UNITED SECURITY BANCSHARES
Form 10-Q
May 10, 2010

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 FOR THE QUARTERLY PERIOD ENDED MARCH 31, 2010.

¨ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 FOR THE TRANSITION PERIOD FROM TO .

Commission file number: 000-32987

UNITED SECURITY BANCSHARES
(Exact name of registrant as specified in its charter)

CALIFORNIA (State or other jurisdiction of incorporation or organization)	91-2112732 (I.R.S. Employer Identification No.)
2126 Inyo Street, Fresno, California (Address of principal executive offices)	93721 (Zip Code)

Registrants telephone number, including area code (559) 248-4943

Indicate by check mark whether 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 whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing 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 (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes o No x

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Act).
Large accelerated filer o Accelerated filer o Non-accelerated filer x Small reporting company o

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

Aggregate market value of the Common Stock held by non-affiliates as of the last business day of the registrant's most recently completed second fiscal quarter - June 30, 2009: $43,114,654

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Common Stock, no par value
(Title of Class)

Shares outstanding as of April 30, 2010: 12,621,452

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PART I. Financial Information

United Security Bancshares and Subsidiaries
Consolidated Balance Sheets – (unaudited)
March 31, 2010 and December 31, 2009

(in thousands except shares)	March 31, 2010	December 31, 2009
Assets		
Cash and due from banks	$ 16,607	$ 17,644
Federal funds sold	21,160	11,585
Cash and cash equivalents	37,767	29,229
Interest-bearing deposits in other banks	3,970	3,313
Investment securities available for sale (at fair value)	68,855	71,411
Loans and leases	521,087	508,573
Unearned fees	(1,047)	(865)
Allowance for credit losses	(16,204)	(15,016)
Net loans	503,836	492,692
Accrued interest receivable	2,430	2,497
Premises and equipment – net	13,121	13,296
Other real estate owned	38,130	36,217
Intangible assets	1,775	2,034
Goodwill	7,391	7,391
Cash surrender value of life insurance	15,099	14,972
Investment in limited partnership	2,168	2,274
Deferred income taxes - net	7,665	7,534
Other assets	9,422	9,708
Total assets	$ 711,629	$ 692,568
Liabilities & Shareholders' Equity		
Liabilities		
Deposits		
Noninterest bearing	$ 134,140	$ 139,724
Interest bearing	448,342	421,936
Total deposits	582,482	561,660
Other borrowings	37,000	40,000
Accrued interest payable	280	376
Accounts payable and other liabilities	4,416	3,995
Junior subordinated debentures (at fair value)	10,616	10,716
Total liabilities	634,794	616,747
Shareholders' Equity		
Common stock, no par value 20,000,000 shares authorized, 12,621,452 and 12,496,499 issued and outstanding, in 2010 and 2009, respectively	38,235	37,575
Retained earnings	40,286	40,499
Accumulated other comprehensive loss	(1,686)	(2,253)
Total shareholders' equity	76,835	75,821
Total liabilities and shareholders' equity	$ 711,629	$ 692,568

See notes to consolidated financial statements

United Security Bancshares and Subsidiaries
Consolidated Statements of Operations and Comprehensive Income

(In thousands except shares and EPS)	Quarters Ended March 31, 2010	2009
Interest Income:		
Loans, including fees	$ 7,540	$ 8,067
Investment securities – AFS – taxable	853	1,190
Investment securities – AFS – nontaxable	15	15
Federal funds sold	8	0
Interest on deposits in other banks	10	40
Total interest income	8,426	9,312
Interest Expense:		
Interest on deposits	1,158	1,705
Interest on other borrowings	107	459
Total interest expense	1,265	2,164
Net Interest Income Before		
Provision for Credit Losses	7,161	7,148
Provision for Credit Losses	1,631	1,351
Net Interest Income	5,530	5,797
Noninterest Income:		
Customer service fees	948	989
Loss on sale of other real estate owned	(56)	(77)
Gain (loss) on fair value of financial liability	157	(59)
Shared appreciation income	0	9
Other	264	279
Total noninterest income	1,313	1,141
Noninterest Expense:		
Salaries and employee benefits	2,281	2,223
Occupancy expense	913	942
Data processing	19	42
Professional fees	387	400
FDIC/DFI insurance assessments	391	146
Director fees	57	66
Amortization of intangibles	203	228
Correspondent bank service charges	76	107
Impairment loss on core deposit intangible	57	57
Impairment loss on investment securities (cumulative total other-than-temporary loss of $3.9 million, net of $3.5 million recognized in other comprehensive loss, pre-tax)	244	163
Impairment loss on OREO	821	166
Loss on California tax credit partnership	106	107
OREO expense	282	305
Other	488	717
Total noninterest expense	6,325	5,669
Income Before Taxes on Income	518	1,269
Provision for Taxes on Income	76	348
Net Income	$ 442	$ 921
Other comprehensive income, net of tax:		
	567	(733)

Unrealized gain (loss) on available for sale securities, and past service costs of employee benefit plans - net income tax expense (benefit) of $378 and $(488)				
Comprehensive Income	$	1,009	$	188
Net Income per common share				
Basic	$	0.04	$	0.07
Diluted	$	0.04	$	0.07
Shares on which net income per common shares were based				
Basic		12,621,452		12,622,238
Diluted		12,621,452		12,622,238

See notes to consolidated financial statements

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United Security Bancshares and Subsidiaries
Consolidated Statements of Changes in Shareholders' Equity
Periods Ended March 31, 2010 (unaudited)

(In thousands except shares)	Common stock Number of Shares	Common stock Amount	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total
Balance January 1, 2009	12,010,372	$ 34,811	$ 47,722	$ (2,923)	$ 79,610
Net changes in unrealized loss on available for sale securities (net of income tax benefit of $489)				(733)	(733)
Dividends on common stock (cash-in-lieu)			(4)		(4)
Repurchase and cancellation of common shares	(488)	(4)			(4)
Common stock dividends	119,622	919	(919)		0
Other		37			37
Stock-based compensation expense		13			13
Net Income			921		921
Balance March 31, 2009	12,219,506	35,776	47,720	(3,656)	79,840
Net changes in unrealized loss on available for sale securities (net of income tax expense of $1,045)				1,568	1,568
Net changes in unrecognized past service Cost on employee benefit plans (net of income tax benefit of $116)				(165)	(165)
Dividends on common stock (cash-in-lieu)			(2)		(2)
Common stock dividends	366,993	1,761	(1,761)		0
Other		(2)			(2)
Stock-based compensation expense		40			40
Net Income			(5,458)		(5,458)
Balance December 31, 2009	12,496,499	37,575	40,499	(2,253)	75,821
Net changes in unrealized loss on available for sale securities (net of income tax expense of $378)				567	567
Common stock dividends	124,953	655	(655)		0
Stock-based compensation expense		5			5
Net Income			442		442
Balance March 31, 2010	12,621,452	$ 38,235	$ 40,286	$ (1,686)	$ 76,835

See notes to consolidated financial statements

United Security Bancshares and Subsidiaries
Consolidated Statements of Cash Flows (unaudited)

(In thousands)	Three Months Ended March 31, 2010	2009
Cash Flows From Operating Activities:		
Net (loss) income	$ 442	$ 921
Adjustments to reconcile net income:		
to cash provided by operating activities:		
Provision for credit losses	1,631	1,351
Depreciation and amortization	539	640
Accretion of investment securities	(10)	(20)
Decrease (increase) in accrued interest receivable	67	(363)
Decrease in accrued interest payable	(96)	(168)
Increase (decrease) in unearned fees	182	(179)
Increase in income taxes payable	8	894
Stock-based compensation expense	5	13
Decrease in accounts payable and accrued liabilities	(58)	(476)
Loss on sale of other real estate owned	56	77
Impairment loss on other real estate owned	821	166
Impairment loss on core deposit intangible	57	57
Impairment loss on investment securities	244	163
Increase in surrender value of life insurance	(126)	(136)
(Gain) loss on fair value option of financial liabilities	(157)	59
Loss on tax credit limited partnership interest	106	107
Net decrease in other assets	513	337
Net cash provided by operating activities	4,224	3,443
Cash Flows From Investing Activities:		
Net (increase) decrease in interest-bearing deposits with banks	(657)	16,464
Purchases of available-for-sale securities	(1,001)	0
Maturities and calls of available-for-sale securities	4,269	3,784
Proceeds from sale of investment in title company	0	99
Net increase in loans	(18,196)	(1,883)
Net proceeds from settlement of other real estate owned	2,143	1,515
Capital expenditures for premises and equipment	(141)	(59)
Net cash (used in) provided by investing activities	(13,583)	19,920
Cash Flows From Financing Activities:		
Net increase in demand deposit and savings accounts	4,781	1,561
Net increase in certificates of deposit	16,041	12,092
Net decrease in federal funds purchased	0	(17,360)
Net decrease in FHLB term borrowings	(3,000)	(24,500)
Proceeds from note payable	75	0
Repurchase and retirement of common stock	0	33
Payment of dividends on common stock	0	(5)
Net cash provided (used in) by financing activities	17,897	(28,179)
Net increase (decrease) in cash and cash equivalents	8,538	(4,816)

