COMMUNITY WEST BANCSHARES /
Form 10-K
March 30, 2012

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-K

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

FOR THE FISCAL YEAR ENDED DECEMBER 31, 2011
Commission File Number: 000-23575

COMMUNITY WEST BANCSHARES
(Exact name of registrant as specified in its charter)

California (State or other jurisdiction of incorporation or organization)	77-0446957 (I.R.S. Employer Identification No.)
445 Pine Avenue, Goleta, California (Address of principal executive offices)	93117 (Zip code)

(805) 692-5821
(Registrant's telephone number, including area code)

Securities registered under Section 12(b) of the Exchange Act:

Title of each class	Name of each exchange on which registered
Common Stock, No Par Value	Nasdaq Global Market

Securities registered under Section 12(g) of the Exchange Act: NONE
Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes o No x

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

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

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 during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes oNo o

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

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

Large accelerated filer o	Accelerated filer o
Non-accelerated filer (Do not check if smaller reporting company) o	Smaller reporting company x

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

The aggregate market value of common stock, held by non-affiliates of the registrant as of June 30, 2011, was $14,831,985 based on a closing price of $3.50 for the common stock, as reported on the Nasdaq Global Market. For purposes of the foregoing computation, all executive officers, directors and five percent beneficial owners of the registrant are deemed to be affiliates. Such determination should not be deemed to be an admission that such executive officers, directors or five percent beneficial owners are, in fact, affiliates of the registrant. As of March 27, 2012, 5,989,510 shares of the registrant's common stock were outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant's definitive proxy statement to be filed with the Securities and Exchange Commission pursuant to Regulation 14A in connection with the 2012 Annual Meeting of Shareholders to be held on or about May 24, 2012 are incorporated by reference into Part III of this Report. The proxy statement will be filed with the Securities and Exchange Commission not later than 120 days after the registrant's fiscal year ended December 31, 2011.

PART I

ITEM 1. BUSINESS

GENERAL

Community West Bancshares (“CWBC”) was incorporated in the State of California on November 26, 1996, for the purpose of forming a bank holding company. On December 31, 1997, CWBC acquired a 100% interest in Community West Bank, National Association ("CWB" or “Bank”). Effective that date, shareholders of CWB became shareholders of CWBC in a one-for-one exchange. The acquisition was accounted at historical cost in a manner similar to pooling-of-interests. CWBC and CWB are referred to herein as the “Company”.

Community West Bancshares is a bank holding company. CWB is the sole bank subsidiary of CWBC. CWBC provides management and shareholder services to CWB.

On January 26, 2012, the Board of Directors of the Bank signed a Consent Agreement (Agreement) with the Office of the Comptroller of the Currency (OCC), its primary regulator. The Agreement includes, among other items, the following requirements:

- Achieving and maintaining a Tier 1 Leverage Capital ratio of 9.00% and Total Risk-Based Capital ratio of 12.00%; such ratios are 8.26% and 11.80%, respectively, at December 31, 2011.
- Writing a 3-year strategic plan, which would incorporate the capital component;
- Continue to improve on the Bank’s credit quality and administration thereof, including the monitoring of problem assets and the allowance for loan losses;
- Continue to adhere to and implement the Bank’s liquidity risk management program.

Failure to comply with the provisions of the Agreement may subject the bank to further regulatory action including but not limited to, being deemed undercapitalized for purposes of the Agreement.

Since the appointment of a new Chief Executive Officer and Chief Credit Officer, the Bank has maintained an intense focus on addressing the areas of concern that have been raised by the regulators. As a result, many of the prudent actions required in the Agreement have been addressed, or will be addressed in the near future. The Bank has made considerable progress in many of the areas and issues raised in the Agreement. To date, the Bank has:

- Developed a strategy to enhance capital ratios for the Bank;
- Expanded and enhanced Board membership and supervision of management, policies and objectives;
- Developed and implemented an asset disposition plan for classified assets to reduce nonperforming loans through collection and negotiations with delinquent borrowers, and to document the improved methodology of its loan loss reserve policy. As a result nonaccrual loans were reduced 21.8% at December 31, 2011 compared to September 30, 2011;
- Developed a plan to systematically diversify its loan portfolio;
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Developed a plan to systematically diversify the deposit base and reduce reliance on non-core funding. As a result core deposits increased 12.7% at December 31, 2011 compared to December 31, 2010;

- Ensured that the senior management team has the talent and expertise needed to implement this strategic realignment and determined a means to retain and recruit seasoned professionals, as necessary; and
- Developed a plan to return the Bank to profitable operations in 2012.

Some of the specific steps that will be taken to both enhance profitability and improve the Bank's capital position are:

- The sale of approximately $10.0 million in SBA loans at premiums approximating 10%
- Prepayment of FHLB advances, thereby reducing the balance sheet and removing higher costs of borrowings
- The sale of certain pre-identified AFS securities all of which were in an unrealized gain position
- Downstream of $500,000 to $1.0 million from CWBC to CWB
- Lowering rates on interest bearing deposits

Additionally, the Bank has downsized the SBA group and will focus lending in California.

PRODUCTS AND SERVICES

CWB offers a range of commercial and retail financial services to professionals, small to mid-sized businesses and individual households. These services include various loan and deposit products. CWB also offers other financial services.

Relationship Banking – Relationship banking is conducted at the community level through five full-service branch offices on the Central Coast of California stretching from Santa Maria to Westlake Village. The primary customers are small to mid-sized businesses in these communities and their owners and managers. CWB's goal is to provide the highest quality service and the most diverse products to meet the varying needs of this highly sought customer base.

CWB offers a range of commercial and retail financial services, including the acceptance of demand, savings and time deposits, and the origination of commercial, real estate, construction, home improvement, home equity lines of credit and other installment and term loans. Its customers are also provided with the choice of a range of cash management services, merchant credit card processing, courier service and online banking. In addition to the traditional financial services offered, CWB offers remote deposit capture, automated clearing house origination, electronic data interchange and check imaging. CWB continues to investigate products and services that it believes address the growing needs of its customers and to analyze new markets for potential expansion opportunities.

One of CWB's key strengths and a fundamental difference that the Company believes enables it to stand apart from the competition is the Bank personnel's ability to develop and maintain lasting relationships with our business community. These individuals are able to develop, structure and underwrite the credit and manage the customer relationship. The Company believes this provides a competitive advantage as CWB's competitors for the most part, have a centralized lending function where developing, underwriting and managing the relationship is split between multiple individuals.

Small Business Administration Lending - CWB has been a preferred lender/servicer of loans guaranteed by the Small Business Administration ("SBA") since 1990. The Company originates SBA loans which are sometimes sold into the secondary market. The Company continues to service these loans after sale and is required under the SBA programs to retain specified amounts. The two primary SBA loan programs that CWB offers are the basic 7(a) Loan Guaranty and the Certified Development Company ("CDC"), a Section 504 ("504") program.

The 7(a) serves as the SBA's primary business loan program to help qualified small businesses obtain financing when they might not be eligible for business loans through normal lending channels. Loan proceeds under this program can be used for most business purposes including working capital, machinery and equipment, furniture and fixtures, land and building (including purchase, renovation and new construction), leasehold improvements and debt refinancing. Loan maturity is generally up to 10 years for working capital and up to 25 years for fixed assets. The 7(a) loan is approved and funded by a qualified lender, guaranteed by the SBA and subject to applicable regulations. In general, the SBA guarantees up to 85% of the loan amount depending on loan size. The Company is required by the SBA to retain a contractual minimum of 5% on all SBA 7(a) loans. The SBA 7(a) loans are always variable interest rate loans. Gains recognized by the Company on the sales of the guaranteed portion of these loans and the ongoing servicing income received have in the past been significant revenue sources for the Company. The servicing spread is a minimum of 1% on the majority of loans.

The 504 program is an economic development-financing program providing long-term, low downpayment loans to expanding businesses. Typically, a 504 project includes a loan secured from a private-sector lender with a senior lien, a loan secured from a CDC (funded by a 100% SBA-guaranteed debenture) with a junior lien covering up to 40% of the total cost, and a contribution of at least 10% equity from the borrower. Debenture limits are $5.0 million for regular 504 loans and $5.5 million for those 504 loans that meet a public policy goal.

CWB also offers Business & Industry ("B & I") loans. These loans are similar to the SBA product, except they are guaranteed by the U.S. Department of Agriculture. The guaranteed amount is generally 80%. B&I loans are made to businesses in designated rural areas and are generally larger loans to larger businesses than the 7(a) loans. Similar to the SBA 7(a) product, they can be sold into the secondary market.

CWB also originates conventional and investor loans which are funded by our secondary-market partners for which the Bank receives a premium.

The SBA has designated CWB as a "Preferred Lender". As a Preferred Lender, CWB has been delegated the loan approval, closing and most servicing and liquidation authority responsibility from the SBA.

Mortgage Lending - CWB has a Wholesale and Retail Mortgage Loan Center. The Mortgage Loan Division originates residential real estate loans primarily in the California counties of Santa Barbara, Ventura and San Luis Obispo. Some retail loans not fitting CWB's wholesale lending criteria are brokered to other lenders. After wholesale origination, most of the real estate loans are sold into the secondary market.

Manufactured Housing - CWB has a financing program for manufactured housing to provide affordable home ownership generally to low to moderate-income families that are purchasing or refinancing their manufactured house. These loans are offered in CWB's primary lending areas of Santa Barbara, Ventura and San Luis Obispo counties and the secondary areas along the California coast. The manufactured homes are located in approved mobile home parks. The parks must meet specific criteria and have amenities commensurate with surrounding parks and be maintained in good to excellent condition. The manufactured housing loans are retained in CWB's loan portfolio.

In addition, in 2011 CWB became an approved lender for the USDA Farm Service Agency, FSA, small farm loans. The Bank is now approved to submit to FSA for guarantees on agricultural loans. The FSA offers a 95% guarantee of the loan amount, not to exceed $1,214,000.

CWB's business is not seasonal in nature nor is CWB's business reliant on just a few major clients.

