PACWEST BANCORP
Form 10-K
March 02, 2015

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
Form 10-K
ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934
For the fiscal year ended December 31, 2014
Commission File No. 00-30747
PACWEST BANCORP
(Exact name of registrant as specified in its charter)

| | |
|---|---|
| Delaware | 33-0885320 |
| (State of Incorporation) | (I.R.S. Employer Identification No.) |

10250 Constellation Blvd., Suite 1640
Los Angeles, CA 90067
(Address of Principal Executive Offices, Including Zip Code)
(310) 286-1144
(Registrant's Telephone Number, Including Area Code)

| | |
|---|---|
| (Title of Each Class) | (Name of Exchange on Which Registered) |
| Common Stock, par value $0.01 per share | The Nasdaq Stock Market, LLC |

Securities Registered Pursuant to Section 12(g) of the Act: None
Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. þ Yes o No
Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. o Yes þ No
Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. þ Yes o No
Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). þ Yes o No
Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. o
Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of “large accelerated filer,” “accelerated filer” and “smaller reporting company” in Rule 12b-2 of the Exchange Act. (Check one):

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

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

As of June 30, 2014, the aggregate market value of the voting common stock held by non-affiliates of the registrant, computed by reference to the average high and low sales prices on The Nasdaq Global Select Market as of the close of business on June 30, 2014, was approximately $4.3 billion. Registrant does not have any nonvoting common equities.
As of February 9, 2015, there were 101,913,512 of registrant's common stock outstanding, excluding treasury shares and 1,108,505 shares of unvested restricted stock.
DOCUMENTS INCORPORATED BY REFERENCE
The information required by Items 10, 11, 12, 13 and 14 of Part III of this Annual Report on Form 10-K will be found in the Company's definitive proxy statement for its 2015 Annual Meeting of Stockholders, to be filed pursuant to Regulation 14A under the Securities Exchange Act of 1934, as amended, and such information is incorporated herein by this reference.

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# PART I
## ITEM 1. BUSINESS
### General
PacWest Bancorp, a Delaware corporation, is a bank holding company registered under the Bank Holding Company Act of 1956, as amended. Our principal business is to serve as the holding company for our wholly-owned subsidiary, Pacific Western Bank, which we refer to as “Pacific Western” or the “Bank.” We are focused on relationship-based business banking to small and middle-market businesses nationwide. The Company offers a broad range of deposit products and services through 80 full-service branches located throughout California. The Company, through offices across the United States, provides loans to middle-market businesses, real estate investment firms, and sophisticated individual real estate investors. References to “we,” “us,” or the “Company” refer to PacWest Bancorp together with its subsidiaries on a consolidated basis. When we refer to “PacWest” or to the “holding company,” we are referring to PacWest Bancorp, the parent company, on a stand-alone basis. References to “Pacific Western Bank” include the Bank’s wholly-owned subsidiaries.

We were established nearly 16 years ago in October 1999 and have achieved strong market positions by developing and maintaining extensive local relationships in the communities we serve. By leveraging our business focus, our service-driven focus, our presence in attractive markets, and maintaining a highly efficient operating model and robust approach to risk management, we have achieved significant and profitable growth, both organically and through disciplined acquisitions. We have successfully completed 27 acquisitions since 2000, including our 2014 acquisition of CapitalSource Inc. with approximately $9.4 billion in assets acquired.

As of December 31, 2014, we had total assets of over $16 billion, gross loans and leases of $11.9 billion, total deposits of $11.8 billion and stockholders’ equity of $3.5 billion. Loans and leases increased $7.6 billion during 2014 driven by the $6.9 billion of loans acquired in the CapitalSource Inc. merger and $682 million of organic loan growth resulting from $3.0 billion of loan production. The Bank’s non-performing assets as of December 31, 2014, totaled $152.6 million, or 0.9% of total assets, compared to $102.7 million, or 1.6% of total assets at December 31, 2013.

Our corporate headquarters is located in Los Angeles, California, and we have 80 full-service, retail bank branches located primarily in southern and central California and three branches in northern California. Our loan origination efforts are conducted nationwide with key offices located in Chevy Chase, Maryland, Southern California, including Los Angeles, St. Louis, Missouri, Denver, Colorado, Chicago, Illinois, New York, New York, and Midvale, Utah. We also maintain a number of smaller lending offices throughout the country.

For the year ended December 31, 2014, we operated as two business segments: Community Banking and National Lending.  The Community Banking segment is focused on the lending and deposit gathering activities conducted primarily through our California-based branch offices and our treasury management function. The National Lending segment comprises our CapitalSource Division through which we offer a broad range of specialized senior secured commercial loan products to small and middle-market businesses on a nationwide basis. For additional information, see “Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operations-Business Segments.”

### Current Developments
#### CapitalSource Inc. Merger
On April 7, 2014, PacWest merged with CapitalSource Inc. As part of the merger, CapitalSource Bank (“CSB”), a wholly-owned subsidiary of CapitalSource Inc., merged with and into Pacific Western. The assets and liabilities, both tangible and intangible, were recorded at their estimated fair values as of the merger date. The application of the acquisition method of accounting resulted in goodwill of $1.5 billion. We completed this merger in order to increase our loan and lease generation capabilities and to diversify our loan portfolio.

First California Financial Group Acquisition

On May 31, 2013, we acquired First California Financial Group, Inc. ("FCAL"). As part of this acquisition, First California Bank, a wholly-owned subsidiary of FCAL, merged with and into Pacific Western. The assets and liabilities, both tangible and intangible, were recorded at their estimated fair values as of the merger date. The application of the acquisition method of accounting resulted in goodwill of $129.1 million. We completed this acquisition to expand our presence in Southern California.