Cash and cash equivalents at beginning of period		29,229		19,426
Cash and cash equivalents at end of period	$	37,767	$	14,610

See notes to consolidated financial statements

United Security Bancshares and Subsidiaries - Notes to Consolidated Financial Statements - (Unaudited)

1. Organization and Summary of Significant Accounting and Reporting Policies

The consolidated financial statements include the accounts of United Security Bancshares, and its wholly owned subsidiary United Security Bank (the “Bank”) and two bank subsidiaries, USB Investment Trust (the “REIT”) and United Security Emerging Capital Fund, (collectively the “Company” or “USB”). Intercompany accounts and transactions have been eliminated in consolidation

These unaudited financial statements have been prepared in accordance with generally accepted accounting principles for interim financial information on a basis consistent with the accounting policies reflected in the audited financial statements of the Company included in its 2009 Annual Report on Form 10-K. These interim financial statements do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments (consisting of a normal recurring, nature) considered necessary for a fair presentation have been included. Operating results for the interim periods presented are not necessarily indicative of the results that may be expected for any other interim period or for the year as a whole.

Certain reclassifications have been made to the 2009 financial statements to conform to the classifications used in 2010.

New Accounting Standards:

In June 2009, the FASB revised ACS Topic 860 “Transfers and Servicing” to amend existing guidance by eliminating the concept of a qualifying special-purpose entity (QSPE), creating more stringent conditions for reporting a transfer of a portion of a financial asset as a sale, clarifying other sale-accounting criteria and changing the initial measurement of a transferor’s interest in transferred financial assets. The new guidance is effective as of the beginning of a company’s first fiscal year that begins after November 15, 2009 and for subsequent interim and annual periods. The adoption of this standard as of January 1, 2010 did not have a material impact on the Company’s consolidated financial condition or results of operations.

In January 2010, the FASB issued ASU No. 2010-06, Fair Value Measurements and Disclosures (Topic 820)—Improving Disclosures about Fair Value Measurements. FASB ASU No. 2010-06 requires (i) fair value disclosures by each class of assets and liabilities (generally a subset within a line item as presented in the statement of financial position) rather than major category, (ii) for items measured at fair value on a recurring basis, the amounts of significant transfers between Levels 1 and 2, and transfers into and out of Level 3, and the reasons for those transfers, including separate discussion related to the transfers into each level apart from transfers out of each level, and (iii) gross presentation of the amounts of purchases, sales, issuances, and settlements in the Level 3 recurring measurement reconciliation. Additionally, the ASU clarifies that a description of the valuation techniques(s) and inputs used to measure fair values is required for both recurring and nonrecurring fair value measurements. Also, if a valuation technique has changed, entities should disclose that change and the reason for the change. Disclosures other than the gross presentation changes in the Level 3 reconciliation are effective for the first reporting period beginning after December 15, 2009. The requirement to present the Level 3 activity of purchases, sales, issuances, and settlements on a gross basis will be effective for fiscal years beginning after December 15, 2010. This update became effective for the Company in the quarter ended March 31, 2010, except that the disclosure on the roll forward activities for Level 3 fair value measurements will become effective with the reporting period beginning January 1, 2011. Other than requiring additional disclosures, adoption of this new guidance did not have a material impact on the Company’s financial statements.

2. Investment Securities Available for Sale

Following is a comparison of the amortized cost and fair value of securities available-for-sale, as of March 31, 2010 and December 31, 2009:

(In thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value (Carrying Amount)
March 31, 2010:				
U.S. Government agencies	$ 34,525	$ 1,500	$ (12)	$ 36,013
U.S. Government agency CMO's	12,724	397	(12)	13,109
Residential mortgage obligations	13,567	0	(3,674)	9,893
Obligations of state and political subdivisions	1,252	37	0	1,289
Other investment securities	9,033	0	(482)	8,551
	$ 71,101	$ 1,934	$ (4,180)	$ 68,855
December 31, 2009:				
U.S. Government agencies	$ 35,119	$ 1,469	$ (2)	$ 36,586
U.S. Government agency CMO's	14,954	376	(10)	15,320
Residential mortgage obligations	14,273	0	(4,559)	9,714
Obligations of state and political subdivisions	1,252	33	0	1,285
Other investment securities	9,004	0	(498)	8,506
	$ 74,602	$ 1,878	$ (5,069)	$ 71,411

Included in other investment securities at March 31, 2010 are a short-term government securities mutual fund totaling $7.5 million and a money-market mutual fund totaling $1.0 million. Included in other investment securities at December 31, 2009, is a short-term government securities mutual fund totaling $7.5 million, and an overnight money-market mutual fund totaling $1.0 million. The short-term government securities mutual fund invests in debt securities issued or guaranteed by the U.S. Government, its agencies or instrumentalities, with a maximum duration equal to that of a 3-year U.S. Treasury Note.

The amortized cost and fair value of securities available for sale at March 31, 2010, by contractual maturity, are shown below. Actual maturities may differ from contractual maturities because issuers have the right to call or prepay obligations with or without call or prepayment penalties. Contractual maturities on collateralized mortgage obligations cannot be anticipated due to allowed paydowns.

(In thousands)	March 31, 2010 Amortized Cost	Fair Value (Carrying Amount)
Due in one year or less	$ 11,042	$ 10,611
Due after one year through five years	3,641	3,677
Due after five years through ten years	11,127	11,727
Due after ten years	19,000	19,838
Collateralized mortgage obligations	26,291	23,002
	$ 71,101	$ 68,855

There were no realized gains or losses on sales of available-for-sale securities during the three months ended March 31, 2010 or 2009. There were other-than-temporary impairment losses on certain of the Company's residential mortgage obligations (private label collateralized mortgage obligations) totaling $244,000 and $163,000 for the three months ended March 31, 2010 and 2009, respectively.

Securities that have been temporarily impaired less than 12 months at March 31, 2010 are comprised of one U.S. government agency security with a weighted average life of 3.0 years and one collateralized mortgage obligation with a weighted average life of 0.8 years. As of March 31, 2010, there were three residential mortgage obligations and one other investment security with a total weighted average life of 3.2 years that have been temporarily impaired for twelve months or more.

The following summarizes the total of temporarily impaired and other-than-temporarily impaired investment securities at Match 31, 2010 (see discussion below for other than temporarily impaired securities included here):

(In thousands)	Less than 12 Months		12 Months or More		Total	
Securities available for sale:	Fair Value (Carrying Amount)	Unrealized Losses	Fair Value (Carrying Amount)	Unrealized Losses	Fair Value (Carrying Amount)	Unrealized Losses
U.S. Government agencies	$ 990	$ (12)	$ 0	$ 0	$ 990	$ (12)
U.S. Government agency CMO's	1,323	(12)	0	0	1,323	(12)
Residential mortgage obligations	0	0	9,893	(3,674)	9,893	(3,674)
Obligations of state and political subdivisions	0	0	0	0	0	0
Other investment securities	0	0	7,518	(482)	7,518	(482)
Total impaired securities	$ 2,313	$ (24)	$ 17,411	$ (4,156)	$ 19,724	$ (4,180)

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Securities that have been temporarily impaired less than 12 months at March 31, 2009 are comprised of two collateralized mortgage obligations and one U.S. government agency security with a total weighted average life of 0.5 years. As of March 31, 2009, there were three residential mortgage obligations and two other investment securities with a total weighted average life of 2.8 years that have been temporarily impaired for twelve months or more.

The following summarizes temporarily impaired investment securities at March 31, 2009:

(In thousands)	Less than 12 Months		12 Months or More		Total	
Securities available for sale:	Fair Value (Carrying Amount)	Unrealized Losses	Fair Value (Carrying Amount)	Unrealized Losses	Fair Value (Carrying Amount)	Unrealized Losses
U.S. Government agencies	$ 143	$ (1)	$ 0	$ 0	$ 143	$ (1)
U.S. Government agency CMO’s	6,870	(68)	0	0	6,870	(68)
Residential mortgage obligations	0	0	9,350	(7,400)	9,350	(7,400)
Obligations of state and political subdivisions	0	0	0	0	0	0
Other investment securities	0	0	12,346	(654)	12,346	(654)
Total impaired securities	$ 7,013	$ (69)	$ 21,696	$ (8,054)	$ 28,709	$ (8,123)

At March 31, 2010 and December 31, 2009, available-for-sale securities with an amortized cost of approximately $63.5 million and $66.5 million (fair value of $62.9 million and $65.4 million) were pledged as collateral for public funds, and treasury tax and loan balances.

