness of its internal control over financial reporting. Management reviewed the results of its assessment with the Audit Committee of our Board of Directors. Based on this evaluation, management determined that the Bank's system of internal controls over financial reporting was effective as of December 31, 2017. Crowe Horwath LLP, an independent registered public accounting firm, has issued its report on the effectiveness of internal control over financial reporting as of December 31, 2017.

Report of Independent Registered Public Accounting Firm

Shareholders and the Board of Directors of Preferred Bank
Los Angeles, California

Opinion on Internal Control over Financial Reporting

We have audited Preferred Bank's (the "Bank") internal control over financial reporting as of December 31, 2017, based on criteria established in Internal Control—Integrated Framework: (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). In our opinion, the Bank maintained, in all material respects, effective internal control over financial reporting as of December 31, 2017, based on criteria established in Internal Control—Integrated Framework: (2013) issued by COSO.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States) ("PCAOB"), the consolidated balance sheets of the Bank as of December 31, 2017 and 2016, the related consolidated statements of operations and comprehensive income, changes in shareholders' equity, and cash flows for each of the years in the three-year period ended December 31, 2017, and the related notes (collectively referred to as the "financial statements") and our report dated March 14, 2018 expressed an unqualified opinion.

Basis for Opinion

The Bank's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management's Report on Internal Control over Financial Reporting. Our responsibility is to express an opinion on the Bank's internal control over financial reporting based on our audit. We are a public accounting firm registered with the Public Company Accounting Oversight Board (United States) ("PCAOB") and are required to be independent with respect to the Bank in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

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

Definition and Limitations of Internal Control over Financial Reporting

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

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that

controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

/s/ Crowe Horwath LLP

Los Angeles, California
March 14, 2018

ITEM 9B. OTHER INFORMATION

None

PART III

ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE

Information concerning directors and executive officers of the Bank, to the extent not included under "Item 1 under the heading "*Executive Officers of the Bank*", will appear in the Bank's definitive proxy statement for the 2018 Annual Meeting of Shareholders (the "2018 Proxy Statement"), and such information either shall be (i) deemed to be incorporated herein by reference from the section entitled "ELECTION OF DIRECTORS" AND "SECTION 16(a) BENEFICIAL OWNERSHIP REPORTING COMPLIANCE" and "THE COMMITTEES OF THE BOARD," if filed with the Federal Deposit Insurance Corporation pursuant to Regulation 14A not later than 120 days after the end of the Bank's most recently completed fiscal year or (ii) included in an amendment to this Annual Report filed with the Federal Deposit Insurance Corporation on Form 10-K/A not later than the end of such 120 day period.

Code of Ethics

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

ITEM 11. EXECUTIVE COMPENSATION

Information concerning executive compensation will appear in the 2018 Proxy Statement, and such information either shall be (i) deemed to be incorporated herein by reference from the sections entitled "COMPENSATION COMMITTEE INTERLOCKS AND INSIDER PARTICIPATION," "COMPENSATION COMMITTEE'S REPORT," "COMPENSATION DISCUSSION AND ANALYSIS," "SUMMARY COMPENSATION TABLE," "OUTSTANDING EQUITY AWARDS, " "NON-QUALIFIED DEFERRED COMPENSATION," "CHANGE OF CONTROL AGREEMENTS, " and "COMPENSATION OF DIRECTORS," if filed with the Federal Deposit Insurance Corporation pursuant to Regulation 14A not later than 120 days after the end of the Bank's most recently completed fiscal year or (ii) included in an amendment to this Annual Report filed with the Federal Deposit Insurance Corporation on Form 10-K not later than the end of such 120 day period.

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

Information concerning security ownership of certain beneficial owners and management and information related to the Bank's equity compensation plans will appear in the 2018 Proxy Statement, and such information either shall be (i) deemed to be incorporated herein by reference from the sections entitled "SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT" and "EQUITY COMPENSATION PLANS," if filed with the Federal Deposit Insurance Corporation pursuant to Regulation 14A not later than 120 days after the end of the Bank's most recently completed fiscal year or (ii) included in an amendment to this Annual Report filed with the Federal Deposit Insurance Corporation on Form 10-K/A not later than the end of such 120 day period.

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

Information concerning certain relationships and related transactions will appear in the 2018 Proxy Statement, and such information either shall be (i) deemed to be incorporated herein by reference from the section entitled "CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS and "BOARD INDEPENDENCE," if filed with the Federal Deposit Insurance Corporation pursuant to Regulation 14A not later

than 120 days after the end of the Bank's most recently completed fiscal year, or (ii) included in an amendment to this Annual Report filed with the Federal Deposit Insurance Corporation on Form 10-K/A not later than the end of such 120 day period.

ITEM 14. PRINCIPAL ACCOUNTING FEES AND SERVICES

Information concerning principal accountant fees and services will appear in the 2018 Proxy Statement, and such information either shall be (i) deemed to be incorporated herein by reference from the section entitled "INDEPENDENT AUDITOR FEES," and "AUDIT COMMITTEE PRE-APPROVAL POLICY" if filed with the Federal Deposit Insurance Corporation pursuant to Regulation 14A not later than 120 days after the end of the Bank's most recently completed fiscal year or (ii) included in an amendment to this Annual Report filed with the Federal Deposit Insurance Corporation on Form 10-K/A not later than the end of such 120 day period.

PART IV

ITEM 15. EXHIBITS, FINANCIAL STATEMENT SCHEDULES

(a)(1) Financial Statements

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(a)(2) Financial Statement Schedules

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

(a)(3) Exhibits

Exhibit No.	Exhibit Description
1.1	Equity Distribution Agreement dated October 3, 2017, by and among Preferred Bank, FBR Capital Markets & Co., Raymond James & Associates, Inc., and Sandler O'Neill & Partners, L.P. (9)
3.1	Amended and Restated Articles of Incorporation(4)
3.2	Certificate of Determination of the Series A Preferred Stock(2)
3.3	Certificate of Amendment of Amended and Restated Articles of Incorporation
3.4	Agreement of Merger by and between Preferred Bank and United International Bank
3.5	Amended and Restated Bylaws(7)
4.1	Common Stock Certificate(3)
4.2	Form of Subordinated Note(5)
4.3	Form of Subordinated Note(5)
4.4	Form of Subordinated Note(5)
10.1*	1992 Stock Option Plan(4)
10.2*	Management Incentive Bonus Plan(4)
10.3*	Deferred Compensation Plan(4)
10.4*	Stock Option Gain Deferred Compensation Plan(4)
10.5*	2004 Equity Incentive Plan(4)
10.6*	2014 Equity Incentive Plan(1)
10.7*	Form of Indemnification Agreement for directors and executive officers(4)
10.8*	Revised Bonus Plan(1)
10.9*	Deferred Compensation Plan-Deferred Stock Unit Agreement and Rabbi Trust
10.10*	Retention and Severance Agreement-Li Yu(1)
10.11	Board of Directors resolution dated December 16, 2014 terminating Deferred Compensation Plan(8)
10.12	Form of Subordinated Note Purchase Agreement(5)
10.13	Form of Subordinated Note Purchase Agreement(5)
10.14	Form of Subordinated Note Purchase Agreement(5)
16.1	Letter from KPMG LLP dated March 30, 2016 (6)
21.1	Subsidiary of Preferred Bank
31.1	Chief Executive Officer Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
31.2	Chief Financial Officer Certification Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
32.1	Chief Executive Officer Certification Pursuant to 18 U.S.C. Section 1350, As Adopted Pursuant To Section 906 of the Sarbanes-Oxley Act of 2002
32.2	Chief Financial Officer Certification Pursuant to 18 U.S.C. Section 1350, As Adopted Pursuant To Section 906 of the Sarbanes-Oxley Act of 2002

(1) Incorporated by reference from Registrant's Registration Statement on Form 10-K filed with the Federal Deposit Insurance Corporation on March 16, 2015.
(2) Incorporated by reference from Registrant's Current Report on Form 8-K filed with the Federal Deposit Insurance Corporation on June 23, 2010.
(3) Incorporated by reference from Registrant's Registration Statement on Form 10 Amendment No. 1 filed with the Federal Deposit Insurance Corporation on February 2, 2005.
(4) Incorporated by reference from Registrant's Registration Statement on Form 10 filed with the Federal Deposit Insurance Corporation on January 18, 2005.
(5) Incorporated by reference from Registrant's Quarterly Report on Form 10-Q filed with the Federal Deposit Insurance Corporation on November 9, 2016.
(6) Incorporated by reference from Registrant's Current Report on Form 8-K/A filed with the Federal Deposit Insurance Corporation on April 8, 2016.
(7) Incorporated by reference from Registrant's Annual Report on Form 10-K filed with the Federal Deposit Insurance Corporation on March 15, 2017.
(8) Incorporated by reference from Registrant's Annual Report on Form 10-K filed with the Federal Deposit Insurance Corporation on March 24, 2016.
(9) Incorporated by reference from Registrant's Current Report on Form 8-K filed with the Federal Deposit Insurance Corporation on October 3, 2017.
* Denotes management contract or compensatory plan or arrangement.

Report of Independent Registered Public Accounting Firm

Shareholders and the Board of Directors of Preferred Bank
Los Angeles, California

Opinion on the Financial Statements

We have audited the accompanying consolidated balance sheets of Preferred Bank (the “Bank”) as of December 31, 2017 and 2016, the related consolidated statements of operations and comprehensive income, changes in shareholders’ equity, and cash flows for each of the three years in the period ended December 31, 2017, and the related notes (collectively referred to as the “financial statements”). In our opinion, the financial statements present fairly, in all material respects, the financial position of the Bank as of December 31, 2017 and 2016, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2017, in conformity with accounting principles generally accepted in the United States of America.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States) (“PCAOB”), the Bank’s internal control over financial reporting as of December 31, 2017, based on criteria established in Internal Control—Integrated Framework: (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) and our report dated March 14, 2018 expressed an unqualified opinion.

Basis for Opinion

These financial statements are the responsibility of the Bank’s management. Our responsibility is to express an opinion on the Bank’s financial statements based on our audits. We are a public accounting firm registered with the Public Company Accounting Oversight Board (United States) (“PCAOB”) and are required to be independent with respect to the Bank in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether due to error or fraud. Our audits included performing procedures to assess the risks of material misstatement of the financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the financial statements. We believe that our audits provide a reasonable basis for our opinion.

/s/ Crowe Horwath LLP

We have served as the Bank’s auditor since 2016.

Los Angeles, California
March 14, 2018

Report of Independent Registered Public Accounting Firm

The Board of Directors and Shareholders
Preferred Bank:

We have audited the accompanying consolidated statements of operations and comprehensive income, shareholders' equity, and cash flows of Preferred Bank for the year ended December 31, 2015. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audit.

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

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the results of operations and the cash flows of Preferred Bank for the year ended December 31, 2015, in conformity with U.S. generally accepted accounting principles.

/s/ KPMG LLP

Los Angeles, California
March 14, 2018

PREFERRED BANK

Consolidated Statements of Financial Condition
December 31, 2017 and 2016
(In thousands, except for shares)

	2017	2016
Assets		
Cash and due from banks	$ 446,822	$ 306,330
Federal funds sold	108,500	97,500
Cash and cash equivalents	555,322	403,830
Securities held-to-maturity, at amortized cost (with fair value of $8,499 and $10,021 at December 31, 2017 and 2016, respectively)	8,780	10,337
Securities available-for-sale, at fair value	188,203	199,833
Loans and leases	2,941,093	2,543,549
Less allowance for loan and lease losses	(29,921)	(26,478)
Less unamortized deferred loan fees, net	(3,099)	(1,682)
Net loans and leases	2,908,073	2,515,389
Loans held for sale, at lower of cost or fair value	440	—
Other real estate owned	4,112	4,112
Customers' liability on acceptances	7,272	772
Bank furniture and fixtures, net	5,684	5,313
Bank-owned life insurance	9,066	8,825
Accrued interest receivable	11,291	9,550
Investment in affordable housing partnerships	34,708	23,670
Federal Home Loan Bank ("FHLB") stock, at cost	11,077	9,331
Net deferred tax assets	17,476	26,605
Income tax receivable	2,713	—
Other assets	5,642	4,031
Total assets	$3,769,859	$3,221,598
Liabilities and Shareholders' Equity		
Deposits:		
Demand	$ 659,487	$ 586,272
Interest-bearing demand	1,353,974	1,019,058
Savings	24,429	34,067
Time certificates of $250,000 or more	621,648	427,172
Other time certificates	603,152	697,155
Total deposits	3,262,690	2,763,724
Acceptances outstanding	7,272	772
Advances from Federal Home Loan Bank	6,401	26,516
Subordinated debt issuance, net of unamortized costs and premium of $1.0 million and $1.2 million at December 31, 2017 and 2016, respectively	98,963	98,839
Accrued interest payable	3,833	3,199
Commitments to fund investment in affordable housing partnership	18,523	10,632
Other liabilities	17,143	19,851
Total liabilities	3,414,825	2,923,533
Commitments and Contingencies—Note 11		
Shareholders' equity:		
Preferred stock. Authorized 25,000,000 shares; no shares issued and outstanding at December 31, 2017 and 2016.	—	—
Common stock, no par value. Authorized 100,000,000 shares; issued and outstanding 15,122,313 and 14,232,907 shares at December 31, 2017 and 2016, respectively.	207,948	169,861
Treasury stock, at cost 430,922 and 158,749 shares at December 31, 2017 and 2016, respectively.	(33,233)	(19,115)
Additional paid-in capital	39,462	39,929
Retained earnings	139,684	108,261
Accumulated other comprehensive income (loss):		
Unrealized gain (loss) on securities available-for-sale, net of tax of $504 and $(632) at December 31, 2017 and December 31, 2016, respectively.	1,173	(871)
Total shareholders' equity	355,034	298,065
Total liabilities and shareholders' equity	$3,769,859	$3,221,598

See accompanying notes to the consolidated financial statements.

