

PAN PACIFIC BANK

FINANCIAL STATEMENTS

AS OF DECEMBER 31, 2008 AND 2007 AND

FOR THE YEARS THEN ENDED

AND

INDEPENDENT AUDITOR'S REPORT

INDEPENDENT AUDITOR'S REPORT

The Shareholders and
Board of Directors
Pan Pacific Bank

We have audited the accompanying balance sheet of Pan Pacific Bank as of December 31, 2008 and 2007 and the related statements of operations, changes in shareholders' equity and cash flows for the years then ended. These financial statements are the responsibility of the Bank's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Pan Pacific Bank as of December 31, 2008 and 2007 and the results of its operations and its cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

Perry-Smith LLP

May 5, 2009

PAN PACIFIC BANK

BALANCE SHEET

December 31, 2008 and 2007

	<u>2008</u>	<u>2007</u>
ASSETS		
Cash and due from banks	\$ 1,238,878	\$ 1,328,405
Federal funds sold		<u>3,325,000</u>
Cash and cash equivalents	1,238,378	4,653,405
Available-for-sale investment securities (Note 2)	4,950,130	6,645,779
Loans less allowance for loan losses of \$1,048,000 in 2008 and \$607,700 in 2007 (Notes 3, 6 and 8)	75,285,708	57,406,917
Federal Home Loan Bank stock	735,800	243,500
Bank premises and equipment (Note 4)	434,004	526,754
Accrued interest receivable and other assets	<u>542,290</u>	<u>579,977</u>
Total assets	<u>\$ 83,186,810</u>	<u>\$ 70,056,332</u>
LIABILITIES AND SHAREHOLDERS' EQUITY		
Deposits:		
Non-interest bearing	\$ 9,999,688	\$ 9,154,928
Interest bearing (Note 5)	<u>45,305,292</u>	<u>48,899,288</u>
Total deposits	55,304,980	58,054,216
Short-term borrowings (Note 6)	15,952,000	
Accrued interest payable and other liabilities	<u>305,112</u>	<u>368,074</u>
Total liabilities	<u>71,562,092</u>	<u>58,422,290</u>
Commitments and contingencies (Note 8)		
Shareholders' equity (Notes 9 and 10):		
Preferred stock – no par value; 10,000,000 shares authorized; none issued or outstanding		
Common stock - no par value; 40,000,000 shares authorized; 1,584,500 shares issued and outstanding at December 31, 2008 and 2007	16,366,964	16,195,964
Accumulated deficit	(4,785,607)	(4,543,745)
Accumulated other comprehensive income (loss)	<u>43,361</u>	<u>(18,177)</u>
Total shareholders' equity	<u>11,624,718</u>	<u>11,634,042</u>
	<u>\$ 83,186,810</u>	<u>\$ 70,056,332</u>

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

PAN PACIFIC BANK
STATEMENT OF OPERATIONS

For the Years Ended December 31, 2008 and 2007

	<u>2008</u>	<u>2007</u>
Interest income:		
Interest and fees on loans	\$ 3,947,099	\$ 3,612,758
Interest on Federal funds sold	26,052	449,933
Interest on investment securities	<u>288,513</u>	<u>503,883</u>
Total interest income	<u>4,261,664</u>	<u>4,566,574</u>
Interest expense:		
Interest on deposits (Note 5)	1,004,761	2,137,987
Interest on borrowed funds (Note 6)	<u>63,067</u>	<u>5,853</u>
Total interest expense	<u>1,067,828</u>	<u>2,143,840</u>
Net interest income before provision for loan losses	3,193,836	2,422,734
Provision for loan losses (Note 3)	<u>440,300</u>	<u>269,700</u>
Net interest income after provision for loan losses	<u>2,753,536</u>	<u>2,153,034</u>
Non-interest income:		
Service charges and fees	<u>90,242</u>	<u>33,863</u>
Other expenses:		
Salaries and employee benefits (Notes 3 and 12)	1,794,270	1,906,167
Occupancy and equipment (Notes 4 and 8)	256,717	327,517
Other (Note 13)	<u>1,034,653</u>	<u>1,140,934</u>
Total other expenses	<u>3,085,640</u>	<u>3,374,618</u>
Net loss	<u>\$ (241,862)</u>	<u>\$ (1,187,721)</u>
Loss per share	<u>\$ (0.15)</u>	<u>\$ (0.75)</u>
Weighted average number of shares outstanding	<u>1,584,500</u>	<u>1,584,500</u>

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

PAN PACIFIC BANK

STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY

For the Years Ended December 31, 2008 and 2007

	<u>Common Stock</u>		<u>Accumulated Deficit</u>	<u>Accumulated Other Comprehensive (Loss) Income</u>	<u>Total Shareholders' Equity</u>
	<u>Shares</u>	<u>Amount</u>			
Balance, January 1, 2007	1,584,500	15,981,748	(3,356,024)	(119,619)	12,506,105
Net loss			(1,187,721)		(1,187,721)
Net change in unrealized loss on available-for-sale investment securities (Note 2)				101,442	101,442
Stock-based compensation (Note 10)		214,216			214,216
Balance, December 31, 2007	1,584,500	16,195,964	(4,543,745)	(18,177)	11,634,042
Net loss			(241,862)		(241,862)
Net change in unrealized loss on available-for-sale investment securities (Note 2)				61,538	61,538
Stock-based compensation (Note 10)		171,000			171,000
Balance, December 31, 2008	<u>1,584,500</u>	<u>\$ 16,366,964</u>	<u>\$ (4,785,607)</u>	<u>\$ 43,361</u>	<u>\$ 11,624,718</u>
				<u>2008</u>	<u>2007</u>
Comprehensive loss:					
Net loss				\$ (241,862)	\$ (1,187,721)
Other comprehensive income:					
Unrealized holding gains on available-for-sale investment securities arising during the period				61,538	101,442
Total comprehensive loss				<u>\$ (180,324)</u>	<u>\$ (1,086,279)</u>