COMPETITION AND SERVICE AREA

The financial services industry is highly competitive with respect to both loans and deposits. Overall, the industry is dominated by a relatively small number of major banks with many offices operating over a wide geographic area. In the markets where the Company's banking branches are present, several de novo banks have increased competition. Some of the major commercial banks operating in the Company's service areas offer types of services that are not offered directly by the Company. Some of these services include leasing, trust and investment services and international banking. The Company has taken several approaches to minimize the impact of competitors' numerous branch offices and varied products. First, CWB provides courier services to business clients, thus discounting the need for multiple branches in one market. Second, through strategic alliances and correspondents, the Company provides a full complement of competitive services. Finally, one of CWB's strategic initiatives is to establish full-service branches or loan production offices in areas where there is a high demand for its lending products. In addition to loans and deposit services offered by CWB's five branches located in Goleta, Ventura, Santa Maria, Santa Barbara and Westlake Village, California, a loan production office currently exists in Roseville, California and a SBA loan production office in the San Francisco Bay area. The remote deposit capture product was put in place to better compete for deposits in areas not serviced by a branch.

EMPLOYEES

As of December 31, 2011, the Company had 121 full-time and 13 part-time employees. The Company's employees are not represented by a union or covered by a collective bargaining agreement.

GOVERNMENT POLICIES

The Company's operations are affected by various state and federal legislative changes and by regulations and policies of various regulatory authorities, including those of the states in which it operates and the U.S. government. These laws, regulations and policies include, for example, statutory maximum legal lending rates, domestic monetary policies by the Board of Governors of the Federal Reserve System which impact interest rates, U.S. fiscal policy, anti-terrorism and money laundering legislation and capital adequacy and liquidity constraints imposed by bank regulatory agencies. Changes in these laws, regulations and policies may greatly affect our operations. See "Item 1A Risk Factors – Curtailment of Government Guaranteed Loan Programs Could Affect a Segment of Our Business" and

"Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations – Supervision and Regulation."

ITEM 1A. RISK FACTORS

Investing in our common stock involves various risks which are particular to our Company, our industry and our market area. Several risk factors that may have a material adverse impact on our business, operating results and financial condition are discussed below. The following should not be considered as an all-inclusive discussion of the risk factors potentially affecting the Company. If any of the following risks were to occur, we may not be able to conduct our business as currently planned and our financial condition or operating results could be negatively impacted.

Regulatory considerations and recent regulatory action.

As a bank holding company under the Bank Holding Company Act, we are regulated, supervised and examined by the Board of Governors of the Federal Reserve System, or Federal Reserve Board. This regulatory framework is intended primarily for the protection of depositors and the federal deposit insurance funds and not for the protection of our shareholders. As a result of this regulatory framework, our earnings are affected by actions of the Federal Reserve Board, the Office of the Comptroller of the Currency (the "Comptroller"), which regulates the Bank, and the FDIC, which insures the deposits of the Bank within certain limits.

In addition, there are numerous governmental requirements and regulations that affect our business activities. A change in applicable statutes, regulations or regulatory policy may have a material effect on our business. Depository institutions, like the Bank, are also affected by various federal laws, including those relating to consumer protection and similar matters.

CWBC is a legal entity separate and distinct from the Bank. However, our principal source of cash revenues is the payment of dividends from the Bank. There are various legal and regulatory limitations on the extent to which the Bank can finance or otherwise supply funds to us.

As a national bank, the prior approval of the Comptroller is required if the total of all dividends declared and paid to CWBC in any calendar year exceeds the Bank's net earnings for that year combined with their retained net earnings less dividends paid for the preceding two calendar years.

Government agencies regulations also dictate the following:

- the amount of capital we must maintain;
- the types of activities in which we can engage;
- the types and amounts of investments we can make;
- the locations of our offices;
- insurance of our deposits and the premiums paid for the insurance; and
- how much cash we must set aside as reserves for deposits.

Regulations impose limitations on operations and may be changed at any time, possibly causing future results to vary significantly from past results. Regulations can significantly increase the cost of doing business such as increased deposit insurance premiums imposed by the FDIC that was paid in 2011. Moreover, certain of these regulations contain significant punitive sanctions for violations, including monetary penalties and limitations on a bank's ability to implement components of its business plan. In addition, changes in regulatory requirements may act to add costs associated with compliance efforts. Furthermore, government policy and regulation, particularly as implemented through the Federal Reserve System, significantly affect credit conditions.

On January 26, 2012, the Board of Directors of the Bank signed an Agreement with the OCC, its primary regulator. The Agreement includes, among other items, the following requirements:

- Achieving and maintaining a Tier 1 Leverage Capital ratio of 9% and Total Risk-Based Capital ratio of 12%.
- Writing a 3-year strategic plan, which would incorporate the capital component.
-

Continue to improve the Bank's credit quality and administration thereof, including the monitoring of and proper accounting for problem assets and the allowance for loan losses.

- Continue to adhere to and implement the Bank's liquidity risk management program.
- Organize a compliance committee to monitor and coordinate the Bank's compliance with and adherence to the provisions of the Agreement.

Failure to comply with the provisions of the Agreement may subject the Bank to further regulatory action including but not limited to, being deemed undercapitalized for purposes of the Agreement. Additional risks associated with compliance with the Agreement include, but are not limited to:

- a reduction in our ability to generate or originate revenue-producing assets as a result of compliance with heightened capital standards;

- an increase in the cost of operations due to greater regulatory oversight, supervision and examination of banks and bank holding companies, and higher deposit insurance premiums;

- a limitation on our ability to expand consumer product and service offerings due to anticipated stricter consumer protection laws and regulations.

Difficult economic and market conditions have adversely affected the banking industry

Dramatic declines in the housing market, with depressed home prices and high delinquencies and foreclosures during 2008 and through 2011, have negatively impacted the credit performance of mortgage, commercial and construction loans and resulted in significant write-downs of assets by many financial institutions and government sponsored entities. General downward economic trends, reduced availability of commercial credit and high unemployment have negatively impacted the credit performance of commercial and consumer credit, resulting in additional write-downs. Concerns over the stability of the financial markets and the economy have resulted in decreased lending by financial institutions to their customers and to each other. This market turmoil and tightening of credit has led to increased commercial and consumer deficiencies, lack of customer confidence, increased market volatility and widespread reduction in general business activity. In some instances, the related write-downs have caused many financial institutions to seek additional capital, to merge with larger and stronger institutions or to fail. The resulting economic pressure on consumers and businesses and the lack of confidence in the financial markets may adversely affect our business, financial condition, results of operations and stock price. A worsening of these conditions would likely exacerbate the adverse effects of these difficult market conditions on our Company. In particular, we may face the following risks in connection with these events:

- We may potentially face increased regulation of our industry. Compliance with such regulation may increase our respective costs and limit our ability to pursue business opportunities.

- 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 respective borrowers to repay their loans. The level of uncertainty concerning economic conditions may adversely affect the accuracy of these estimates which may, in turn, impact the reliability of the process.

- We could be affected by an increase in the number of clients and counterparties who become delinquent, file for protection under bankruptcy laws or default on their loans or other obligations to our Bank.

- In a sustained economic downturn, we may have an increase in the number of delinquencies, bankruptcies or defaults that could result in a higher level of nonperforming assets, net charge-offs and provision for loan losses.

- We may experience a decrease in the demand for loans and other products and services that we offer.

- Liquidity may be affected by an increase or decrease in the usage of unfunded commitments.

- We may be required to pay significantly higher FDIC premiums because market developments have significantly depleted the insurance fund of the FDIC and reduced the ratio of reserves to insured deposits.

If current levels of market disruption and volatility continue or worsen, there can be no assurance that we will not experience an adverse effect, which may be material, on our business, financial condition and results of operations.

Reserve for credit losses may not be adequate to cover actual loan losses.

The risk of nonpayment of loans is inherent in all lending activities, and nonpayment, if it occurs, may have an adverse effect on our financial condition and/or results of operations. We maintain a reserve for credit losses to absorb estimated probable credit losses inherent in the loan and commitment portfolios as of the balance sheet date. After a provision of $14.6 million for the year, as of December 31, 2011, our allowance for loan losses was $15.3 million, or 3.24% of loans held for investment. In addition, as of December 31, 2011, we had $42.3 million in loans on nonaccrual, $13.7 million of which are SBA guaranteed, and $3.1 million in loans 30 to 89 days past due with interest accruing. In determining the level of the reserve for credit losses, our management makes various assumptions and judgments about the loan portfolio. We rely on an analysis of the loan portfolio based on historical loss experience, volume and types of loans, trends in classifications, volume and trends in delinquencies and non-accruals, national and local economic conditions and other pertinent information known at the time of the analysis. If management's assumptions are incorrect, the reserve for credit losses may not be sufficient to cover losses, which could have a material adverse effect on our financial condition and/or results of operations. While the allowance was determined to be adequate at December 31, 2011, based on the information available to us at the time, there can be no assurance that the allowance will be adequate in the future.

All of our lending involves underwriting risks.

As of December 31, 2011, commercial business loans represented 7.7% of our total loan portfolio; real estate loans represented 33.5% of our total loan portfolio; SBA loans represented 20.4% of our total loan portfolio; manufactured housing loans represented 34.6% of our total portfolio and HELOC represented 3.8% of our total loan portfolio. All such lending, even when secured by the assets of a business, involves considerable risk of loss in the event of failure of the business. To reduce such risk, we typically take additional security interests in other collateral of the borrower, such as real property, certificates of deposit or life insurance, and/or obtain personal guarantees. In light of the economic downturn, our efforts to reduce risk of loss may not prove sufficient as the value of the additional collateral or personal guarantees may be significantly reduced. There can be no assurances that we have taken sufficient collateral or the values thereof will be sufficient to repay loans in accordance with their terms.

Our dependence on real estate concentrated in the State of California.

As of December 31, 2011, approximately $183.8 million, or 33.5%, of our loan portfolio is secured by various forms of real estate, including residential and commercial real estate. A further decline in current economic conditions or rising interest rates could have an adverse effect on the demand for new loans, the ability of borrowers to repay outstanding loans and the value of real estate and other collateral securing loans. The real estate securing our loan portfolio is concentrated in California. The decline in real estate values could harm the financial condition of our borrowers and the collateral for our loans will provide less security and we would be more likely to suffer losses on defaulted loans.

Legislative and regulatory initiatives to address difficult market and economic conditions may not stabilize the U.S. banking system.