PREFERRED BANK

Consolidated Statements of Operations and Comprehensive Income
Years Ended December 31, 2017, 2016 and 2015
(In thousands, except share and per share data)

	2017	2016	2015
Interest income:			
Loans and leases	$ 144,678	$ 114,148	$ 88,235
Investment securities, available for sale	11,792	8,292	6,304
Federal funds sold	1,130	473	163
Total interest income	157,600	122,913	94,702
Interest expense:			
Interest-bearing demand	7,901	4,730	3,160
Savings	72	76	59
Time certificates of $250,000 or more	5,907	3,423	2,285
Other time certificates	7,726	7,432	5,170
FHLB borrowings	167	259	182
Subordinated debt	6,123	2,814	—
Total interest expense	27,896	18,734	10,856
Net interest income before provision for credit losses	129,704	104,179	83,846
Provision for credit losses	5,500	6,400	1,800
Net interest income after provision for credit losses	124,204	97,779	82,046
Noninterest income:			
Fees and service charges on deposit accounts	1,269	1,212	1,178
Letter of credit fee income	2,635	2,371	1,630
BOLI income	351	346	339
Net gain on sale or call of investment securities	4	169	—
Other	1,565	1,361	745
Total noninterest income	5,824	5,459	3,892
Noninterest expense:			
Salaries and employee benefits	30,041	25,813	20,960
Net occupancy expense	4,942	4,830	3,681
Business development and promotion expense	883	845	593
Professional services	4,390	5,297	4,906
Office supplies and equipment expense	1,340	1,422	1,119
OREO related expense, net	563	825	(480)
Other	7,389	4,506	4,931
Total noninterest expense	49,548	43,538	35,710
Income before income taxes	80,480	59,700	50,228
Income tax expense	37,086	23,331	20,485
Net income	$ 43,394	$ 36,369	$ 29,743
Income allocated to participating shares	(361)	(428)	(410)
Dividends allocated to participating shares	(138)	(119)	(126)
Net income available to common shareholders	$ 42,895	$ 35,822	$ 29,207
Other comprehensive income (loss):			
Unrealized net gain (loss) on securities available-for-sale	3,180	(3,028)	(1,644)
Less reclassification adjustments included in net income	—	169	—
Other comprehensive (loss) income, before tax	3,180	(3,197)	(1,644)
Income tax (benefit) related to items of other comprehensive income (loss)	1,344	(1,344)	(691)
Other comprehensive income (loss), net of tax	1,836	(1,853)	(953)
Comprehensive income	$ 45,230	$ 34,516	$ 28,790
Net income per share			
Basic	$ 2.97	$ 2.58	$ 2.17
Diluted	$ 2.96	$ 2.56	$ 2.14
Weighted-average common shares outstanding			
Basic	14,438,964	13,883,497	13,484,216
Diluted	14,492,671	13,987,257	13,677,892
Dividends per share	$ 0.80	$ 0.63	$ 0.51

See accompanying notes to the consolidated financial statements.

PREFERRED BANK

Consolidated Statements of Changes in Shareholders' Equity
Years Ended December 31, 2017, 2016 and 2015
(In thousands, except share and dividends declared per share data)

	Preferred Stock	Common Stock Shares	Common Stock Amount	Treasury Stock	Additional Paid-In Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total Shareholders' Equity
Balance as of January 1, 2015	$—	13,503,458	$164,023	$(19,115)	$29,631	$ 58,552	$ 1,935	$235,026
Cash dividend declared ($0.51 per share)	—	—	—	—	—	(7,032)	—	(7,032)
Stock dividend accrued for deferred stock unit	—	—	—	—	217	(217)	—	—
Restricted stock awards	—	128,400	—	—	3,207	—	—	3,207
Restricted stock award forfeitures	—	(4,232)	—	—	—	—	—	—
Share-based compensation	—	—	—	—	781	—	—	781
Stock options exercised	—	257,316	2,537	—	—	—	—	2,537
Tax effect of stock plans, net	—	—	—	—	836	—	—	836
Net income	—	—	—	—	—	29,743	—	29,743
Other comprehensive income (loss), net of tax	—	—	—	—	—	—	(953)	(953)
Balance as of December 31, 2015	$—	13,884,942	$166,560	$(19,115)	$34,672	$ 81,046	$ 982	$264,145
Cash dividend declared ($0.63 per share)	—	—	—	—	—	(8,959)	—	(8,959)
Stock dividend accrued for deferred stock unit	—	—	—	—	195	(195)	—	—
Restricted stock awards	—	117,769	—	—	3,188	—	—	3,188
Restricted stock award forfeitures	—	(200)	—	—	—	—	—	—
Share-based compensation	—	—	—	—	532	—	—	532
Stock options exercised	—	230,396	3,301	—	—	—	—	3,301
Tax effect of stock plans, net	—	—	—	—	1,342	—	—	1,342
Net income	—	—	—	—	—	36,369	—	36,369
Other comprehensive income (loss), net of tax	—	—	—	—	—	—	(1,853)	(1,853)
Balance as of December 31, 2016	$—	14,232,907	$169,861	$(19,115)	$39,929	$108,261	$ (871)	$298,065
Cash dividend declared ($0.80 per share)	—	—	—	—	—	(11,763)	—	(11,763)
Final distribution of deferred compensation plan	—	437,254	3,154	—	(3,154)	—	—	—
Issuance of common stock	—	541,975	33,489	—	—	—	—	33,489
Common stock issuance cost	—	—	—	—	(939)	—	—	(939)
Restricted stock award grant	—	92,000	—	—	3,585	—	—	3,585
Restricted stock award forfeitures	—	(1,875)	—	—	—	—	—	—
Share-based compensation	—	—	—	—	41	—	—	41
Stock options exercised	—	90,350	1,444	—	—	—	—	1,444
Stock surrendered due to employee tax liability	—	(270,298)	—	(14,118)	—	—	—	(14,118)
Net income	—	—	—	—	—	43,394	—	43,394
Impact of change in enacted tax rate	—	—	—	—	—	(208)	208	—
Other comprehensive income (loss), net of tax	—	—	—	—	—	—	1,836	1,836
Balance as of December 31, 2017	$—	15,122,313	$207,948	$(33,233)	$39,462	$139,684	$ 1,173	$355,034

PREFERRED BANK

Consolidated Statements of Cash Flows
Years Ended December 31, 2017, 2016 and 2015
(In thousands)

	2017	2016	2015
Cash flows from operating activities:			
Net income	$ 43,394	$ 36,369	$ 29,743
Adjustments to reconcile net income to net cash provided by operating activities:			
Provision for credit losses	5,500	6,400	1,800
Amortization of deferred loan fees, net	(3,265)	(2,512)	(1,505)
Gain on sale and call of securities available-for-sale	(4)	(169)	—
Amortization of investment securities discounts and premiums, net	731	625	545
Amortization of investment in affordable housing partnerships	3,962	2,382	1,947
Amortization of premium on borrowings	(171)	(119)	—
Amortization of subordinated debt issuance costs	180	—	—
Loans originated for sale	(440)	—	—
Depreciation and amortization	990	929	623
Share-based compensation expense	3,626	2,378	3,153
Benefit from bank owned life insurance	(241)	(62)	(238)
Deferred tax (benefit) expense	7,784	(1,458)	(1,755)
Change in income taxes (payable) receivable	(2,713)	1,641	536
Net gain on sale of other real estate owned	—	—	(325)
Change in accrued interest receivable and other assets	(3,352)	348	(7,647)
Change in accrued interest payable and other liabilities	(2,801)	5,874	1,360
Net cash provided by operating activities	53,180	52,626	28,237
Cash flows from investing activities:			
Acquisitions, net of cash paid	—	—	3,115
Proceeds from maturities and redemptions of securities held-to-maturity	1,428	1,260	1,789
Proceeds from maturities and redemptions of securities available-for-sale	22,474	24,385	5,792
Purchase of securities held-to-maturity	—	(5,905)	—
Purchase of securities available-for-sale	(8,262)	(58,230)	(26,748)
Purchase of investments in affordable housing partnerships	(7,109)	(3,326)	(4,193)
Purchase of FHLB stock	(1,746)	(2,169)	(1,007)
Proceeds from sale of other real estate owned	—	—	9,136
Proceeds from recoveries of written off loans	218	1,743	1,152
Net increase in loans	(395,137)	(487,298)	(460,206)
Purchase of bank premises and equipment	(1,360)	(641)	(2,092)
Net cash used in investing activities	(389,494)	(530,181)	(473,262)
Cash flows from financing activities:			
Increase in deposits	498,966	477,166	510,300
Issuance of subordinated debt	—	100,531	—
Increase in subordinated debt issuance cost	—	(1,692)	—
(Decrease) increase in other borrowings	(20,000)	—	6,635
Proceeds from issuance of stock, net	32,550	—	—
Treasury shares repurchased	(14,118)	—	—
Excess tax benefit from share-based payment arrangement	—	1,342	836
Cash dividends paid	(11,036)	(8,438)	(6,302)
Proceeds from the exercise of stock options	1,444	3,301	2,537
Net cash provided by financing activities	487,806	572,210	514,006
Net increase in cash and cash equivalents	151,492	94,655	68,981
Cash and cash equivalents at beginning of year	403,830	309,175	240,194
Cash and cash equivalents at end of year	555,322	403,830	309,175
Supplemental disclosure of cash flow information			
Cash paid during the period for:			
Interest	$ 27,262	$ 17,454	$ 10,356
Income taxes	$ 29,596	$ 19,155	$ 19,650
Noncash activities:			
Real estate acquired in settlement of loans	$ —	$ —	$ 4,112
Common stock dividend declared, but not paid	$ 3,331	$ 2,604	$ 2,083

See accompanying notes to consolidated financial statements.

(1) Summary of Significant Accounting Policies

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

(a) Basis of Presentation

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

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

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

(b) Principles of Consolidation

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

(c) Cash and Cash Equivalents

Cash and cash equivalents include cash on hand and cash due from banks, and federal funds sold, all of which have original or purchased maturities of less than 90 days.

(d) Investment Securities

The Bank classifies its debt and equity securities in two categories: held-to-maturity or available-for-sale. Securities that could be sold in response to changes in interest rates, increased loan demand, liquidity needs, capital requirements, or other similar factors are classified as securities available-for-sale. These securities are carried at fair value. Unrealized holding gains or losses, net of the related tax effect, on available-for-sale securities are excluded from income and are reported as a separate component of shareholders' equity as other comprehensive income net of applicable taxes until realized. Realized gains and losses from the sale of available-for-sale securities are determined on a specific-identification basis. Securities classified as held-to-maturity are those that the Bank has the positive intent and ability to hold until maturity. These securities are carried at amortized cost, adjusted for the amortization or accretion of premiums or discounts. At December 31, 2017 and 2016, there were $8.8 million and $10.3 million, respectively, classified in the held-to-maturity portfolio.

At each reporting date, the Bank performs an impairment analysis on its investment securities portfolio, following FASB standards in identifying whether a market for an asset or liability is distressed or inactive,

determining whether an entity has the intent and ability to hold a security to its anticipated recovery and whether an investment is other-than-temporarily-impaired. If it is determined that the impairment is other-than-temporary for debt securities, the Bank will recognize the credit component of an other-than-temporary impairment in earnings and the non-credit component in other comprehensive income when the Bank does not intend to sell the security and it is more likely than not that the Bank will not be required to sell the security prior to recovery. The new cost basis is not changed for subsequent recoveries in fair value.

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

(e) Loans and Loan Origination Fees and Costs

Loans held for sale are recorded at the lower of cost or fair value as determined on an aggregate basis. Fees received from the borrower and the direct costs of loan originations are deferred and recorded as an adjustment to the sales price, when such loans are sold.

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

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

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

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

The Bank measures a loan for impairment when it is “probable” that it will be unable to collect all amounts due (i.e. both principal and interest) according to the contractual terms of the loan agreement. A loan is also considered impaired when the recorded investment in the loan is less than the present value of expected future cash flows (discounted at the loan’s effective interest rate). By definition, all loans classified as troubled debt restructures are considered impaired and measured for impairment. The measurement of impairment is based on (1) the present value of the expected future cash flows of the impaired loan discounted at the loan’s original effective interest rate, (2) the observable market price of the impaired loan, or (3) the fair value of the collateral of a collateral-dependent loan. The amount by which the recorded

investment of the loan exceeds the measure of the impaired loan is recognized by recording a valuation allowance with a corresponding charge to the provision for loan losses. All loans classified as "substandard" or "doubtful" are analyzed for impairment. The Bank recognizes interest income on impaired loans based on its existing methods of recognizing interest income on non-accrual loans.

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

(f) Allowance for Loan and Lease Losses

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

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

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

The bank applies a systematic process to determine the required allowance for loan and leases losses:

1. Loans are separated into homogeneous pools by loan type and risk factor. The Bank segments the loan portfolio into 14 pools with similar characteristics and primarily based on loan product type.
2. Estimated loss rates are determined for each pool of homogeneous loans. The pool rates are established by examining historical charge-off data for the pools of homogeneous loans. For the FAS 5 pools, the bank applies the actual losses against the average outstanding balances within those pools to come to historical loss rates. The pool rates are multiple by the loan balance of each pool to estimate the probable loss (in dollars) for each group of loans. The pass loan pools include commercial, international, real estate by loan type, construction, and residential mortgage loans.
3. Problem credits are evaluated for specific loss exposure and establish specific reserves as needed. The bank reviews non-accrual loans, classified loans, and TDR loans individually to determine if they are impaired, and establish specific reserves as needed for impairment. For collateral dependent loans, impairment is typically measured by comparing the loan amount to the fair value of collateral less cost to sell, with a prompt charge-off taken for the 'shortfall' amount once the value is confirmed. Other methods can be used in estimated impairment including loan sale market price or present value of expected future cash flows discounted at the loan's effective interest rate.
4. Adjustments, if warranted, are made to estimate reserves for each loan pool to account for qualitative factors. Such adjustments are intended to account for current performance or risk factors in the loan

portfolio and the impact of recent trends and conditions that management believes directly impact loss potential in the portfolio that is not currently being captured in the ALLL model. The adjustments incorporate recent trends and economic conditions to the allowance methodology including credit concentrations, delinquency trends, economic and business conditions, the quality of lending management and staff, lending policies and procedures, loss and recovery trends, nature and volume of the portfolio, non-accrual and problem loan trends, and other adjustments for items not covered by other factors.

4. The sums of the estimates of probable loss for each category with the specific reserves are aggregated to arrive at the total estimated ALLL. The bank also establishes a reserve for unfunded commitments, calculated by applying the International historical pass reserve percentage to the total Outstanding L/C, Standby L/C, and Acceptance balance.