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

PAN PACIFIC BANK
STATEMENT OF CASH FLOWS

For the Years Ended December 31, 2008 and 2007

	<u>2008</u>	<u>2007</u>
Cash flows from operating activities:		
Net loss	\$ (241,862)	\$ (1,187,721)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:		
Provision for loan losses	440,300	269,700
Depreciation and amortization	139,342	142,662
Share-based compensation	171,000	214,216
Increase in deferred loan origination fees, net	20,552	115,777
Net amortization of investment security premiums and discounts	(11,666)	(53,987)
Decrease (increase) in interest receivable and other assets	37,687	(69,682)
(Decrease) increase in interest payable and other liabilities	<u>(62,962)</u>	<u>129,472</u>
Net cash provided by (used in) operating activities	<u>492,391</u>	<u>(439,563)</u>
Cash flows from investing activities:		
Maturity of available-for-sale investment securities	500,000	5,875,000
Principle repayments received from available-for-sale investment securities	1,268,853	1,366,528
Net increase in loans	(18,339,643)	(32,480,401)
Purchase of leasehold improvements and equipment	(46,592)	(51,266)
Purchase of Federal Home Loan Bank stock	<u>(492,300)</u>	<u>(41,400)</u>
Net cash used in investing activities	<u>(17,109,682)</u>	<u>(25,331,539)</u>
Cash flows from financing activities:		
Net (decrease) increase in demand, interest bearing and savings deposits	(11,502,274)	17,645,616
Net increase (decrease) in time deposits	8,753,038	(9,703,795)
Net increase in short-term borrowings	<u>15,952,000</u>	<u> </u>
Net cash provided by financing activities	<u>13,202,764</u>	<u>7,941,821</u>
Decrease in cash and cash equivalents	(3,414,527)	(17,829,281)
Cash and cash equivalents at beginning of period	<u>4,653,405</u>	<u>22,482,686</u>
Cash and cash equivalents at end of year	<u>\$ 1,238,878</u>	<u>\$ 4,653,405</u>
Supplemental disclosure of cash flow information:		
Cash paid during the year for:		
Interest expense	\$ 1,204,193	\$ 2,123,236
Non-cash investing activities:		
Net change in unrealized gain on available-for-sale investment securities	\$ 61,538	\$ 101,442

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

PAN PACIFIC BANK

NOTES TO FINANCIAL STATEMENTS

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Pan Pacific Bank (the Bank) is a state-chartered financial institution headquartered in Fremont, California. The Bank was organized March 10, 2005, and opened for business on July 18, 2005 following the successful offering of 1,584,500 shares of the Bank's common stock. The Bank engages in traditional banking activities offered through its financial center in Fremont, California. The Bank's deposits are insured up to applicable legal limits by the Federal Deposit Insurance Corporation (FDIC), which also regulates the Bank together with the California Department of Financial Institutions (DFI).

The Bank is participating in the FDIC's Transaction Account Guarantee Program. Under this program, through December 31, 2009, all noninterest-bearing transaction accounts are fully guaranteed by the FDIC for the entire amount in the account and the Bank is assessed an annual fee of 10 basis points for all deposit amounts exceeding the existing deposit insurance limit of \$250,000. Coverage under the Transaction Account Guarantee Program is in addition to and separate from the coverage available under the FDIC's general deposit insurance rules.

The financial statements of the Bank are prepared in conformity with accounting principles generally accepted in the United States of America and prevailing practices within the banking industry. The following is a summary of the significant accounting and reporting policies used in preparing the Bank's financial statements.

Use of Estimates

In preparing the financial statements, management is required to make estimates and assumptions that affect reported amounts as of the date of the balance sheet and revenues and expenses for the period. These estimates are based on information available as of the date of the financial statements. Therefore, actual results could differ from those estimates.

Cash and Cash Equivalents

For purposes of the statement of cash flows, the Bank has defined cash and cash equivalents as those amounts included in the balance sheet captions cash and due from banks and Federal Funds sold. Generally, Federal Funds sold are for one-day periods. For these instruments, the carrying amount is a reasonable estimate of fair value.

Investment Securities

Investment securities are classified into the following categories:

- Available-for-sale securities, reported at fair value, with unrealized gains and losses excluded from earnings and reported, net of taxes, as accumulated other comprehensive income (loss) within shareholders' equity.
- Held-to-maturity securities, which management has both the positive intent and ability to hold to maturity, reported at amortized cost, adjusted for the accretion of discounts and amortization of premiums.

PAN PACIFIC BANK

NOTES TO FINANCIAL STATEMENTS

(Continued)

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Investment Securities (Continued)

Management determines the appropriate classification of its investments at the time of purchase and may only change the classification in certain limited circumstances. All transfers between categories are accounted for at fair value. At December 31, 2008, all securities were classified as available-for-sale and there were no transfers between classifications during 2008 or 2007.

Gains or losses on the sale of securities are computed using the specific identification method. Interest earned on investment securities is reported in interest income, net of applicable adjustments for accretion of discounts and amortization of premiums.

Investment securities are impaired when their carrying value is greater than their fair value.

Investment securities are evaluated for impairment on at least a quarterly basis and more frequently when economic or market conditions warrant such an evaluation to determine whether a decline in their value below amortized cost is other than temporary. Management utilizes criteria such as the magnitude and duration of the decline and the intent and ability of the Bank to retain its investment in the issues for a period of time sufficient to allow for an anticipated recovery in fair value, in addition to the reasons underlying the decline, to determine whether the loss in value is other than temporary. The term "other than temporary" is not intended to indicate that the decline is permanent, but indicates that the prospects for a near-term recovery of value is not necessarily favorable, or that there is a lack of evidence to support a realizable value equal to or greater than the carrying value of the investment. Once a decline in value is determined to be other than temporary, the value of the security is reduced and a corresponding charge to earnings is recognized. Management determined that none of the Bank's investment securities were impaired at December 31, 2008.

Investment in Federal Home Loan Bank Stock

As a member of the Federal Home Loan Bank of San Francisco, the Bank is required to maintain an investment in the capital stock of the Federal Home Loan Bank (FHLB). The investment is carried at cost. At December 31, 2008 and 2007, FHLB stock totaled \$735,800 and \$243,500, respectively.

On January 8, 2009, the FHLB notified its members that it would not pay a dividend for the fourth quarter of 2008 and would not purchase excess capital stock on January 31, 2009.