Our Business Strategy

General Overview

We believe that stable, long-term growth and profitability are the result of building strong customer relationships while maintaining disciplined underwriting standards. We continue to focus on originating high-quality loans and growing our low-cost deposit base through our relationship-based business lending. We believe that focusing on our core strengths will enable us to continue to maintain our operational efficiency and increase profitability, increase our core deposits and grow loans and leases in a sound manner.

Our loan portfolio consists primarily of commercial real estate loans, or "CRE" loans, commercial and industrial loans and leases, or "C&I" loans and leases, and, to a lesser extent, consumer loans. We pursue attractive growth opportunities to expand and enter new markets aligned with our business model and strategic plans. We will continue to opportunistically consider growth opportunities we believe exist in growing economies in and adjacent to our existing markets.

Our reputation, expertise and relationship-based banking model enable us to deepen our relationships with our customers. We look to leverage our relationships with existing customers by cross-selling our products and services, including attracting deposits from, and offering alternative cash management solutions to, our CapitalSource Division customers.

Focusing on operational efficiency is critical to our profitability and future growth. We intend to carefully manage our cost structure and continuously refine and implement internal processes and systems to create further efficiencies and enhance our earnings. We are also continuing our efforts to shift our deposit base from certificates of deposit to lower cost core deposits, a strategic initiative that was undertaken following the CapitalSource Inc. merger.

Our management team has extensive expertise and a successful track record in evaluating, executing and integrating attractive, franchise-enhancing acquisitions. We have successfully completed 27 acquisitions since 2000, including the $9.4 billion CapitalSource Inc. acquisition in 2014. We will continue to consider acquisitions that are consistent with our business strategy and financial model as opportunities arise.

The following chart summarizes the acquisitions completed since our inception:

| | Date | Institution/Company Acquired |
|---|---|---|
| (1) | May 2000 | Rancho Santa Fe National Bank |
| (2) | May 2000 | First Community Bank of the Desert |
| (3) | January 2001 | Professional Bancorp, Inc. |
| (4) | October 2001 | First Charter Bank |
| (5) | January 2002 | Pacific Western National Bank |
| (6) | March 2002 | W.H.E.C., Inc. |
| (7) | August 2002 | Upland Bank |
| (8) | August 2002 | Marathon Bancorp |
| (9) | September 2002 | First National Bank |
| (10) | January 2003 | Bank of Coronado |
| (11) | August 2003 | Verdugo Banking Company |
| (12) | March 2004 | First Community Financial Corporation |
| (13) | April 2004 | Harbor National Bank |
| (14) | August 2005 | First American Bank |
| (15) | October 2005 | Pacific Liberty Bank |
| (16) | January 2006 | Cedars Bank |
| (17) | May 2006 | Foothill Independent Bancorp |
| (18) | October 2006 | Community Bancorp Inc. |
| (19) | June 2007 | Business Finance Capital Corporation |
| (20) | November 2008 | Security Pacific Bank (deposits only)[1] |
| (21) | August 2009 | Affinity Bank[1] |
| (22) | August 2010 | Los Padres Bank[1] |
| (23) | January 2012 | Pacific Western Equipment Finance (formerly Marquette Equipment Finance) |
| (24) | April 2012 | Celtic Capital Corporation |
| (25) | August 2012 | American Perspective Bank |
| (26) | May 2013 | First California Financial Group, Inc.[2] |
| (27) | April 2014 | CapitalSource Inc. |

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(1) FDIC assisted.
(2) Includes assets covered by two FDIC loss sharing agreements.

Depository Products and Services

Deposits are our primary source of funds to support our revenue-generating assets, and our bank branch offices provide a source of low-cost funds and deposit-related fee income to support our continued operations. We offer traditional deposit products to businesses and other customers with a variety of rates and terms, including demand, money market, and time deposits. We also provide international banking services, multi-state deposit services and investment services, and out-of-service area services, as well as product offerings through other correspondent banks. The Bank’s deposits are insured by the Federal Deposit Insurance Corporation, or "FDIC," up to statutory limits.

Our branch network enhances our ability to gather deposits, expand our brand presence, service our customers’ needs, originate loans and leases and maintain our lending relationships. In addition, as the banking industry continues to experience broader customer acceptance of on-line and mobile banking tools for conducting basic banking functions, and which allows us to attract new depositors without a commensurate increase in branch traffic, we also serve our customers through a wide range of non-branch channels, including on-line and telephone banking platforms.

At December 31, 2014, we had ATMs at 62 of our branches and had another two company-owned ATMs at off-site locations located in California. We are part of the MoneyPass network, enabling our customers to take out cash surcharge-free and service charge-free at over 25,000 ATM locations across the country. We provide access to customer accounts via a 24 hour seven-day-a-week, toll-free, automated telephone customer service and secure on-line banking services.

We price our deposit products with a view to maximizing our share of each customer's financial services business and prudently managing our cost of funds. At December 31, 2014, our total deposits consisted of $6.1 billion in core deposits, $5.5 billion in time deposits and $0.2 billion in brokered non-maturity deposits. Core deposits represent 52% of total deposits at December 31, 2014, and are comprised of $2.9 billion in noninterest-bearing deposits, $0.7 billion in checking accounts, $1.7 billion in money market accounts and $0.8 billion in savings accounts. Our deposit base is also diversified by client type. As of December 31, 2014, no individual depositor represented more than 1.1% of our total deposits, and our top ten depositors represented 6.9% of our total deposits.

The composition of our deposit mix changed as a result of the CapitalSource Inc. merger with a lowered proportion of core deposits and a higher proportion of more expensive time deposits. This shift in deposit mix has been largely responsible for the recent increase in overall deposit cost. As a result of the CapitalSource Inc. merger and our ongoing deposit transformation initiatives, we established a dedicated team of professionals focused solely on growing our low-cost, customer deposit base by attracting deposits from our business customers and offering alternative cash management solutions intended to help retain business customers.