5. To validate the adequacy of the estimated loan and lease losses, the ALLL to total loans level is assessed and compared to historical charge off, delinquency, nonperforming, and classified loan trends. In addition, the bank also runs parallel a Loan Loss Analyzer program to test the adequacy of the loan and leases reserve.

Impaired loans are identified at each reporting date based on certain criteria and individually reviewed for impairment. A loan is considered impaired when it is probable that the Bank will be unable to collect all amounts due according to the original contractual terms of the loan agreement. If a loan is impaired, a portion of the allowance is allocated so that the loan is reported, net, at a present value of estimated future cash flows using the loan’s existing rate or at the fair value of collateral if repayment is expected solely from the collateral.

Our loan portfolio, excluding impaired loans which are evaluated individually, is categorized into several segments for purposes of determining allowance amounts by loan segment. The loan segments we currently evaluate are: commercial & industrial, trade finance, real estate—land, mini-perm, real estate construction and other loans. Each of these segments is then further broken down based on property type. Within these loan segments, we then evaluate loans rated as pass credits, separately from adversely classified loans. The allowance amounts for pass rated loans are determined using historical loss rates developed through a historical analysis over a period of 12-months. The adversely classified loans are further grouped into three credit risk rating categories: special mention, substandard and doubtful.

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

(g) Other Real Estate Owned (OREO)

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

(h) Bank Furniture and Fixtures

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

(i) Investments in Affordable Housing Partnerships

The Bank invests in qualified affordable housing projects (low income housing) and previously accounted for them under the equity method of accounting. The Bank recognized its share of partnership losses in other operating expenses with the tax benefits recognized in the income tax provision using the proportional amortization method.

(j) Comprehensive Income

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

(k) Income Taxes

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

(l) Earnings per Share

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

(m) Share-Based Compensation

Employees and directors participate in the Bank's 2004 Equity Incentive Plan and 2014 Equity Incentive Plan. Share-based compensation expense for all share-based payment awards is based on the

grant-date fair value estimated in accordance with the provisions of ASC 718. The Bank recognizes these compensation costs on a straight-line basis over the requisite service period for the entire award of generally three to five years, and options expire between four and ten years from the date of grant. The Bank's policy is to recognize costs net of estimated forfeitures. See Note 14 for further discussion.

(n) Bank-Owned Life Insurance (BOLI)

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

(o) Use of Estimates

Management of the Bank has made a number of estimates and assumptions relating to the reporting of assets and liabilities and the disclosure of contingent assets and liabilities to prepare these financial statements in conformity with accounting principles generally accepted in the United States of America. Actual results could differ from these estimates. Fair values of financial instruments are estimated using relevant market information and other assumptions, as more fully disclosed in a separate note. Fair value estimates involve uncertainties and matters of significant judgement regarding interest rates, credit risk, prepayments, and other factors, especially in the absence of broad markets for particular items. Changes in assumptions or in market conditions could significantly affect these estimates.

(p) Segment Reporting

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

(q) Business Combinations

Business combinations are accounted for under the acquisition method of accounting in accordance with ASC 805, *Business Combinations*. Under the acquisition method, the acquiring entity in a business combination recognizes 100 percent of the acquired assets and assumed liabilities, regardless of the percentage owned, at their estimated fair values as of the date of acquisition. Any excess of the purchase price over the fair value of net assets and other identifiable intangible assets acquired is recorded as goodwill. To the extent the fair value of net assets acquired, including other identifiable assets, exceed the purchase price, a bargain purchase gain is recognized. Assets acquired and liabilities assumed from contingencies must also be recognized at fair value, if the fair value can be determined during the measurement period. Results of operations of an acquired business are included in the statement of operations from the date of acquisition. Acquisition-related costs, including conversion and restructuring charges, are expensed as incurred. The Bank applied this guidance to the UIB acquisition that was consummated during 2015.

(r) Recently Issued Accounting Standards

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

FASB Accounting Standards Update (“ASU”) 2014-09*, Revenue from Contracts with Customers (Topic 606),* replaces existing revenue recognition guidance for contracts to provide goods or services to customers and amends existing guidance related to recognition of gains and losses on the sale of certain nonfinancial assets such as real estate. ASU 2014-09 established a principles-based approach to recognizing revenue that applies to all contracts other than those covered by other authoritative U.S. GAAP guidance. Quantitative and qualitative disclosures regarding the nature, amount, timing and uncertainty of revenue and cash flows are also required. ASU 2014-09 was to be effective for interim and annual periods beginning after December 15, 2016 and was to be applied on a retrospective basis or a retrospective basis on uncompleted contracts (modified retrospective) through a cumulative adjustment to equity. In August 2015, the FASB issued ASU 2015-14 which defers the original effective date for all entities by one year. Public business entities should apply the guidance in ASU 2015-14 to annual reporting periods beginning after December 15, 2017, including interim reporting periods within that reporting period. Earlier application is permitted only as of annual reporting periods beginning after December 15, 2016, including interim reporting periods within that reporting period.

The majority of the Bank’s revenue consists of net interest income on financial assets and financial liabilities, which is explicitly excluded from the scope of ASU 2014-09, and therefore there are no changes expected in the timing or measurement of net interest income. The Bank completed its analysis for determining the extent ASU 2014-09 will affect its noninterest income, primarily in the areas of fees and service charges on deposit accounts and trade finance activities. Based on the analysis performed, the Bank does not expect a material change in the timing or measurement of revenues related to noninterest income. We adopted the new standard using the modified retrospective method beginning January 1, 2018. The adoption did not have a material impact on the Bank’s consolidated financial statements.

FASB ASU 2016-02*, Leases (Topic 842),* introduces the most significant change for lessees including the requirement under the new guidance to recognize right-of-use assets and lease liabilities for all leases not considered short-term leases. By definition, a short-term lease is one in which: (a) the lease term is 12 months or less; and (b) there is not an option to purchase the underlying asset that the lessee is reasonably certain to exercise. For short-term leases, lessees may elect an accounting policy by class of underlying asset under which right-of-use assets and lease liabilities are not recognized and lease payments are generally recognized as expense over the lease term on a straight-line basis. This change will result in lessees recognizing right-of-use assets and lease liabilities for most leases currently accounted for as operating leases under the legacy lease accounting guidance. Examples of changes in the new guidance affecting both lessees and lessors include: (a) defining initial direct costs to only include those incremental costs that would not have been incurred if the lease had not been entered into, (b) requiring related party leases to be accounted for based on their legally enforceable terms and conditions, (c) eliminating the additional requirements that must be applied today to leases involving real estate and (d) revising the circumstances under which the transfer contract in a sale-leaseback transaction should be accounted for as the sale of an asset by the seller-lessee and the purchase of an asset by the buyer-lessor. In addition, both lessees and lessors are subject to new disclosure requirements. ASU 2016-02 is effective for public entities for interim and annual periods beginning after December 15, 2018. The Bank has future operating lease obligations for its locations of $16.6 million that are being evaluated as potential lease assets and liabilities, as defined in ASU 2016-02.

FASB ASU 2016-09, *Compensation-Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting* was issued as a part of the FASB’s simplification initiative, and intends to improve the accounting for share-based payment transactions. The ASU changes several aspects of the accounting for share-based payment award transactions, including accounting for excess tax benefits and deficiencies, income statement recognition, cash flow classification, forfeitures, and tax withholding requirements. The Bank adopted ASU 2016-09 in the first quarter of 2017. As a result of the adoption of

ASU 2016-09, the Bank now recognizes excess tax benefits on share-based payment awards in income tax provision on the Consolidated Income Statement and Comprehensive Income rather than in additional paid-in capital on the Consolidated Statement of Changes in Stockholders' Equity. The Bank recorded $2.5 million of income tax benefits related to excess tax benefits from share-based payment awards for the year ended December 31, 2017.

FASB ASU 2016-13, ***Financial Instruments—Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments***, introduces new guidance for the accounting for credit losses on instruments within its scope. The new guidance introduces an approach based on expected losses to estimate credit losses on certain types of financial instruments. It also modifies the impairment model for available-for-sale (AFS) debt securities and provides for a simplified accounting model for purchased financial assets with credit deterioration since their origination. Current expected credit losses ("CECL") model, will apply to: (1) financial assets subject to credit losses and measured at amortized cost; and (2) certain off-balance sheet credit exposures. This includes loans, held-to-maturity debt securities, loan commitments, financial guarantees, and net investments in leases, as well as reinsurance and trade receivables. Upon initial recognition of the exposure, the CECL model requires an entity to estimate the credit losses expected over the life of an exposure (or pool of exposures). The estimate of expected credit losses (ECL) should consider historical information, current information, and reasonable and supportable forecasts, including estimates of prepayments. Financial instruments with similar risk characteristics should be grouped together when estimating ECL. ASU 2016-13 is effective for public entities for interim and annual periods beginning after December 15, 2019. Early application of the guidance will be permitted for all entities for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. The Bank is currently evaluating the effects of ASU 2016-13 on its consolidated financial statements and disclosures, and expects ASU 2016-13 to add complexity and costs to its current credit loss evaluation process. In connection with its evaluation of the effects of ASU 2016-13 on its consolidated financial statements and disclosures, the Bank is currently gathering information and considering the extent possible vendors may be utilized to assist in formulating the methodology to be used to implement ASU 2016-13.

FASB ASU 2017-01, ***Business Combinations (Topic 805): Clarifying the Definition of a Business***, clarifies the definition of a business with the objective of adding guidance to assist entities with evaluating whether transactions should be accounted for as acquisitions (or disposals) of assets or businesses. ASU 2017-01 is effective for interim and annual periods beginning after December 15, 2017. ASU 2017-01 must be applied prospectively and upon adoption the standard will impact how the Bank accounts for acquisitions (or disposals) of assets or businesses. The Bank is in the process of evaluating the impact of this new guidance on its consolidated financial position, but does not expect the guidance to have a material impact on its results of operations.

FASB ASU 2017-04, ***Intangibles—Goodwill and Other (Topic 350): Simplifying the Test for Goodwill Impairment*** simplifies how an entity is required to test goodwill for impairment by eliminating Step 2 from the goodwill impairment test. Step 2 measures a goodwill impairment loss by comparing the implied fair value of a reporting unit's goodwill with the carrying amount of that goodwill. ASU 2017-04 amends the guidance to require an entity to perform its annual, or interim, goodwill impairment test by comparing the fair value of a reporting unit with its carrying amount. An entity still has the option to perform the qualitative assessment for a reporting unit to determine if the quantitative impairment test is necessary. ASU 2017-04 is effective for annual or interim goodwill impairment tests in fiscal years beginning after December 15, 2019. Early adoption is permitted for interim or annual goodwill impairment tests performed on testing dates after January 1, 2017. The Bank is in the process of evaluating the impact of this new guidance on its consolidated financial position, but does not expect the guidance to have a material impact on its results of operations.

FASB ASU 2017-05, ***Other Income—Gains and Losses from the Derecognition of Nonfinancial Assets (Subtopic 610-20): Clarifying the Scope of Asset Derecognition Guidance and Accounting for Partial Sales of Nonfinancial Assets,*** clarifies that Subtopic 610-20 applies to the derecognition of nonfinancial assets and in substance nonfinancial assets unless other specific guidance applies. ASU 2017-05 also adds guidance for partial sales of nonfinancial assets and eliminates rules specifically addressing sales of real estate. For public business entities, this ASU is effective for annual periods and interim periods within those annual periods beginning after December 15, 2017. The adoption of ASU 2017-05 on January 1, 2018 did not have a material on the Bank's consolidated financial statements and disclosures.

FASB ASU 2017-08, ***Receivables—Nonrefundable Fees and Other Costs (Subtopic 310-20),*** shortens the amortization period for certain purchased callable debt securities held at a premium. Prior to the issuance of this guidance, premiums were amortized as an adjustment of yield over the contractual life of the instrument. ASU 2017-08 requires premiums on purchased callable debt securities that have explicit, non-contingent call features that are callable at fixed prices to be amortized to the earliest call date. ASU 2017-08 is effective for annual periods and interim periods within those annual periods beginning after December 15, 2018, and early adoption is permitted. ASU 2017-08 will be applied through a cumulative effect adjustment through retained earnings (modified-retrospective approach). The Bank is currently evaluating the effects of ASU 2017-08 on its financial statements and disclosures but the adoption of ASU 2017-08 is not expected to have a material impact on the its consolidated financial statements.

FASB ASU 2017-09, ***Compensation—Stock Compensation (Topic 718): Scope of Modification Accounting***, which provides guidance about which changes to the terms or conditions of a share-based payment award require an entity to apply modification accounting in Topic 718. An entity should account for the effects of a modification unless all the following are met: (a) the fair value of the modified award is the same as the fair value of the original award, (b) the vesting conditions of the modified award are the same as the vesting conditions of the original award and (c) the classification of the modified award as an equity instrument or a liability instrument is the same as the classification of the original award immediately before the original award is modified. The amendments in ASU 2017-09 are effective for annual periods beginning after December 15, 2017, including interim periods within those annual periods. Early adoption is permitted, including adoption in any interim period, for reporting periods for which financial statements have not been issued. The amendments in ASU 2017-09 are applied prospectively to an award modified on or after the adoption date. The adoption of ASU 2017-09 on January 1, 2018 did not have a material impact on the Bank's consolidated financial statements.

FASB ASU 2017-12, ***Derivatives and Hedging (Topic 815): Targeted Improvements to Accounting for Hedging Activities***, which amends the hedge accounting recognition and presentation requirements in ASC 815 to improve the transparency and understandability of information conveyed to financial statement users about an entity's risk management activities to better align the entity's financial reporting for hedging relationships with those risk management activities and to reduce the complexity of and simplify the application of hedge accounting. ASU 2017-12 is to be applied to all existing hedging relationships on the date of adoption and will be effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2018. Early adoption is permitted in any interim period, with the effect of adoption reflected as of the beginning of the fiscal year of adoption. The Bank is currently evaluating the potential impact of ASU 2017-12 on its consolidated financial statements, but does not expect the guidance to have a material impact on its results of operations.

FASB ASU 2018-02, ***Income Statement-Reporting Comprehensive Income (Topic 220): Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income,*** which requires companies to reclassify the stranded effects in other comprehensive income to retained earnings as a result

of the change in the tax rates under the Tax Cuts and Jobs Act (the "2017 Tax Act"). The Company has opted to early adopt this pronouncement by retrospective application to each period in which the effect of the change in the tax rate under the 2017 Tax Act is recognized. The $208 thousand impact of the reclassification from accumulated other comprehensive income(loss) to retained earnings is included in the consolidated statements of changes in shareholders' equity.