PAN PACIFIC BANK

NOTES TO FINANCIAL STATEMENTS

(Continued)

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Loans

Loans are stated at principal balances outstanding and interest is accrued daily based upon outstanding loan balances. However, when, in the opinion of management, loans are considered to be impaired and the future collectibility of interest and principal is in serious doubt, loans are placed on nonaccrual status and the accrual of interest income is suspended. Any interest accrued but unpaid is charged against income. Payments received are applied to reduce principal to the extent necessary to ensure collection. Subsequent payments on these loans, or payments received on nonaccrual loans for which the ultimate collectibility of principal is not in doubt, are applied first to earned but unpaid interest and then to principal.

A loan is considered impaired when, based on current information and events, it is probable that the Bank will be unable to collect all amounts due (including both principal and interest) in accordance with the contractual terms of the loan agreement. An impaired loan is measured based on the present value of expected future cash flows discounted at the loan's effective interest rate or, as a practical matter, at the loan's observable market price or the fair value of collateral if the loan is collateral dependent.

Substantially all loan origination fees, commitment fees, direct loan origination costs and purchase premiums and discounts on loans are deferred and recognized as an adjustment of yield, to be amortized to interest income over the contractual term of the loan. The unamortized balance of deferred fees and costs is reported as a component of net loans.

Allowance for Loan Losses

The allowance for loan losses is established through a provision for loan losses which is charged to expense. Additions to the allowance are expected to maintain the adequacy of the total allowance after credit losses (net of recoveries) and loan growth. The allowance for loan losses at December 31, 2008 and 2007 reflects management's estimate of probable losses in the portfolio.

The determination of the allowance is based on estimates made by management, to include consideration of the character of the loan portfolio, specifically identified problem loans, potential losses inherent in the portfolio taken as a whole and economic conditions in the Bank's service area.

Loans determined to be impaired or classified are individually evaluated by management for specific risk of loss. In addition, reserve factors are assigned to currently performing loans based on management's assessment of the following for each identified loan type: (1) inherent credit risk, (2) historical losses, (3) where the Bank has not experienced losses, the loss experience of peer banks and (4) other qualitative factors.

These estimates are particularly susceptible to changes in the economic environment and market conditions.

PAN PACIFIC BANK

NOTES TO FINANCIAL STATEMENTS

(Continued)

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Allowance for Loan Losses (Continued)

The Bank's Board of Directors reviewed the adequacy of the allowance for loan losses at December 31, 2008 and 2007. The Board of Directors reviews the adequacy of the allowance for loan losses at least quarterly. The allowance is adjusted based on that review if, in the judgment of the Board of Directors and management, changes are warranted. In addition, the FDIC and DFI, as an integral part of their examination process, review the allowance for loan losses. These agencies may require additions to the allowance for loan losses based on their judgment about information at the time of their examinations.

Premises and Equipment

Premises, equipment and leasehold improvements are stated at cost, less accumulated depreciation and amortization. Depreciation is computed principally by the straight line method over the estimated useful lives of the assets. Estimated useful lives for furniture and equipment are from three to five years. Leasehold improvements are amortized over the lesser of the terms of the respective leases, or their useful lives, which are generally 5 to 10 years. Remodeling and capital improvements are capitalized while maintenance and repairs are charged directly to occupancy expense.

Income Taxes

Deferred tax assets and liabilities are recognized for the tax consequences of temporary differences between the financial statement and tax basis of existing assets and liabilities. Deferred tax assets and liabilities are adjusted for the effects of changes in tax laws and rates on the date of enactment. A valuation allowance is recognized if, based on the weight of available evidence, management believes it is more likely than not that some portion or all of the deferred tax assets will not be realized.

The Bank accounts for uncertainty in income taxes under Financial Accounting Standards Board (FASB) Interpretation No. 48, *Accounting for Uncertainty in Income Taxes* (FIN 48). Under the provisions of FIN 48, only tax positions that meet the more-likely-than-not recognition threshold are recognized. The application of FIN 48 has not had a material impact on the Bank's financial position, results of operations or cash flows.

Interest expense associated with unrecognized tax benefits is classified as income tax expense in the statement of income. Penalties associated with unrecognized tax benefits are classified as income tax expense in the statement of income.

PAN PACIFIC BANK

NOTES TO FINANCIAL STATEMENTS

(Continued)

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Loss Per Share

Loss per share is computed by dividing net loss by the weighted average number of common shares outstanding for the period. Diluted loss per share reflects the potential dilution that could occur if securities or other contracts to issue common stock, such as stock options, result in the issuance of common stock which shares in the earnings of the Bank. The treasury stock method is applied to determine the dilutive effect of stock options in computing diluted loss per share. However, diluted per share amounts are not presented when a net loss occurs because the conversion of potential common stock is antidilutive.

Comprehensive Income (Loss)

Comprehensive income (loss) is a more inclusive financial reporting methodology that includes disclosure of other comprehensive income or loss that historically has not been recognized in the calculation of net income or loss. Unrealized gains and losses on the Bank's available-for-sale investment securities are included in other comprehensive income or loss, adjusted for realized gains or losses included in net income or loss. Total comprehensive income (loss) and the components of accumulated other comprehensive income (loss) are presented in the statement of changes in shareholders' equity.

Share-Based Compensation

The Bank has one share-based compensation plan, the Pan Pacific Bank Equity Incentive Plan, which was approved by the shareholders of the Bank. The Plan does not provide for the settlement of awards in cash and new shares are issued upon option exercise. The Plan is more fully described in Note 10.

The Bank accounts for share-based compensation using a fair-value based method and requires that share-based compensation expense be recorded for all stock options that are ultimately expected to vest as the requisite service is rendered.

The Bank measures the fair value of the options on the date of grant using a Black-Scholes option pricing model that uses assumptions based on expected option life, expected stock volatility and the risk-free interest rate. Stock volatility is based on historical volatility of similar entities over a preceding period commensurate with the expected term of the option because the Bank's common stock has been publicly traded for a shorter period than the expected term for the options. The risk-free rate is based on the U.S. Treasury yield curve and the expected term of the options. The "simplified" method described in Securities and Exchange Commission Staff Accounting Bulletin No. 110 was used to determine the expected term of the Bank's options in 2007 and 2005.

PAN PACIFIC BANK

NOTES TO FINANCIAL STATEMENTS

(Continued)

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Share-Based Compensation (Continued)

The fair value of each option was estimated on the date of grant using the following weighted-average assumptions.