We face strong competition in gathering deposits. Our most direct competition for deposits comes from nationwide, regional, and local banks, savings banks and associations, credit unions, insurance companies, money market funds, brokerage firms, other non-bank financial services companies and service-focused community banks that target the same customers we do. We compete actively for deposits and emphasize solicitation of noninterest-bearing deposits. We seek to provide a higher level of personal service than is generally offered by our larger competitors, many of whom have more assets, capital and resources than we do and may be able to conduct more intensive and broader based promotional efforts to reach both commercial and retail customers. We also compete based on interest rates. Our cost of funds fluctuates with market interest rates and may be affected by higher rates being offered by other financial institutions. In certain interest rate environments, additional significant competition for deposits may be expected to arise from corporate and government debt securities and money market mutual funds. Competition for deposits is also affected by the ease with which customers can transfer deposits from one institution to another.

Lending Activities

Through the Bank, the Company concentrates its lending activities in three principal areas:

- Real Estate Loans
- Commercial and Industrial Loans and Leases
- Consumer Loans

The Bank's lending activity is governed by its comprehensive credit policies which consider lending regulations and prudent credit acceptance standards by loan product. The Bank prices its loans to preserve our interest spread and maintain our net interest margin ("NIM") for our various lending lines. While individual loans may be below the target based on risk or other factors, the lending lines are expected to meet NIM targets on an aggregate basis. The Bank strives for consistency in pricing similar transactions.

Real Estate Loans

The Bank provides real estate loans for the acquisition, refinancing and construction of commercial real estate to professional developers and real estate investors. The majority of the real estate loans are mini-perm loans collateralized by first deeds of trust on specific commercial properties. To a lesser extent, mini-perm loans may otherwise be collateralized by junior deeds of trust on specific commercial properties. Mini-perm loans are generally made with an amortization schedule ranging from 15 to 25 years with a lump sum balloon payment due in one to ten years. Mini-perm loans may also have an initial interest-only period followed by an amortization schedule with a lump sum balloon payment due in one to ten years. The Bank prices its loans to preserve our interest spread and maintain our net interest margin. Loan interest rates may be floating throughout the term or fixed. The rate on fixed-rate loans typically resets after the fifth year.

Construction loans finance from 50% to 70% of the costs to construct commercial or residential properties. The terms are generally two years. Home equity lines of credit are revolving lines of credit collateralized by junior deeds of trust on residential real estate properties.

The properties collateralizing real estate loans are located throughout the United States primarily in central business districts. However, our primary market areas for real estate loans are in California.

The Bank also makes real estate secured loans under the Small Business Administration's 7(a) Program and 504 Program. Compliant Small Business Administration (or "SBA") 7(a) loans have an SBA guaranty for 75% of the loan. SBA 504 loans are 50% loan-to-value first deed of trust mortgage loans on owner-occupied commercial real estate where a second deed of trust is also provided by a nonprofit certified development company.

The Bank's real estate portfolio is subject to certain risks including, but not limited to, the following:

- the economic conditions of the United States and Southern California;
- interest rate increases;
- decreased real estate values in the markets where we lend;
- increased competition in pricing and loan structure;
- the borrower's ability to refinance or payoff our loan upon maturity; and
- various environmental risks, including natural disasters.

In addition to the foregoing, construction loans are also subject to project specific risks including, but not limited to, the following:

- construction costs being more than anticipated;
- construction taking longer than anticipated;
- failure by developers and contractors to meet project specifications;
- disagreement between contractors, subcontractors and developers;
- demand for completed projects being less than anticipated;
- buyers of the completed projects not being unable to secure financing; and
- loss of our loan principal stemming from a collateral foreclosure.

The risks related to buyer inability to secure financing and loss through foreclosure are not controllable. When considering the markets in which to pursue real estate loans, we consider the market conditions, our current loan portfolio concentrations by property type and by market, and our past experience with the borrower, the specific market, and the property type.

When underwriting loans, we seek to mitigate risk by using the following framework:

- reviewing each loan request and renewal individually;
- using a credit committee approval process for the approval of each loan request over a certain dollar amount;
- adhering to written loan policies including, among other factors, minimum collateral requirements, maximum loan to value ratio requirements, cash flow requirements and full or partial guaranty requirements;
- obtaining independent third-party appraisals which are reviewed by the Bank's appraisal department;
- obtaining preliminary environmental risk assessments; and
- obtaining seismic studies where appropriate.

With respect to construction loans, in addition to the foregoing, we attempt to mitigate project specific risks by:

- implementing a controlled disbursement process for loan proceeds in accordance with an agreed upon schedule;
- conducting project site visits; and
- monitoring the construction costs compared to the budgeted costs and the remaining costs to complete.

SBA 7(a) and 504 program loans are subject to the risks outlined above and the risk that an SBA guaranty may be invalid if SBA specific procedures are not followed. We seek to mitigate this risk by maintaining and following additional policies specific to SBA loans which align with SBA requirements.

Commercial and Industrial Loans and Leases

Commercial and industrial loans and leases can be extended with a wide range of purposes, terms and maturities. The primary commercial and industrial loans and leases made by the Bank are in the form of working capital loans, loans to finance companies secured by finance receivables, equipment financings, term business loans, or loans to entities in conjunction with equity contributions from private equity groups to purchase businesses. The primary source of repayment of these loans and leases is the borrowers' cash flow from operations. Our underwriting practices assess the levels of the past, current, and budgeted cash flows from operations relative to a borrower's total debt service obligations which would include the full repayment of our loan principal and interest.

More specifically, within our commercial and industrial loan and lease activities are asset secured loans, cash flow secured loans, and equipment secured loans and leases. Asset secured loans are first liens on or interests in readily quantifiable collateral that the Bank believes can be liquidated. This collateral includes, but is not limited to, trade accounts receivable, loans receivable, or inventory. Cash flow secured loans are provided to sophisticated buyers and private equity groups, financial investors, strategic companies and sponsors to finance the acquisition or recapitalization of a business. Equipment secured loans and leases fund capital expenditures and are secured by equipment that is essential to the operations of the borrowers or lessees.