(2) Business Combination

On November 20, 2015, the Bank completed the acquisition of United International Bank ("UIB"), a New York state-chartered bank with one full-service location in Flushing, New York. This acquisition allowed us to enter the Northeast market, greatly expanding opportunities for loan and deposit growth. Consideration for the purchase was $22.2 million and was paid in cash. As a result of the acquisition, we assumed approximately $150.4 million in loans and $157.7 million in deposits at the acquisition date.

Assets acquired and liabilities assumed in the acquisition have been accounted for under the acquisition method of accounting, in accordance with ASC 805-20-30. At the acquisition date, the Bank recorded total fair value of assets acquired of $187.5 million. These assets included $25.3 million in cash and cash equivalents, $8.5 million in investment securities available-for-sale, $559,000 in FHLB stock, $148.7 million in loans receivable, $1.1 million in fixed assets, $1.5 million in deferred tax assets, and $965,000 in other assets. Liabilities with a total fair value of $165.7 million were acquired, which included $158.0 million in deposits, $6.6 million in FHLB advances, and $721,000 in other liabilities. The assets and liabilities were recorded at their estimated fair values as of the November 20, 2015 acquisition date. Goodwill resulting from the acquisition was not material.

The Bank has included the financial results of the full business combination in the Consolidated Statements of Operation and Comprehensive Income beginning at the acquisition date. Supplemental financial information regarding the operations of the former UIB from the date of acquisition through December 31, 2017 has not been presented, as the acquisition of UIB does not represent the acquisition of a business which has continuity both before and after the acquisition.

The following table presents the Bank's unaudited pro forma results of operations for the periods presented as if the UIB acquisition had been completed January 1, 2015. This pro forma information combines UIB's 2015 historical results with the Bank's 2015 historical results, and includes UIB's results of operations prior to the acquisition date. This unaudited pro forma information is not necessarily indicative of the Bank's future operating results or results that would have occurred if the acquisition had occurred at the beginning of 2015. No assumptions have been applied to the pro forma results of operations regarding possible revenue enhancements, expense efficiencies, or asset dispositions. Actual results will therefore differ from the pro forma information presented.

(In thousands)	Pro forma Year ended December 31, 2015 (unaudited)
Net interest income	$89,108
Net income after tax	$29,178

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

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

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

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

The carrying value of our held-to-maturity investment securities was $8.8 million at December 31, 2017 and $10.3 million at December 31, 2016. The tables below show the amortized cost, gross unrealized gains and losses and estimated fair value of securities held-to-maturity as of December 31, 2017 and December 31, 2016:

	December 31, 2017			
	Amortized cost	Gross unrecognized gains	Gross unrecognized losses	Estimated fair value
	(In thousands)			
Mortgage-backed securities	$8,780	$—	$(281)	$8,499

	December 31, 2016			
	Amortized cost	Gross unrecognized gains	Gross unrecognized losses	Estimated fair value
	(In thousands)			
Mortgage-backed securities	$10,337	$—	$(316)	$10,021

The tables below show the amortized cost, gross unrealized gains and losses, and estimated fair value of securities available for sale as of December 31, 2017 and 2016.

	December 31, 2017			
	Amortized cost	Gross unrealized gains	Gross unrealized losses	Estimated fair value
	(In thousands)			
Asset-backed securities	$ 4,390	$ —	$ (93)	$ 4,297
Corporate notes	97,618	2,254	(250)	99,622
U.S. Agency mortgage-backed securities	26,512	215	(265)	26,462
Collateralized mortgage obligations	3,736	12	(3)	3,745
Municipal securities	46,291	453	(354)	46,390
U.S. Agency principal-only strip securities	1,679	—	(26)	1,653
SBA securities	1,300	7	—	1,307
Mutual funds—government bond funds	5,000	—	(273)	4,727
Total securities available-for-sale	$186,526	$2,941	$(1,264)	$188,203

	December 31, 2016			
	Amortized cost	Gross unrealized gains	Gross unrealized losses	Estimated fair value
	(In thousands)			
Asset-backed securities	$ 4,944	$ —	$ (556)	$ 4,388
Corporate notes	98,749	1,733	(1,206)	99,276
U.S. Agency mortgage-backed securities	30,832	300	(243)	30,889
Collateralized mortgage obligations	5,589	38	(32)	5,595
Municipal securities	52,109	311	(1,620)	50,800
U.S. Agency principal-only strip securities	2,210	—	(10)	2,200
SBA securities	1,902	11	—	1,913
Mutual funds—government bond funds	5,000	—	(228)	4,772
Total securities available-for-sale	$201,335	$2,393	$(3,895)	$199,833

Gross unrealized losses on securities available-for-sale and the fair value of the related securities, aggregated by investment category and length of time that the individual securities have been in a continuous unrealized loss position, at December 31, 2017 and 2016 are as follows:

	December 31, 2017					
	Less than 12 months		12 months or greater		Total	
	Estimated fair value	Unrealized losses	Estimated fair value	Unrealized losses	Estimated fair value	Unrealized losses
	(In thousands)					
Corporate notes	$ 7,826	$ (78)	$18,742	$ (172)	$26,568	$ (250)
U.S. Agency mortgage-backed securities	5,054	(41)	8,684	(224)	13,738	(265)
Collateralized mortgage obligations	123	(1)	2,189	(2)	2,312	(3)
Municipal securities	587	(8)	20,104	(346)	20,691	(354)
Mutual funds—government bond funds	—	—	4,727	(273)	4,727	(273)
Asset-backed securities	1,929	(9)	2,368	(84)	4,297	(93)
SBA securities	79	—	—	—	79	—
U.S. Agency principal-only strip securities	—	—	1,653	(26)	1,653	(26)
Total securities available-for-sale	$15,598	$(137)	$58,467	$(1,127)	$74,065	$(1,264)

	December 31, 2016					
	Less than 12 months		12 months or greater		Total	
	Estimated fair value	Unrealized losses	Estimated fair value	Unrealized losses	Estimated fair value	Unrealized losses
	(In thousands)					
Corporate notes	$42,979	$ (649)	$14,138	$ (557)	$ 57,117	$(1,206)
U.S. Agency mortgage-backed securities	3,492	(35)	10,638	(208)	14,130	(243)
Collateralized mortgage obligations	3,169	(32)	—	—	3,169	(32)
Municipal securities	30,850	(1,620)	—	—	30,850	(1,620)
Mutual funds—government bond funds	—	—	4,772	(228)	4,772	(228)
Asset-backed securities	—	—	4,388	(556)	4,388	(556)
U.S. Agency principal-only strip securities	2,200	(10)	—	—	2,200	(10)
Total securities available-for-sale	$82,690	$(2,346)	$33,936	$(1,549)	$116,626	$(3,895)

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

The Bank performs a regular impairment analysis on its investment securities portfolio and management has analyzed all investment securities which have an amortized cost that exceeds fair value as of December 31, 2017.

As of December 31, 2017 the Bank owned 5 corporate securities where the amortized cost exceeded fair value for greater than 12 months. The total amortized cost of these securities was $18.9 million and their fair value was $18.7 million. Management performed an analysis on all of the issuers of these securities which focused on the recent financial results of the companies, capital ratios, debt ratings, and long-term prospects of the issuers and deemed all 5 corporate securities to be temporarily impaired. Management has concluded that the market value decline is a result of the interest rate environment and not credit impairment, and that the fair value of these securities will recover as the macroeconomic environment improves. The intent of the Bank is to hold these securities until a recovery in value, and management has determined that it is not more likely than not that the Bank will be required to sell the securities prior to recovery of the amortized cost basis.

The Bank owns 42 available-for-sale mortgage-backed securities, 4 of which were in an unrealized loss position for longer than 12 months as of December 31, 2017. The total amortized cost of these securities was $8.9 million and the total fair value was $8.7 million. Based on factors including the Bank's intent to hold the securities until a recovery in value and the determination that it is not more likely than not that the Bank will be required to sell the securities prior to recovery of amortized cost basis, management determined that the securities were not other-than-temporarily impaired as of December 31, 2017.

As of December 31, 2017, the Bank owned one asset-backed security ("ABS") where the amortized cost exceeded fair value for greater than 12 months. The total amortized cost of this security was $2.5 million and the total fair value was $2.4 million. Management determined that the ABS was not other-than-temporarily impaired as of December 31, 2017. This determination was made based on several factors such as debt rating of the security, amount of credit protection, the Bank's intent and ability to hold the security until a recovery in value and the determination that it is not more likely than not that the Bank will be required to sell the security prior to recovery of amortized cost basis.

The Bank owns 80 available-for-sale municipal securities, 33 of which were in an unrealized loss position for longer than 12 months as of December 31, 2017. The total amortized cost of these securities was $20.4 million and the total fair value was $20.1 million. Based on factors including the Bank's intent to hold the securities until a recovery in value and the determination that it is not more likely than not that the Bank will be required to sell the securities prior to recovery of amortized cost basis, management determined that the securities were not other-than-temporarily impaired as of December 31, 2017.

The Bank owns one mutual fund investment, which was in an unrealized loss position for longer than 12 months as of December 31, 2017. The amortized cost of this investment was $5.0 million and the fair value was $4.7 million. This mutual fund invests primarily in short to intermediate maturity U.S. government obligations (i.e. Treasury bonds, notes, and bills and other bonds and obligations guaranteed by the U.S. government) and its decline in value was primarily due to interest rate movements and not any credit related event. Based on this factor and including the Bank's intent to hold the security until a recovery in value and the determination that it is not more likely than not that the Bank will be required to sell the security prior to recovery of amortized cost basis, management determined that the security was not other-than-temporarily impaired as of December 31, 2017.

As of December 31, 2017, the Bank owned one collateralized mortgage obligation ("CMO") where the amortized cost exceeded fair value for greater than 12 months. The total amortized cost of this security was

$2.2 million and the total fair value was $2.2 million. Management determined that the CMO were not other-than-temporarily impaired as of December 31, 2017. This determination was made based on several factors such as debt rating of the security, amount of credit protection, the Bank's intent and ability to hold the security until a recovery in value and the determination that it is not more likely than not that the Bank will be required to sell the security prior to recovery of amortized cost basis.

As of December 31, 2017, the Bank owned one U.S. Agency principal-only strip where the amortized cost exceeded fair value for greater than 12 months. The total amortized cost of this security was $1.7 million and the total fair value was $1.8 million. Based on factors including the Bank's intent to hold the securities until a recovery in value and the determination that it is not more likely than not that the Bank will be required to sell the securities prior to recovery of amortized cost basis, management determined that the securities were not other-than-temporarily impaired as of December 31, 2017.

In accordance with Section 939A of the Dodd-Frank Wall Street Reform and Consumer Protection Act, the Bank performs a thorough annual review of each of the investment securities in its portfolio (other than US Government and Agency securities) to determine, among other things, the current financial status of the issuer as well as the issuer's ability to repay the debt. This analysis is performed in addition to the quarterly review that is performed on all investment securities which are in an unrealized loss position.

We do not intend to sell these securities until recovery and have determined that it is not more likely than not that we will be required to sell the securities prior to recovery of their amortized cost basis.

Cash proceeds from calls of securities available-for-sale totaled $11.7 million and $10.9 million in 2017 and 2016, respectively. Net realized gains or losses for sales and calls of securities totaled a gain of $4,000 and $169,000 for the years ended December 31, 2017 and 2016, respectively. There were no sales and calls of securities available-for-sale in 2015. Investment securities having a fair value of approximately $192.1 million and $204.4 million were pledged to secure governmental deposits, treasury tax and loan deposits, borrowing lines from the Federal Reserve Bank and FHLB as of December 31, 2017 and 2016, respectively. At December 31, 2017 and 2016, approximately $52.4 million and $62.3 million, respectively, of the Bank's investment securities were pledged as collateral for certain public deposits.

The amortized cost and estimated fair value of securities available-for-sale at December 31, 2017 and 2016, by contractual maturity, are shown below. Investment securities are classified in accordance with their estimated average life. Expected maturities differ from contractual maturities mainly due to prepayment rates; changes in prepayment rates will affect a security's average life.

	2017		2016	
	Available-for-Sale		Available-for-Sale	
	Amortized cost	Estimated fair value	Amortized cost	Estimated fair value
	(In thousands)			
Due in one year or less	$ 5,257	$ 4,984	$ 5,983	$ 6,075
Due after one year through five years	33,727	34,822	34,851	36,219
Due after five years through ten years	72,352	73,252	54,198	53,948
Due after ten years	75,190	75,145	106,303	103,591
Total	$186,526	$188,203	$201,335	$199,833

The Bank had no debt securities that have been other-than-temporarily-impaired as of or during the years ended December 31, 2017, 2016, or 2015.

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

The Bank's loan portfolio includes originated loans as well as purchased loans.

The loans and leases portfolio as of December 31, 2017 and 2016 is summarized as follows:

	2017	2016
	(In thousands)	
Real estate mortgage	$1,769,301	$1,550,178
Real estate construction	283,802	233,394
Commercial	866,672	733,708
Trade finance	21,310	21,702
Consumer & other	8	4,567
Gross loans	2,941,093	2,543,549
Less:		
Allowance for loan and lease losses	(29,921)	(26,478)
Deferred loan fees, net	(3,099)	(1,682)
Total loans, net	$2,908,073	$2,515,389

The Bank had $6.5 million of non-accrual loans and leases at December 31, 2017 compared to $7.6 million at December 31, 2016. These loans and leases had interest due, but not recognized, of approximately $409,000 and $540,000 in 2017 and 2016, respectively. The Bank had no loans past due 90 or more days and still accruing interest as of December 31, 2017 or December 31, 2016.