The Emergency Economic Stabilization Act ("EESA"), the Financial Stability Plan ("FSP"), the American Recovery and Reinvestment Act ("ARRA") and the Homeowner Affordability and Stabilization Plan ("HASP"), and the numerous actions by the Board of Governors of the Federal Reserve System, the Treasury, the Federal Deposit Insurance Corporation ("FDIC"), the Securities and Exchange Commission ("SEC") and others are intended to address the liquidity and credit crisis, and to stabilize the U.S. banking, financial securities and housing markets. These measures include homeowner relief that encourage loan restructuring and modification; the establishment of significant liquidity and credit facilities for financial institutions and investment banks; the lowering of the federal funds rate; emergency action against short selling practices; a temporary guaranty program for money market funds; the establishment of a commercial paper funding facility to provide “back-stop” liquidity to commercial paper issuers; and coordinated international efforts to address illiquidity and other weaknesses in the banking sector. The EESA and the other regulatory initiatives described above may not have their desired effects. If the volatility in the markets continues and economic conditions fail to improve or worsen, our business, financial condition and results of operations could be materially and adversely affected.

Recently enacted legislative reforms and future regulatory reforms required by such legislation could have a significant impact on our business, financial condition and results of operations.

On July 21, 2010, President Obama signed the Dodd-Frank Wall Street Reform and Consumer Protection Act (“Dodd-Frank Act”) into law. The Dodd-Frank Act will have a broad impact on the financial services industry, including significant regulatory and compliance changes. Many of the requirements called for in the Dodd-Frank Act will be implemented over time and most will be subject to implementing regulations over the course of several years. Given the uncertainty associated with the manner in which the provisions of the Dodd-Frank Act will be implemented by the various regulatory agencies, the full extent of the impact such requirements will have on our operations is unclear. Certain provisions of the Dodd-Frank Act are expected to have a near term impact on us. For example, the Dodd-Frank Act:

- eliminates, effective one year after the date of enactment, the federal prohibitions on paying interest on demand deposits, thus allowing businesses to have interest-bearing checking accounts. Depending on competitive responses, this significant change to existing law could have an adverse impact on our interest expense;

- broadens the base for FDIC insurance assessments. Assessments will now be based on the average consolidated total assets less tangible equity capital of a financial institution;

- permanently increases the maximum amount of deposit insurance for banks, savings institutions and credit unions to $250,000 per depositor, retroactive to January 1, 2008, and noninterest-bearing transaction accounts have unlimited deposit insurance through December 31, 2013;

- requires publicly traded companies to give shareholders a non-binding vote on executive compensation and so-called “golden parachute” payments in certain circumstances;

- authorizes the SEC to promulgate rules that would allow stockholders to nominate their own candidates using a company's proxy materials, and the SEC has recently promulgated such rules;

- directs the Federal Reserve Board to promulgate rules prohibiting excessive compensation paid to bank holding company executives; and

- creates a new Consumer Financial Protection Bureau with broad powers to supervise and enforce consumer protection laws. The Consumer Financial Protection Bureau has broad rule-making authority for a wide range of consumer protection laws that apply to all banks and savings institutions, including the authority to prohibit “unfair, deceptive or abusive” acts and practices. The Consumer Financial Protection Bureau has examination and enforcement authority over all banks and savings institutions with more than $10 billion in assets. Institutions with $10 billion or less in assets, like our Company, will continued to be examined for compliance with the consumer laws by their primary bank regulators.

In addition, we anticipate that the potential impact of the Dodd-Frank Act on our operations and activities, both currently and prospectively, may include, among others:

- a reduction in our ability to generate or originate revenue-producing assets as a result of compliance with heightened capital standards;

- an increase in the cost of operations due to greater regulatory oversight, supervision and examination of banks and bank holding companies, and higher deposit insurance premiums;

- a limitation on our ability to raise capital through the use of trust preferred securities as these securities may no longer be included as Tier 1 capital going forward; and

- a limitation on our ability to expand consumer product and service offerings due to anticipated stricter consumer protection laws and regulations.

Further, we may be required to invest significant management attention and resources to evaluate and make any changes necessary to comply with new statutory and regulatory requirements under the Dodd-Frank Act. Failure to comply with the new requirements may negatively impact results of operations and financial condition. While it is difficult to predict at this time what specific impact the Dodd-Frank Act and the yet to be written implementing rules and regulations will have on us, we expect that at a minimum, operating and compliance costs and interest expense will increase.

FDIC deposit insurance premiums have increased substantially and may increase further, which will adversely affect our results of operations.

The Bank's FDIC insurance expense for the years ended December 31, 2011 and 2010 amounted to $957,000, and $1.2 million, respectively. We expect deposit insurance premiums will continue to increase for all banks, including the possibility of additional special assessments, due to recent strains on the FDIC deposit insurance fund resulting from the cost of recent bank failures. Our current level of FDIC insurance expense as well as any further increases thereto will continue to adversely affect our operating results.

Under the Federal Deposit Insurance Act, the FDIC, absent extraordinary circumstances, must establish and implement a plan to restore the deposit insurance reserve ratio to 1.15% of insured deposits at any time that the reserve ratio falls below 1.15%. Recent bank failures coupled with deteriorating economic conditions have significantly reduced the deposit insurance fund's reserve ratio. The FDIC expects insured institution failures will continue to put pressure on the Deposit Insurance Fund and result in continued charges against the Fund. Therefore, the FDIC has implemented a restoration plan that changes both its risk-based assessment system and its base assessment rates. As part of this plan, the FDIC imposed a special assessment in 2009. The recently enacted Dodd-Frank Act provides for a new minimum reserve ratio of not less than 1.35% of estimated insured deposits and required that the FDIC take steps necessary to attain this 1.35% ratio by September 30, 2010; however, the Dodd-Frank Act exempts institutions with assets of less than $10 billion, like us, from the cost of this increase. See "Supervision and Regulation– Recent Regulatory Developments." It is generally expected that assessment rates will continue to increase in the near term due to the significant cost of bank failures, the relatively large number of troubled banks and the requirement that the FDIC increase the reserve ratio. Any increase in assessments will adversely impact our future earnings.

We are subject to certain executive compensation and corporate governance restrictions as a result of our participation in the TARP-CPP.

As a result of our participation in the TARP-CPP, we have adopted the Treasury's standards for executive compensation and corporate governance for the period during which the Treasury holds an equity position acquired under the TARP-CPP. These standards generally apply to our Chief Executive Officer, our Chief Financial Officer, our Chief Credit Officer and up to the two next most highly compensated executive officers (collectively, the "senior executive officers") and with respect to certain requirements, to some or all of the Company's other employees. The standards include, without limitation: (i) ensuring that incentive compensation for senior executive officers does not encourage unnecessary and excessive risks that threaten the value of our Company, (ii) requiring the Company's compensation committee to conduct an assessment at least once every six months of the Company's compensation programs in relation to excessive risk taking and earnings manipulations, (iii) prohibiting the payment of any bonus, retention or incentive compensation to the most-highly compensated employee which may include a senior executive officer; (iv) requiring clawback of any bonus, retention or incentive compensation paid to any senior executive officer or any of the next twenty most highly-compensated employees based on statements of earnings, gains or other criteria that are later proven to be materially inaccurate, (v) prohibiting golden parachute payments to a senior executive officer, and the next five most-highly compensated employees including severance payments for any reason, (vi) prohibiting payment of any tax gross-ups with respect to any severance payments, perquisites or any other form of compensation for the senior executive officers and the next twenty highly compensated employees and (vii) our agreement not to deduct for tax purposes compensation to a senior executive officer in excess of $500,000. In particular, the change to the deductibility limit on executive compensation may increase the overall cost of our compensation programs in future periods or impact our ability to attract and retain quality executive personnel. We will be subject to the executive compensation and corporate governance restrictions for so long as the Treasury holds any equity securities issued as a result of our participation in TARP-CPP. This period could be more than ten years.

Curtailment of government guaranteed loan programs could affect a segment of our business.

A major segment of our business consists of originating and periodically selling government guaranteed loans, in particular those guaranteed by the Small Business Administration. From time to time, the government agencies that guarantee these loans reach their internal limits and cease to guarantee loans. In addition, these agencies may change their rules for loans or Congress may adopt legislation that would have the effect of discontinuing or changing the loan programs. Non-governmental programs could replace government programs for some borrowers, but the terms might not be equally acceptable. Therefore, if these changes occur, the volume of loans to small business, industrial and agricultural borrowers of the types that now qualify for government guaranteed loans could decline. Also, the profitability of these loans could decline. As the funding of the guaranteed portion of 7(a) loans is a major portion of our business, the long-term resolution to the funding for the 7(a) loan program may have an unfavorable impact on our future performance and results of operations.

Our small business customers may lack the resources to weather a downturn in the economy.

One of the primary focal points of our business development and marketing strategy is serving the banking and financial services needs of small- and medium-sized businesses and professional organizations. Small businesses generally have fewer financial resources in terms of capital or borrowing capacity than do larger entities. If economic conditions are generally unfavorable in our service areas, the businesses of our lending clients and their ability to repay outstanding loans may be negatively affected. As a consequence, our results of operations and financial condition may be adversely affected.

Environmental laws could force the Company to pay for environmental problems.

When a borrower defaults on a loan secured by real property, we generally purchase the property in foreclosure or accept a deed to the property surrendered by the borrower. We may also take over the management of commercial properties when owners have defaulted on loans. While we have guidelines intended to exclude properties with an unreasonable risk of contamination, hazardous substances may exist on some of the properties that we own, manage or occupy and unknown hazardous risks could impact the value of real estate collateral. We face the risk that environmental laws could force us to clean up the properties at our expense. It may cost much more to clean a property than the property is worth. We could also be liable for pollution generated by a borrower's operations if we took a role in managing those operations after default. Resale of contaminated properties may also be difficult.

Fluctuations in interest rates may reduce profitability.

Changes in interest rates affect interest income, the primary component of our gross revenue, as well as interest expense. The Company's earnings depend largely on the relationship between the cost of funds, primarily deposits and borrowings, and the yield on earning assets, primarily loans and investment securities. This relationship, known as the interest rate spread, is subject to fluctuation and is affected by the monetary policies of the Federal Reserve Board, the shape of the yield curve, the international interest rate environment, as well as by economic, regulatory and competitive factors which influence interest rates, the volume and mix of interest-earning assets and interest-bearing liabilities, and the level of nonperforming assets. Many of these factors are beyond our control. Fluctuations in interest rates may affect the demand of customers for products and services. As interest rates change, we expect to periodically experience "gaps" in the interest rate sensitivities of its assets and liabilities. This means that either interest-bearing liabilities will be more sensitive to changes in market interest rates than interest-earning assets, or vice versa. In either event, changes in market interest rates may have a negative impact on our earnings.