The Bank's portfolio of commercial loans and leases is subject to certain risks including, but not limited to, the following:

- the economic conditions of the United States;
- interest rate increases;
- deterioration of the value of the underlying collateral;
- increased competition in pricing and loan structure;
- the deterioration of a borrower's or guarantor's financial capabilities; and
- various environmental risks, including natural disasters, which can negatively affect a borrower's business.

When considering the types of businesses with which to pursue commercial and industrial loans and leases, we consider the prospects for the borrower's industry, our current loan portfolio concentration by loan type and collateral type, and our past experience with the borrower, the borrower's industry, and the collateral type. When underwriting loans, we attempt to mitigate risk by reviewing each loan request and renewal individually; using our credit committee approval process for the approval of each loan request over a certain dollar amount; and adhering to written loan underwriting policies and procedures.

We also, to a lesser extent, make SBA 7(a) loans secured by the value of a business and its equipment. These loans are subject to the risks outlined above and the risk that an SBA guaranty may be invalid if SBA specific procedures are not followed. We attempt to mitigate this risk by maintaining and following additional policies specific to SBA loans which align with SBA requirements.

Consumer Loans

Consumer loans include personal loans, auto loans, home equity lines of credit, revolving lines of credit, other loans typically made by banks to individual borrowers, and purchased 95% participation interests in student loans originated and serviced by a third-party lender. The Bank does not currently originate first trust deed home mortgage loans. The student loans that we purchased are not guaranteed by any program of the U.S. Government, and are made to refinance the outstanding student loan debt of borrowers who meet certain underwriting criteria, and have terms that fully amortize the debt over five, ten or fifteen years.

The Bank's consumer loan portfolio is subject to certain risks, including: amount of credit offered to consumers in the market; interest rate increases; and (with the exception of the purchased student loan portfolio), consumer bankruptcy laws which allow consumers to discharge certain debts. The Bank's student loan participation interests are also subject to further risks, including the ability of the sub-servicer to service the loans in accordance with the terms of the loan purchase agreement; and compliance with consumer lending regulations, additional regulations and oversight by the Consumer Financial Protection Bureau ("CFPB").

We seek to mitigate the exposure to such risks through the direct approval of all internally originated consumer loans by reviewing each loan request and renewal individually and adhering to written credit policies. For all purchased student loan participation interests, we monitor the performance of the originator and the enforcement of our rights under the loan purchase agreement.

Business Concentrations

The following table presents the composition of our loan portfolio as of the dates indicated:

| | December 31, 2014 | | December 31, 2013 | |
|---|---|---|---|---|
| | Amount | % of Total | Amount | % of Total |
| | (Dollars in thousands) | | | |
| Real estate mortgage: | | | | |
| Hospitality | $570,634 | 5 % | $181,735 | 4 % |
| SBA | 380,890 | 3 % | 45,166 | 1 % |
| Other | 4,645,478 | 39 % | 2,566,340 | 60 % |
| Total real estate mortgage | 5,597,002 | 47 % | 2,793,241 | 65 % |
| Real estate construction: | | | | |
| Residential | 96,749 | 1 % | 58,898 | 1 % |
| Commercial | 217,297 | 2 % | 159,308 | 4 % |
| Total real estate construction | 314,046 | 3 % | 218,206 | 5 % |
| Total real estate | 5,911,048 | 50 % | 3,011,447 | 70 % |
| Commercial: | | | | |
| Collateralized | 439,567 | 4 % | 587,326 | 13 % |
| Unsecured | 131,939 | 1 % | 153,881 | 4 % |
| Asset-based | 1,794,907 | 15 % | 202,428 | 5 % |
| Cash flow | 2,486,411 | 21 % | — | — % |
| Equipment finance | 969,489 | 8 % | 273,483 | 6 % |
| SBA | 47,304 | — % | 28,641 | 1 % |
| Total commercial | 5,869,617 | 49 % | 1,245,759 | 29 % |
| Consumer | 101,767 | 1 % | 55,146 | 1 % |
| Total gross loans and leases[(1)] | $11,882,432 | 100 % | $4,312,352 | 100 % |

(1) Includes purchased credit impaired ("PCI") loans of $290.8 million and $382.8 million at December 31, 2014 and 2013, of which the majority are included in the Real Estate Mortgage - "Other" category in this table.

Real estate mortgage loans and real estate construction loans (which are predominantly commercial real estate loans) together comprised 50% and 70% of our total portfolio at December 31, 2014 and December 31, 2013, The decline in real estate loans as a percentage of total loans was attributable to commercial loans acquired in connection with the CapitalSource Inc. merger and net loan originations and repayment activity throughout 2014.

The commercial real estate mortgage loans are diversified among various property types. At December 31, 2014, our largest property type concentration was healthcare property, totaling $1.0 billion or 19% of real estate mortgage loans. Healthcare property types include skilled nursing facilities, hospitals, assisted living facilities, independent living facilities, and owner-occupied medical office facilities. At December 31, 2013, healthcare property totaled $189.7 million and comprised 7% of real estate mortgage loans. The increase in healthcare real estate mortgage loans from December 31, 2013 to December 31, 2014 is attributable to loans acquired in the CapitalSource Inc. merger and loans originated during 2014.

Other significant real estate concentrations were office properties at 14% and 16% of real estate mortgage loans at December 31, 2014 and December 31, 2013, and multi-family properties at 14% and 12% of real estate mortgage loans at December 31, 2014 and December 31, 2013.

Commercial loans and leases comprised 49% and 29% of our total portfolio at December 31, 2014 and December 31, 2013. The increase in the commercial loan and lease portfolio composition from 29% to 49% is attributable to commercial loans acquired in connection with the CapitalSource Inc. merger and net loan originations and repayment activity throughout 2014.