The Company evaluates investment securities for other-than-temporary impairment (“OTTI”) at least quarterly, and more frequently when economic or market conditions warrant such an evaluation. The investment securities portfolio is evaluated for OTTI by segregating the portfolio into two general segments and applying the appropriate OTTI model. Investment securities classified as available for sale or held-to-maturity are generally evaluated for OTTI under ASC Topic 320, “Investments – Debt and Equity Instruments.” Certain purchased beneficial interests, including non-agency mortgage-backed securities, asset-backed securities, and collateralized debt obligations, are evaluated using the model outlined in ASC Topic 320 (formerly EITF Issue No. 99-20, “Recognition of Interest Income and Impairment on Purchased Beneficial Interests and Beneficial Interests that Continue to be Held by a Transfer in Securitized Financial Assets.”)

In the first segment, the Company considers many factors in determining OTTI, including: (1) the length of time and the extent to which the fair value has been less than cost, (2) the financial condition and near-term prospects of the issuer, (3) whether the market decline was affected by macroeconomic conditions, and (4) whether the entity has the intent to sell the debt security or more likely than not will be required to sell the debt security before its anticipated recovery. The assessment of whether an other-than-temporary decline exists involves a high degree of subjectivity and judgment and is based on the information available to the Company at the time of the evaluation.

The second segment of the portfolio uses the OTTI guidance that is specific to purchased beneficial interests including non-agency collateralized mortgage obligations. Under this model, the Company compares the present value of the remaining cash flows as estimated at the preceding evaluation date to the current expected remaining cash flows. An OTTI is deemed to have occurred if there has been an adverse change in the remaining expected future cash flows.

Effective the first quarter 2009, the Company adopted an amendment to existing guidance on other-than-temporary impairments for debt securities, which establishes a new model for measuring and disclosing OTTI for all debt securities. Other-than-temporary-impairment occurs under the new guidance when the Company intends to sell the security or more likely than not will be required to sell the security before recovery of its amortized cost basis less any current-period credit loss. If an entity intends to sell or more likely than not will be required to sell the security before recovery of its amortized cost basis less any current-period credit loss, the other-than-temporary-impairment shall be recognized in earnings equal to the entire difference between the investment's amortized cost basis and its fair value at the balance sheet date. If an entity does not intend to sell the security and it is not more likely than not that the entity will be required to sell the security before recovery of its amortized cost basis less any current-period loss, the other-than-temporary-impairment shall be separated into the amount representing the credit loss and the amount related to all other factors. The amount of the total other-than-temporary-impairment related to the credit loss is recognized in earnings, and is determined based on the difference between the present value of cash flows expected to be collected and the current amortized cost of the security. The amount of the total other-than-temporary-impairment related to other factors shall be recognized in other comprehensive (loss) income, net of applicable taxes. The previous amortized cost basis less the other-than-temporary-impairment recognized in earnings shall become the new amortized cost basis of the investment.

At March 31, 2010, the decline in market value for all but three (see below) of the impaired securities is attributable to changes in interest rates and illiquidity, and not credit quality. Because the Company does not have the intent to sell these impaired securities and it is likely that it will not be required to sell the securities before their anticipated recovery, the Company does not consider these securities to be other-than-temporarily impaired at March 31, 2010.

At March 31, 2010, the Company had three non-agency collateralized mortgage obligations which have been impaired more than twelve months. The three non-agency collateralized mortgage obligations had a market value of $9.9 million and unrealized losses of approximately $3.7 million at March 31, 2010. All three non-agency mortgage-backed securities were rated less than high credit quality at March 31, 2010. The Company evaluated these three non-agency collateralized mortgage obligations for OTTI by comparing the present value of expected cash flows to previous estimates to determine whether there had been adverse changes in cash flows during the quarter. The OTTI evaluation was conducted utilizing the services of a third party specialist and consultant in MBS and CMO products. The cash flow assumptions used in the evaluation included a number of factors including changes in delinquency rates, anticipated prepayment speeds, loan-to-value ratios, changes in agency ratings, and market prices. As a result of the impairment evaluation, the Company determined that there had been adverse changes in cash flows in all three of the three non-agency collateralized mortgage obligations reviewed, and concluded that these three non-agency collateralized mortgage obligations were other-than-temporarily impaired. The three CMO securities had other-than-temporary-impairment losses of $3.9 million, of which $244,000 was recorded as expense and $3.7 million was recorded in other comprehensive loss. These three non-agency collateralized mortgage obligations remained classified as available for sale at March 31, 2010.

The following table details the three non-agency collateralized mortgage obligations with other-than-temporary-impairment, their credit rating at March 31, 2010, the related credit losses recognized in earnings during the quarter, and impairment losses in other comprehensive loss:

	RALI 2006-QS1G A10 Rated CCC	RALI 2006 QS8 A1 Rated CCC	CWALT 2007-8CB A9 Rated CCC	Total
Amortized cost – before OTTI	$ 4,676,372	$ 1,401,642	$ 7,733,440	$ 13,811,454
Credit loss – Quarter ended March 31, 2010	(192,179)	(24,148)	(28,137)	(244,464)
Other impairment (OCI)	(1,304,357)	(356,215)	(2,013,400)	(3,673,972)
Carrying amount – March 31, 2010	$ 3,179,836	$ 1,021,279	$ 5,691,903	$ 9,893,018
Total impairment - YTD March 31, 2010	$ (1,496,536)	$ (380,363)	$ (2,041,537)	$ (3,918,436)

The total other comprehensive loss (OCI) balance of $3.7 million in the above table is included in unrealized losses of 12 months or more at March 31, 2010.

3. Loans and Leases

Loans include the following:

(In thousands)	March 31, 2010	% of Loans	December 31, 2009	% of Loans
Commercial and industrial	$ 178,617	34.4%	$ 167,930	33.0%
Real estate – mortgage	173,737	33.3%	165,629	32.6%
RE construction and development	98,618	18.9%	105,220	20.7%
Agricultural	51,113	9.8%	50,897	10.0%
Installment/other	18,340	3.5%	18,191	3.6%
Lease financing	662	0.1%	706	0.1%

Total Gross Loans	$	521,087	100.0%	$	508,573	100.0%

The Company had $1.3 million in loans over 90 days past due and still accruing at March 31, 2010. Loans over 90 days past due and still accruing totaled $486,000 at December 31, 2009. Nonaccrual loans totaled $32.7 million and $34.8 million at March 31, 2010 and December 31, 2009, respectively.

An analysis of changes in the allowance for credit losses is as follows:

(In thousands)	March 31, 2010	December 31, 2009	March 31, 2009
Balance, beginning of year	$ 15,016	$ 11,529	$ 11,529
Provision charged to operations	1,631	13,375	1,351
Losses charged to allowance	(449)	(10,145)	(2,598)
Recoveries on loans previously charged off	6	257	166
Balance at end-of-period	$ 16,204	$ 15,016	$ 10,448

The allowance for credit losses represents management's estimate of the risk inherent in the loan portfolio based on the current economic conditions, collateral values and economic prospects of the borrowers. The formula allowance for unfunded loan commitments totaling $195,000 and $234,000 at March 31, 2010 and December 31, 2009, respectively, is carried in other liabilities. The Company's market areas of the San Joaquin Valley, the greater Oakhurst area, East Madera County, and Santa Clara County, have all been impacted by the economic downturn related to depressed real estate markets and the tightening of liquidity markets. The Company has taken these events into account when reviewing estimates of factors that may impact the allowance for credit losses.

The Company grades "problem" or "classified" loans according to certain risk factors associated with individual loans within the loan portfolio. Classified loans consist of loans which have been graded substandard, doubtful, or loss based upon inherent weaknesses in the individual loans or loan relationships. Classified loans include not only impaired loans (as defined under SFAS No. 114), but also loans which based upon inherent weaknesses result in a risk grading of substandard, doubtful, or loss. The following table summarizes the Company's classified loans at March 31, 2010 and December 31, 2009.