Responding to economic sluggishness and recession concerns, the Federal Reserve Board, through its Federal Open Market Committee ("FOMC"), cut the target federal funds rate beginning in September 2007 to historically low levels. The actions of the Federal Reserve Board, while designed to help the economy overall, may negatively impact the Bank's earnings.

Changes in the level of interest rates also may negatively affect our ability to originate loans, the value of loans and the ability to realize gains from the sale of loans, all of which ultimately affect earnings. A decline in the market value of our assets may limit our ability to borrow additional funds. As a result, we could be required to sell some of our loans and investments under adverse market conditions, under terms that are not favorable, to maintain liquidity. If those sales are made at prices lower than the amortized costs of the investments, losses may be incurred.

Risks due to economic conditions and environmental disasters in the regions we serve may adversely affect our operations.

The Company serves two primary regions: the Tri-Counties region, which consists of San Luis Obispo, Santa Barbara and Ventura counties in the state of California; and, the SBA Region where the Bank originates SBA loans. The current economic slowdown in those regions as well as natural disasters such as hurricanes, floods, fires and earthquakes could result in the following consequences, any of which could hurt our business:

- loan delinquencies may increase;
- problem assets and foreclosures may increase;
- demand for our products and services may decline; and
- collateral for loans made by us, especially real estate, may decline in value, in turn reducing customers' borrowing power, and reducing the value of assets and collateral associated with our existing loans.

Competition with other banking institutions could adversely affect profitability.

The banking industry is highly competitive. We face increased competition not only from other financial institutions within the markets we serve, but deregulation has resulted in competition from companies not typically associated with financial services as well as companies accessed through the internet. As a community bank, the Bank attempts to combat this increased competition by developing and offering new products and increased quality of services. Ultimately, competition can drive down the Bank's interest margins and reduce profitability and make it more difficult to increase the size of the loan portfolio and deposit base.

Operational risks may result in losses.

Operational risk represents the risk of loss resulting from our operations, including but not limited to, the risk of fraud by employees or persons outside the Company, the execution of unauthorized transactions by employees, transaction processing errors and breaches of internal control system and compliance requirements. This risk of loss also includes the potential legal actions that could arise as a result of an operational deficiency or as a result of noncompliance with applicable regulatory standards, adverse business decisions or their implementation and customer attrition due to potential negative publicity.

Operational risks are inherent in all business activities and the management of these risks is important to the achievement of our objectives. In the event of a breakdown in the internal control system, improper operation of systems or improper employee actions, we could suffer financial loss, face regulatory action and suffer damage to our reputation. We manage operational risks through a risk management framework and our internal control processes. While we believe that we have designed effective methods to minimize operational risks, there is no absolute assurance that business disruption or operational losses would not occur in the event of disaster.

We are subject to cybersecurity risks and may incur increasing costs in an effort to minimize those risks.

Our business employs systems that allow for the secure storage and transmission of customers' proprietary information. Security breaches could expose us to a risk of loss or misuse of this information, litigation and potential liability. We may not have the resources or technical sophistication to anticipate or prevent rapidly evolving types of cyber attacks. Any compromise of our security could result in a violation of applicable privacy and other laws, significant legal and financial exposure, damage to our reputation, and a loss of confidence in our security measures, which could harm our business.

A cybersecurity incident could have a negative impact on the Company

A cyber-attack that bypasses our information technology (IT) security systems causing an IT security breach, may lead to a material disruption of our IT business systems and/or the loss of business information resulting in an adverse business impact. Risks may include:

- future results could be adversely affected due to the theft, destruction, loss, misappropriation or release of confidential data or intellectual property;
- operational or business delays resulting from the disruption of IT systems and subsequent clean-up and mitigation activities; and
- negative publicity resulting in reputation or brand damage with customers, partners or industry peers.

An information systems interruption or breach in security might result in loss of customers.

We rely heavily on communications and information systems to conduct business. In addition, we rely on third parties to provide key components of information system infrastructure, including loan, deposit and general ledger processing, internet connections, and network access. Any disruption in service of these key components could adversely affect our ability to deliver products and services to customers and otherwise to conduct operations. Furthermore, any security breach of information systems or data, whether managed by the Company or by third parties, could harm our reputation or cause a decrease in the number of our customers.

We may depend on technology and technological improvements.

The financial services industry is undergoing rapid technological changes with frequent introductions of new technology-driven products and services. In addition to providing better service to customers, the effective use of technology increases efficiency and enables financial institutions to reduce costs. Many of our competitors have substantially greater resources to invest in technological improvements. We face the risk of having to keep up with the rapid technological changes.

Loss of key management personnel may adversely affect our operations.

The Bank is operated by key management personnel in each department of the Bank, including executive, lending, finance, operations and retail banking. Many of these key staff members have been employed by the Bank for a number of years and, accordingly, have developed expertise and a loyal customer following. In the event that a key management member were to terminate employment with the Bank, the effect may be to impair the Bank’s ability to operate as effectively as it does at the present time, or in the case of a former employee being hired by a competitor, may result in a loss of customers to a competitor. In addition, the loss of services of any of our executive officers, or their failure to adequately perform their management functions, would make it difficult for us to continue to grow our business, obtain and retain customers, and set up and maintain appropriate internal controls for our operations. If any member of our executive officers does not perform up to expectations, our results of operations could suffer. Finally, if any of our executive officers decides to leave, it may be difficult to replace her or him and we would lose the benefit of the knowledge she or he gained during her or his tenure with us.

Changes in accounting policies may adversely affect the reported results of operations.

The financial statements prepared by the Company are subject to various guidelines and requirements promulgated by the Financial Accounting Standards Board, the Securities and Exchange Commission and bank regulatory agencies. The adoption of new or revised accounting standards may adversely affect the reported results of operation.

Litigation risks may have a material impact on our assets or results of operations.

We are involved in various matters of litigation in the ordinary course of business which, historically, have not been material to our assets or results of operations. No assurances can be given that future litigation may not have a material impact on our assets or results of operations.

Geopolitical concerns and the heightened risk of terrorism have negatively affected the stock market and the global economy.

Stock prices domestically and around the world have been and continue to be adversely affected by geopolitical concerns and the heightened risk of terrorism. In addition to negatively affecting the stock markets, the geopolitical concerns and the heightened risk of terrorism have adversely affected, and may continue to adversely affect, the national and global economy because of the uncertainties that exist as to the instabilities in the Middle East and elsewhere, and as to how the U.S. and other countries will respond to terrorist threats or actions. All of these uncertainties may contribute to a global slowdown in economic activity. An overall weakened economy may have the effect of decreasing loan demand, increasing loan delinquencies and generally causing our results of operations and our financial condition to suffer.

Certain restrictions will affect our ability to declare or pay dividends and repurchase our shares as a result of our decision to participate in the TARP-CPP.

As a result of our participation in the TARP-CPP, our ability to declare or pay dividends on any of our common stock will be limited. Specifically, we will not be able to declare dividends payments on common, junior preferred or pari passu preferred shares if we are in arrears on the dividends on the shares of fixed rate cumulative perpetual preferred stock, Series A (the “Series A Preferred Stock”). Further, common, junior preferred or pari passu preferred shares may not be repurchased if we are in arrears on the Series A Preferred Stock dividends to the Treasury.

The Series A Preferred Stock impacts net income available to our common shareholders and earnings per common share and the Warrant we issued to the Treasury may be dilutive to holders of our common stock.

The dividends on the Series A Preferred Stock will reduce the net income available to common shareholders and our earnings per common share. The Series A Preferred Stock will also receive preferential treatment in the event of liquidation, dissolution or winding up of the Company. Additionally, the ownership interest of the existing holders of our common stock will be diluted to the extent the warrant we issued to the Treasury (“Warrant”) in conjunction with the sale to the Treasury of the Series A Preferred Stock is exercised. The shares of common stock underlying the Warrant represent approximately 8.0% of the shares of our common stock outstanding as of December 31, 2011 (including the shares issuable upon exercise of the Warrant in total shares outstanding). Although the Treasury has agreed not to vote any of the shares of common stock it receives upon exercise of the Warrant, a transferee of any portion of the Warrant or of any shares of common stock acquired upon exercise of the Warrant is not bound by this restriction.

The 9% Convertible Subordinated Debentures also impacts the net income available to our common shareholders and if converted may be dilutive to holders of our common stock.

On August 9, 2010, CWBC sold $8,085,000 of 9% Convertible Subordinated Debentures due in 2020 (“Debentures”) in a public offering in the principal amount of $1,000. The payment of the interest on the Debentures will reduce the net income available to our common shareholders and our earnings per share. The Debentures are convertible into shares of our common stock at $3.50 per share, if converted on or before July 1, 2013; at $4.50 per share if converted during the period from July 2, 2013 to July 1, 2016; and, at $6.00 per share if converted during the period from July 2, 2016 to August 9, 2020. If the Debentures are converted at a price that is less than book value per share, the holders of our common stock will be diluted and the ownership interest of the existing holders of our common stock who do not convert may also be diluted.

ITEM 1B. UNRESOLVED STAFF COMMENTS

Not applicable.

ITEM 2. PROPERTIES

The Company owns the property on which the CWB full-service branch office is located in Goleta, California. All other properties are leased by the Company, including the principal executive office in Goleta. This facility houses the Company's corporate offices, comprised of various departments, including executive management, electronic business services, finance, human resources, information technology, loan operations, marketing, the mortgage loan division, SBA administration, risk management and special assets.

The Company continually evaluates the suitability and adequacy of the Company's offices and has a program of relocating or remodeling them as necessary to maintain efficient and attractive facilities. Management believes that the Company has sufficient insurance to cover its interests in its properties, both owned and leased, and that its existing facilities are adequate for its present purposes. There are no material capital expenditures anticipated.

ITEM 3. LEGAL PROCEEDINGS

The Company is involved in various litigation matters of a routine nature that are being handled and defended in the ordinary course of the Company's business. In the opinion of Management, based in part on consultation with legal counsel, the resolution of these litigation matters will not have a material impact on the Company's financial position or results of operations. There are no pending legal proceedings to which the Company or any of its directors, officers, employees or affiliates, or any principal security holder of the Company or any associate of any of the foregoing, is a party or has an interest adverse to the Company, or of which any of the Company's properties are subject.