The following tables depict the Bank's recorded investment in past due loans by class as of December 31, 2017 and 2016:

December 31, 2017 Loan Class:	30-89 Days Accruing	90+ Days Still Accruing	Non-accrual Non-current	Total Past Due	Non-accrual Current
			(in thousands)		
Real estate mortgage					
R/E—Residential	$ 275	$—	$462	$ 737	$ —
R/E—Commercial	—	—	—	—	—
Total R/E mortgage	275	—	462	737	—
Real estate construction					
Construction—Residential	—	—	—	—	—
Construction—Commercial	—	—	—	—	—
Total R/E—Construction	—	—	—	—	—
Commercial and Industrial	1,500	—	175	1,675	4,762
Trade Finance	—	—	—	—	1,087
Consumer	—	—	—	—	—
Other	—	—	—	—	—
Total as of December 31, 2017	$1,775	$—	$637	$2,412	$5,849

December 31, 2016 Loan Class:	30-89 Days Accruing	90+ Days Still Accruing	Non-accrual Non-current	Total Past Due	Non-accrual Current
			(in thousands)		
Real estate mortgage					
R/E—Residential	$ 472	$—	$ —	$ 472	$ —
R/E—Commercial	—	—	—	—	—
Total R/E mortgage	472	—	—	472	—
Real estate construction					
Construction—Residential	—	—	—	—	—
Construction—Commercial	—	—	—	—	—
Total R/E—Construction	—	—	—	—	—
Commercial and Industrial	1,299	—	1,660	2,959	4,750
Trade Finance	—	—	—	—	1,238
Consumer	—	—	—	—	—
Other	2	—	—	2	—
Total as of December 31, 2016	$1,773	$—	$1,660	$3,433	$5,988

The following table depicts the Bank's total recorded investment in non-accrual loans by class for the years ended December 31, 2017 and 2016:

Loan Class	December 31, 2017	December 31, 2016
	(In thousands)	
Real estate mortgage:		
R/E—Residential	$ 462	$ —
R/E—Commercial	—	—
Total R/E mortgage	462	—
Real estate construction:		
Construction-Residential	—	—
Construction-Commercial	—	—
Total R/E construction	—	—
Commercial and Industrial	4,937	6,410
Trade Finance	1,087	1,238
Consumer	—	—
Other	—	—
Loans held for sale	—	—
Total non-accrual loans	$6,486	$7,648

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

TDRs may be designated as performing or non-performing. A TDR may be designated as performing if the loan has demonstrated sustained performance under the modified terms. The period of sustained performance

may include the periods prior to modification if prior performance met or exceeded the modified terms. For non-performing restructured loans, the loan will remain on non-accrual status until the borrower demonstrates a sustained period of performance, generally six consecutive months of payments. The Bank had no performing restructured loans as of December 31, 2017 and 2016. Non-performing restructured loans were $5.9 million at December 31, 2017, and $6.0 at December 31, 2016. The $5.9 million in TDRs as of December 31, 2017 consists of two commercial real estate loan relationship renewals totaling $4.8 million, and one trade finance loan relationship renewal with a balance of $1.1 million. There were no balance reductions or rate concessions associated with the renewals designated as TDRs during the year ended December 31, 2017.

	December 31, 2017			December 31, 2016		
	# of Contracts	Pre-modification Outstanding Recorded Investment	Pre-modification Outstanding Recorded Investment	# of Contracts	Pre-modification Outstanding Recorded Investment	Pre-modification Outstanding Recorded Investment
Troubled debt restructurings:						
Real estate—commercial	3	4,750	4,777	3	4,750	4,750
Commercial & industrial	1	1,238	1,087	1	1,238	1,238
Total	4	5,988	5,864	4	5,988	5,988

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

Subsequent to restructuring, a TDR that becomes delinquent, generally beyond 90 days for commercial and industrial and real estate mini-perm commercial loans, becomes non-accrual. There were no loans modified as TDRs that subsequently defaulted during the years ended December 31, 2017, 2016 or 2015.

All TDRs are included in the impaired loan valuation allowance process. All portfolio segments of TDRs are reviewed for necessary specific reserves in the same manner as impaired loans of the same portfolio segment which have not been identified as TDRs. The modification of the terms of each TDR is considered in the current impairment analysis of the respective TDR. For all portfolio segments of delinquent TDRs and when the restructured loan is less than the recorded investment in the loan, the deficiency is charged-off against the allowance for loan and lease losses. If the loan is a performing TDR the deficiency is included in the specific allowance, as appropriate. As of December 31, 2017, all TDRs were non-performing with an associated allowance for loan and lease losses of $2.0 million.

Impaired loans and leases are those for which it is probable that we will not be able to collect all amounts due according to the contractual terms of the loan or lease agreement. The category of impaired loans and leases is not comparable with the category of non-accrual loans and leases. Management may choose to place a loan or lease on non-accrual status due to payment delinquency or uncertain collectability, while not classifying the loan or lease as impaired if it is probable that we will collect all amounts due in accordance with the original contractual terms of the loan or lease. Impaired loans totaled $7.6 million and $8.8 million at December 31, 2017 and 2016, respectively. The total allowance for loan and lease losses related to these loans was $2.0 million and $1.7 million at December 31, 2017 and 2016, respectively. Interest income recognized on impaired loans during 2017, 2016 and 2015 was $164,000, $320,000 and $0, respectively. At December 31, 2017, the Bank had $65,000 of commitments to lend additional funds to debtors whose loans are impaired.

Impaired loans, disaggregated by loan class and excluding loans held for sale, as of December 31, 2017 and 2016 are set forth in the following tables. Interest income recognized approximates cash basis interest income.

	Unpaid Principal Balance	Recorded Investment with allowance	Recorded Investment without allowance	Total Recorded investment	Related Allowance	Average Recorded Investment	Interest Income Recognized
				(in thousands)			
2017							
Real estate mortgage:							
Residential	$ 462	$ —	$ 462	$ 462	$ —	$ 372	$—
Commercial	454	—	454	454	—	454	95
Total R/E mortgage	916	—	916	916	—	826	95
Real estate construction:							
Residential	—	—	—	—	—	—	—
Commercial	—	—	—	—	—	—	—
Total R/E construction	—	—	—	—	—	—	—
Commercial	5,636	4,778	858	5,636	1,648	6,265	69
Trade Finance	1,087	1,087	—	1,087	374	1,140	—
Consumer	—	—	—	—	—	—	—
Other loans	—	—	—	—	—	—	—
Total impaired loans	$7,639	$5,865	$1,774	$7,638	$2,022	$8,231	$164

	Unpaid Principal Balance	Recorded Investment with allowance	Recorded Investment without allowance	Total Recorded investment	Related Allowance	Average Recorded Investment	Interest Income Recognized
				(in thousands)			
2016							
Real estate—mini-perm:							
Residential	$ —	$ —	$ —	$ —	$ —	$ —	$—
Commercial	927	—	454	454	—	547	125
Total R/E mini-perm	927	—	454	454	—	547	125
Real estate—construction:							
Residential	—	—	—	—	—	—	—
Commercial	—	—	—	—	—	—	—
Total R/E construction	—	—	—	—	—	—	—
Commercial	12,227	6,081	1,027	7,108	1,735	6,344	143
Trade Finance	1,238	—	1,238	1,238	—	1,088	52
Consumer[(2)]	—	—	—	—	—	—	—
Other loans	—	—	—	—	—	—	—
Total impaired loans	$14,392	$6,081	$2,719	$8,800	$1,735	$7,979	$320

During 2017, one residential mortgage loan was transferred to loans held for sale and remained held for sale as of December 31, 2017. During 2016 and 2015, no loans were sold, and no loans were transferred to or out of loans held for sale. No loans remained held for sale as of December 31, 2016 or December 31, 2015.

The following table details activity in the allowance for credit losses by portfolio segment for the year ended December 31, 2017. Allocation of a portion of the allowance to one particular portfolio segment does not indicate that it is no longer available to absorb losses in other portfolio segments.

	Real estate mortgage		Real estate construction						
2017	**Residential**	**Commercial**	**Residential**	**Commercial**	**Commercial & Industrial**	**Trade Finance**	**Consumer & Other**	**Unallocated**	**Total**
	(In thousands)								
Balance at beginning of period	$2,228	$11,350	$1,158	$ 809	$10,412	$177	$ 67	$277	$26,478
Provision for credit losses	408	1,363	(587)	505	3,397	381	(67)	100	5,500
Loans and leases charged off	—	—	—	—	(2,274)	—	—	—	(2,274)
Recoveries	—	145	—	17	55	—	—	—	217
Net (charge offs) recoveries	—	145	—	17	(2,219)	—	—	—	(2,057)
Balance at end of period	$2,636	$12,858	$ 571	$1,331	$11,590	$558	$—	$377	$29,921

The Bank's recorded investment in loans as of December 31, 2017 related to each balance in the allowance for loan and lease losses by portfolio segment and disaggregated on the basis of the Bank's impairment methodology was as follows:

	Real estate mortgage		Real estate construction						
December 31, 2017	Residential	Commercial	Residential	Commercial	Commercial & Industrial	Trade Finance	Consumer & Other	Unallocated	Total
					(In thousands)				
Allowance for loan and lease losses:									
Loans individually evaluated for impairment	$ —	$ —	$ —	$ —	$ 1,648	$ 374	$—	$—	$ 2,022
Loans collectively evaluated for impairment	2,636	12,858	571	1,331	9,942	184	—	377	27,899
Total	$ 2,636	$ 12,858	$ 571	$ 1,331	$ 11,590	$ 558	$—	$377	$ 29,921
Loans outstanding:									
Loans individually evaluated for impairment	$ 462	$ 454	$ —	$ —	$ 5,636	$ 1,087	$—	$—	$ 7,639
Loans collectively evaluated for impairment	370,309	1,398,076	85,199	198,603	861,036	20,223	8	—	2,933,454
Total	$370,771	$1,398,530	$85,199	$198,603	$866,672	$21,310	$ 8	$—	$2,941,093

The following table details activity in the allowance for credit losses by portfolio segment for the year ended December 31, 2016. Allocation of a portion of the allowance to one particular portfolio segment does not indicate that it is no longer available to absorb losses in other portfolio segments.

	Real estate mortgage		Real estate construction						
2016	Residential	Commercial	Residential	Commercial	Commercial & Industrial	Trade Finance	Consumer & Other	Unallocated	Total
	(In thousands)								
Balance at beginning of period	$2,098	$11,562	$1,019	$385	$ 6,993	$ 385	$ 4	$212	$22,658
Provision for credit losses	130	(944)	113	424	6,757	(208)	63	65	6,400
Loans and leases charged off	—	—	—	—	(4,323)	—	—	—	(4,323)
Recoveries	—	732	26	—	985	—	—	—	1,743
Net (charge offs) recoveries	—	732	26	—	(3,338)	—	—	—	(2,580)
Balance at end of period	$2,228	$11,350	$1,158	$809	$10,412	$ 177	$ 67	$277	$26,478

The Bank's recorded investment in loans as of December 31, 2016 related to each balance in the allowance for credit losses by portfolio segment and disaggregated on the basis of the Bank's impairment methodology was as follows:

	Real estate mortgage		Real estate construction						
December 31, 2016	**Residential**	**Commercial**	**Residential**	**Commercial**	**Commercial & Industrial**	**Trade Finance**	**Consumer & Other**	**Unallocated**	**Total**
					(In thousands)				
Allowance for loan and lease losses:									
Loans individually evaluated for impairment	$ —	$ —	$ —	$ —	$ 1,735	$ —	$ —	$—	$ 1,735
Loans collectively evaluated for impairment	2,228	11,350	1,158	809	8,677	177	67	277	24,743
Total	$ 2,228	$ 11,350	$ 1,158	$ 809	$ 10,412	$ 177	$ 67	$277	$ 26,478
Loans outstanding:									
Loans individually evaluated for impairment	$ —	$ 454	$ —	$ —	$ 7,108	$ 1,238	$ —	$—	$ 8,800
Loans collectively evaluated for impairment	334,794	1,214,930	104,960	128,434	726,600	20,464	4,567	—	2,534,749
Total	$334,794	$1,215,384	$104,960	$128,434	$733,708	$21,702	$4,567	$—	$2,543,549

The following table details activity in the allowance for credit losses by portfolio segment for the year ended December 31, 2015. Allocation of a portion of the allowance to one particular portfolio segment does not indicate that it is no longer available to absorb losses in other portfolio segments.

2015	Real estate mortgage		Real estate construction		Commercial & Industrial	Trade Finance	Consumer & Other	Unallocated	Total
	Residential	Commercial	Residential	Commercial					
	(In thousands)								
Balance at beginning of period	$1,258	$10,117	$ 2,241	$ 605	$ 6,621	$408	$ 6	$ 1,718	$22,974
Provision for credit losses	740	2,337	(1,222)	(240)	1,716	(23)	(2)	(1,506)	1,800
Loans and leases charged off	—	(1,793)	—	—	(1,475)	—	—	—	(3,268)
Recoveries	100	901	—	20	131	—	—	—	1,152
Net (charge offs) recoveries	100	(892)	—	20	(1,344)	—	—	—	(2,116)
Balance at end of period	$2,098	$11,562	$ 1,019	$ 385	$ 6,993	$385	$ 4	$ 212	$22,658

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

The following tables present the recorded investment in risk grades and classified loans by class of loan as of December 31, 2017 and 2016. Classified loans include loans in risk grades 6 and 7, which correlate to substandard and doubtful for risk classification purposes.

2017	Real Estate		Construction		Commercial & Industrial	Trade Finance	Consumer & Other	Total Loans
Grade:	Residential	Commercial	Residential	Commercial				
(In thousands)								
Pass	$367,040	$1,393,968	$85,199	$198,603	$852,159	$20,223	$ 8	$2,917,200
Special Mention	2,644	3,609	—	—	8,877	—	—	15,130
Substandard	1,087	953	—	—	5,476	1,087	—	8,603
Doubtful	—	—	—	—	160	—	—	160
Total	$370,771	$1,398,530	$85,199	$198,603	$866,672	$21,310	$ 8	$2,941,093

2016	Real Estate		Construction					
Grade:	Residential	Commercial	Residential	Commercial	Commercial & Industrial	Trade Finance	Consumer & Other	Total Loans
(In thousands)								
Pass	$334,794	$1,210,559	$104,960	$128,434	$719,328	$20,464	$4,567	$2,523,106
Special Mention	—	3,756	—	—	6,807	—	—	10,563
Substandard	—	1,069	—	—	5,913	1,238	—	8,220
Doubtful	—	—	—	—	1,660	—	—	1,660
Total	$334,794	$1,215,384	$104,960	$128,434	$733,708	$21,702	$4,567	$2,543,549

(5) Bank, Premises, Furniture and Fixtures

As of December 31, 2017 and 2016, furniture and fixtures consists of the following:

	2017	2016
	(In thousands)	
Land and Building	$ 2,782	$ 2,782
Leasehold improvements	8,791	7,998
Furniture and fixtures	6,676	6,108
	18,249	16,888
Less accumulated depreciation and amortization	(12,565)	(11,575)
	$ 5,684	$ 5,313

Depreciation and amortization expense was $990,000, $929,000 and $623,000 for the years ended December 31, 2017, 2016 and 2015, respectively. There were zero fixed asset sales during 2017, 2016 and 2015.