(in 000's)	March 31, 2010	December 31, 2009
Impaired loans	$ 51,932	$ 53,794
Classified loans not considered impaired	12,792	15,816
Total classified loans	$ 64,724	$ 69,610

The following table summarizes the Company's investment in loans for which impairment has been recognized for the periods presented:

(in thousands)	March 31, 2010	December 31, 2009	March 31, 2009
Total impaired loans at period-end	$ 51,932	$ 53,794	$ 58,030
Impaired loans which have specific allowance	32,938	26,266	29,711
Total specific allowance on impaired loans	9,339	7,974	4,393
Total impaired loans which as a result of write-downs or the fair value of the collateral, did not have a specific allowance	18,994	27,528	28,319

(in thousands)	YTD – 3/31/10	YTD - 12/31/09	YTD – 3/31/09

Average recorded investment in impaired loans during period	$	52,863	$	59,595	$	56,201
Income recognized on impaired loans during period	$	155	$	326	$	0

4. Deposits

Deposits include the following:

(In thousands)	March 31, 2010	December 31, 2009
Noninterest-bearing deposits	$ 134,140	$ 139,724
Interest-bearing deposits:		
NOW and money market accounts	167,547	158,795
Savings accounts	35,759	34,146
Time deposits:		
Under $100,000	66,064	64,481
$100,000 and over	178,972	164,514
Total interest-bearing deposits	448,342	421,936
Total deposits	$ 582,482	$ 561,660
Total brokered deposits included in time deposits above	$ 120,303	$ 129,352

5. Short-term Borrowings/Other Borrowings

At March 31, 2010, the Company had collateralized and uncollateralized lines of credit with the Federal Reserve Bank of San Francisco and other correspondent banks aggregating $136.5 million, as well as Federal Home Loan Bank ("FHLB") lines of credit totaling $43.0 million. These lines of credit generally have interest rates tied to the Federal Funds rate or are indexed to short-term U.S. Treasury rates or LIBOR. FHLB advances are collateralized by all of the Company's stock in the FHLB and certain qualifying mortgage loans. At March 31, 2010, the Company had total outstanding balances of $37.0 million drawn against its FHLB line of credit. The weighted average cost of borrowings outstanding at March 31, 2010 was 0.19%. The $37.0 million in FHLB borrowings outstanding at March 31, 2010 are summarized in the table below.

FHLB term borrowings at March 31, 2010 (in 000's):

Term	Balance at 3/31/10	Fixed Rate	Maturity
6-month	$ 28,000	0.18%	7/29/10
6-month	9,000	0.21%	7/29/10
	$ 37,000	0.19%	

At December 31, 2009, the Company had collateralized and uncollateralized lines of credit with the Federal Reserve Bank of San Francisco and other correspondent banks aggregating $124.2 million, as well as Federal Home Loan Bank ("FHLB") lines of credit totaling $40.8 million. At December 31, 2009, the Company had total outstanding balances of $40.0 million in borrowings drawn against its FHLB lines of credit at an average rate of 0.86%. Of the $40.0 million in FHLB borrowings outstanding at December 31, 2009, all will mature in three months or less. The weighted average cost of borrowings for the year ended December 31, 2009 was 0.80%. As of December 31, 2009, $14.2 million in real estate-secured loans, and $42.6 million in investment securities at FHLB, were pledged as collateral for FHLB advances. Additionally, $256.7 million in real estate-secured loans were pledged at December 31, 2009 as collateral for used and unused borrowing lines with the Federal Reserve Bank totaling $120.7 million. All lines of credit are on an "as available" basis and can be revoked by the grantor at any time.

6. Supplemental Cash Flow Disclosures

(In thousands)	Three Months Ended March 31, 2010		2009	
Cash paid during the period for:				
Interest	$	1,360	$	2,232
Income Taxes	$	68		59
Noncash investing activities:				
Dividends declared not paid	$	0	$	4
Loans transferred to foreclosed assets	$	5,180	$	721

7. Common Stock Dividend

On March 23, 2010, the Company's Board of Directors declared a one-percent (1%) stock dividend on the Company's outstanding common stock. Based upon the number of outstanding common shares on the record date of April 9, 2010, an additional 124,965 shares were issued to shareholders on April 21, 2010. Because the stock dividend was considered a "small stock dividend", approximately $655,000 was transferred from retained earnings to common stock based upon the $5.24 closing price of the Company's common stock on the declaration date of March 23, 2010. There were no fractional shares paid. Other than for earnings-per-share calculations, shares issued for the stock dividend have been treated prospectively for financial reporting purposes. For purposes of earnings per share calculations, the Company's weighted average shares outstanding and potentially dilutive shares used in the computation of earnings per share have been restated after giving retroactive effect to a 1% stock dividend to shareholders for all periods presented.

8. Net (Loss) Income per Common Share

The following table provides a reconciliation of the numerator and the denominator of the basic EPS computation with the numerator and the denominator of the diluted EPS computation:

	Three Months Ended March 31,	
(In thousands except earnings per share data)	2010	2009
Net income available to common shareholders	$ 442	$ 921
Weighted average shares issued	12,621	12,622
Add: dilutive effect of stock options	0	0
Weighted average shares outstanding adjusted for potential dilution	12,621	12,622
Basic earnings per share	$ 0.04	$ 0.07
Diluted earnings per share	$ 0.04	$ 0.07
Anti-dilutive shares excluded from earnings per share calculation	194	185

The Company's average weighted shares outstanding and potentially dilutive shares used in the computation of earnings per share have been restated after giving retroactive effect to a 1% stock dividend to shareholders of record on April 9, 2010.

9. Stock Based Compensation

All share-based payments to employees, including grants of employee stock options, are recognized in the financial statements based on the grant-date fair value of the award. The fair value is amortized over the requisite service period (generally the vesting period).

Included in salaries and employee benefits for the three months ended March 31, 2010 and 2009 is $5,000 and $13,000 of share-based compensation, respectively. The related tax benefit on share-based compensation recorded in the provision for income taxes was not material to either quarter.

A summary of the Company's options as of January 1, 2010 and changes during the three months ended March 31, 2010 is presented below.

	Weighted Average	Weighted Average

	2005 Plan		Exercise Price	1995 Plan		Exercise Price
Options outstanding January 1, 2010	160,820	$	15.38	16,984	$	11.50
Options granted during period	25,000		4.75	0		—
1% common stock dividends – 2010	1,858		(0.14)	170		(0.11)
Options outstanding March 31, 2010	187,678	$	13.81	17,154	$	11.39
Options exercisable at March 31, 2010	127,744	$	15.17	16,942	$	11.39

As of March 31, 2010 and 2009, there was $70,000 and $68,000, respectively, of total unrecognized compensation expense related to nonvested stock options. This cost is expected to be recognized over a weighted average period of approximately 0.9 years and 0.5 years, respectively. No options were exercised during the three months ended March 31, 2010 or 2009.

	Three Months Ended March 31, 2010	Three Months Ended March 31, 2009
Weighted average grant-date fair value of stock options granted	$ 2.22	n/a
Total fair value of stock options vested	$ 61,543	$ 68,690
Total intrinsic value of stock options exercised	n/a	n/a

The Bank determines fair value at grant date using the Black-Scholes-Merton pricing model that takes into account the stock price at the grant date, the exercise price, the expected life of the option, the volatility of the underlying stock and the expected dividend yield and the risk-free interest rate over the expected life of the option.

The weighted average assumptions used in the pricing model are noted in the table below. The expected term of options granted is derived using the simplified method, which is based upon the average period between vesting term and expiration term of the options. The risk free rate for periods within the contractual life of the option is based on the U.S. Treasury yield curve in effect at the time of the grant. Expected volatility is based on the historical volatility of the Bank's stock over a period commensurate with the expected term of the options. The Company believes that historical volatility is indicative of expectations about its future volatility over the expected term of the options.

The Bank expenses the fair value of options on a straight-line basis over the vesting period for each separately vesting portion of the award. The Bank estimates forfeitures and only recognizes expense for those shares expected to vest. Based upon historical evidence, the Company has determined that because options are granted to a limited number of key employees rather than a broad segment of the employee base, expected forfeitures, if any, are not material.

	Three Months Ended March 31, 2010
Risk Free Interest Rate	2.71%
Expected Dividend Yield	0.00%
Expected Life in Years	6.50 Years
Expected Price Volatility	43.07%

The Black-Scholes-Merton option valuation model requires the input of highly subjective assumptions, including the expected life of the stock based award and stock price volatility. The assumptions listed above represent management's best estimates, but these estimates involve inherent uncertainties and the application of management judgment. As a result, if other assumptions had been used, the Bank's recorded stock-based compensation expense could have been materially different from that previously reported in proforma disclosures. In addition, the Bank is required to estimate the expected forfeiture rate and only recognize expense for those shares expected to vest. If the Bank's actual forfeiture rate is materially different from the estimate, the share-based compensation expense could be materially different.