ITEM 4. NOT APPLICABLE

PART II

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

Market Information, Holders and Dividends

The Company’s common stock is traded on the Nasdaq Global Market (“NASDAQ”) under the symbol CWBC. The following table sets forth the high and low sales prices on a per share basis for the Company’s common stock as reported by NASDAQ for the period indicated:

	2011 Quarters				2010 Quarters			
	Fourth	Third	Second	First	Fourth	Third	Second	First
Stock Price Range:								
High	$2.60	$3.90	$4.66	$4.95	$3.80	$3.70	$3.65	$3.15
Low	1.36	1.88	3.38	3.59	2.87	2.34	2.36	2.75
Common Dividends								
Declared	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00	$0.00

As of March 23, 2012 the year to date high and low stock sales prices were $2.72 and $1.27, respectively. As of March 23, 2012, the last reported sale price per share for the Company's common stock was $2.60.

As of March 23, 2012, the Company had 306 stockholders of record of its common stock.

Preferred Stock Dividends

On December 19, 2008, as part of TARP-CPP, in exchange for an aggregate purchase price of $15,600,000, the Company issued 15,600 shares of Fixed Rate Cumulative Perpetual Preferred Stock, Series A, no par value, with a liquidation preference of $1,000 per share which pays cumulative dividends at a rate of 5% per year for the first five years and 9% per year thereafter. The Series A Preferred Stock has no maturity date and ranks senior to the common stock with respect to the payment of dividends and distributions. Preferred dividends are paid quarterly in accordance with the terms of the Series A Preferred Stock. During 2011, the Company recorded $780,000 for dividends and $267,000 in amortization of the discount on preferred stock, for a total of $1,047,000 in Series A Preferred Stock dividends. Actual Series A Preferred Stock dividends paid was $780,000 in 2011 and 2010. See “Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operations – Capital Resources – TARP-CPP.”

Common Stock Dividends

It is the Company’s intention to review its dividend policy on a quarterly basis. The Company’s last declared dividend was in April 2008. The sources of funds for dividends paid to shareholders are the Company’s capital and dividends received from its subsidiary bank, CWB. CWB’s ability to pay dividends to the Company is limited by California law and federal banking law. In addition, as a result of the Company's participation in the TARP-CPP, the Company's ability to declare or pay dividends on its common stock will be limited. See "Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations – Capital Resources –– TARP-CPP" and see “Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operations – Supervision and Regulation -CWBC - Limitations on Dividend Payments.”

Repurchases of Securities

The Company did not repurchase any of its securities during 2011 and does not currently have any publicly announced repurchase plan. The Company's ability to repurchase shares of its common stock is subject to prior approval of the FRB and the Treasury pursuant to the agreements the Company entered into in connection with its participation in the TARP-CCP.

Securities Authorized for Issuance under Equity Compensation Plans

The following table summarizes the securities authorized for issuance as of December 31, 2011:

Plan Category	Number of securities to be issued upon exercise of outstanding options, warrants and rights	Weighted-average exercise price of outstanding options, warrants and rights	Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a))
	(a)	(b)	(c)
Plans approved by shareholders	376,864	$ 6.76	281,600
Plans not approved by shareholders			
Total	376,864	$ 6.76	281,600

ITEM 6. SELECTED FINANCIAL DATA

The following selected financial data have been derived from the Company's consolidated financial condition and results of operations, as of and for the years ended December 31, 2011, 2010, 2009, 2008 and 2007, and should be read in conjunction with the consolidated financial statements and the related notes included elsewhere in this report.

	Year Ended December 31,				
	2011	2010	2009	2008	2007
STATEMENT OF OPERATIONS :	(in thousands, except per share data and ratios)				
Interest income	$36,512	$39,234	$40,903	$45,532	$46,841
Interest expense	8,250	9,957	14,945	22,223	22,834
Net interest income	28,262	29,277	25,958	23,309	24,007
Provision for loan losses	14,591	8,743	18,678	5,264	1,297
Net interest income after provision for loan losses	13,671	20,534	7,280	18,045	22,710
Non-interest income	3,144	4,015	4,418	5,081	4,845
Non-interest expenses	23,223	20,991	21,479	20,516	21,000
Income (loss) before income taxes	(6,408)	3,558	(9,781)	2,610	6,555
Provision (benefit) for income taxes	4,077	1,467	(4,018)	1,129	2,766
NET INCOME (LOSS)	$(10,485)	$2,091	$(5,763)	$1,481	$3,789
Preferred stock dividends	1,047	1,047	1,046	35	-
NET INCOME (LOSS) APPLICABLE TO COMMON STOCKHOLDERS	$(11,532)	$1,044	$(6,809)	$1,446	$3,789
PER COMMON SHARE DATA:					
Income (loss) per share – Basic	$(1.93)	$0.18	$(1.15)	$0.24	$0.65
Weighted average shares used in income per share calculation – Basic	5,980	5,915	5,915	5,913	5,862
Income (loss) per share – Diluted	$(1.93)	$0.18	$(1.15)	$0.24	$0.63
Weighted average shares used in income per share calculation – Diluted	5,980	6,833	5,915	5,941	6,022
Book value per share	$5.94	$7.92	$7.74	$8.84	$8.51
BALANCE SHEET:					
Net loans	$532,716	$580,632	$603,440	$581,075	$539,165
Total assets	633,348	667,604	684,216	656,981	609,850
Total deposits	511,262	529,893	531,392	475,439	433,739
Total liabilities	582,722	605,962	623,909	590,363	559,691
Total stockholders' equity	50,626	61,642	60,307	66,618	50,159
OPERATING AND CAPITAL RATIOS:					
Return on average equity	(16.98)%	3.42%	(9.24)%	2.85%	7.72%
Return on average assets	(1.60)	0.31	(0.85)	0.23	0.67
Dividend payout ratio	-	-	-	49.07	36.92
Equity to assets ratio	7.99	9.23	8.81	10.14	8.22
Tier 1 leverage ratio	7.91	9.08	8.81	10.28	8.39
Tier 1 risk-based capital ratio	10.08	11.40	10.93	12.45	9.87
Total risk-based capital ratio	12.92	14.16	12.20	13.70	10.74

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

The following discussion is designed to provide insight into management's assessment of significant trends related to the consolidated financial condition, results of operations, liquidity, capital resources and interest rate risk for Community West Bancshares ("CWBC") and its wholly-owned subsidiary, Community West Bank ("CWB" or "Bank"). Unless otherwise stated, "Company" refers to CWBC and CWB as a consolidated entity. The following discussion should be read in conjunction with the Company's Consolidated Financial Statements and Notes thereto and the other financial information appearing elsewhere in this 2011 Annual Report on Form 10-K.

Forward-Looking Statements

This 2011 Annual Report on Form 10-K contains statements that constitute forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. Those forward-looking statements include statements regarding the intent, belief or current expectations of the Company and its management. Any such forward-looking statements are not guarantees of future performance and involve risks and uncertainties, and actual results may differ materially from those projected in the forward-looking statements.

Overview of Earnings Performance

Net loss applicable to common shareholders of the Company was $11.5 million, or $(1.93) per basic and diluted common share for 2011 compared to net income applicable to common shareholders of $1.0 million, or $0.18 per basic and diluted common share for 2010. The Company's earnings performance was impacted in 2011 by:

§ The provision for loan losses increased to $14.6 million for 2011 compared to $8.7 million for 2010. Net charge-offs increased from $9.2 million for 2010 to $12.6 million for 2011.

§ Recognition of a deferred tax valuation allowance of $6.7 million in 4Q 2011 which resulted in a tax provision of $4.1 million for 2011 compared to a tax provision of $1.5 million for 2010.

§ A decrease in net interest income of $1.0 million, or 3.5%, from $29.3 million for 2010 to $28.3 million for 2011.

§ Interest income declined by $2.7 million, from $39.2 million for 2010 to $36.5 million for 2011, primarily due to a decline in volume.

§ Interest expense declined $1.7 million, due in relatively equal parts to a decline in rate and volume.

§ The net impact of the decline in both interest income and interest expense was a slight increase in the margin to 4.58% for 2011 compared to 4.50% for 2010.

§ Non-interest expenses for 2011 were impacted by an increase of $1.4 million in the loss on sale and write-down of foreclosed real estate and repossessed assets.

The impact to the Company from these items, and others of both a positive and negative nature, will be discussed in more detail as they pertain to the Company's overall comparative performance for the year ended December 31, 2011 throughout the analysis sections of this Annual Report.

Recent Regulatory Action

On January 26, 2012, the Board of Directors of the Bank signed a Consent Agreement (Agreement) with the Office of the Comptroller of the Currency (OCC), its primary regulator. The Agreement includes, among other things, the following requirements:

- Achieving and maintaining a Tier 1 Leverage Capital ratio of 9.00% and Total Risk-Based Capital ratio of 12.00%;
- Writing a 3-year strategic plan, which would incorporate the capital component;
- Continue to improve on the Bank's credit quality and administration thereof, including the monitoring of problem assets and the allowance for loan losses;
- Continue to adhere to and implement the Bank's liquidity risk management program.

Since the appointment of a new Chief Executive Officer and Chief Credit Officer, the Bank has maintained an intense focus on addressing the areas of concern that have been raised by the regulators. As a result, many of the prudent actions required in the Agreement have been addressed, or will be addressed in the near future. The Bank has made considerable progress in many of the areas and issues raised in the Agreement. To date, the Bank has:

- Developed a strategy to enhance capital ratios for the Bank;
- Expanded and enhanced Board membership and supervision of management, policies and objectives;
- Developed and implemented an asset disposition plan for classified assets to reduce nonperforming loans through collection and negotiations with delinquent borrowers, and to document the improved methodology of its loan loss reserve policy. As a result nonaccrual loans were reduced 21.8% at December 31, 2011 compared to September 30, 2011;
- Developed a plan to systematically diversify its loan portfolio;
- Developed a plan to systematically diversify the deposit base and reduce reliance on non-core funding. As a result core deposits increased 12.7% at December 31, 2011 compared to December 31, 2010;
- Ensured that the senior management team has the talent and expertise needed to implement this strategic realignment and determined a means to retain and recruit seasoned professionals, as necessary; and
- Developed a plan to return the Bank to profitable operations.

Some of the specific steps that will be taken to both enhance profitability and improve the Bank's capital position are:

- The sale of approximately $10.0 million in SBA loans at premiums approximating 10%
- Prepayment of FHLB advances, thereby reducing the balance sheet and removing higher costs borrowings
- The sale certain pre-identified AFS securities all of which were in an unrealized gain position
- Downstream of $500,000 to $1.0 million from the CWBC to CWB
- Lowering rates on interest bearing deposits

Additionally, the Bank has downsized the SBA group and will focus lending in California.