(6) Deposits

Time deposit accounts at December 31, 2017 mature as follows:

Year	Maturities of time deposits
	(In thousands)
2018	$1,111,541
2019	112,713
2020	51
2021	245
2022	250
Thereafter	—
	$1,224,800

The aggregate amount of overdrafts that have been reclassified as loan balances was $8,000 and $30,000 at December 31, 2017 and 2016, respectively.

(7) Income Taxes

The income taxes expense (benefit) for the years ended December 31, 2017, 2016 and 2015 was as follows:

	2017	2016	2015
		(In thousands)	
Current income tax expense:			
Federal	$20,818	$18,422	$15,656
State	8,279	6,777	5,349
	29,097	25,199	21,005
Deferred income tax (benefit) expense:			
Federal	1,334	(834)	(1,001)
State	618	(1,034)	481
Change in enacted tax rate	6,037	—	—
	7,989	(1,868)	(520)
Income tax expense:	$37,086	$23,331	$20,485

At December 31, 2017 and 2016, the current net income tax receivable was $2.7 million and net payable of $1.6 million, respectively.

The components of the deferred tax assets and deferred tax liabilities as of December 31, 2017 and 2016 are as follows:

	2017	2016
	(in thousands)	
Deferred tax assets:		
Allowance for loan and lease losses	$ 8,983	$10,934
State taxes	1,398	1,828
Deferred compensation	—	471
Bank furniture and fixtures, net	533	736
Deferred stock units	—	1,334
Non-qualified stock options	1,418	2,443
Net operating loss carryforward	2,489	2,662
Other	999	1,313
Excess realized build in loss	1,464	2,767
Accrued bonuses	1,892	3,361
Fair value adjustment on acquired loans	120	259
Unrealized losses on securities available-for-sale	—	634
Alternative minimum tax credits	820	820
Gross deferred tax assets	20,116	29,562
Deferred tax liabilities:		
Unrealized gains on securities available-for-sale	(504)	—
Deferred loan costs	(1,581)	(2,166)
FHLB stock	(286)	(402)
Core deposit intangible from acquisition	(197)	(318)
Other	(72)	(71)
Gross deferred liabilities	(2,640)	(2,957)
Valuation allowance	—	—
Net deferred tax assets	$17,476	$26,605

On December 22, 2017, President Trump signed the Tax Cuts and Jobs Act into legislation, substantially amending the Internal Revenue Code. Under FASB ASC 740, the effects of changes in tax rates and laws are recognized in the period in which the new legislation is enacted. As a result of this new legislation, the Company incurred a one-time increase in tax expense of $6.0 million from the re-measurement of deferred tax assets and liabilities resulting from the legislation's decrease in the corporate Federal income tax rate from 35% to 21%.

In assessing the realizability of deferred tax assets, management considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income during the periods in which those temporary differences become deductible. Management considers the projected future taxable income and tax planning strategies in making this assessment. Based upon the level of historical taxable income and projections for future taxable income over the periods in which the deferred tax assets are deductible, management believes it is more likely than not that the Bank will realize all benefits related to these deductible differences at December 31, 2017.

Pursuant to Sections 382 and 383 of the Internal Revenue Code, annual use of NOL and credit carryforwards may be limited in the event a cumulative change in ownership of more than 50 percent points occurs within a three-year period. We determined that such an ownership change occurred as of June 21, 2010 as

a result of stock issuances in 2010 and 2009. This ownership change resulted in estimated limitations on the utilization of tax attributes, including NOL carryforwards and tax credits. Although we fully expect to utilize all of the federal NOL carryforward prior to their expiration, the California NOL carryover has been significantly impacted by the IRC Sec. 382 limitation. We estimate that of approximately $79.0 million of the California NOL as of December 31, 2017, $55.8 million is expected to expire in 2029 and $3.2 million is expected to expire in 2030 as it will be unutilized as a result of IRS Sec 382 limitation. This amounts to approximately $5.1 million of deferred tax assets which would not be realized. The remaining California NOL carryforward of the approximately $19.9 million at December 31, 2017, is subject to IRC Sec. 382 annual limitation amount of approximately $1.5 million. Additionally, the bank has $5.2 million of Federal excess realized built in losses and $6.1 million of California excess built in losses as of December 31, 2017 which are also subject to IRC Sec. 382 annual limitation amount of approximately $1.5 million.

As a result of the UIB acquisition the Bank has an additional $1.6 million of federal NOLs and $3.3 million of New York NOLs that are subject to annual Sec. 382 limitation of $0.6 million remaining as of December 31, 2017. Management fully expects to use the acquired NOL carryforwards before their expiration beginning in 2025 for New York NOLs and 2033 for federal NOLs.

As of December 31, 2017 we had federal and state NOL carryforwards of $1.6 million and $23.2 million, respectively.

A reconciliation of the income tax expense (benefit) and the amount computed by applying the statutory federal income tax rate to the loss before income taxes is as follows for the years ended December 31, 2017, 2016 and 2015:

	2017		2016		2015	
	Amount	Percentage	Amount	Percentage	Amount	Percentage
			(In thousands)			
Statutory U.S. federal income tax	$28,168	35.0%	$20,895	35.0%	$17,580	35.0%
State taxes, net of federal benefit	5,783	7.2	3,733	6.2	3,789	7.5
Share-based compensation	(2,515)	(3.1)	(39)	(0.1)	44	0.1
Change in federal tax rate	6,037	7.5	—	—	—	—
Life insurance policies	(84)	(0.1)	(83)	(0.1)	(83)	(0.2)
Low income housing credits	(525)	(0.7)	(790)	(1.3)	(608)	(1.2)
Other	222	0.3	(385)	(0.6)	(237)	(0.4)
	$37,086	46.1%	$23,331	39.1%	$20,485	40.8%

The Bank is subject to U.S. Federal income tax as well as various state and local income taxes. The Bank is generally no longer subject to examination by taxing authorities for years prior to 2013.

There were no unrecognized tax benefits for the years ended December 31, 2017 and 2016.

(8) Other Real Estate Owned

At December 31, 2017 and at December 31, 2016, OREO was comprised of one property. Expenses related to this property are included in Gain on Sale of OREO and Related Expense in the Consolidated Statements of Operations and Comprehensive Income. There was no activity in the valuation allowance for other real estate for the years ended December 31, 2017, 2016 and 2015. At December 31, 2017, 2016 and 2015, there was no

valuation allowance for other real estate. The following table details the Bank's OREO properties by loan class as of December 31, 2017, and 2016:

	2017		2016	
	#	$	#	$
	(dollar amounts in thousands)			
Loan class:				
Real estate—Mini-perm				
Commercial	1	$4,112	1	$4,112
Total as of year end	1	$4,112	1	$4,112

(9) Long-Term Debt

On June 13, 2016, the Bank completed a private placement of $62.5 million in principal amount of fixed-to-floating rate subordinated notes to certain qualified investors. On July 8, 2016, and September 30, 2016, the Bank issued additional debt under the same terms of $10.0 million and $27.5 million, respectively, bringing the total debt issuance to $100.0 million. The proceeds from the placement of the notes are to be used for general corporate purposes, capital management, and to support future growth. The subordinated notes have a maturity date of June 15, 2026 and bear interest, payable semi-annually, at the rate of 6.0% per annum until June 15, 2021. On that date, the interest rate will be adjusted to float at a rate equal to the three-month LIBOR rate plus 467.3 basis points (4.673%) until maturity. The notes include a right of prepayment, on or after June 15, 2021 and, in certain limited circumstances, before that date. The indebtedness evidenced by the subordinated notes, including principal and interest, is unsecured and subordinate and junior in right to payment to general and secured creditors and depositors of Preferred Bank. The subordinated notes have been structured to qualify as Tier 2 capital for regulatory purposes. Debt issuance costs incurred in conjunction with the offering were $1.7 million, and a premium of $545,000 was recorded associated with the $27.5 million additional issuance on September 30, 2016.

Debt issuance costs are reported as a direct deduction from the face of the note. The premium and related debt issuance costs are being amortized into interest expense over a 10-year period. A summary of outstanding long-term debt at December 31, 2017 is as follows:

	Long-Term Debt Summary				
(in thousands)	As of December 31, 2017	As of December 31, 2016	Interest rate	Maturity date	Earliest call date
Subordinated notes payable ($100,000 face amount, net of cost and premium)	$98,963	$98,839	6.00%	June 15, 2026	June 15, 2021

Advances from the Federal Home Loan Bank was $6.4 million at December 31, 2017, and $26.5 million at December 31, 2016. Each advance is payable at its maturity date. All advances are collateralized by commercial or residential real estate loans, Fixed Rate Credit advances or by certain marketable investment securities (SBC). At December 31, 2017, approximately $591.3 million of the Bank's real estate loans was pledged as collateral with Federal Home Loan Bank and the remaining borrowing capacity was $305.1 million. As of December 31, 2017 and 2016, advances from the FHLB, net of discount, are summarized as follows:

Federal Home Loan Bank Advances

(in thousands)	As of December 31, 2017	As of December 31, 2016
Fixed Rates:		
FHLB advances (Maturities from 6/19/17 through 5/28/19, fixed rates from 0.91% to 5.09%)	$6,334	$26,516
Weighted average interest rate	2.54%	1.31%

Contractual maturities (ranging from August 13, 2018 through May 28, 2019) over the next five years are as follows (in thousands):

2018	$5,000
2019	1,334
2020	—
2021	—
2022	—
Total	$6,334

The Bank had an approved short-term borrowings line available through the discount window at the Federal Reserve Bank of San Francisco (FRBSF) in the amount of $134.3 million. The Bank had no borrowing outstanding through the discount window outstanding as of December 31, 2017 or 2016.

(10) Affordable Housing Partnerships

The Bank has invested in limited partnerships that are formed to develop and operate high-quality affordable housing for lower income tenants within the United States. These partnerships must meet the regulatory requirements for affordable housing for a minimum 15-year compliance period to fully utilize the tax credits. The Bank is not the primary beneficiary and therefore does not consolidate these partnerships. If the partnerships cease to qualify during the compliance period, the credits may be denied for any period in which the projects are not in compliance, and credits previously taken may be partially subject to recapture with interest.

The Bank amortizes investment in affordable housing partnerships in proportion with tax credits and benefits realized. As of December 31, 2017, the Bank had four investments, with a net carrying value of $34.7 million. Commitments to fund investment in affordable housing partnerships as of December 31, 2017 totaled $18.5 million. As of December 31, 2016, the Bank had three investments with a net carrying value of $23.7 million and commitments to fund $10.6 million. As of December 31, 2017, there was no impairment in investment in affordable housing partmenships.

(11) Commitments and Contingencies

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

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

The Bank's exposure to credit risk under commitments to extend credit, standby letters of credit, commercial letters of credit, commitments to fund investments in affordable housing partnerships, operating lease commitments, and financial guarantees written is limited to the contractual amount of those instruments.

At December 31, 2017 and 2016, the Bank had commitments to fund loans of $828.2 million and $673.7 million, respectively. Financial instruments with off-balance-sheet risk at December 31, 2017 and 2016 are as follows:

	At December 31,			
	2017		2016	
	Fixed Rate	Variable Rate	Fixed Rate	Variable Rate
	(In thousands)			
Commitments to extend credit	$ 81,143	$747,0755	$ 49,060	$624,598
Commercial letters of credit	5,328	—	100,018	—
Standby letters of credit	138,920	—	3,423	—
Total	$225,391	$ 747,075	$152,501	$624,598

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

Lease Commitments: The Bank is obligated under non-cancellable operating leases for the premises of its head office and certain branch offices. As of December 31, 2017, the future total minimum lease payments for the Bank's premises are as follows:

Year:	Total lease payment
	(In thousands)
2018	$ 3,358
2019	3,090
2020	2,813
2021	2,158
2022	1,753
Thereafter	3,470
	$16,642

Rental expense was $3.0 million, $2.9 million and $2.2 million for the years ended December 31, 2017, 2016 and 2015, respectively.

(12) Related Party Transactions

Loan and Commitments: The Bank has extended credit to certain directors and officers and companies in which they have an interest and certain shareholders which beneficially own more than 5% of the Bank's capital stock.

At December 31, 2017 and 2016, the aggregate loans (including commitments) to related parties were approximately $5.3 million (of which $1.3 million was outstanding) and $6.5 million (of which $1.3 million was outstanding), respectively. All related party loans were current at December 31, 2017 and 2016.

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

	2017	2016	2015
		(In thousands)	
Balance at beginning of year	$1,347	$ 501	$ 303
New loans	—	1,347	500
Net drawdowns (repayments)	(69)	(501)	(302)
Balance at end of year	$1,278	$1,347	$ 501

Deposits: The amount of deposits from related parties was $12.4 million and $10.6 million at December 31, 2017 and 2016, respectively.

(13) Restrictions on Cash Dividends, Regulatory Capital Requirements

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

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

Banks and bank holding companies are subject to regulatory capital requirements administered by federal banking agencies. Capital adequacy guidelines and, additionally for banks, prompt corrective action regulations, involve quantitative measures of assets, liabilities, and certain off-balance-sheet items calculated under regulatory accounting practices. Capital amounts and classifications are also subject to qualitative judgments by regulators. Failure to meet capital requirements can initiate regulatory action. The final rules implementing Basel Committee on Banking Supervision's capital guidelines for U.S. banks ("Basel III rules") became effective for the Bank on January 1, 2015 with full compliance with all of the requirements being phased in over a multi-year schedule, and fully phased in by January 1, 2019. Under the Basel III rules, the Bank must hold a capital conversation buffer above the adequately capitalized risk-based capital ratios. The capital conservation buffer is

being phased in from 0.0% for 2015 to 2.50% by 2019. The required capital conservation buffer for 2017 is 1. 25%. The Bank's capital conservation buffer was 4.07% and 3.83% as of December 31, 2017 and 2016, respectively. Management believes that as of December 31, 2017 the Bank meets all capital adequacy requirements to which it is subject.