The commercial loans and leases are diversified among various loan types and industries. At December 31, 2014, our largest commercial loan type concentration was cash flow loans, totaling $2.5 billion or 21% of our total portfolio. Cash flow secured loans are provided to sophisticated buyers and private equity groups, financial investors, strategic companies and sponsors to finance the acquisition or recapitalization of a business. The cash flow loans outstanding at December 31, 2014 are attributable to loans acquired in the CapitalSource Inc. merger and loans originated by the CapitalSource Division during 2014. Other significant commercial concentrations were asset-based loans at 15% and 5% of the total portfolio at December 31, 2014 and December 31, 2013, and equipment finance at 8% and 6% of the total portfolio at December 31, 2014 and December 31, 2013. Asset-based loans are first liens on or interests in readily quantifiable collateral. This collateral includes, but is not limited to, trade accounts receivable, loans receivable, or inventory.

Financing

We depend on deposits and external financing sources to fund our operations. We employ a variety of financing arrangements, including term debt, subordinated debt and equity. As a member of the Federal Home Loan Bank of San Francisco (“FHLB”), the Bank had financing availability with the FHLB as of December 31, 2014 of $2.4 billion, or 15% of the Bank's total assets, subject to pledging adequate collateral.

Information Technology Systems

We devote significant resources to maintain stable, reliable, efficient and scalable information technology systems. Where possible, we utilize third-party software systems that are hosted and supported by nationally recognized vendors. We selectively employ proprietary software systems to support our specialty lending products. We work with our third-party vendors to monitor and maximize the efficiency of our use of their applications. We use integrated systems to originate and process loans and deposit accounts, which reduces processing time, improves customer experiences and reduces costs. Most customer records are maintained digitally. We are also currently executing several initiatives to enhance our on-line and telephone banking services to further improve the overall client experience.

Protecting our systems to ensure the safety of our customers’ information is critical to our business. We use multiple layers of protection to control access and reduce risk, including conducting a variety of audits and vulnerability and penetration tests on our platforms, systems and applications to reduce the risk that any attacks are successful. To protect against disasters, we have a backup offsite core processing system and recovery plans.

We invested in an enterprise data warehouse system in order to capture, analyze and report key metrics associated with customer and product profitability. Data that previously was arduous to collect across multiple systems is now available daily through standard and ad hoc reports to assist with managing our business and competing effectively in the marketplace.

Risk Oversight and Management

We believe risk management is another core competency of our business. We have a comprehensive risk management process that monitors, evaluates and manages the risks we assume in conducting our activities. Our oversight of this risk management process is conducted through the responsibilities of certain of the Company’s Board of Directors (the “Board”) standing committees. The committees each report to the Board and the Board has overall oversight responsibility with respect to risk awareness and risk management.

Our risk framework is structured to guide decisions regarding the appropriate balance between risk and return considerations in our business. Our risk framework is informed by our strategy, risk appetite and financial plans approved by our Board. This framework includes risk policies, procedures, measured and reported limits and targets, and reporting. Our Board approves our risk appetite statement, which sets forth the amount and type of risks we are willing to accept in pursuit of achieving our strategic, business and financial objectives. Our risk appetite statement provides the context for our risk management tools, including, among others, risk policies, delegated authorities, limits, portfolio composition, underwriting standards and operational processes.

Competition

The banking business in California, and specifically in the Bank’s primary service areas and lending markets, is highly competitive.The Bank competes for loans, deposits and customers nationwide with other commercial banks and financial services institutions. Some of these competitors are larger in total assets and capitalization, with more offices over a wider geographic area and offer a broader range of financial services than the Bank. Our most direct competition for loans comes from larger regional and national banks, savings banks and associations, credit unions, insurance companies and service-focused community banks that target the same customers we do. In recent years, competition has increased from institutions not subject to the same regulatory restrictions as domestic banks and bank holding companies. Those competitors include savings and loan associations, brokerage houses, insurance companies, mortgage companies, credit unions, credit card companies, and other financial and non-financial institutions and entities.

Economic factors, along with legislative and technological changes, will have an ongoing impact on the competitive environment within the financial services industry. We work to anticipate and adapt to dynamic competitive conditions whether it is by developing and marketing innovative products and services, adopting or developing new technologies that differentiate our products and services, cross marketing, or providing highly personalized banking services. We strive to distinguish ourselves from other community banks and financial services providers in our marketplace by providing an extremely high level of service to enhance customer loyalty and to attract and retain business. However, we can provide no assurance as to the effectiveness of these efforts on our future business or results of operations, as to our continued ability to anticipate and adapt to changing conditions, and as to sufficiently improving our services and/or banking products in order to successfully compete in our primary service areas.

We compete for loans principally through the quality of service we provide to borrowers while maintaining competitive interest rates, loan fees and other loan terms. We emphasize personalized relationship banking services and the local and efficient decision-making of our banking businesses. Because of economies of scale, our larger, nationwide competitors may offer loan pricing that is more attractive than what we can offer.

Competition is based on a number of factors, including: interest rates charged on loans and paid on deposits, the scope and type of banking and financial services offered, convenience of our branch locations, customer service, technological changes and regulatory constraints. Many of our competitors are large companies that have substantial capital, technological and marketing resources. Some of our competitors have substantial market positions and have access to a lower cost of capital or a less expensive source of funds. We principally compete based on:

- in-depth knowledge of our borrowers' industries and their business needs based upon information received from our borrowers' key decision-makers, analysis by our experienced professionals and interaction between these two groups;
- our breadth of loan product offerings and flexible and creative approach to structuring products that meet our borrowers' business and timing needs; and
- our dedication to superior client service.

Employees

As of January 30, 2015, we had 1,443 full time equivalent employees.