	<u>2008</u>	<u>2007</u>
Dividend yield	None	None
Expected volatility	28.36%	30.06%
Risk-free interest rate	2.87%	4.90%
Expected option life	6 years	6 years
Fair value of options	\$1.93	\$2.57

Impact of New Financial Accounting Standards

Fair Value Measurements

In September 2006, the FASB issued SFAS No. 157, *Fair Value Measurements*, which defines and establishes a framework for measuring fair value used in FASB pronouncements issued by FASB that require or permit fair value measurement. This statement expands disclosures using fair value to measure assets and liabilities in interim and annual periods subsequent to the period of initial recognition. SFAS No. 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those years. Management adopted this statement on January 1, 2008. The impact of adoption was not material to the Bank's financial condition or results of operations. See Note 13 – Fair Value Measurements.

Determining the Fair Value of a Financial Asset When the Market for That Asset Is Not Active

In October 2008, the FASB issued FASB Staff Position (FSP) Financial Accounting Standard No. 157-3, *Determining the Fair Value of a Financial Asset When the Market for That Asset Is Not Active*. The FSP clarifies the application of FASB Statement No. 157, *Fair Value Measurements* and provides an example to illustrate key considerations in determining the fair value of a financial asset when the market for that financial asset is not active. The FSP is effective immediately, and includes prior period financial statements that have not yet been issued. The Bank is subject to the provisions of the FSP effective immediately; however, the impact of adoption was not material to the Bank's financial condition or results of operations.

PAN PACIFIC BANK

NOTES TO FINANCIAL STATEMENTS

(Continued)

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Impact of New Financial Accounting Standards (Continued)

The Fair Value Option for Financial Assets and Financial Liabilities

In February 2007, the FASB issued Statement of Financial Accounting Standards No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities* (SFAS No. 159), including an amendment of FASB Statement No. 115. SFAS No.159 permits fair value accounting to be irrevocably elected for certain financial assets and liabilities on an individual contract basis at the time of acquisition or at a remeasurement event date. Upon adoption of SFAS No. 159, fair value accounting may also be elected for existing financial assets and liabilities. For those instruments for which fair value accounting is elected, changes in fair value will be recognized in earnings and fees and costs associated with origination or acquisition will be recognized as incurred rather than deferred. The Bank adopted SFAS No. 159 on January 1, 2008, but did not elect the fair value option for any assets or liabilities for the year ended December 31, 2008.

Determining Fair Value When the Volume and Level of Activity for the Asset or Liability Have Significantly Decreased and Identifying Transactions That Are Not Orderly

In April 2009, the FASB issued FSP FAS 157-4, *Determining Fair Value When the Volume and Level of Activity for the Asset or Liability Have Significantly Decreased and Identifying Transactions That Are Not Orderly*, provides additional guidance for estimating fair value in accordance with SFAS No. 157 when the volume and level of activity for the asset or liability have decreased significantly. FSP FAS 157-4 also provides guidance on identifying circumstances that indicate a transaction is not orderly. The provisions of FSP FAS 157-4 were adopted by the Bank on January 1, 2009 and did not have a significant effect on the Bank's financial position or results of operations.

Recognition and Presentation of Other-Than-Temporary Impairments

In April 2009, the FASB issued FSP FAS 115-2 and FAS 124-2, *Recognition and Presentation of Other-Than-Temporary Impairments*, which amends current other-than-temporary impairment guidance in GAAP for debt securities to make the guidance more operational and to improve the presentation and disclosure of other-than-temporary impairments on debt and equity securities in the financial statements. This FSP does not amend existing recognition and measurement guidance related to other-than-temporary impairments of equity securities. The provisions of FSP FAS 115-2 and FAS 124-2 were adopted by the Bank on April 1, 2009 and did not have a significant effect on the Bank's financial position or results of operations.

PAN PACIFIC BANK

NOTES TO FINANCIAL STATEMENTS

(Continued)

2. AVAILABLE-FOR-SALE INVESTMENT SECURITIES

The amortized cost, unrealized losses and estimated fair value of available-for-sale investment securities at December 31, 2008 and 2007 consisted of the following:

	2008			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Debt securities:				
Mortgage-backed securities	\$ 4,906,769	\$ 45,823	\$ (2,462)	\$ 4,950,130

Unrealized gains on available-for-sale investment securities totaling \$43,361 were recorded as accumulated other comprehensive income within shareholders' equity at December 31, 2008. There were no sales or transfers of available-for-sale investment securities for the year ended December 31, 2008.

	2007			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Debt securities:				
U.S. Government agencies	\$ 499,899	\$ 256		\$ 500,155
Mortgage-backed securities	6,164,057	19,800	\$ (38,233)	6,145,624
	<u>\$ 6,663,956</u>	<u>\$ 20,056</u>	<u>\$ (38,233)</u>	<u>\$ 6,645,779</u>

Unrealized losses on available-for-sale investment securities totaling \$18,177 were recorded as accumulated other comprehensive loss within shareholders' equity at December 31, 2007. There were no sales or transfers of available-for-sale investment securities for the year ended December 31, 2007.

The amortized cost and estimated fair value of investment securities at December 31, 2008 by contractual maturity are shown below. Expected maturities may differ from contractual maturities because the issuers of the securities may have the right to call or prepay obligations.

	Amortized Cost	Estimated Fair Value
After one year but within five years	\$ 3,976,876	\$ 3,992,751
After five years but within ten years	929,893	957,379
Total debt securities	<u>\$ 4,906,769</u>	<u>\$ 4,950,130</u>

Investment securities were pledged to secure short-term borrowing arrangements at December 31, 2008. See Note 6.