The Board and Management will continue to work closely with the OCC to achieve compliance with the terms of the Agreement and to improve Bank's strength, security and performance.

Critical Accounting Policies

The Company's accounting policies are more fully described in Note 1 of the Consolidated Financial Statements. As disclosed in Note 1, the preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions about future events that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ significantly from those estimates. The Company believes that the following discussion addresses the Company's most critical accounting policies, which are those that are most important to the portrayal of the Company's financial condition and results of operations and require management's most difficult, subjective and complex judgments.

Provision and Allowance for Loan Losses – The Company maintains a detailed, systematic analysis and procedural discipline to determine the amount of the allowance for loan losses ("ALL"). The ALL is based on estimates and is intended to be adequate to provide for probable losses inherent in the loan portfolio. This process involves deriving probable loss estimates that are based on migration analysis/historical loss rates and qualitative factors that are based on management's judgment. The migration analysis and historical loss rate calculations are based upon the annualized loss rates utilizing a twelve quarter loss history. Migration analysis is utilized for the Commercial Real Estate, Commercial and SBA portfolio segments. The historical loss rate method is utilized for the homogeneous loan segments which include Manufactured Housing, HELOC's, Single Family Residential and Consumer loans. The migration analysis takes into account the risk rating of loans that are charged off in each loan segment.

Foreclosed Real Estate and Repossessed Assets – Foreclosed real estate and repossessed assets includes real estate and other repossessed assets and the collateral property is recorded at fair value at the time of foreclosure less estimated costs to sell. Any excess of loan balance over the fair value less costs to sell of the other assets is charged-off against the allowance for loan losses. Subsequent to the legal ownership date, management periodically performs a new valuation and the asset is carried at the lower of carrying amount or fair value. Operating expenses or income, and gains or losses on disposition of such properties, are recorded in current operations.

Servicing Rights – The guaranteed portion of certain SBA loans can be sold into the secondary market. Servicing rights are recognized as separate assets when loans are sold with servicing retained. Servicing rights are amortized in proportion to, and over the period of, estimated future net servicing income. The Company uses industry prepayment statistics and its own prepayment experience in estimating the expected life of the loans. Management evaluates its servicing rights for impairment quarterly. Servicing rights are evaluated for impairment based upon the fair value of the rights as compared to amortized cost. Fair value is determined using discounted future cash flows calculated on a loan-by-loan basis and aggregated by predominated risk characteristics. The initial servicing rights and resulting gain on sale are calculated based on the difference between the best actual par and premium bids on an individual loan basis.

Recent Accounting Pronouncements – In April 2011, the FASB issued ASU No. 2011-02, "A Creditor's Determination of Whether a Restructuring is a Troubled Debt Restructuring." The provisions of ASU No. 2011-02 provide additional guidance related to determining whether a creditor has granted a concession, include factors and examples for creditors to consider in evaluating whether a restructuring results in a delay in payment that is insignificant, prohibit creditors from using the borrower's effective rate test to evaluate whether a concession has been granted to the borrower, and adds factors for creditors to use in determining whether a borrower is experiencing financial difficulties. A provision in ASU No. 2011-02 also ends the FASB's deferral of the additional disclosures related to troubled debt restructurings as required by ASU No. 2010-20. The provisions of ASU No. 2011-02 were effective for the Company's reporting period beginning on or after June 15, 2011. In the third quarter of 2011, the Company adopted the provisions of ASU No. 2010-20 retrospectively to all modifications and restructuring activities that have occurred from January 1, 2011.

In May 2011, the FASB issued ASU No. 2011-04, "Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs." ASU No. 2011-04 results in a consistent definition of fair value and common requirements for measurement of and disclosure about fair value between U.S. GAAP and International Financial Reporting Standards ("IFRS"). The changes to U.S. GAAP as a result of ASU No. 2011-04 are as follows: (1) The concepts of highest and best use and valuation premise are only relevant when measuring the fair value of nonfinancial assets (that is, it does not apply to financial assets or any liabilities); (2) U.S. GAAP currently prohibits application of a blockage factor in valuing financial instruments with quoted prices in active markets. ASU No. 2011-04 extends that prohibition to all fair value measurements; (3) An exception is provided to the basic fair value measurement principles for an entity that holds a group of financial assets and financial liabilities with offsetting positions in market risks or counterparty credit risk that are managed on the basis of the entity's net exposure to either of those risks. This exception allows the entity, if certain criteria are met, to measure the fair value of the net asset or liability position in a manner consistent with how market participants would price the net risk position; (4) Aligns the fair value measurement of instruments classified within an entity's shareholders' equity with the guidance for liabilities; and (5) Disclosure requirements have been enhanced for recurring Level 3 fair value measurements to disclose quantitative information about unobservable inputs and assumptions used, to describe the valuation processes used by the entity, and to describe the sensitivity of fair value measurements to changes in unobservable inputs and interrelationships between those inputs. In addition, entities must report the level in the fair value hierarchy of items that are not measured at fair value in the balance sheet but whose fair value must be disclosed. The provisions of ASU No. 2011-04 are effective for the Company's interim reporting period beginning on or after December 15, 2011. The adoption of ASU No. 2011-04 is not expected to have a material impact on the Company's statements of income and condition.

In June 2011, the FASB issued ASU No. 2011-05, "Presentation of Comprehensive Income." The provisions of ASU No. 2011-05 allow an entity the option to present the total of comprehensive income, the components of net income, and the components of other comprehensive income (OCI) either in a single continuous statement of comprehensive income or in two separate but consecutive statements. In both choices, an entity is required to present each component of net income along with total net income, each component of OCI along with a total for OCI, and a total amount for comprehensive income. The statement(s) are required to be presented with equal prominence as the other primary financial statements. ASU No. 2011-05 eliminates the option to present the components of OCI as part of the statement of changes in shareholders' equity but does not change the items that must be reported in OCI or when an item of OCI must be reclassified to net income. The provisions of ASU No. 2011-05 are effective for the Company's interim reporting period beginning on or after December 15, 2011, with retrospective application required. The adoption of ASU No. 2011-05 is expected to result in presentation changes to the Company's statements of income and the addition of a statement of comprehensive income. The adoption of ASU No. 2011-05 will have no impact on the Company's balance sheets.

In December 2011, the FASB issued ASU 2011-12 "Deferral of the Effective Date for Amendments to the Presentation of Reclassifications of Items Out of Accumulated Other Comprehensive Income in Accounting Standards Update No. 2011-05". The amendments are being made to allow the FASB time to re-deliberate whether to present on the face of the financial statements the effects of reclassifications out of accumulated other comprehensive income on the components of net income and OCI for all periods presented. Entities should continue to report reclassifications out of accumulated other comprehensive income consistent with the presentation requirements in effect before ASU 2011-05. The adoption of ASU 2011-12 will have no impact on the Company's balance sheets.

Changes in Interest Income and Interest Expense

The Company primarily earns income from the management of its financial assets and from charging fees for services it provides. The Company's income from managing assets consists of the difference between the interest income received from its loan portfolio and investments and the interest expense paid on its funding sources, primarily interest paid on deposits. This difference or spread is net interest income. The amount by which interest income will exceed interest expense depends on the volume or balance of interest-earning assets compared to the volume or balance of interest-bearing deposits and liabilities and the interest rate earned on those interest-earning assets compared to the interest rate paid on those interest-bearing liabilities.

Net interest income, when expressed as a percentage of average total interest-earning assets, is referred to as net interest margin on interest-earning assets. The Company's net interest income is affected by the change in the level and the mix of interest-earning assets and interest-bearing liabilities, referred to as volume changes. The Company's net yield on interest-earning assets is also affected by changes in the yields earned on assets and rates paid on liabilities, referred to as rate changes. Interest rates charged on the Company's loans are affected principally by the demand for such loans, the supply of money available for lending purposes, competitive factors and general economic conditions such as federal economic policies, legislative tax policies and governmental budgetary matters. To maintain its net interest margin, the Company must manage the relationship between interest earned and paid.

The following table sets forth, for the period indicated, the increase or decrease in dollars and percentages of certain items in the consolidated statement of operations as compared to the prior periods:

	Year Ended December 31,			
	2011 vs. 2010		2010 vs. 2009	
	Amount of Increase (Decrease)	Percent of Increase (Decrease)	Amount of Increase (Decrease)	Percent of Increase (Decrease)
INTEREST INCOME	(dollars in thousands)			
Loans	$(2,374)	(6.3)%	$(1,285)	(3.3)%
Investment securities	(335)	(23.9)%	(338)	(19.4)%
Other	(13)	(56.5)%	(46)	(66.7)%
Total interest income	(2,722)	(6.9)%	(1,669)	(4.1)%
INTEREST EXPENSE				
Deposits	(1,646)	(21.7)%	(3,643)	(32.4)%
Other borrowings and convertible debentures	(61)	(2.6)%	(1,345)	(36.3)%
Total interest expense	(1,707)	(17.1)%	(4,988)	(33.4)%
NET INTEREST INCOME	(1,015)	(3.5)%	3,319	12.8%
Provision for loan losses	5,848	66.9%	(9,935)	(53.2)%
NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES	(6,863)	(33.4)%	13,254	182.1%
NON-INTEREST INCOME				
Other loan fees	(585)	(29.8)%	72	3.8%
Gains from loan sales, net	(97)	(20.8)%	104	28.7%
Document processing fees, net	(126)	(23.2)%	(259)	(32.3)%
Loan servicing fees, net	(28)	(8.5)%	(445)	(57.6)%
Service charges	(26)	(4.9)%	75	16.4%
Other	(9)	(5.0)%	50	38.5%
Total non-interest income	(871)	(21.7)%	(403)	(9.1)%
NON-INTEREST EXPENSES				
Salaries and employee benefits	(7)	(0.1)%	(73)	(0.6)%
Occupancy and equipment expenses	(36)	(1.8)%	(107)	(5.1)%
FDIC assessment	(253)	(20.9)%	(386)	(24.2)%
Professional services	241	29.5%	(84)	(9.3)%
Advertising and marketing	94	31.2%	(43)	(12.5)%
Depreciation	(51)	(12.0)%	(66)	(13.4)%
Loss on sale and write-down of foreclosed real estate and repossessed assets	1,382	120.1%	536	87.2%
Data processing	(8)	(1.5)%	(83)	(13.4)%
Other	870	32.0%	(182)	(6.3)%
Total non-interest expenses	2,232	10.6%	(488)	(2.3)%
Income (loss) before provision for income taxes	(9,966)		13,339	
Provision for income taxes	2,610		5,485	
NET INCOME (LOSS)	$(12,576)		$7,854	
Preferred stock dividends	-		1	
NET INCOME (LOSS) APPLICABLE TO COMMON STOCKHOLDERS	$(12,576)		$7,853	

Comparison of 2011 to 2010

Net interest income declined by $1.0 million, or 3.5%, for 2011 compared to 2010.