10. Income Taxes

The Company periodically reviews its tax positions under the guidance of ASC Topic 740, "Income Taxes", based upon the criteria that an individual tax position would have to meet for some or all of the income tax benefit to be recognized in a taxable entity's financial statements. Under the guidelines, an entity should recognize the financial statement benefit of a tax position if it determines that it is more likely than not that the position will be sustained on examination. The term, "more likely than not", means a likelihood of more than 50 percent. In assessing whether the more-likely-than-not criterion is met, the entity should assume that the tax position will be reviewed by the applicable taxing authority and all available information is known to the taxing authority.

The Company and a subsidiary file income tax returns in the U.S federal jurisdiction, and several states within the U.S. There are no filings in foreign jurisdictions. The Company is not currently aware of any tax jurisdictions where the Company or any subsidiary is subject examination by federal, state, or local taxing authorities before 2001. The Internal Revenue Service (IRS) has not examined the Company's or any subsidiaries federal tax returns since before 2001, and the Company currently is not aware of any examination planned or contemplated by the IRS.

The Company again reviewed its REIT tax position as of March 31, 2010. There have been no changes to the Company's tax position with regard to the REIT during the quarter ended March 31, 2010. The Company had approximately $684,000 and $653,000 accrued for the payment of interest and penalties at March 31, 2010 and December 31, 2009, respectively. It is the Company's policy to recognize interest expense related to unrecognized tax benefits, and penalties, as a component tax expense. A reconciliation of the beginning and ending amount of unrecognized tax benefits is as follows (in 000's):

Balance at January 1, 2010	$	1,560
Additions for tax provisions of prior years		21
Balance at March 31, 2010	$	1,581

11. Junior Subordinated Debt/Trust Preferred Securities

Effective September 30, 2009 and beginning with the quarterly interest payment due October 1, 2009, the Company elected to defer interest payments on the Company's $15.0 million of junior subordinated debentures relating to its trust preferred securities. The terms of the debentures and trust indentures allow for the Company to defer interest payments for up to 20 consecutive quarters without default or penalty. During the period that the interest deferrals are elected, the Company will continue to record interest expense associated with the debentures. Upon the expiration of the deferral period, all accrued and unpaid interest will be due and payable. During the deferral period, the Company is precluded from paying cash dividends to shareholders or repurchasing its stock.

The fair value guidance generally permits the measurement of selected eligible financial instruments at fair value at specified election dates. Effective January 1, 2008, the Company elected the fair value option for its junior subordinated debt issued under USB Capital Trust II. The rate paid on the junior subordinated debt issued under USB Capital Trust II is 3-month LIBOR plus 129 basis points, and is adjusted quarterly.

At March 31, 2010 the Company performed a fair value measurement analysis on its junior subordinated debt using a cash flow valuation model approach to determine the present value of those cash flows. The cash flow model utilizes the forward 3-month Libor curve to estimate future quarterly interest payments due over the thirty-year life of the debt instrument, adjusted for deferrals of interest payments per the Company's election at March 31, 2010. These cash flows were discounted at a rate which incorporates a current market rate for similar-term debt instruments, adjusted for additional credit and liquidity risks associated with the junior subordinated debt. Although there is little market data in the current relatively illiquid credit markets, we believe the 8.7% discount rate used represents what a market participant would consider under the circumstances.

The fair value calculation performed at March 31, 2010 resulted in a pretax gain adjustment of $157,000 ($92,000, net of tax) for the quarter ended March 31, 2010. The previous year's fair value calculation performed at March 31, 2009 resulted in a pretax loss adjustment of $59,000 ($34,000 net of tax) for the quarter ended March 31, 2009.

12. Fair Value Measurements and Disclosure

The following summary disclosures are made in accordance with the guidance provided by ASC Topic 825 "Fair Value Measurements and Disclosures" (formerly Statement of Financial Accounting Standards No. 107, "Disclosures about Fair Value of Financial Instruments,") which requires the disclosure of fair value information about both on- and off-balance sheet financial instruments where it is practicable to estimate that value.

(In thousands)	March 31, 2010 Carrying Amount	March 31, 2010 Estimated Fair Value	December 31, 2009 Carrying Amount	December 31, 2009 Estimated Fair Value
On-Balance sheet:				
Financial Assets:				
Cash and cash equivalents	$ 16,607	$ 16,607	$ 17,644	$ 17,644
Interest-bearing deposits	3,970	4,133	3,313	3,449
Investment securities	68,855	68,855	71,411	71,411
Loans, net	520,040	507,784	507,708	496,543
Cash surrender value of life insurance	15,099	15,099	14,972	14,972
Investment in bank stock	143	143	143	143
Financial Liabilities:				
Deposits	582,482	581,926	561,660	561,150
Borrowings	37,000	36,972	40,000	39,970
Junior Subordinated Debt	10,616	10,616	10,716	10,716
Off-Balance sheet:				
Commitments to extend credit	—	—	—	—
Standby letters of credit	—	—	—	—

ASC Topic 820 (formerly SFAS 157, “Fair Value Measurements”) clarifies the definition of fair value, describes methods used to appropriately measure fair value in accordance with generally accepted accounting principles and expands fair value disclosure requirements. This statement applies whenever other accounting pronouncements require or permit fair value measurements.

The fair value hierarchy prioritizes the inputs to valuation techniques used to measure fair value into three broad levels (Level 1, Level 2, and Level 3). Level 1 inputs are unadjusted quoted prices in active markets (as defined) for identical assets or liabilities that the reporting entity has the ability to access at the measurement date. Level 2 inputs are inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly. Level 3 inputs are unobservable inputs for the asset or liability, and reflect the reporting entity’s own assumptions about the assumptions that market participants would use in pricing the asset or liability (including assumptions about risk).

The Company performs fair value measurements on certain assets and liabilities as the result of the application of current accounting guidelines. Some fair value measurements, such as for available-for-sale securities (AFS) and junior subordinated debt are performed on a recurring basis, while others, such as impairment of loans, goodwill and other intangibles, are performed on a nonrecurring basis.

The Company’s Level 1 financial assets consist of money market funds and highly liquid mutual funds for which fair values are based on quoted market prices. The Company’s Level 2 financial assets include highly liquid debt instruments of U.S. government agencies, collateralized mortgage obligations, and debt obligations of states and political subdivisions, whose fair values are obtained from readily-available pricing sources for the identical underlying security that may, or may not, be actively traded. Level 2 financial assets also include certain impaired loans which are evaluated based on the observable inputs, specifically current appraisals. From time to time, the Company recognizes transfers between Level 1, 2, and 3 when a change in circumstances warrants a transfer. There were no significant transfers in or out of Level 1 and Level 2 fair value measurements during the three months ended March 31, 2010.

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The following tables summarize the Company's assets and liabilities that were measured at fair value on a recurring and non-recurring basis as of March 31, 2010 (in 000's):

Description of Assets	March 31, 2010	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
AFS Securities (2):				
Other investment securities	$ 8,694	$ 8,694		
U.S. government agencies	36,013		$ 36,013	
U.S. government agency CMO's	13,109		13,109	
Obligations of states & political subdivisions	1,289		1,289	
Residential mortgage obligations	9,893			$ 9,893
Total AFS securities	68,998	8,694	50,411	9,893
Impaired loans (1):				
Commercial and industrial	2,878		29	2,849
Real estate mortgage	6,240		451	5,789
RE construction & development	13,722		2,734	10,988
Agricultural	760		0	760
Total impaired loans	23,600		3,214	20,386
Core deposit intangibles (1)	619			619
Total	$ 93,217	$ 8,694	$ 53,625	$ 30,898

(1) nonrecurring

(2) Includes $143 in equity securities reported in other assets on the balance sheet

Description of Liabilities	March 31, 2010	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Junior subordinated debt	$ 10,616			$ 10,616
Total	$ 10,616	$ 0	$ 0	$ 10,616

The following tables summarize the Company's assets and liabilities that were measured at fair value on a recurring and nonrecurring basis during the year ended December 31, 2009 (in 000's):

Description of Assets	December 31, 2009	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
AFS securities (1)	$ 71,554	$ 8,648	$ 53,192	$ 9,714
Impaired loans	18,347		1,976	16,371
Goodwill	5,764			5,764
Core deposit intangible (2)	777			777
Total	$ 96,442	$ 8,648	$ 55,168	$ 32,626

(1) Includes $143 in equity securities reported in other assets

(2) Nonrecurring items

Description of Liabilities	December 31, 2009	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Junior subordinated debt	$ 10,716			$ 10,716
Total	$ 10,716	$ 0	$ 0	$ 10,716

The nonrecurring fair value measurements performed during the three months ended March 31, 2010 resulted in pretax fair value impairment adjustments of $57,000 ($33,000 net of tax) to the core deposit intangible asset. The impairment adjustments are reflected as a component of noninterest expense for the nine months ended March 31, 2010.