PAN PACIFIC BANK

NOTES TO FINANCIAL STATEMENTS

(Continued)

2. AVAILABLE-FOR-SALE INVESTMENT SECURITIES (Continued)

The following tables show the gross unrealized losses and estimated fair values, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position, at December 31, 2008 and 2007:

	December 31, 2008					
	Less than 12 Months		12 Months or More		Total	
	Estimated Fair Value	Unrealized Losses	Estimated Fair Value	Unrealized Losses	Estimated Fair Value	Unrealized Losses
Debt securities:						
Mortgage-backed securities	\$ -	\$ -	\$ 1,960,286	\$ (2,462)	\$ 1,960,286	\$ (2,462)

	December 31, 2007					
	Less than 12 Months		12 Months or More		Total	
	Estimated Fair Value	Unrealized Losses	Estimated Fair Value	Unrealized Losses	Estimated Fair Value	Unrealized Losses
Debt securities:						
Mortgage-backed securities	\$ -	\$ -	\$ 3,326,352	\$ (38,233)	\$ 3,326,352	\$ (38,233)

Mortgage-backed Securities

At December 31, 2008, the Bank held ten mortgage-backed securities of which three were in a loss position for twelve months or more. The unrealized losses on the Bank's investments in mortgage obligations were caused by interest rate fluctuations. Because the decline in market value is attributable to changes in interest rates and not credit quality, and because the Bank has the ability and intent to hold those investments until a recovery of fair value, which may be maturity, the Bank does not consider those investments to be other-than-temporarily impaired at December 31, 2008.

3. LOANS

Outstanding loans are summarized below:

	December 31,	
	2008	2007
Real estate	\$ 42,644,912	\$ 29,696,169
Commercial	33,741,247	28,490,339
Consumer	139,992	
	76,526,151	58,186,508
Deferred loan origination fees, net	(192,443)	(171,891)
Allowance for loan losses	(1,048,000)	(607,700)
	\$ 75,285,708	\$ 57,406,917

PAN PACIFIC BANK

NOTES TO FINANCIAL STATEMENTS

(Continued)

3. LOANS (Continued)

There were no nonaccrual loans at December 31, 2008 or 2007. There were no accruing loans past due 90 days or more at December 31, 2008 or 2007.

At December 31, 2008, the recorded investment in impaired loans was \$1,732,215. there were no loans considered to be impaired at December 31, 2007. The Bank had \$213,325 of specific allowance for loan losses on impaired loans of \$1,066,623 at December 31, 2008. The average outstanding balance of impaired loans for the year ended December 31, 2008 was \$373,484, on which \$0 was recognized as interest income on a cash basis.

Provision charged to operations totaled \$440,300 and \$269,700 for the years ended December 31, 2008 and 2007, respectively, with no losses charged to the allowance.

Salaries and employee benefits totaling \$114,500 and \$104,048 have been deferred as loan origination costs during the years ended December 31, 2008 and 2007, respectively.

4. BANK PREMISES AND EQUIPMENT

Bank premises and equipment consisted of the following:

	<u>December 31,</u>	
	<u>2008</u>	<u>2007</u>
Leasehold improvements	\$ 408,359	\$ 407,110
Furniture, fixtures and equipment	<u>490,700</u>	<u>445,357</u>
	899,059	852,467
Less accumulated depreciation and amortization	<u>(465,055)</u>	<u>(325,713)</u>
	<u>\$ 434,004</u>	<u>\$ 526,754</u>

Depreciation and amortization on premises and equipment included in occupancy and equipment expense totaled \$139,342 and \$142,662 for the years ended December 31, 2008 and 2007, respectively.

PAN PACIFIC BANK

NOTES TO FINANCIAL STATEMENTS

(Continued)

5. INTEREST-BEARING DEPOSITS

Interest-bearing deposits consisted of the following:

	December 31,	
	2008	2007
Savings	\$ 118,332	\$ 33,477
Money market	25,377,059	37,637,077
Interest-bearing transactions	1,594,589	1,766,460
Time, \$100,000 or more	16,740,792	5,529,349
Other time	1,474,520	3,932,925
	<u>\$ 45,305,292</u>	<u>\$ 48,899,288</u>

The Bank has \$8,000,000 of brokered certificates of deposit that will mature in the year ending December 31, 2009.

Aggregate annual maturities of time deposits are as follows:

Year Ending December 31,	
2009	\$ 17,521,312
2010	200,000
2011	494,000
	<u>\$ 18,215,312</u>

Interest expense recognized on interest-bearing deposits for the years ended December 31, 2008 and 2007 consisted of the following:

	2008	2007
Savings	\$ 352	\$ 195
Money market	590,995	1,331,550
Interest-bearing transactions	7,629	8,059
Time, \$100,000 or more	337,617	436,099
Other time	68,168	362,084
Total interest expense	<u>\$ 1,004,761</u>	<u>\$ 2,137,987</u>

6. SHORT-TERM BORROWING ARRANGEMENTS

The Bank has an unsecured Federal funds line of credit with The Independent Bankers Bank under which it can borrow up to \$3,000,000. There were no borrowings outstanding under this arrangement at December 31, 2008.

PAN PACIFIC BANK

NOTES TO FINANCIAL STATEMENTS

(Continued)

6. SHORT-TERM BORROWING ARRANGEMENTS (Continued)

In addition, the Bank has an unsecured Federal funds line of credit with the Pacific Coast Bankers Bank under which it may borrow amounts not to exceed \$2,000,000. There were \$300,000 of borrowings outstanding under this arrangement at December 31, 2008.

The Bank has an arrangement with the Federal Home Loan Bank of San Francisco (FHLB) under which it may borrow amounts not to exceed 20% of the Bank's total assets. At December 31, 2008, the Bank's total borrowing capacity under this arrangement was \$15,658,000. There were \$15,652,000 of borrowings outstanding under this arrangement at December 31, 2008, which matured on January 2, 2009. The Bank is required to pledge loans and investment securities to secure any advances from this arrangement. There were \$24,422,592 in loans and \$4,950,130 in securities pledged at December 31, 2008.

7. INCOME TAXES

The provision for Federal and State income taxes is as follows for the years ended December 31, 2008 and 2007:

	Federal	State	Total
<u>2008</u>			
Current			
Deferred	\$ (45,000)	\$ (16,000)	\$ (61,000)
Change in valuation allowance	45,000	16,000	61,000
Income tax benefit	\$ -	\$ -	\$ -
<u>2007</u>			
Current			
Deferred	\$ (330,000)	\$ (117,000)	\$ (447,000)
Change in valuation allowance	330,000	117,000	447,000
Income tax benefit	\$ -	\$ -	\$ -

The primary differences between the federal statutory tax rate and the tax expense recorded in the financial statements includes the impositions of state taxes and the establishment of a valuation allowance against the net deferred tax assets.