Financial and Statistical Disclosure

Certain of our statistical information is presented within “Item 6. Selected Financial Data,” “Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operations,” and “Item 7A. Qualitative and Quantitative Disclosure About Market Risk.” This information should be read in conjunction with the consolidated financial statements contained in “Item 8. Financial Statements and Supplementary Data.”

## Supervision and Regulation

### General

The Company is subject to extensive regulation under federal and state banking laws that establish a comprehensive framework for our operations. Such regulation is intended, among other things, to protect the interests of customers, including depositors, and the federal deposit insurance fund, as well as to minimize risk to the banking system as a whole. These regulations are not, however, generally charged with protecting the interests of our stockholders or creditors. Described below are the material elements of selected laws and regulations applicable to our Company. The descriptions are not intended to be complete and are qualified in their entirety by reference to the full text of the statutes and regulations described. Changes in applicable law or regulations, and in their application by regulatory agencies, cannot be predicted, but they may have a material effect on the business and results of our Company.

Our business is also influenced by the monetary and fiscal policies of the federal and state governments in those states in which we operate. In addition, we adhere to the policies of the Board of Governors of the Federal Reserve System (the "FRB"). The FRB implements national monetary policies (with the dual mandate of price stability and maximum employment) by its open market operations in United States Government securities, by adjusting the required level of and paying interest on reserves for financial intermediaries subject to its reserve requirements and by varying the discount rates applicable to borrowings by depository institutions. The actions of the FRB in these areas influence the growth of bank loans, investments and deposits and also affect interest rates charged on loans and paid on deposits. Indirectly, such actions may also impact the ability of non bank financial institutions to compete with the Bank. The nature and impact of any future changes in monetary policies cannot be predicted.

The events of the past several years have led to numerous new laws for financial institutions in the United States and internationally. The Dodd Frank Wall Street Reform and Consumer Protection Act (the “Dodd Frank Act” or “Dodd Frank”), which was enacted in July 2010, significantly restructured the financial regulatory landscape in the United States, including the creation of a new systemic risk oversight body, the Financial Stability Oversight Council (the “FSOC”). The FSOC oversees and coordinates the efforts of the primary U.S. financial regulatory agencies (including the FRB, the Securities and Exchange Commission (“SEC”), the Commodity Futures Trading Commission and the FDIC) in establishing regulations to address financial stability concerns. In addition to the systemic risk oversight framework implemented through the FSOC, the Dodd Frank Act broadly affected the financial services industry by creating a resolution authority, mandating higher capital and liquidity requirements, mandating risk management requirements, requiring banks to pay increased fees to regulatory agencies, establishing the CFPB, and establishing numerous other provisions aimed at strengthening the sound operation of the financial services sector. As discussed further throughout this section, some aspects of Dodd Frank continue to be subject to rulemaking and will take effect over several additional years, making it difficult to anticipate the overall financial impact on the Company or across the industry.

The Dodd-Frank Act and the FRB’s implementing regulations impose increasingly stringent regulatory requirements on financial institutions as their size and scope of activities increases. With the April 7, 2014 CapitalSource Inc. merger, the Company’s total consolidated assets exceeded $15 billion, which subjects the Company to additional regulatory requirements for financial institutions with over $10 billion in total consolidated assets. This substantially increased the regulations we are required to meet, particularly with respect to risk management, capital planning, and stress testing in various parts of the Company and the Bank. In addition, the Company and the Bank are now subject to the examination and supervision of the CFPB.

### Bank Holding Company Regulation

As a bank holding company, PacWest is registered with and subject to supervision, regulation and examination by the FRB under the Bank Holding Company Act of 1956, as amended, or "BHCA." FRB policy historically has required bank holding companies to act as a source of financial strength to their bank subsidiaries and to commit capital and financial resources to support those subsidiaries in circumstances where it might not be in our, or our stockholders’ or creditors’, best interest to do so. The Dodd Frank Act codified this policy as a statutory requirement. Under this requirement, the Company is expected to commit resources to support the Bank, including at times when we may not be in a financial position to do so. Similarly, under the cross guarantee provisions of the Federal Deposit Insurance Act, or "FDIA," the FDIC can hold any FDIC insured depository institution liable for any loss suffered or anticipated by the FDIC in connection with (i) the default of a commonly controlled FDIC insured depository institution or (ii) any assistance provided by the FDIC to such a commonly controlled institution. We are also required to file with the FRB periodic reports of our operations and such additional information regarding the Company and its subsidiaries as the FRB may require.

Pursuant to the BHCA, we are required to obtain the prior approval of the FRB before we acquire all or substantially all of the assets of any bank or the ownership or control of voting shares of any bank if, after giving effect to such acquisition, we would own or control, directly or indirectly, more than 5 percent of such bank. Pursuant to the Bank Merger Act, the prior approval of the FDIC is required for our bank to merge with another bank or purchase all or substantially all of the assets or assume any of the deposits of another FDIC-insured depository institution. In reviewing applications seeking approval of merger and acquisition transactions, bank regulators consider, among other things, the competitive effect and public benefits of the transactions, the capital position and managerial resources of the combined organization, the risks to the stability of the U.S. banking or financial system, the applicant's performance record under the Community Reinvestment Act of 1977, or "CRA," the applicant's compliance with fair housing and other consumer protection laws, and the effectiveness of all organizations involved in combating money laundering activities. In addition, failure to implement or maintain adequate compliance programs could cause bank regulators not to approve an acquisition where regulatory approval is required or to prohibit an acquisition even if approval is not required. Our ability to engage in certain merger or acquisition transactions, whether or not any regulatory approval is required, will be dependent upon our regulators' assessment of the foregoing factors.

Under the BHCA, we may not engage in any business other than managing or controlling banks or furnishing services to our subsidiaries and such other activities that the FRB deems to be so closely related to banking as "to be a proper incident thereto." We are also prohibited, with certain exceptions, from acquiring direct or indirect ownership or control of more than 5 percent of the voting shares of any company unless the company is engaged in banking activities or the FRB determines that the activity is so closely related to banking as to be a proper incident to banking. The FRB's approval must be obtained before the shares of any such company can be acquired and, in certain cases, before any approved company can open new offices.