The following tables provide a reconciliation of assets and liabilities at fair value using significant unobservable inputs (Level 3) on a recurring and non-recurring basis during the three months ended March 31, 2010 and 2009 (in 000's):

Reconciliation of Assets:	3/31/10 Impaired loans	3/31/10 CMO's	3/31/10 Intangible assets	3/31/09 Impaired loans	3/31/09 CMO's	3/31/09 Intangible assets
Beginning balance	$ 16,371	$ 9,714	$ 77	$ 15,967	$ 12,800	$ 1,489
Total gains or (losses) included in earnings (or other comprehensive loss)	(731)	179	(158)	(3,685)	(3,286)	(176)
Transfers in and/or out of Level 3	4,746	0	0	10,930	0	(206)
Ending balance	$ 20,386	$ 9,893	$ 619	$ 23,212	$ 9,514	$ 1,107
The amount of total gains or (losses) for the period included in earnings (or other comprehensive loss) attributable to the change in unrealized gains or losses relating to assets still held at the reporting date	$ (568)	$ 179	$ (158)	$ (1,256)	$ (3,286)	$ (176)

Reconciliation of Liabilities:	3/31/2010 Junior Sub Debt	3/31/2009 Junior Sub Debt
Beginning balance	$ 10,716	$ 11,926
Total gains included in earnings (or changes in net assets)	(100)	(39)
Transfers in and/or out of Level 3	0	0
Ending balance	$ 10,616	$ 11,887
The amount of total gains for the period included in earnings attributable to the change in unrealized gains or losses relating to liabilities still held at the reporting date	$ (100)	$ (39)

The following methods and assumptions were used in estimating the fair values of financial instruments:

Cash and Cash Equivalents - The carrying amounts reported in the balance sheets for cash and cash equivalents approximate their estimated fair values.

Interest-bearing Deposits – Interest bearing deposits in other banks consist of fixed-rate certificates of deposits. Accordingly, fair value has been estimated based upon interest rates currently being offered on deposits with similar characteristics and maturities.

Investments – Available for sale securities are valued based upon open-market price quotes obtained from reputable third-party brokers that actively make a market in those securities. Market pricing is based upon specific CUSIP identification for each individual security. To the extent there are observable prices in the market, the mid-point of the bid/ask price is used to determine fair value of individual securities. If that data are not available for the last 30 days, a Level 2-type matrix pricing approach based on comparable securities in the market is utilized. Level-2 pricing may include using a spread forward from the last observable trade or may use a proxy bond like a TBA mortgage to come up with a price for the security being valued. Changes in fair market value are recorded in other comprehensive loss as the securities are available for sale. At March 31, 2010 and December 31, 2009, the Company held three non-agency (private-label) collateralized mortgage obligations (CMO's). Fair value of these securities (as well as review for other-than-temporary impairment) was performed by a third-party securities broker specializing in CMO's. Fair value was based upon estimated cash flows which included assumptions about future prepayments, default rates, and the impact of credit risk on this type of investment security. Although the pricing of the CMO's has certain aspects of Level 2 pricing, many of the pricing inputs are based upon unobservable assumptions of future economic trends and as a result the Company considers this to be Level 3 pricing.

Loans - Fair values of variable rate loans, which reprice frequently and with no significant change in credit risk, are based on carrying values. Fair values for all other loans, except impaired loans, are estimated using discounted cash flows over their remaining maturities, using interest rates at which similar loans would currently be offered to borrowers with similar credit ratings and for the same remaining maturities.

Impaired Loans - Fair value measurements for impaired loans are performed pursuant to the criteria defined in the Receivables Topic of the FASB ASC, which was originally issued under FAS No. 114, and are based upon either collateral values supported by appraisals, or observed market prices. Changes are not recorded directly as an adjustment to current earnings or comprehensive income, but rather as an adjustment component in determining the overall adequacy of the loan loss reserve. Such adjustments to the estimated fair value of impaired loans may result in increases or decreases to the provision for credit losses recorded in current earnings.

Bank-owned Life Insurance – Fair values of life insurance policies owned by the Company approximate the insurance contract's cash surrender value.

Investment in limited partnerships – Investment in limited partnerships which invest in qualified low-income housing projects generate tax credits to the Company. The investment is amortized using the effective yield method based upon the estimated remaining utilization of low-income housing tax credits. The Company's carrying value approximates fair value.

Investments in Bank Stock – Investment in Bank equity securities is classified as available for sale and is valued based upon open-market price quotes obtained from an active stock exchange. Changes in fair market value are recorded in other comprehensive income.

Deposits – In accordance with ASC Topic 820 (formerly SFAS No. 107), fair values for transaction and savings accounts are equal to the respective amounts payable on demand at March 31, 2010 and December 31, 2009 (i.e., carrying amounts). The Company believes that the fair value of these deposits is clearly greater than that prescribed by ASC Topic 820. Fair values of fixed-maturity certificates of deposit were estimated using the rates currently offered for deposits with similar remaining maturities.

Borrowings - Borrowings consist of federal funds sold, securities sold under agreements to repurchase, and other short-term borrowings. Fair values of borrowings were estimated using the rates currently offered for borrowings with similar remaining maturities.

Junior Subordinated Debt – The fair value of the junior subordinated debt was determined based upon a valuation discounted cash flows model utilizing observable market rates and credit characteristics for similar instruments. In its analysis, the Company used characteristics that distinguish market participants generally use, and considered factors specific to (a) the liability, (b) the principal (or most advantageous) market for the liability, and (c) market participants with whom the reporting entity would transact in that market. For the three month period ended March 31, 2010, cash flows were discounted at a rate which incorporates a current market rate for similar-term debt instruments, adjusted for additional credit and liquidity risks associated with the junior subordinated debt. The Company believes the inputs to the model are subjective enough to the fair value determination of the junior subordinated debt to make them Level 3 inputs.

Off-balance sheet Instruments - Off-balance sheet instruments consist of commitments to extend credit, standby letters of credit and derivative contracts. Fair values of commitments to extend credit are estimated using the interest rate currently charged to enter into similar agreements, taking into account the remaining terms of the agreements and the present counterparties' credit standing. There was no material difference between the contractual amount and the estimated value of commitments to extend credit at March 31, 2010 and December 31, 2009.

Fair values of standby letters of credit are based on fees currently charged for similar agreements. The fair value of commitments generally approximates the fees received from the customer for issuing such commitments. These fees are not material to the Company's consolidated balance sheet and results of operations.

13. Goodwill and Intangible Assets

At March 31, 2010 and December 31, 2009 the Company had goodwill, core deposit intangibles, and other identified intangible assets which were recorded in connection with various business combinations and purchases. The following table summarizes the carrying value of those assets at March 31, 2010 and December 31, 2009.

	March 31, 2010	December 31, 2009
Goodwill	$ 7,391	$ 7,391
Core deposit intangible assets	1,381	1,585
Other identified intangible assets	394	449
Total goodwill and intangible assets	$ 9,166	$ 9,425

Core deposit intangibles and other identified intangible assets are amortized over their useful lives, while goodwill is not amortized. The Company conducts periodic impairment analysis on goodwill and intangible assets and goodwill at least annually or more often as conditions require.

Goodwill: The largest component of goodwill is related to the Legacy merger (Campbell reporting unit) completed during February 2007 and totaled approximately $8.8 million at March 31, 2009. The Company conducted its annual impairment testing of the goodwill related to the Campbell reporting unit effective March 31, 2010. Impairment testing for goodwill is a two-step process.

The first step in impairment testing is to identify potential impairment, which involves determining and comparing the fair value of the operating unit with its carrying value. If the fair value of the operating unit exceeds its carrying value, goodwill is not impaired. If the carrying value exceeds fair value, there is an indication of possible impairment and the second step is performed to determine the amount of the impairment, if any. The fair value determined in the step one testing was determined based on a discounted cash flow methodology using estimated market discount rates and projections of future cash flows for the Campbell operating unit. In addition to projected cash flows, the Company also utilized other market metrics including industry multiples of earnings and price-to-book ratios to estimate what a market participant would pay for the operating unit in the current business environment. Determining the fair value involves a significant amount of judgment, including estimates of changes in revenue growth, changes is discount rates, competitive forces within the industry, and other specific industry and market valuation conditions. The 2009 impairment analysis was impacted by to a large degree by the current economic environment, including significant declines in interest rates, and depressed valuations within the financial industry. Based on the results of step one of the impairment analysis, the Company concluded that the potential for goodwill impairment exists and, therefore, step-two testing will be required to determine if there is goodwill impairment and the amount of goodwill that might be impaired, if any.