PAN PACIFIC BANK

NOTES TO FINANCIAL STATEMENTS

(Continued)

7. INCOME TAXES (Continued)

Deferred income taxes reflect temporary differences between the tax basis of assets and liabilities and the reported amounts of assets and liabilities for financial statement reporting purposes. The Bank's total net deferred tax assets and corresponding valuation allowance at December 31, 2008 and 2007 consist of the following:

	2008	2007
Deferred tax assets:		
Net operating losses and other credits	\$ 802,000	\$ 899,000
Organization costs	238,000	259,000
Allowance for loan losses	333,000	183,000
Share-based compensation	64,000	34,000
Securities accretion	56,000	48,000
Other	12,000	17,000
State deferred tax assets	<u>308,000</u>	<u>298,000</u>
Deferred tax assets before valuation allowance	1,813,000	1,738,000
Valuation allowance	<u>(1,774,000)</u>	<u>(1,713,000)</u>
Total deferred tax assets	<u>39,000</u>	<u>25,000</u>
Deferred tax liabilities:		
Deferred loan costs	(34,000)	(25,000)
FHLB stock	<u>(5,000)</u>	<u></u>
Total deferred tax liabilities	<u>(39,000)</u>	<u>(25,000)</u>
Net deferred tax assets	<u>\$ -</u>	<u>\$ -</u>

The amounts above include a valuation allowance which is provided to reduce deferred tax assets to a level which, more likely than not, will be realized. Due to the losses recognized during the organizational period and since operations commenced, management has determined a valuation allowance is required and has been recorded for the Bank's net deferred tax asset. The need for this valuation allowance will be periodically reviewed and benefits will be recognized when they are determined to be realizable.

At December 31, 2008, the Bank had Federal and State net operating loss carryforwards (NOLs) of approximately \$2,357,000 and \$2,298,000, respectively. The Federal NOLs begin to expire in 2025 and the State NOLs begin to expire in 2015.

The Bank is subject to U.S. Federal income tax and California state franchise tax. Federal and California tax returns for 2007, 2006 and 2005 are currently open for examination.

The Bank does not have any unrecognized tax benefits related to uncertain tax positions at December 31, 2008.

PAN PACIFIC BANK

NOTES TO FINANCIAL STATEMENTS

(Continued)

8. COMMITMENTS AND CONTINGENCIES

Commitments to Extend Credit

The Bank is a party to financial instruments with off-balance-sheet risk in the normal course of business in order to meet the financing needs of its customers and to reduce its own exposure to fluctuations in interest rates. These financial instruments consist of commitments to extend credit and standby letters of credit. These instruments involve, to varying degrees, elements of credit and interest rate risk in excess of the amount recognized on the balance sheet.

The Bank's exposure to credit loss in the event of nonperformance by the other party for commitments to extend credit and standby letters of credit is represented by the contractual amount of those instruments. The Bank uses the same credit policies in making commitments and standby letters of credit as it does for loans included on the balance sheet.

The following financial instruments represent off-balance-sheet credit risk:

	<u>December 31,</u>	
	<u>2008</u>	<u>2007</u>
Commitments to extend credit	\$ 9,859,518	\$ 12,536,000

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since some of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The Bank evaluates each customer's creditworthiness on a case-by-case basis. The amount of collateral obtained, if deemed necessary by the Bank upon extension of credit, is based on management's credit evaluation of the borrower. Collateral held varies, but may include accounts receivable, inventory, and deeds of trust on residential real estate and income-producing commercial properties.

Standby letters of credit are conditional commitments issued by the Bank to guarantee the performance or financial obligation of a customer to a third party. The credit risk involved in issuing standby letters of credit is essentially the same as that involved in extending loans to customers. The fair value of the liability related to these standby letters of credit, which represents the fees received for issuing the guarantees, was not significant at December 31, 2008 and 2007. The Bank recognizes these fees as revenue over the term of the commitment or when the commitment is used.

At December 31, 2008, real estate loan commitments represent approximately 23% of total commitments and are generally secured by property with a loan-to-value ratio not to exceed 75%. Commercial lines of credit and other commitments represent the remaining 77% of total commitments. In addition, the majority of the Bank's loan commitments have variable interest rates.

PAN PACIFIC BANK

NOTES TO FINANCIAL STATEMENTS

(Continued)

8. COMMITMENTS AND CONTINGENCIES (Continued)

Concentrations of Credit Risk

The Bank grants real estate, commercial and consumer loans to customers in Fremont, Alameda and Santa Clara Counties. In management's judgment, a concentration exists in real estate related loans which represented approximately 56% and 51% of the Bank's loan portfolio at December 31, 2008 and 2007, respectively. Although management believes such concentrations to have no more than the normal risk of collectibility, a substantial decline in the economy in general, or a decline in real estate values in the Bank's primary market area in particular, could have an adverse impact on collectibility of these loans. Personal and business income represent the primary source of repayment for a majority of these loans.

Operating Lease

The Bank leases its branch and headquarters under a non-cancelable operating lease.

Future minimum lease payments are as follows:

<u>Year Ending</u> <u>December 31,</u>	
2009	\$ 103,038
2010	119,128
2011	125,608
2012	132,581
2013	134,200
Thereafter	<u>162,670</u>
	<u>\$ 777,225</u>

Rental expense included in occupancy and equipment expense totaled \$136,233 and \$201,530 for the years ended December 31, 2008 and 2007, respectively.

Contingencies

The Bank may be subject to legal proceedings and claims which arise in the ordinary course of business. In the opinion of management, the amount of ultimate liability with respect to such actions will not materially affect the financial position or results of operations of the Bank.

PAN PACIFIC BANK

NOTES TO FINANCIAL STATEMENTS

(Continued)

8. COMMITMENTS AND CONTINGENCIES (Continued)

Correspondent Banking Agreements

The Bank maintains funds on deposit with other federally insured financial institutions under correspondent banking agreements. Those insured financial institutions have elected to participate in the FDIC sponsored Transaction Account Guarantee Program. Under that program, through December 31, 2009, all noninterest-bearing transaction accounts are fully guaranteed by the FDIC for the entire amount in the account. Coverage under the Transaction Account Guarantee Program is in addition to and separate from the coverage available under the FDIC's general deposit insurance rules. Deposits at the FHLB are not insured by the FDIC and totaled \$15,280 at December 31, 2008. This program was not in effect in 2007.