Additionally, bank holding companies that meet certain eligibility requirements prescribed by the BHCA and elect to operate as financial holding companies may engage in, or own shares in companies engaged in, a wider range of nonbanking activities, including securities and insurance activities and any other activity that the FRB, in consultation with the Secretary of the Treasury, determines by regulation or order is financial in nature, incidental to any such financial activity or complementary to any such financial activity and does not pose a substantial risk to the safety or soundness of depository institutions or the financial system generally. As of the date of this filing, we have not elected to be treated as a financial holding company. and currently have no plans to make a financial holding company election.

Our earnings and activities are affected by legislation, by regulations and by local legislative and administrative bodies and by decisions of courts in the jurisdictions in which we and the Bank conduct business. For example, these activities include limitations on the ability of the Bank to pay dividends to us and our ability to pay dividends to our stockholders. It is the policy of the FRB that bank holding companies should pay cash dividends on common stock only out of income available over the past year and only if prospective earnings retention is consistent with the organization's expected future needs and financial condition. The policy provides that bank holding companies should not maintain a level of cash dividends that undermines the bank holding company's ability to serve as a source of strength to its banking subsidiaries. Various federal and state statutory provisions limit the amount of dividends that our subsidiary Bank can pay to us without regulatory approval. The BHCA and regulations of the FRB also impose certain constraints on the redemption or purchase by a bank holding company of its own shares of stock.

In addition to these explicit limitations, the federal regulatory agencies have general authority to prohibit a banking subsidiary or bank holding company from engaging in an unsafe or unsound banking practice. Depending upon the circumstances, the agencies could take the position that paying a dividend would constitute an unsafe or unsound banking practice. Further, as discussed below under "-Capital Requirements," a bank holding company, such as the Company, is required to maintain minimum ratios of Common Equity Tier 1 capital, Tier 1 capital, and total capital to total risk weighted assets, and a minimum ratio of Tier 1 capital to total adjusted quarterly average assets as defined in such regulations. The level of our capital ratios may affect our ability to pay dividends or repurchase our shares. See "Item 5. Market for Registrant's Common Equity and Related Stockholder Matters-Dividends" and Note 20, Dividend Availability and Regulatory Matters, of the Notes to Consolidated Financial Statements contained in "Item 8. Financial Statements and Supplementary Data."

Transactions between the Bank and its subsidiaries, on the one hand, or PacWest and any subsidiary, on the other hand, are regulated under federal banking law. Subject to certain exceptions set forth in the Federal Reserve Act, a bank can make a loan or extend credit to an affiliate, purchase or invest in the securities of an affiliate, purchase assets from an affiliate, accept securities of an affiliate as collateral for a loan or extension of credit to any person or company, issue a guaranty, accept letters of credit on behalf of an affiliate, or enter into derivative transactions with credit exposures with an affiliate only if the aggregate amount of the above transactions of such subsidiary does not exceed 10 percent of such subsidiary's capital stock and surplus on an individual basis or 20 percent of such subsidiary's capital stock and surplus on an aggregate basis. Such transactions must be on terms and conditions that are consistent with safe and sound banking practices and at least as favorable to our bank as if the transaction were conducted with an unaffiliated third party. A bank and its subsidiaries generally may not purchase a "low quality asset," as that term is defined in the Federal Reserve Act, from an affiliate. Such restrictions also prevent a holding company and its other affiliates from borrowing from a banking subsidiary of the holding company unless the loans are secured by collateral. The Dodd Frank Act significantly expanded the coverage and scope of the limitations on affiliate transactions within a banking organization.

The FRB has cease and desist powers over parent bank holding companies and non banking subsidiaries where the action of a parent bank holding company or its non financial institution subsidiaries represents an unsafe or unsound practice or violation of law. The FRB has the power to order any bank holding company or its subsidiaries to terminate any activity or to terminate its ownership or control of any subsidiary when the FRB has reasonable grounds to believe that continuing such activity, ownership or control constitutes a serious risk to the financial soundness, safety or stability of any bank subsidiary of the bank holding company.

In October 2012, as required by the Dodd-Frank Act, the FRB and FDIC published final rules regarding company-run stress testing. The rules require institutions, such as the Company and the Bank, with average total consolidated assets greater than $10 billion to conduct an annual company-run stress test of capital, consolidated earnings and losses under one base scenario and at least two stress scenarios provided by the federal bank regulators. Stress test results must be reported to the regulatory agencies, and the stress testing rules require the public disclosure of a summary of the stress test results. The Company's and Bank's capital ratios reflected in the stress test calculations will be an important factor considered by the FRB and FDIC in evaluating the capital adequacy of the Company and the Bank, respectively, and whether any proposed payments of dividends or stock repurchases may be deemed an unsafe or unsound practice. The Company will be required to publish its first stress test results in July 2016.

The Dodd Frank Act requires the federal financial regulatory agencies to adopt rules that prohibit banks and their affiliates from engaging in proprietary trading and investing in and sponsoring certain unregistered investment companies (hedge funds and private equity funds, defined as "covered funds"). The statutory provision is commonly called the "Volcker Rule". On December 10, 2013, the federal financial regulatory agencies adopted final rules implementing the Volcker Rule, and, in connection with the final Volcker Rule, the FRB granted a blanket one year extension of the Volcker Rule conformance period so that banking organizations had until July 21, 2015 to fully comply with most requirements of the Volcker Rule. On December 18, 2014, the FRB granted a second one-year extension of the Volcker Rule conformance period to July 21, 2016 for existing investments in and relationships with covered funds (relationships existing prior to December 31, 2013). A similar one-year extension by the FRB is expected to further extend the Volcker Rule conformance period to July 21, 2017. We do not currently anticipate that the Volcker Rule will have a material effect on our operations. Because many of the effects of the Volcker Rule may become apparent only over several years as the federal financial regulatory agencies apply the rule in practice, the precise financial impact of the rule on the Company, its customers or the financial industry more generally cannot currently be determined.