Prompt corrective action regulations provide five classifications: well capitalized, adequately capitalized, undercapitalized, significantly undercapitalized, and critically undercapitalized, although these terms are not used to represent overall financial condition. If adequately capitalized, regulatory approval is required to accept brokered deposits. If undercapitalized, capital distributions are limited as is asset growth and expansion, and capital restoration plans are required. At December 31, 2017 and 2016, the most recent regulatory notifications categorized the Bank as well capitalized under the regulatory framework for prompt corrective action. There are no conditions or events since that notification that management believes have changed the institution's category.

The quantitative measures established by the regulation to ensure capital adequacy require the Bank to maintain amounts and ratios (set forth in the table below) of total and Tier 1 risk-based capital (as defined in the regulation) to risk-weighted assets (as defined) and of Tier 1 risk-based capital (as defined) to average assets (as defined). Management believes, as of December 31, 2017, that the Bank meets all capital adequacy requirements to which it is subject.

The Bank's actual capital and various regulatory required capital thresholds without conservation capital buffer are presented in the following table:

	Actual		For capital adequacy purposes		To be well capitalized under prompt corrective action provision	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
			(In thousands)			
As of December 31, 2017:						
Total risk-based capital	$480,542	13.83%	$277,877	≥ 8.00%	$347,347	≥ 10.00%
Tier 1 risk-based capital	349,746	10.07%	208,408	6.00%	277,877	8.00%
Common equity tier 1 risk-based capital ratio	349,746	10.07%	156,306	4.50%	225,775	6.50%
Leverage ratio	349,746	9.52%	146,913	4.00%	183,642	5.00%
As of December 31, 2016:						
Total risk-based capital	$421,294	14.09%	$239,234	≥ 8.00%	$299,042	≥ 10.00%
Tier 1 risk-based capital	294,004	9.83%	179,425	6.00%	239,234	8.00%
Common equity tier 1 risk-based capital ratio	294,004	9.83%	134,569	4.50%	194,377	6.50%
Leverage ratio	294,004	9.43%	124,740	4.00%	155,925	5.00%

(14) Share-Based Compensation

The Bank remunerates employees and directors through its stock compensation plans—the 2004 Equity Incentive Plan and 2014 Equity Incentive Plan which are discussed below. Effective January 1, 2007, the Bank adopted FASB ASC 718 "Compensation—Stock Compensation" ("ASC 718"). Share-based compensation expense for all share-based payment awards is based on the grant-date fair value estimated in accordance with the provisions of ASC 718. The Bank recognizes these compensation costs on a straight-line basis over the requisite service period for the entire award, which is the vesting term of generally three to five years, for only those options expected to vest. The fair value of stock options and awards was estimated using the Black-Scholes

option pricing model with the grant-date assumptions and weighted-average fair value. When options are exercised, the Bank's policy is to issue new shares of stock.

For the year ended December 31, 2017, 2016 and 2015, the Bank recognized share-based compensation expense of $1.9 million, $3.7 million and $3.7 million, respectively, resulting in the recognition of $2.5 million, $211,000 and $231,000 in related tax benefits, respectively.

2004 Equity Incentive Plan

The Bank's 2004 Equity Incentive Plan (the "2004 Plan") provides for granting of non-statutory stock options, incentive stock options and restricted stock awards ("RSAs") to key full-time employees, officers, and the directors of the Bank. Stock options granted under the 2004 Plan have an exercise price equal to the fair value of the underlying common stock on the date of grant. Stock options granted under the 2004 Plan generally vest in installments between 20-33% each year, become fully vested after three to five years and expire between four to ten years from the date of grant. Certain option and share awards provide for accelerated vesting if there is a change in control (as defined in the 2004 Plan). There were 1,455,330 shares authorized under this plan.

The total intrinsic value of share options exercised during the years ended December 31, 2017, 2016 and 2015 was $3.6 million, $4.7 million, and $5.3 million, respectively. As of December 31, 2017, there was no unrecognized compensation cost that relates to unvested options granted under the 2004 Plan. The Bank recognized tax benefits of $2.5 million, $211,000 and $231,000 for the years ended December 31, 2017, 2016, and 2015 under the 2004 Plan.

The 2004 Plan expired in March 2014, and as such there were zero options granted during 2017, 2016, or 2015 under the 2004 Plan.

The following information under the 2004 Plan is presented for the years ended December 31:

	2017	2016	2015
		(In thousands)	
Grant date fair value of options granted	$ —	$ —	$ —
Fair value of options vested	916	442	1,154
Total intrinsic value of options exercised	3,566	4,725	5,304
Cash received from options exercised	1,444	3,301	2,537

The following is a summary of the transactions under the 2004 Plan for the years ended December 31.

	2004 Plan		
	Number of Options	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life
Options outstanding as of January 1, 2015	663,362	$12.99	
Granted	—	—	
Exercised	(257,316)	9.88	
Forfeited or expired	(12,000)	14.65	
Options outstanding as of December 31, 2015	394,046	$14.98	
Granted	—	—	
Exercised	(230,396)	14.32	
Forfeited or expired	—	—	
Options outstanding as of December 31, 2016	163,650	$15.89	
Granted	—	—	
Exercised	(90,350)	15.98	
Forfeited or expired	—	—	
Options outstanding as of December 31, 2017	73,300	$15.79	0.1 years
Options exercisable as of December 31, 2017	73,300	$15.79	0.1 years

As of December 31, 2017, 2016 and 2015, the aggregate intrinsic value of options outstanding under the 2004 Plan was $3.3 million, $6.0 million and $6.2 million, respectively. As of December 31, 2017, stock options outstanding under the 2004 Plan were as follows:

	Options Outstanding			Options Exercisable		
Exercise Price Range	Number of Outstanding Options	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life	Number of Outstanding Options	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life
$0.00—$24.99	73,300	$15.89	0.10	73,300	$15.89	0.10

2014 Equity Incentive Plan

During the second quarter of 2014, the Bank's Board of Directors adopted and the Bank's shareholders approved a new stock option plan, the 2014 Equity Incentive Plan, (the "2014 Plan"). Similar to the 2004 Plan, the Plan provides for granting of nonstatutory stock options, and incentive stock options and restricted stock awards ("RSAs") to key full-time employees, officers, and the directors of the Bank. Stock options granted under the 2014 Plan have an exercise price equal to the fair value of the underlying common stock on the date of grant. Stock options and share awards granted under the 2014 Plan are generally expected to vest in installments between 20-25% each year, become fully vested after three to five years, and expire four to six years from the date of grant. All option and share awards provide for accelerated vesting if there is a change in control (as defined in the 2014 Plan). There are 2,500,000 shares reserved for issuance under the 2014 Plan. As of December 31, 2017, there have been no stock options granted under the 2014 Plan.

The following is a summary of the transactions for non-vested stock options under the 1992 Plan, the Interim Plan the 2004 Plan, and the 2014 Plan for the year ended December 31, 2017:

	Number of Shares	Weighted Average Grant Date Fair Value
Non-Vested Options outstanding as of December 31, 2016	57,000	$7.56
Granted	—	$ —
Forfeited or expired	—	$ —
Vested	(57,000)	$7.56
Non-Vested Options outstanding as of December 31, 2017	—	$ —

Restricted Stock Awards

The Bank's 2004 Plan provides for granting of RSAs to key full-time employees, officers, and the directors of the Bank. The Bank began granting RSAs in calendar year 2009. During the year ended December 31, 2017, the Bank granted 92,000 RSAs and recognized $1.8 million of compensation expense related to RSAs. The RSAs granted under the 2004 Plan or the 2014 Plan have a one to four year vesting period and are to be distributed at the end of the vesting period. The total unrecognized compensation expense for outstanding RSAs was $3.0 million as of December 31, 2017, and will be recognized over a weighted average of 1.4 years.

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

	Number of Shares	Weighted Average Grant Date Fair Value
Non-Vested RSAs outstanding as of January 1, 2015	145,411	$20.87
Granted	128,400	$27.35
Forfeited or expired	(4,232)	$25.16
Vested	(11,268)	$25.94
Non-Vested RSAs outstanding as of December 31, 2015	258,311	$23.80
Granted	117,769	$31.80
Forfeited or expired	(200)	$27.33
Vested	(278,511)	$24.41
Non-Vested RSAs outstanding as of December 31, 2016	97,369	$31.73
Granted	92,000	$54.36
Forfeited or expired	(1,875)	$43.87
Vested	(14,225)	$31.71
Non-Vested RSAs outstanding as of December 31, 2017	173,269	$43.62

As of December 31, 2017, there was $3.0 million of total unrecognized compensation cost related to nonvested shares granted under the Plan. The cost is expected to be recognized over a weighted average period of 1.36 years. The total fair value of shares vested during the years ended December 31, 2017, 2016 and 2015 was $0.5 million, $6.8 million and $0.3 million, respectively.

(15) Employee Benefit Plan

Effective January 1, 1994, the Bank began a 401k profit sharing plan for its eligible employees. Under the plan, the Bank matches 50% of a participant's contributions up to 6% of his/her salary subject to federal limitations on maximum contributions. Contributions made by the Bank for the years ended December 31, 2017, 2016 and 2015 totaled $392,000, $346,000 and $276,000, respectively.

(16) Bonus Plan

The Bonus Plan is administered by the Compensation Committee of the Board of Directors (the "Compensation Committee"). The Compensation Committee determines which employees may participate in the plan, the total amount of bonus payable to our employees each year, the amount of bonus to be carried over and paid in subsequent years and the allocation of the total amounts among our chairman, officers, and other employees. All awards are contingent upon the Bank attaining certain financial objectives with the exception of certain bonuses which may be awarded by the Compensation Committee irrespective of the certain financial targets as part of new employees' first year compensation. This is typically done as an alternative to a signing bonus. For the years ended December 31, 2017, 2016 and 2015, financial objectives required under the plan were met. Total expense of the plan recorded by the Bank was $9.0 million, $6.2 million and $5.0 million for 2017, 2016 and 2015, respectively. As of December 31, 2017 and 2016, the total bonus accrual included in the other liabilities amounted to $6.7 million and $7.9 million, respectively.

(17) Deferred Compensation Arrangements

The Bank adopted a Deferred Compensation Plan in 1999. The plan was a nonqualified unfunded plan for a select group of management and highly compensated employees. The plan permitted eligible executives to elect to defer base salary and/or bonuses up to a maximum of 30% of salary and bonus combined. Deferred amounts accrued interest at a rate of prime plus 1%, unless the deferred amounts were invested in employer stock, in which case no interest accrued on the deferred amounts and the executives became entitled to receive the shares allocated to their deferred compensation account upon a plan distribution event. The plan provided for distribution of deferred compensation upon normal or early retirement dates, termination of employment, disability, change of control, death or hardship. The Deferred Compensation Plan was terminated as of January 1, 2015. On January 1, 2017, payments under the plan of cash and converted shares were made to the plan participants including issuance of 437,254 shares of the Bank's common stock to plan participants. Participants collectively surrendered 205,822 shares to pay employee tax liabilities, resulting in 231,432 net shares issued.

At December 31, 2017 and 2016, liabilities recorded for the deferred compensation plan totaled approximately zero and $1.1 million, respectively.

In order to economically fund its obligation under the deferred compensation arrangements, the Bank purchased single-premium life insurance policies under which the executive officers and directors are the insured, while the Bank is the owner and beneficiary thereof. At December 31, 2017 and 2016, the cash surrender value of the policies totaled $9.1 million and $8.8 million, respectively. During 2017, 2016 and 2015, the income on the insurance policies was $351,000, $346,000 and $339,000, respectively.

(18) Litigation

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

(19) Earnings per Share

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

	2017	2016	2015
	(In thousands, except per share data)		
Basic earnings per share:			
Net income	$ 43,394	$ 36,369	$ 29,743
Less: income and dividends allocated to participating securities	(499)	(547)	(536)
Net income allocated to common shareholders-basic	$ 42,895	$ 35,822	$ 29,207
Basic weighted average common shares outstanding	14,438,964	13,883,497	13,484,216
Basic earnings per share	$ 2.97	$ 2.58	$ 2.17
Diluted earnings per share:			
Net income	$ 43,394	$ 36,369	$ 29,743
Less: income and dividends allocated to participating securities	(499)	(547)	(536)
Add: reallocation of income to dilutive securities	1	3	5
Net income allocated to common shareholders-diluted	$ 42,896	$ 35,825	$ 29,212
Basic weighted average common shares outstanding	14,438,964	13,883,497	13,484,216
Effect of dilutive securities—stock options	53,707	103,760	193,676
Diluted weighted average shares outstanding	14,492,671	13,987,257	13,677,892
Diluted earnings per share	$ 2.96	$ 2.56	$ 2.14

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

At December 31, 2017, 2016 and 2015, there were no shares related to such awards which were excluded from the computation of diluted EPS due to their anti-dilutive effect.

(20) Quarterly Financial Data (Unaudited)

The following tables summarize the quarterly unaudited financial data for 2017 and 2016:

Quarterly Financial Data (Unaudited)

Year Ended December 31, 2017	Three months ended March 31	June 30	September 30	December 31
	(In thousands, except per share data)			
Interest income	$34,632	$38,113	$42,854	$42,001
Interest expense	6,190	6,835	7,432	7,439
Interest income before provision for credit losses	28,442	31,278	35,422	34,562
Provision for credit losses	1,500	1,200	1,300	1,500
Noninterest income	2,090	1,275	1,243	1,215
Noninterest expense	13,178	12,414	12,179	11,776
Income tax expense	5,573	7,222	9,516	14,775
Net income	$10,281	$11,717	$13,670	$ 7,726
Earnings per share				
Basic[(1)]	$ 0.71	$ 0.81	$ 0.94	$ 0.52
Diluted[(1)]	$ 0.71	$ 0.80	$ 0.94	$ 0.52

Year Ended December 31, 2016	Three months ended March 31	June 30	September 30	December 31
	(In thousands, except per share data)			
Interest income	$27,321	$29,723	$31,889	$33,980
Interest expense	3,442	3,982	5,394	5,916
Interest income before provision for credit losses	23,879	25,741	26,495	28,064
Provision for credit losses	800	2,300	1,400	1,900
Noninterest income	1,163	1,660	1,350	1,286
Noninterest expense	11,038	10,791	10,486	11,223
Income tax expense	5,361	5,724	6,080	6,166
Net income	$ 7,843	$ 8,586	$ 9,879	$10,061
Earnings per share				
Basic	$ 0.56	$ 0.61	$ 0.70	$ 0.71
Diluted	$ 0.56	$ 0.61	$ 0.69	$ 0.70

(1) Basic and diluted earnings per share during the fourth quarter of 2017 were negatively impacted by the recognition of $6.0 million in additional income tax expense as a result of changes in enacted Federal tax rates. See Note 7—*Income Taxes* for further discussion.