9. REGULATORY MATTERS

Dividend Restrictions

Upon declaration by the Board of Directors, all shareholders of record will be entitled to receive dividends. The California Financial Code restricts the total dividend payment of any state banking association in any calendar year to the lesser of (1) the bank's retained earnings or (2) the bank's net income for its last three fiscal years, less distributions made to shareholders during the same three-year period. At December 31, 2008, no amounts were free of such restrictions.

Regulatory Agreement

In connection with certain regulatory matters which arose as a result of a joint regulatory examination of the Bank by the FDIC and DFI, the Bank entered into a Stipulation and Consent to the Issuance of an Order to Cease and Desist dated October 17, 2007 (Stipulation) and a related Order to Cease and Desist dated October 18, 2007 (Order), each issued jointly by the FDIC and DFI. The Order required affirmative action by the Bank to correct cited regulatory deficiencies and noncompliance within specified time frames. The Bank complied with all terms and requirements of the Stipulation and the Order and both were terminated on September 30, 2008.

Regulatory Capital

The Bank is subject to certain regulatory capital requirements administered by the FDIC. Failure to meet these minimum capital requirements can initiate certain mandatory, and possibly additional discretionary, actions by regulators that, if undertaken, could have a direct material effect on the Bank's financial statements.

Under capital adequacy guidelines, the Bank must meet specific capital guidelines that involve quantitative measures of their assets, liabilities and certain off-balance-sheet items as calculated under regulatory accounting practices. These quantitative measures are established by regulation and require that minimum amounts and ratios of total and Tier 1 capital to risk-weighted assets and of Tier 1 capital to average assets be maintained. Capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings and other factors.

PAN PACIFIC BANK

NOTES TO FINANCIAL STATEMENTS

(Continued)

9. REGULATORY MATTERS (Continued)

Regulatory Capital (Continued)

The Bank is also subject to additional capital guidelines under the regulatory framework for prompt corrective action. To be categorized as well capitalized, the Bank must maintain minimum total risk-based, Tier 1 risk-based and Tier 1 leverage ratios as set forth in the table below. The most recent notification from the FDIC categorized the Bank as well capitalized under these guidelines. There are no conditions or events since that notification that management believes have changed the Bank's category.

To be categorized as well capitalized, the Bank must maintain minimum total risk-based, Tier 1 risk-based and Tier 1 leverage ratios as set forth below.

	2008		2007	
	Amount	Ratio	Amount	Ratio
<u>Leverage Ratio</u>				
Pan Pacific Bank	\$ 11,581,000	14.5%	\$ 11,652,000	16.0%
Minimum requirement for "Well-Capitalized" institution	\$ 3,992,000	5.0%	\$ 3,634,000	5.0%
Minimum regulatory requirement	\$ 3,193,000	4.0%	\$ 2,907,000	4.0%
<u>Tier 1 Risk-Based Capital Ratio</u>				
Pan Pacific Bank	\$ 11,581,000	13.9%	\$ 11,652,000	19.2%
Minimum requirement for "Well-Capitalized" institution	\$ 4,989,000	6.0%	\$ 3,647,000	6.0%
Minimum regulatory requirement	\$ 3,326,000	4.0%	\$ 2,431,000	4.0%
<u>Total Risk-Based Capital Ratio</u>				
Pan Pacific Bank	\$ 12,629,000	15.2%	\$ 12,260,000	20.2%
Minimum requirement for "Well-Capitalized" institution	\$ 8,315,000	10.0%	\$ 6,078,000	10.0%
Minimum regulatory requirement	\$ 6,652,000	8.0%	\$ 4,862,000	8.0%

PAN PACIFIC BANK

NOTES TO FINANCIAL STATEMENTS

(Continued)

10. SHARE-BASED COMPENSATION

During 2005, the shareholders approved the Bank's Amended and Restated 2005 Equity Incentive Plan (the "Plan"). The Plan is intended to attract and retain the best available personnel for positions of substantial responsibility, encourage ownership of stock by employees and directors of the Bank and any of its affiliates, to provide additional incentive for them to promote the success of the Bank's business, and to reward organizers of the Bank for placing personal funds at risk by contributing to the pre-opening funds utilized to organize the Bank. The Plan issues incentive stock option awards within the meaning of Section 422 of the Code, but not all awards are required to be incentive options. At December 31, 2008, 475,350 options to purchase shares of the Bank's common stock are authorized under this Plan. The Plan requires that the option price may not be less than the fair market value of the stock at the date the option is granted, and that the stock must be paid in full at the time the option is exercised. The options expire on a date determined by the Board of Directors, but not later than ten years from the date of grant. The vesting period is determined by the Board of Directors and is generally over three years.

A summary of the activity of the Plan for the years ended December 31, 2008 and 2007 follows:

	<u>Number of Stock Options Outstanding</u>	<u>Weighted Average Exercise Price</u>	<u>Weighted Average Remaining Contractual Term (Years)</u>
Options outstanding at January 31, 2007	333,750	\$ 10.00	
Options granted	65,500	\$ 6.50	
Options forfeited	<u>(68,500)</u>	<u>\$ 10.00</u>	
Options outstanding at December 31, 2007	330,750	\$ 9.31	
Options granted	62,000	\$ 5.68	
Options forfeited	<u>(62,250)</u>	<u>\$ 10.00</u>	
Options outstanding at December 31, 2008	<u>330,500</u>	<u>\$ 8.50</u>	<u>7.4 years</u>
Options vested or expected to vest at December 31, 2008	<u>283,000</u>	<u>\$ 8.24</u>	<u>7.6 years</u>
Options exercisable at December 31, 2008	<u>248,021</u>	<u>\$ 9.35</u>	<u>6.9 years</u>

There were no options exercised in 2008 or 2007.

As of December 31, 2008, there was \$157,384 of total unrecognized compensation cost related to non-vested share-based compensation arrangements. The cost is expected to be recognized over a weighted average period of 2.0 years. Total compensation expense for share-based awards was \$171,000 and \$214,216 in 2008 and 2007, respectively.