Core Deposit Intangibles: During the first quarter of 2010, the Company performed an annual impairment analysis of the core deposit intangible assets associated with the Legacy Bank merger completed during February 2007 (Campbell operating unit). The core deposit intangible asset, which totaled $3.0 million at the time of merger, is being amortized over an estimated life of approximately seven years. The Company recognized $101,000 and $119,000 in amortization expense related to the Legacy operating unit during the three months ended March 31, 2010 and 2009, respectively. At March 31, 2010, the carrying value of the core deposit intangible related to the Legacy Bank merger was $619,000.

During the impairment analysis performed as of March 31, 2010, it was determined that the original deposits purchased from Legacy Bank during February 2007 continue to decline faster than originally anticipated. As a result of increased deposit runoff, particularly in noninterest-bearing checking accounts and savings accounts, the estimated value of the Campbell core deposit intangible was determined to be $619,000 at March 31, 2010 rather than the pre-adjustment carrying value of $675,000. As a result of the impairment analysis, the Company recorded a pre-tax impairment loss of $57,000 ($33,000, net of tax) reflected as a component of noninterest expense for the quarter ended March 31, 2010.

As a result of impairment testing of core deposit intangible assets related to the Campbell operating unit conducted during the first quarter of 2009, the Company recorded a pre-tax impairment loss of $57,000 ($33,000, net of tax) reflected as a component of noninterest expense for the quarter ended March 31, 2009.

14. Subsequent Events

Subsequent events are events or transactions that occur after the balance sheet date but before financial statements are issued. Recognized subsequent events are events or transactions that provide additional evidence about conditions that existed at the date of the balance sheet, including the estimates inherent in the process of preparing financial statements. Nonrecognized subsequent events are events that provide evidence about conditions that did not exist at the date of the balance sheet but arose after that date. Management has reviewed events occurring through the date the financial statements were issued and no subsequent events occurred requiring accrual or disclosure.

Item 2 - Management's Discussion and Analysis of Financial Condition and Results of Operations

Overview

Certain matters discussed or incorporated by reference in this Quarterly Report of Form 10-Q are forward-looking statements that are subject to risks and uncertainties that could cause actual results to differ materially from those projected in the forward-looking statements. Such risks and uncertainties include, but are not limited to, those described in Management's Discussion and Analysis of Financial Condition and Results of Operations. Such risks and uncertainties include, but are not limited to, the following factors: i) competitive pressures in the banking industry and changes in the regulatory environment; ii) exposure to changes in the interest rate environment and the resulting impact on the Company's interest rate sensitive assets and liabilities; iii) decline in the health of the economy nationally or regionally which could reduce the demand for loans or reduce the value of real estate collateral securing most of the Company's loans; iv) credit quality deterioration that could cause an increase in the provision for loan losses; v) Asset/Liability matching risks and liquidity risks; volatility and devaluation in the securities markets, vi) expected cost savings from recent acquisitions are not realized, and, vii) potential impairment of goodwill and other intangible assets. Therefore, the information set forth therein should be carefully considered when evaluating the business prospects of the Company. For additional information concerning risks and uncertainties related to the Company and its operations, please refer to the Company's Annual Report on Form 10-K for the year ended December 31, 2009.

United Security Bancshares (the "Company" or "Holding Company") is a California corporation incorporated during March of 2001 and is registered with the Board of Governors of the Federal Reserve System as a bank holding company under the Bank Holding Company Act of 1956, as amended.. United Security Bank (the "Bank") is a wholly-owned bank subsidiary of the Company and was formed in 1987. References to the Company are references to United Security Bancshares (including the Bank). References to the Bank are to United Security Bank, while references to the Holding Company are to the parent-only, United Security Bancshares. The Company currently has eleven banking branches, which provide financial services in Fresno, Madera, Kern, and Santa Clara counties in the state of California.

Trends Affecting Results of Operations and Financial Position

The following table summarizes the nine-month and year-to-date averages of the components of interest-bearing assets as a percentage of total interest-bearing assets and the components of interest-bearing liabilities as a percentage of total interest-bearing liabilities:

	YTD Average 3/31/10	YTD Average 12/31/09	YTD Average 3/31/09
Loans and Leases	83.78%	85.09%	83.89%
Investment securities available for sale	11.60%	13.38%	14.06%
Interest-bearing deposits in other banks	0.42%	0.94%	2.05%
Federal funds sold	4.20%	0.59%	0.00%
Total earning assets	100.00%	100.00%	100.00%
NOW accounts	9.90%	8.80%	8.21%
Money market accounts	22.96%	22.68%	19.85%
Savings accounts	7.06%	6.86%	7.05%
Time deposits	50.16%	39.94%	33.00%
Other borrowings	7.77%	19.44%	29.64%
Subordinated debentures	2.15%	2.28%	2.25%

Total interest-bearing liabilities	100.00%	100.00%	100.00%

The Company's overall operations are impacted by a number of factors, including not only interest rates and margin spreads, which impact results of operations, but also the composition of the Company's balance sheet. One of the primary strategic goals of the Company is to maintain a mix of assets that will generate a reasonable rate of return without undue risk, and to finance those assets with a low-cost and stable source of funds. Liquidity and capital resources must also be considered in the planning process to mitigate risk and allow for growth.

Continued weakness in the real estate markets and the general economy have impacted the Company's operations during the past year with increased levels of nonperforming assets, increased expenses related to foreclosed properties, and decreased profit margins. Although the Company continues its business development and expansion efforts throughout its market area, increased attention has been placed on reducing nonperforming assets and providing customers more options to help work through this difficult economic period.

With market rates of interest remaining at historically low levels for more than a year, the Company continues to experience compressed net interest margins, although margins have increased to some degree during the first quarter of 2010. The Company's net interest margin was 4.78% for the three months ended March 31, 2010, as compared to 4.51% for the year ended December 31, 2009, and 4.48% for the three months ended March 31, 2009. With approximately 58% of the loan portfolio in floating rate instruments at March 31, 2010, the effects of low market rates continue to impact loan yields. The Company has sought to mitigate the low-interest rate environment with loan floors applied to new and renewed loans over the past year. Loans yielded 6.01% during the three months ended March 31, 2010, as compared to 5.83% for the year ended December 31, 2009, and 6.03% for the three months ended March 31, 2009. The Company's cost of funds has continued to decline over the past year and is largely responsible for the increase in net interest margin experienced during the quarter ended March 31, 2010. The cost of interest-bearing liabilities was 1.04% for the three months ended March 31, 2010, as compared to 1.43% for the year ended December 31, 2009, and 1.68% for the three months ended March 31, 2009. Wholesale borrowing and brokered deposit rates have remained low since late 2008, resulting in overnight and short-term borrowing rates of less than 0.50% during much of the past year. The Company has benefited from these rate declines, as it has continued to utilize overnight and short-term borrowing lines through the Federal Reserve and Federal Home Loan Bank. The company will continue to utilize these funding sources as required to maintain prudent liquidity levels, while seeking to increase core deposits when possible.

Total noninterest income of $1.3 million reported for the three months ended March 31, 2010 increased $172,000 or 15.1% as compared to the three months ended March 31, 2009. The increase in noninterest income between the two quarterly periods is primarily the result of the fair value gain adjustments on the Company's junior subordinated debt which included fair value gains of $157,000 recognized during the three months ended March 31, 2010, as compared to fair value losses of 59,000 recognized during the three months ended March 31, 2009, an increase of $216,000 between the two periods. Noninterest income continues to be driven by customer service fees, which totaled $948,000 for the three months ended March 31, 2010, representing a decrease of $41,000 or 4.2% over the $989,000 in customer service fees reported for the three months ended March 31, 2009. Customer service fees represented 72.2% and 86.7% of total noninterest income for the three-month periods ended March 31, 2010 and 2009, respectively.

Noninterest expense increased approximately 656,000 or 11.6% between the three-month periods ended March 31, 2009 and March 31, 2010. The primary reason for the increase in noninterest expense experienced during the first three months of 2010 was the result of increases in impairment losses on other real estate owned through foreclosure and investment securities, as well as increases in FDIC insurance assessments during the period.