(21) Fair Value of Financial Instruments

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

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

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

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

(b) Securities held-to-maturity and Securities available-for-sale

For securities held-to maturity and securities available-for-sale, fair values were based on quoted market prices obtained from market quotes, a Level 1 measurement. If a quoted market price was not available, fair value was estimated using quoted market prices for similar securities or if no quotes on similar securities were available, a Level 2 measurement, or a discounted cash flow analysis was used based on a market discount rate and adjusted for pre-payments and defaults, a Level 3 measurement.

(c) Federal Home Loan Bank Stock

It is not practical to determine the fair value of FHLB stock due to the restrictions placed on its transferability.

(d) Loans

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

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

(e) Accrued Interest Receivable and Accrued Interest Payable

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

(f) Deposits

The fair value of demand deposits, saving accounts, and certain money market deposits were assumed to be the amount payable on demand at the reporting date. The fair value of interest bearing deposits and fixed maturity certificates of deposit was estimated based on discounted cash flow analysis. The discount rate used for fair valuation is based on interest rates currently offered on deposits with similar remaining maturities. This is a Level 2 measurement.

(g) FHLB Borrowings

The fair value of FHLB borrowings was based on discounted cash flow analysis. The discount rate used for fair valuation is based on rates currently offered for borrowings with similar remaining maturities, a Level 2 measurement.

(h) Commitment to Extend Credit and Letters of Credit

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

(i) Subordinated Debt Issuance

The fair value of subordinated debt is estimated by discounting the cash flows through the maturity date based on observable market rates which the Bank would pay for new issuances, a Level 2 measurement.

The carrying amount and estimated fair value of assets and liabilities as of December 31, 2017 and 2016 is detailed on the table below.

	December 31, 2017				
	Carrying amount	Estimated fair value	Level 1	Level 2	Level 3
	(In thousands)				
Assets:					
Cash and cash equivalents	$ 555,322	$ 555,322	$555,322	$ —	$ —
Securities held-to-maturity	8,780	8,499	—	8,499	—
Securities available-for-sale	188,203	188,203	4,727	183,476	—
Loans, net of allowance and net deferred loan fees	2,908,073	2,898,593	—	—	2,898,593
Loans held for sale	440	440	440	—	—
Accrued interest receivable	11,291	11,291	9	2,201	9,081
Federal Home Loan Bank stock	11,077	N/A	N/A	N/A	N/A
Liabilities:					
Demand deposits and savings:					
Noninterest-bearing	$ 659,487	$ 659,487	$ —	$ 659,487	$ —
Interest-bearing	1,378,403	1,378,403	—	1,378,408	—
Time deposits	1,224,800	1,220,645	—	1,220,645	—
FHLB borrowings	6,401	6,401	—	6,401	—
Subordinated debt issuance	98,963	94,101	—	94,101	—
Accrued interest payable	3,833	3,833	—	3,833	—

	December 31, 2016				
	Carrying amount	Estimated fair value	Level 1	Level 2	Level 3
	(In thousands)				
Assets:					
Cash and cash equivalents	$ 403,830	$ 403,830	$403,830	$ —	$ —
Securities held-to-maturity	10,337	10,021	—	10,021	—
Securities available-for-sale	199,833	199,833	4,772	195,061	—
Loans, net of allowance and net deferred loan fees	2,515,389	2,508,371	—	—	2,508,371
Accrued interest receivable	9,550	9,550	6	1,946	7,598
Federal Home Loan Bank stock	9,331	N/A	N/A	N/A	N/A
Liabilities:					
Demand deposits and savings:					
Noninterest-bearing	$ 586,272	$ 586,272	$ —	$ 586,272	$ —
Interest-bearing	1,053,125	1,053,125	—	1,053,125	—
Time deposits	1,124,327	1,118,672	—	1,118,672	—
FHLB borrowings	26,516	26,516	—	26,516	—
Subordinated debt issuance	98,839	91,878	—	91,878	—
Accrued interest payable	3,199	3,199	—	3,199	—

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

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

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

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

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

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

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

- Corporate notes—The Bank measures fair value of corporate notes by using quoted market prices for similar securities or dealer quotes, a level 2 measurement.
- Asset-backed securities—The Bank measures fair value of asset-backed securities by using quoted market prices for similar securities or dealer quotes, a level 2 measurement.
- Municipal securities—The Bank measures fair value of state and municipal securities by using quoted market prices for similar securities or dealer quotes, a level 2 measurement.
- U.S. Agency mortgage-backed securities—The Bank measures fair value of mortgage-backed securities by using quoted market prices for similar securities or dealer quotes, a level 2 measurement.
- Collateralized mortgage obligations—The Bank measures fair value of collateralized mortgage obligations by using quoted market prices for similar securities or dealer quotes, a level 2 measurement.
- U.S. Agency principal-only strip securities—The Bank measures fair value of principal-only strip securities by using quoted market prices for similar securities or dealer quotes, a level 2 measurement.
- SBA securities—The Bank measures fair value of small business administration (SBA) securities by using quoted market prices for similar securities or dealer quotes, a level 2 measurement.
- Mutual funds (government bond funds)—The Bank measures fair value based on the quoted market price at the reporting date, a level 1 measurement.

The following table presents the Bank's hierarchy for its assets and liabilities measured at fair value on a recurring basis at December 31, 2017:

(In thousands)	Fair Value Measurements Using			
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Balance at December 31, 2017
Assets				
Securities, available-for-sale:				
Mutual funds—government bond funds	$4,727	$ —	$—	$ 4,727
Asset-backed securities	—	4,297	—	4,297
Corporate notes	—	99,622	—	99,622
U.S. Agency principal-only strips	—	1,653	—	1,653
U.S. Agency mortgage-backed securities	—	26,462	—	26,462
Collateralized mortgage obligations	—	3,745	—	3,745
SBA securities	—	1,307	—	1,307
Municipal securities	—	46,390	—	46,390
Total	$4,727	$183,476	$—	$188,203

The following table presents the Bank's hierarchy for its assets and liabilities measured at fair value on a recurring basis at December 31, 2016:

(In thousands)	Fair Value Measurements Using			
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Balance at December 31, 2016
Assets				
Securities, available-for-sale:				
Mutual funds—government bond funds	$4,772	$ —	$—	$ 4,772
Asset-backed securities	—	4,388	—	4,388
Corporate notes	—	99,276	—	99,276
U.S. Agency principal-only strips	—	2,200	—	2,200
U.S. Agency mortgage-backed securities	—	30,889	—	30,889
Collateralized mortgage obligations	—	5,595	—	5,595
SBA securities	—	1,913	—	1,913
Municipal securities	—	50,800	—	50,800
Total	$4,772	$195,061	$—	$199,833

There were no transfers in or out of Level 1 and Level 2 fair value measurements during the years ended December 31, 2017 and 2016.

There were no securities with fair value measurements using significant unobservable inputs (Level 3) during the years ended December 31, 2017 and December 31, 2016.

Impaired loans—On a non-recurring basis, the Bank measures the fair value of impaired collateral dependent loans based on fair value of the collateral value which is derived from appraisals that take into consideration prices in observable transactions involving similar assets in similar locations in accordance with

Receivables Topic of FASB ASC covering loan impairments. Collateral value determined based on recent independent appraisals are considered a level 2 measurement. Collateral values based on unobservable inputs that are supported by little or no market data and less current appraisals are considered a level 3 measurement.

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

The following table presents the Bank's hierarchy for its assets measured at estimated fair value on a nonrecurring basis through twelve months ended December 31, 2017, and the total losses resulting from these fair value adjustments for the twelve months ended December 31, 2017:

(In thousands)	Fair Value Measurements Using				
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Balance at December 31, 2017	Year Ended December 31, 2017 Total Losses
Assets					
Impaired loans	$—	$—	$—	$—	$1,290

The following table presents the Bank's hierarchy for its assets measured at estimated fair value on a nonrecurring basis through twelve months ended December 31, 2016, and the total losses resulting from these fair value adjustments for the year ended December 31, 2016:

(In thousands)	Fair Value Measurements Using				
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Balance at December 31, 2016	Year Ended December 31, 2016 Total Losses
Assets					
Impaired loans	$—	$—	$844	$844	$487

There were no assets measured on a non-recurring basis at December 31, 2017. The following table represents quantitative information regarding the significant unobservable inputs used in significant Level 3 assets measured at fair value on a non-recurring basis at 2016.

	At December 31, 2016 (Dollars In thousands)			
	Fair Value	Valuation Technique	Unobservable Inputs	Range
Assets:				
Impaired loans	$844	Liquidation of collateral	Valuation of accounts receivable and inventory	50.0%

(22) Common Stock Issuances

On September 25, 2017, the Bank was granted a Stock Permit (the "Stock Permit") from the California Department of Business Oversight ("DBO") authorizing it to sell, from time-to-time, up to $50 million in shares of the Bank's common stock, by means of an "at the market offering" program (the "ATM Program"). The authorization to sell shares granted by the Stock Permit expires on March 26, 2018. During the year ended December 31, 2017, the Bank sold 541,975 shares through the ATM Program for the net proceeds of $32.8 million.

(23) Subsequent Events

None.

ITEM 16. FORM 10-K SUMMARY

None.

SIGNATURES

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

Dated: March 14, 2018

PREFERRED BANK
(Registrant)

By /s/ LI YU
Li Yu
Chairman and Chief Executive Officer

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

Signature	Title	Date
/s/ LI YU **Li Yu**	Chairman and Chief Executive Officer (Principal executive officer)	March 14, 2018
/s/ EDWARD J. CZAJKA **Edward J. Czajka**	Executive Vice President and Chief Financial Officer (Principal financial and accounting officer)	March 14, 2018
/s/ J. RICHARD BELLISTON **J. Richard Belliston**	Director	March 14, 2018
/s/ WILLIAM C. Y. CHENG **William C.Y. Cheng**	Director	March 14, 2018
/s/ CLARK HSU **Clark Hsu**	Director	March 14, 2018
/s/ GARY S. NUNNELLY **Gary S. Nunnelly**	Director	March 14, 2018
/s/ CHIH-WEI WU **Chih-Wei Wu**	Director	March 14, 2018
/s/ WAYNE WU **Wayne Wu**	Director	March 14, 2018

Exhibit 21.1

SUBSIDIARIES OF THE REGISTRANT

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

Exhibit 31.1

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

I, Li Yu, certify that:

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

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

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

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

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

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

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

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

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

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

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

Date: March 14, 2018

/s/ Li Yu

Li Yu
Chairman and Chief Executive Officer

Exhibit 31.2

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

I, Edward J. Czajka, certify that:

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

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

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

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

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

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

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

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

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

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

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

Date: March 14, 2018

/s/ Edward J. Czajka

Edward J. Czajka
Executive Vice President and Chief Financial Officer

Exhibit 32.1

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

In connection with the Annual Report of Preferred Bank (the "Bank") on Form 10-K for the period ending December 31, 2017 as filed with the Federal Deposit Insurance Corporation on the date hereof (the "Report"), I, Li Yu, Chairman, President and Chief Executive Officer of the Bank, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

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

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

Date: March 14, 2018

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

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

Exhibit 32.2

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

In connection with the Annual Report of Preferred Bank (the "Bank") on Form 10-K for the period ending December 31, 2017 as filed with the Federal Deposit Insurance Corporation on the date hereof (the "Report"), I, Edward J. Czajka, Executive Vice President and Chief Financial Officer of the Bank, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

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

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

Date: March 14, 2018

/s/ Edward J. Czajka

Edward J. Czajka
Executive Vice President & Chief Financial Officer

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

Board of Directors

Clark Hsu
Vice Chairman
Chairman & CEO
Lotus Creek Investments

J. Richard Belliston
Vice Chairman, Retired
Tokai Bank of California
CPA (Inactive)

William C. Y. Cheng
President
H & C Industries

Gary S. Nunnelly
Chairman
American Thermoform Corporation

Li Yu
Chairman & CEO
Preferred Bank

Chih-Wei Wu
Former CEO,
Taiwan Operations
Credit Suisse Bank

Wayne Wu
Founder, CEO and President
Pacific Health Investments, Inc.

Executive Officers

Li Yu
Chairman
Chief Executive Officer

Wellington Chen
President
Chief Operating Officer

Edward J. Czajka
Executive Vice President
Chief Financial Officer

Nick Pi
Executive Vice President
Chief Credit Officer

Executive Vice Presidents

Erika Chi

Sandy Ho

Johnny Hsu

Ted Hsu

Gary Hu

Alice Huang

Robert J. Kosof

Pamela Lau

Kathy Yen

Senior Vice Presidents

Anna Bagdasarian

Craig Bavaro

James Belanic

Calvin Chan

Stella Chen

Ann Cheung

Christina Ching

M. K. Chow

Julio Gallud

Madelyn Hayashi

Muna Issa

Debbie Kong

Sam Leung

Dominic Li

Martin Liska

William Oberholzer

Jenny Own

Nancy Pepper

John Stipanov

Lee Huei Wang

Corporate Headquarters

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213.891.1188

Investor Relations Contact

Kristen Papke
Financial Profiles, Inc.
310.663.8007

Independent Accountants for 2017

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Sherman Oaks, California

Corporate Counsel

Manatt, Phelps & Phillips, LLP
Los Angeles, California

Transfer Agent

Computershare
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818.254.3161

Preferred Bank is a publicly traded company with its common stock traded on the NASDAQ Global Select Market under the ticker symbol PFBC. Although a public company, Preferred Bank is not a Securities & Exchange Commission (SEC) Registrant. The Bank is however, subject to all SEC rules and reporting regulations. Preferred Bank files all of its SEC-required documents with the Federal Deposit Insurance Corporation (FDIC) and the Bank's filings may be found at their website or at preferredbank.com. To view our filings there, click on the *Investor Relations* tab and then click on the *Company Filings* tab.

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