PAN PACIFIC BANK

NOTES TO FINANCIAL STATEMENTS

(Continued)

11. OTHER OPERATING EXPENSES

Other expenses for the years ended December 31, 2008 and 2007 consisted of the following:

	<u>2008</u>	<u>2007</u>
Legal and professional fees	\$ 248,303	\$ 406,606
Technology	328,641	289,172
Communication	24,900	26,792
Stationery and supplies	24,453	37,487
Marketing	14,240	74,055
Loan expenses	12,902	34,852
Other	<u>381,214</u>	<u>271,970</u>
	<u>\$ 1,034,653</u>	<u>\$ 1,140,934</u>

12. BENEFIT PLAN

401(k) Plan

The Bank sponsors a "safe harbor 401(k) plan" for substantially all full-time employees of the Bank with three or more months of service. Bank employees are permitted, within limitations imposed by tax law, to make pretax contributions to the plan. The Bank makes a matching contribution equal to 100% of each employee's salary deferrals that do not exceed 3% of compensation plus 50% of salary deferrals between 3% and 5% of compensation. For these purposes, compensation is measured annually. This matching contribution is fully vested and is referred to as a Basic Matching Contribution. The Bank contributed \$41,309 and \$40,698 to the plan during the years ended December 31, 2008 and 2007, respectively.

PAN PACIFIC BANK

NOTES TO FINANCIAL STATEMENTS

(Continued)

13. FAIR VALUE MEASUREMENTS

Fair Value of Financial Instruments

The carrying amounts and estimated fair values of the Bank's financial instruments are as follows:

	December 31, 2008		December 31, 2007	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Financial assets:				
Cash and cash equivalents	\$ 1,238,878	\$ 1,238,878	\$ 4,653,405	\$ 4,653,405
Available-for-sale investment securities	4,950,130	4,950,130	6,645,779	6,645,779
Loans, net	75,285,708	75,046,000	57,406,917	56,455,482
FHLB stock	735,800	735,800	243,500	243,500
Pacific Coast Bankers' Bancshares stock	190,000	190,000	190,000	190,000
Accrued interest receivable	226,460	226,460	284,271	284,271
Financial liabilities:				
Deposits	\$ 55,304,980	\$ 55,495,000	\$ 58,054,216	\$ 57,914,431
Short-term borrowings	15,952,000	15,963,000		
Accrued interest payable	51,540	51,540	187,906	187,906

These estimates do not reflect any premium or discount that could result from offering the Bank's entire holdings of a particular financial instrument for sale at one time, nor do they attempt to estimate the value of anticipated future business related to the instruments. In addition, the tax ramifications related to the realization of unrealized gains and losses can have a significant effect on fair value estimates and have not been considered in any of these estimates.

The following methods and assumptions were used to estimate the fair value of financial instruments. For cash and cash equivalents, variable-rate loans and leases, accrued interest receivable and payable, FHLB and Pacific Coast Bankers' Bancshares stock, demand deposits and short-term borrowings, the carrying amount is estimated to be fair value. For available-for-sale investment securities, fair values are based on quoted market prices, quoted market prices for similar securities and indications of value provided by brokers. The fair values for fixed-rate loans and leases are estimated using discounted cash flow analyses, using interest rates currently being offered at each reporting date for loans with similar terms to borrowers of comparable creditworthiness. Fair values for fixed-rate certificates of deposit are estimated using discounted cash flow analyses using interest rates offered at each reporting date by the Bank for certificates with similar remaining maturities. The fair values of commitments to extend credit and standby letters of credit are estimated using the fees currently charged to enter into similar agreements and are not significant and, therefore, not included in the above table.

PAN PACIFIC BANK

NOTES TO FINANCIAL STATEMENTS

(Continued)

13. FAIR VALUE MEASUREMENTS (Continued)

Fair Value Measurements Under SFAS 157

On January 1, 2008, the Bank adopted FASB Statement of Financial Accounting Standard No. 157 (SFAS No. 157), *Fair Value Measurements*. SFAS No. 157 defines fair value, establishes a framework for measuring fair value under generally accepted accounting principles, and expands disclosures about fair value measurement. Upon adoption of SFAS No. 157, there was no cumulative effect adjustment to beginning retained earnings and no impact on the consolidated financial statements.

Fair Value Hierarchy

In accordance with SFAS No. 157, the Bank groups its assets and liabilities measured at fair value within three levels, based on the markets in which the assets and liabilities are traded and the reliability of the assumptions used to determine fair value. Valuations within these levels are based upon:

Level 1 – Quoted market prices for identical instruments traded in active exchange markets.

Level 2 – Quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-based valuation techniques for which all significant assumptions are observable or can be corroborated by observable market data.

Level 3 – Model-based techniques that use at least one significant assumption not observable in the market. These unobservable assumptions reflect the Bank's estimates of assumptions that market participants would use on pricing the asset or liability. Valuation techniques include management judgment and estimation which may be significant.

Assets Recorded at Fair Value

The following tables present information about the Bank's assets and liabilities measured at fair value on a recurring and nonrecurring basis as of December 31, 2008:

Recurring Basis

The Bank is required or permitted to record the following assets at fair value on a recurring basis under other accounting pronouncements.

<u>Description</u>	<u>Fair Value</u>	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>
Available-for-sale investment securities	<u>\$ 4,950,130</u>	<u>\$ -</u>	<u>\$ 4,950,130</u>	<u>\$ -</u>

Fair values for available-for-sale investment securities, which include government-guaranteed mortgage-backed securities, are based on quoted market prices for similar securities.

PAN PACIFIC BANK

NOTES TO FINANCIAL STATEMENTS

(Continued)

13. FAIR VALUE MEASUREMENTS (Continued)

Fair Value Measurements Under SFAS 157 (Continued)

Assets Recorded at Fair Value (Continued)

Non-recurring Basis

The Bank may be required, from time to time, to measure certain assets at fair value on a non-recurring basis. These include assets that are measured at the lower of cost or market value that were recognized at fair value which was below cost at the reporting date.

<u>Description</u>	<u>Fair Value</u>	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>
Impaired loans	<u>\$ 1,518,890</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 1,518,890</u>

The fair value of impaired loans is based on the fair value of the collateral for all collateral dependent loans and for other impaired loans is estimated using a discounted cash flow model. Impaired loans which were determined to be not collateral dependent and were categorized as Level 3 due to their valuation using a discounted cash flow projection, which in turn required the use of unobservable inputs and assumptions in fair value measurements.