Effective September 30, 2009 and beginning with the quarterly interest payment due October 1, 2009, the Company elected to defer interest payments on the Company's $15.0 million of junior subordinated debentures relating to its trust preferred securities. This is the result of regulatory restraints which have precluded the Bank from paying dividends to the Holding Company. The terms of the debentures and trust indentures allow for the Company to defer interest payments for up to 20 consecutive quarters without default or penalty. During the period that the interest deferrals are elected, the Company will continue to record interest expense associated with the debentures. Upon the expiration of the deferral period, all accrued and unpaid interest will be due and payable. Under the terms of the debenture, the Company is precluded from paying cash dividends to shareholders or repurchasing its stock during the deferral period.

The Company has not paid any cash dividends on its common stock since the second quarter of 2008 and does not expect to resume cash dividends on its common stock for the foreseeable future. Because the Company has elected to defer the quarterly payments of interest on its junior subordinated debentures issued in connection with the trust preferred securities as discussed above, the Company is prohibited from paying cash dividends on its common stock during the deferral period. In addition, pursuant to a formal agreement entered into with the Federal Reserve Bank during the first quarter of 2010, the Company and the Bank are precluded from paying cash dividends without prior consent of the Federal Reserve. On March 23, 2010 the Company's Board of Directors again declared a one-percent (1%) stock dividend on the Company's outstanding common stock. The Company believes, given the current uncertainties in the economy and unprecedented declines in real estate valuations in our markets, it is prudent to retain capital in this environment, and better position the Company for future growth opportunities. Based upon the number of outstanding common shares on the record date of April 9, 2010, an additional 124,965 shares were issued to shareholders on April 21, 2010. For purposes of earnings per share calculations, the Company's weighted average shares outstanding and potentially dilutive shares used in the computation of earnings per share have been restated after giving retroactive effect to the 1% stock dividend to shareholders for all periods presented.

The Company has sought to maintain a strong, yet conservative balance sheet while continuing to reduce the level of nonperforming assets during the three months ended March 31, 2010. Total assets increased approximately $19.1 million during the three months ended March 31, 2010, with an increase of $12.5 million in loans. Decreases of $3.0 million in FHLB term borrowings were partially offset by increases in brokered and other deposits. Net increases of $17.8 million in deposits and borrowings experienced during the three months ended March 31, 2010, were utilized to fund increases in loans during the period as well as increases in federal funds sold to enhance liquidity. Average loans comprised approximately 84% of overall average earning assets during the three months ended March 31, 2010, a percentage that has remained stable over the past three years.

Nonperforming assets, which are primarily related to the real estate loan and property portfolio, have declined slightly during the first quarter of 2010 but remain high as real estate markets continue to suffer from the mortgage crisis which began during mid-2007. Nonaccrual loans totaling $32.7 million at March 31, 2010, decreased $2.0 million from the balance reported at December 31, 2009. In determining the adequacy of the underlying collateral related to these loans, management monitors trends within specific geographical areas, loan-to-value ratios, appraisals, and other credit issues related to the specific loans. Impaired loans decreased $1.9 million during the three months ended March 31, 2010 to a balance of $51.9 million at March 31, 2010. Other real estate owned through foreclosure increased $1.9 million between December 31, 2009 and March 31, 2010, as transfers of $5.2 million in loans to other real estate owned during the quarter more than offset write-downs and sales of those assets during the period. As a result of these events, nonperforming assets as a percentage of total assets decreased from 12.56% at December 31, 2009 to 12.22% at March 31, 2010.

Management continues to monitor economic conditions in the real estate market for signs of further deterioration or improvement which may impact the level of the allowance for loan losses required to cover identified losses in the loan portfolio. Greater focus has been placed on identifying and reducing the level of problem assets, while working with borrowers to find more options, including loan restructures, to work through these difficult economic times. Provisions made to the allowance for credit losses, totaled $1.6 million during the three months ended March 31, 2010, as compared to $13.4 million for the year ended December 31, 2009 and $1.4 million for the three months ended March 31, 2009. Net loan and lease charge-offs during the three months ended March 31, 2010 totaled $443,000, as compared to $9.9 million and $2.4 million for the year ended December 31, 2009 and three months ended March 31, 2009, respectively.

Deposits increased by $20.8 million during the three months ended March 31, 2010, with increases experienced in all interest-bearing deposit accounts. Increases in time deposits experienced during the quarter ended March 31, 2010 were primarily the result of increases in brokered deposits, allowing the Company to continue to reduce its reliance on borrowed funds, while enhancing liquidity.

Although balances have declined during the most recent quarter, the Company continues to utilize overnight borrowings and other term credit lines, with borrowings totaling $37.0 million at March 31, 2010 as compared to $40.0 million at December 31, 2009. The average rate of those term borrowings was 0.19% at March 31, 2010, as compared to 0.86% at December 31, 2009. Although the Company continues to realize significant interest expense reductions by utilizing these overnight and term borrowings lines, the use of such lines are monitored closely to ensure sound balance sheet management in light of the current economic and credit environment.

The cost of the Company’s subordinated debentures issued by USB Capital Trust II has remained low as market rates declined during most of 2009. With pricing at 3-month-LIBOR plus 129 basis points, the effective cost of the subordinated debt was 1.58% and 1.54% at March 31, 2010 and December 31, 2009, respectively. Pursuant to fair value accounting guidance, the Company has recorded $157,000 in pretax fair value gains on its junior subordinated debt during the three months ended March 31, 2010, bringing the total cumulative gain recorded on the debt to $5.0 million at March 31, 2010.

The Company continues to emphasize relationship banking and core deposit growth, and has focused greater attention on its market area of Fresno, Madera, and Kern Counties, as well as Campbell, in Santa Clara County. The San Joaquin Valley and other California markets continue to exhibit weak demand for construction lending and commercial lending from small and medium size businesses, as commercial and residential real estate markets declined during much of 2008, and 2009, a condition which still persists at this time. Although we have seen some improvement during the first quarter of 2010, the past year has presented significant challenges for the banking industry with tightening credit markets, weakening real estate markets, and increased loan losses adversely affecting the industry.

The Company continually evaluates its strategic business plan as economic and market factors change in its market area. Balance sheet management, enhancing revenue sources, and maintaining market share will be of primary importance during 2010 and beyond. The banking industry is currently experiencing continued pressure on net margins as well as asset quality resulting from conditions in the real estate market, and weak credit markets. During March 2010, the Company and the Bank entered into a regulatory agreement with the Federal Reserve Bank which, among other things, requires improvements in the overall condition of the Company and the Bank. As a result, market rates of interest, asset quality, as well as regulatory oversight will continue be an important factor in the Company's ongoing strategic planning process.

Results of Operations

For the three months ended March 31, 2010, the Company reported net income of $442,000 or $0.04 per share ($0.04 diluted) as compared to net income of $921,000 or $0.07 per share ($0.07 diluted) for the three months ended March 31, 2009. The decline in earnings between the two three month periods ended March 31, 2009 and 2010 is primarily the result of increases in provisions for loan losses and impairment losses taken during 2010, combined with declines in market rates of interest.

The Company's return on average assets was 0.25% for the three months ended March 31, 2010 as compared to 0.50% for the three months ended March 31, 2009. The Bank's return on average equity was 2.33% for the three months ended March 31, 2010 as compared to 4.46% for the same three-month period of 2009.

Net Interest Income

Net interest income before provision for credit losses totaled $7.2 million for the three months ended March 31, 2010, representing an increase of $13,000, or 0.2% when compared to the $7.1 million reported for the same three months of the previous year.

The Company's net interest margin, as shown in Table 1, increased to 4.78% at March 31, 2010 from 4.48% at March 31, 2009, an increase of 30 basis points (100 basis points = 1%) between the two periods. While average market rates of interest have remained level between the three-month periods ended March 31, 2009 and 2010 (the Prime rate averaged 3.2% during both periods), significant declines in the Company's cost of funds enhanced the net margin between the two quarters.

Table 1. Distribution of Average Assets, Liabilities and Shareholders' Equity:
Interest rates and Interest Differentials
Three Months Ended March 31, 2010 and 2009

(dollars in thousands)	2010 Average Balance	Interest	Yield/ Rate	2009 Average Balance	Interest	Yield/ Rate
Assets:						
Interest-earning assets:						
Loans and leases (1)	$ 509,099	$ 7,540	6.01%	$ 542,512	$ 8,067	6.03%
Investment Securities – taxable	69,271	853	4.99%	89,676	1,190	5.38%
Investment Securities – nontaxable (2)	1,252	15	4.86%	1,252	15	4.86%
Interest-bearing deposits in other banks	2,555	10	1.59%	13,287	40	1.22%
	25,553	8	0.13%	10	0	0.00%

Federal funds sold and reverse repos				
Total interest-earning assets	607,730	$ 8,426	5.62%	646,737