Total interest income declined by $2.7 million, or 6.9%, from $39.2 million in 2010 to $36.5 million in 2011. Of this decline, $2.1 million resulted from the decline in interest earnings assets from $650.4 million for 2010 to $617.0 million for 2011. Also contributing to the decline was an increase in non-accrual loans from $35.0 million at December 31, 2010 to $42.3 million at December 31, 2011. Yields on interest earning-assets also declined from 6.03% for 2010 to 5.92% for 2011.

The decline in interest income was partly offset by the reduction of interest expense from $10.0 million for 2010 to $8.3 million for 2011. Of this decline, $822,000 resulted from lower rates paid on deposits and borrowings. Rates on interest-bearing deposits declined from 1.52% for 2010 to 1.27% for 2011. Overall, rates on deposits and borrowings were 1.53% for 2011 compared to 1.73% for 2010.

The combination of the decline in rates paid on deposits and borrowings and the decline in yields on interest-earning assets resulted in a margin improvement of 0.08% from 4.50% for 2010 to 4.58% for 2011.

Comparison of 2010 to 2009

Net interest income increased by $3.3 million, or 12.8%, for 2010 compared to 2009.

Total interest income declined by $1.7 million, or 4.1%, from $40.9 million in 2009 to $39.2 million in 2010. Of this decline, $1.3 million was due to a decline in yields on interest-earning assets, which declined from 6.17% for 2009 to 6.03% for 2010. The remaining decline resulted from the decline in the average balance of interest-earning assets from $663.2 million for 2009 to $650.4 million for 2010.

The decline in interest income was more than offset by the reduction of interest expense from $14.9 million for 2009 to $10.0 million for 2010. Of this decline, $4.2 million resulted from lower rates paid on deposits and borrowings. Rates on interest-bearing deposits declined from 2.42% for 2009 to 1.52% for 2010. Overall, rates on deposits and borrowings were 1.73% for 2010 compared to 2.60% for 2009.

The combination of the decline in rates paid on deposits and borrowings and the decline in yields on interest-earning assets resulted in a margin improvement of 0.59% from 3.91% for 2009 to 4.50% for 2010.

The following table sets forth the changes in interest income and expense attributable to changes in rate and volume:

	Year Ended December 31,					
	2011 versus 2010			2010 versus 2009		
	Total change	Change due to Rate	Change due to Volume	Total change	Change due to Rate	Change due to Volume
	(in thousands)					
Interest-earning deposits in other financial institutions (including time deposits)	$ (11)	$ (4)	$ (7)	$ (14)	$ -	$ (14)
Federal funds sold	(2)	-	(2)	(32)	(4)	(28)
Investment securities	(335)	(339)	4	(338)	(318)	(20)
Loans, net	(2,374)	(299)	(2,075)	(1,285)	(1,012)	(273)
Total interest-earning assets	(2,722)	(642)	(2,080)	(1,669)	(1,334)	(335)
Interest-bearing demand	(235)	(734)	499	1,000	(515)	1,515
Savings	(58)	(81)	23	(4)	(65)	61
Time certificates of deposit	(1,353)	(107)	(1,246)	(4,639)	(3,308)	(1,331)
Other borrowings	(61)	100	(161)	(1,345)	(303)	(1,042)
	(1,707)	(822)	(885)	(4,988)	(4,191)	(797)

Total interest-bearing liabilities																	
Net interest income	$	(1,015	)	$	180		$	(1,195	)	$	3,319		$	2,857		$	462

The following table presents the net interest income and net interest margin for the three years indicated:

	Year Ended December 31, 2011	2010	2009
	(dollars in thousands)		
Interest income	$36,512	$39,234	$40,903
Interest expense	8,250	9,957	14,945
Net interest income	$28,262	$29,277	$25,958
Net interest margin	4.58 %	4.50 %	3.91 %

Provision for Loan Losses

The provision for loan losses increased $5.8 million to $14.6 million for 2011 compared to $8.7 million for 2010.

The following schedule summarizes the provision, charge-offs and recoveries by loan segment for the year ended December 31, 2011:

	Allowance 12/31/10	Provision	Charge-offs	Recoveries	Net Charge-offs	Allowance 12/31/11
			(in thousands)			
Manufactured housing	$4,168	$3,384	$(2,996)	$73	$ (2,923)	$4,629
Commercial real estate	2,532	5,215	(4,224)	5	(4,219)	3,528
Commercial	2,094	2,718	(2,153)	75	(2,078)	2,734
SBA	3,753	2,755	(2,930)	299	(2,631)	3,877
HELOC	547	(197)	(1)	-	(1)	349
Single family real estate	135	786	(788)	17	(771)	150
Consumer	73	(70)	-	-	-	3
Total	$13,302	$14,591	$(13,092)	$469	$ (12,623)	$15,270

The following schedule summarizes the provision, charge-offs and recoveries by loan segment for the year ended December 31, 2010:

	Allowance 12/31/09	Provision	Charge-offs	Recoveries	Net Charge-offs	Allowance 12/31/10
			(in thousands)			
Manufactured housing	$2,255	$4,072	$(2,202)	$43	$ (2,159)	$4,168
Commercial real estate	2,843	873	(1,192)	8	(1,184)	2,532
Commercial	3,448	(398)	(1,055)	99	(956)	2,094
SBA	4,837	3,184	(4,628)	360	(4,268)	3,753
HELOC	124	873	(458)	8	(450)	547
Single family real estate	143	172	(186)	6	(180)	135
Consumer	83	(33)	(1)	24	23	73
Total	$13,733	$8,743	$(9,722)	$548	$ (9,174)	$13,302

The allowance for loan losses increased 14.8% in response to key metric increases including a rise in the level of charge-offs, the balance of non-accrual and impaired loans and overall loan portfolio classifications. While past due loans have increased in several categories, overall there has been a decline from $27.1 million to $24.9 million. SBA loans past due declined from $20.1 million to $10.0 million and are primarily responsible for the overall reduction. While impaired loans increased $25.0 million, the specific valuation allowance on impaired loans remained relatively stable. The specific allowance of $248,000 to total impaired loans of $39.9 million indicates an expectation, based on current known facts, that principal will be recovered on most of these loans. However, challenges remain in the portfolio in which net non-accrual loans have increased from $12.7 million at December 31, 2010 to $28.7 million at December 31, 2011 and net charge-offs increased from $9.2 million for 2010 to $12.6 for 2011. Past portfolio performance is not necessarily indicative of future results.

Included in the Company's held-to-maturity portfolio is home equity loans, "HELOC", which guidance issued by the SEC characterizes as higher-risk. The HELOC portfolio of $20.3 million consists of credits secured by residential real estate in Santa Barbara and Ventura counties. In 2011, the net charge-offs in this portfolio were $1,000. As of December 31, 2011, $333,000 of the portfolio is past due and $29,000 is on non-accrual status. The allowance for loan losses for this portfolio is $349,000, or 1.7%. The Company believes that, overall, this portfolio is adequately supported by real estate collateral.

The percentage of net non-accrual loans to the total loan portfolio has increased to 5.23% as of December 31, 2011 from 2.13% at December 31, 2010. The allowance for loan losses compared to net non-accrual loans has decreased to 53.3% as of December 31, 2011 from 105% as of December 31, 2010.

Non-Interest Income

The following table summarizes the Company's non-interest income for the three years indicated:

	Year Ended December 31,		
Non-interest income	2011	2010	2009
		(in thousands)	
Other loan fees	$1,380	$1,965	$1,893
Gains from loan sales, net	370	467	363
Document processing fees, net	418	544	803
Loan servicing fees, net	300	328	773
Service charges	505	531	456
Other	171	180	130
Total non-interest income	$3,144	$4,015	$4,418

Comparison of 2011 to 2010

Non-interest income declined by $871,000 to $3.1 million for 2011 compared to $4.0 million for 2010, due to the decline in loan origination and document processing fees associated with mortgage originations and SBA related loan fees.

Comparison of 2010 to 2009

Non-interest income declined by $403,000 to $4.0 million for 2010 compared to $4.4 million for 2009, primarily due to the decline in loan servicing fees. No SBA loans were sold in 2010 and servicing income has declined as the principle balance of loans on which servicing is earned pay down. The amortization of the servicing asset and adjustments to the valuation of the interest only strip were higher in 2010 by $250,000, also contributing to a reduction in servicing income.

Non-Interest Expenses

The following table summarizes the Company's non-interest expenses for the three years indicated:

	Year Ended December 31,		
Non-interest expenses	2011	2010	2009
		(in thousands)	
Salaries and employee benefits	$11,816	$11,823	$11,896
Occupancy and equipment expenses	1,969	2,005	2,112
FDIC assessment	957	1,210	1,596
Professional services	1,058	817	901
Advertising and marketing	395	301	344
Depreciation	374	425	491
Loss on sale and write-down of foreclosed real estate and repossessed assets	2,533	1,151	615
Data processing	529	537	620

Other	3,592	2,722	2,904
Total non-interest expenses	$23,223	$20,991	$21,479

Comparison of 2011 to 2010

Non-interest expenses increased $2.2 million, or 10.6%, to $23.2 million for 2011 compared to $21.0 million for 2010. The largest increase resulted from loss on sale and write-down of foreclosed real estate and repossessed assets. This expense was $2.5 million for 2011 compared to $1.2 million for 2010, an increase of $1.4 million. Other non-interest expenses increased by $870,000, or 32%, over 2010. Contributing to higher other non-interest expenses was an increase of $470,000 related to the reserve for undisbursed loans. Loan collection expense and costs related to foreclosed real estate and repossessed assets increased $105,000 and $234,000, respectively, for 2011 compared to 2010.

Comparison of 2010 to 2009

Non-interest expenses declined $488,000, to $21.0 million for 2010 from $21.5 million for 2009. Expenses declined in all categories except for the loss on sale and write-down of foreclosed real estate and repossessed assets. The FDIC assessment declined in 2010 by $386,000 in comparison to 2009 which was subject to a special assessment in June 2009 of $306,000. The loss on sale and write-down of foreclosed real estate and repossessed assets increased $536,000 primarily due to losses and write-downs of manufactured housing properties.

The following table compares the various elements of non-interest expenses as a percentage of average assets and the efficiency ratio which is the ratio of non-interest expense to the total of net interest income and non-interest income:

Year Ended December 31, (dollars in thousands)	Average Assets	Total Non-Interest Expenses	Salaries and Employee Benefits	Occupancy and Depreciation Expenses	Efficiency Ratio
2011	$653,822	3.55 %	1.81 %	0.36 %	74 %
2010	$676,776	3.10 %	1.75 %	0.36 %	63 %
2009	$675,672	3.18 %	1.76 %	0.39 %	71 %

Income Taxes

The provision for income taxes was $4.1 million for 2011 compared to a provision of $1.5 million in 2010 and a benefit for income taxes of $4.0 million in 2009. The effective income tax rate was (63.6)%, 41.2%, and 41.1% for 2011, 2010 and 2009, respectively.

The Company recognizes deferred tax assets and liabilities for the future tax consequences related to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax base, and for tax credits. The deferred tax assets, net of valuation allowance, totaled $306,000 and $5.9 million as of December 31, 2011 and 2010, respectively. Management evaluates the Company's deferred tax assets for recoverability using a consistent approach which considers the relative impact of negative and positive evidence, including the Company's historical profitability and projections of future taxable income. The Company is required to establish a valuation allowance for deferred tax assets and record a charge to income if Management determines, based on available evidence at the time the determination is made, that it is more likely than not that some portion or all of the deferred tax assets may not be realized.

For the three year period ended December 31, 2011, the Company is in a cumulative pretax loss position. For purposes of establishing a deferred tax valuation allowance, this cumulative pretax loss position is considered significant, objective evidence that the Company may not be able to realize some portion of the deferred tax asset in the future. As a result, the Company has established a valuation allowance for the deferred tax asset of $6.7 million as of December 31, 2011. The net deferred tax asset of $306,000 represents the estimated amount of tax that Management has determined may be recoverable through carryback of tax losses to prior years. Also included in other assets is a $2.7 million tax receivable resulting from estimated tax payments and carryback of tax losses to prior years.

See Note 12, "Income Taxes", in the notes to the Consolidated Financial Statements.

Schedule of Average Assets, Liabilities and Stockholders' Equity

As of the dates indicated below, the following schedule shows the average balances of the Company's assets, liabilities and stockholders' equity accounts and, for each balance, the percentage of average total assets:

	December 31,					
	2011		2010		2009	
	Amount	%	Amount	%	Amount	%
ASSETS			(dollars in thousands)			
Cash and due from banks	$16,440	2.5 %	$11,748	1.7 %	$4,949	0.7 %
Time and interest-earning deposits in other financial institutions	317	-	607	0.1 %	1,081	0.2 %
Federal funds sold	927	0.1 %	1,748	0.3 %	10,751	1.6 %
Investment securities available-for-sale	23,857	3.7 %	19,776	2.9 %	14,178	2.1 %
Investment securities held-to-maturity	15,279	2.3 %	18,435	2.7 %	24,619	3.6 %
Federal Reserve Bank & Federal Home Loan Bank stock	5,977	0.9 %	6,741	1.0 %	6,781	1.0 %
Loans held for sale, net	76,951	11.8 %	90,560	13.4 %	100,823	14.9 %
Loans held for investment, net	480,012	73.4 %	499,018	73.7 %	493,016	73.0 %
Servicing rights	717	0.1 %	875	0.1 %	1,086	0.2 %
Foreclosed real estate and repossessed assets	8,462	1.3 %	4,745	0.7 %	2,496	0.4 %
Premises and equipment, net	3,006	0.5 %	3,103	0.5 %	3,506	0.5 %
Other assets	21,877	3.4 %	19,420	2.9 %	12,386	1.8 %
TOTAL ASSETS	$653,822	100.0 %	$676,776	100.0 %	$675,672	100.0 %
LIABILITIES						
Deposits:						
Non-interest-bearing demand	$50,144	7.6 %	$39,025	5.8 %	$37,408	5.5 %
Interest-bearing demand	280,950	43.0 %	232,540	34.3 %	119,923	17.8 %
Savings	20,701	3.2 %	19,452	2.9 %	16,807	2.5 %
Time certificates of $100,000 or more	124,397	19.0 %	173,860	25.7 %	149,291	22.1 %
Other time certificates	43,580	6.7 %	72,576	10.7 %	178,744	26.4 %
Total deposits	519,772	79.5 %	537,453	79.4 %	502,173	74.3 %
Other borrowings	71,175	10.9 %	76,138	11.3 %	109,767	16.3 %
Other liabilities	1,116	0.2 %	2,053	0.3 %	1,379	0.2 %
Total liabilities	592,063	90.6 %	615,644	91.0 %	613,319	90.8 %
STOCKHOLDERS' EQUITY						
Preferred stock	14,931	2.3 %	14,668	2.2 %	14,407	2.1 %
Common stock	33,370	5.1 %	33,121	4.9 %	33,097	4.9 %
Retained earnings	13,311	2.0 %	13,161	1.9 %	14,763	2.2 %
Accumulated other comprehensive income	147	-	182	-	86	-
Total stockholders' equity	61,759	9.4 %	61,132	9.0 %	62,353	9.2 %
	$653,822	100.0 %	$676,776	100.0 %	$675,672	100.0 %

TOTAL LIABILITIES AND
STOCKHOLDERS' EQUITY

Interest Rates and Differentials

The following table illustrates average yields on interest-earning assets and average rates paid on interest-bearing liabilities for the years indicated. These average yields and rates are derived by dividing interest income by the average balances of interest-earning assets and by dividing interest expense by the average balances of interest-bearing liabilities for the years indicated. Amounts outstanding are averages of daily balances during the period.

	Year Ended December 31,					
Interest-earning assets:	2011		2010		2009	
	(dollars in thousands)					
Time and interest-earning deposits in other financial institutions:						
Average outstanding	$318		$607		$1,081	
Interest income	7		18		32	
Average yield	2.27	%	3.00	%	2.95	%
Federal funds sold:						
Average outstanding	$927		$1,748		$10,751	
Interest income	3		5		37	
Average yield	0.30	%	0.31	%	0.34	%
Investment securities:						
Average outstanding	$45,113		$44,952		$45,578	
Interest income	1,067		1,402		1,740	
Average yield	2.37	%	3.12	%	3.82	%
Gross loans:						
Average outstanding (1)	$570,684		$603,141		$605,741	
Interest income	35,435		37,809		39,094	
Average yield	6.21	%	6.27	%	6.45	%
Total interest-earning assets:						
Average outstanding	$617,042		$650,448		$663,151	
Interest income	36,512		39,234		40,903	
Average yield	5.92	%	6.03	%	6.17	%
Interest-bearing liabilities:						
Interest-bearing demand deposits:						
Average outstanding	$280,950		$232,540		$119,923	
Interest expense	2,894		3,130		2,130	
Average effective rate	1.03	%	1.35	%	1.78	%
Savings deposits:						
Average outstanding	$20,701		$19,452		$16,807	
Interest expense	389		447		451	
Average effective rate	1.88	%	2.30	%	2.68	%
Time certificates of deposit:						
Average outstanding	$167,977		$246,436		$328,035	
Interest expense	2,668		4,020		8,659	
Average effective rate	1.59	%	1.63	%	2.64	%
Other borrowings:						
Average outstanding	$63,299		$72,926		$109,767	
Interest expense	1,590		2,071		3,705	
Average effective rate	2.51	%	2.84	%	3.38	%
Convertible debentures:						

Average outstanding	$7,876		$3,212		-	
Interest expense	709		289		-	
Average effective rate	9.00	%	9.00	%	-	
Total interest-bearing liabilities:						
Average outstanding	$540,803		$574,566		$574,532	
Interest expense	8,250		9,957		14,945	
Average effective rate	1.53	%	1.73	%	2.60	%
Net interest income	$28,262		$29,277		$25,958	
Net interest spread	4.39	%	4.30	%	3.57	%
Average net margin	4.58	%	4.50	%	3.91	%

(1) Nonaccrual loans are included in the average balance of loans outstanding

Loan Portfolio

The Company's largest categories of loans held in the portfolio are commercial, commercial real estate and construction, SBA and manufactured housing loans. Loans are carried at face amount, net of payments collected, the allowance for loan loss and deferred loan fees/costs. Interest on all loans is accrued daily, primarily on a simple interest basis. For all loan segments, the accrual of interest is discontinued when substantial doubt exists as to collectability of the loan, generally at the time the loan is 90 days delinquent, unless the credit is well secured and in process of collection. Any unpaid but accrued interest is reversed at that time. Thereafter, interest income is usually no longer recognized on the loan. Interest on non-accrual loans is accounted for on the cash-basis or cost-recovery method, until qualifying for return to accrual. Loans are returned to accrual status when all of the principal and interest amounts contractually due are brought current and future payments are reasonably assured.

The rates charged on variable rate loans are set at specific increments. These increments vary in relation to the Company's published prime lending rate or other appropriate indices. At December 31, 2011 and 2010, approximately 70.5% and 68.4%, respectively, of the Company's loan portfolio was comprised of variable interest rate loans. Management monitors the maturity of loans and the sensitivity of loans to changes in interest rates.

The following table sets forth, as of the dates indicated, the amount of gross loans outstanding based on the remaining scheduled repayments of principal, which could either be repriced or remain fixed until maturity, classified by scheduled principal payments:

	December 31,									
	2011		2010		2009		2008		2007	
In Years					(in thousands)					
	Fixed	Variable	Fixed	Variable	Fixed	Variable	Fixed	Variable	Fixed	Variable
Less than One	$19,822	$53,168	$20,542	$62,708	$20,571	$81,132	$16,405	$78,005	$16,445	$83,356
One to Five	85,870	126,661	85,103	121,569	87,062	130,364	87,034	82,298	79,549	67,549
Over Five	56,085	206,596	81,915	222,363	111,243	187,200	137,632	187,525	129,335	167,878
Total	$161,777	$386,425	$187,560	$406,640	$218,876	$398,696	$241,071	$347,828	$225,329	$318,783
	29.5 %									