Dividends

The ability of the Company to pay dividends on its common stock, and the ability of the Bank to pay dividends to the Company, may be restricted due to several factors including: (a) the Delaware General Corporation Law, (b) covenants contained in our subordinated debentures and borrowing agreements, and (c) the regulatory authority of the FRB and the California Department of Business Oversight, or "DBO."

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Our ability to pay dividends to our stockholders is subject to the restrictions set forth in the Delaware General Corporation Law, or "DGCL." The DGCL provides that a corporation, unless otherwise restricted by its certificate of incorporation, may declare and pay dividends out of its surplus or, if there is no surplus, out of net profits for the fiscal year in which the dividend is declared and/or for the preceding fiscal year, as long as the amount of capital of the corporation is not less than the aggregate amount of the capital represented by the issued and outstanding stock of all classes having a preference upon the distribution of assets. Surplus is defined as the excess of a corporation’s net assets (i.e., its total assets minus its total liabilities) over the capital associated with issuances of its common stock. Moreover, DGCL permits a board of directors to reduce its capital and transfer such amount to its surplus. In determining the amount of surplus of a Delaware corporation, the assets of the corporation, including stock of subsidiaries owned by the corporation, must be valued at their fair market value as determined by the board of directors, regardless of their historical book value.

Our ability to pay cash dividends to our stockholders may be limited by certain covenants contained in the indentures governing trust preferred securities issued by us or entities that we have acquired, and the debentures underlying the trust preferred securities. Generally the indentures provide that if an Event of Default (as defined in the indentures) has occurred and is continuing, or if we are in default with respect to any obligations under our guarantee agreement which covers payments of the obligations on the trust preferred securities, or if we give notice of any intention to defer payments of interest on the debentures underlying the trust preferred securities, then we may not, among other restrictions, declare or pay any dividends with respect to our common stock.

The unsecured borrowing facility at the parent company may also limit our ability to pay cash dividends to our stockholders if an Event of Default (as defined in the credit agreement) has occurred and is continuing.

Notification to the FRB is also required prior to our declaring and paying a cash dividend to our stockholders during any period in which our quarterly and/or cumulative twelve month net earnings are insufficient to fund the dividend amount, among other requirements. Under such circumstances, we may not pay a dividend should the FRB object until such time as we receive approval from the FRB or no longer need to provide notice under applicable regulations.

Holders of Company common stock may receive dividends declared by the Board of Directors out of funds legally available under state law governing the Company and certain federal laws and regulations governing the banking and financial services business. Our Board of Directors will take into account such matters as general business conditions; our financial results; projected cash flows; capital requirements; contractual, legal and regulatory restrictions on the payment of dividends by us to our stockholders or by our subsidiary to the holding company; and such other factors as our Board of Directors may deem relevant. During 2014, 2013, and 2012, the Company paid $114.3 million, $41.0 million, and $28.8 million in cash dividends on common stock. We can provide no assurance that we will continue to declare dividends on a quarterly basis or otherwise. The declaration of dividends by the Company is subject to the discretion of our Board of Directors.

PacWest’s primary source of liquidity is the receipt of cash dividends from Pacific Western. Various statutes and regulations limit the availability of cash dividends from Pacific Western. It is possible, depending upon the financial condition of the bank in question, and other factors, that the FRB, the FDIC or the DBO could assert that payment of dividends or other payments is an unsafe or unsound practice. Pacific Western is subject to restrictions under certain federal and state laws and regulations governing banks which limit its ability to transfer funds to the holding company through intercompany loans, advances or cash dividends.

Dividends paid by state banks, such as Pacific Western, are regulated by the DBO and FDIC under their general supervisory authority as it relates to a bank’s capital requirements. A state bank may declare a dividend without the approval of the DBO and FDIC as long as the total dividends declared in a calendar year do not exceed either the retained earnings or the total of net earnings for three previous fiscal years less any dividend paid during such period. During 2014, 2013, and 2012, the Bank paid $137.0 million, $48.0 million, and $50.0 million in dividends to the Company. For the foreseeable future, any further cash dividends from the Bank to the Company will require DBO and FDIC approval.

See “Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operations-Liquidity” and Note 20, Dividend Availability and Regulatory Matters, of the Notes to Consolidated Financial Statements contained in “Item 8. Financial Statements and Supplementary Data” for a discussion of other factors affecting the availability of dividends and limitations on the ability to declare dividends.

Capital Requirements

The Company is subject to consolidated regulatory capital requirements administered by the FRB, and the Bank is subject to similar capital requirements administered by the FDIC. The Dodd Frank Act applies the same leverage and risk based capital requirements that apply to insured depository institutions to bank holding companies, such as the Company. The guidelines of the FRB and FDIC are intended to ensure that banking organizations have adequate capital given the risk levels of assets and off balance sheet financial instruments.

General Risk Based Capital Rules. Prior to January 1, 2015, the FDIC and FRB risk-based capital guidelines were based upon the 1988 Capital Accord ("Basel I") of the Basel Committee on Banking Supervision (the "Basel Committee"). The Basel Committee is a committee of central banks and bank supervisors/regulators from the major industrialized countries that develops broad policy guidelines that each country's supervisors can use to determine the supervisory policies that apply.

Under the general risk-based capital rules, applicable through December 31, 2014, banking organizations are required to maintain minimum ratios of Tier 1 capital and total capital to total risk weighted assets (including certain off balance sheet items, such as letters of credit). For purposes of calculating the ratios, a banking organization's assets and some of its specified off balance sheet commitments and obligations are assigned to various risk categories. A depository institution's or holding company's capital, in turn, is classified in one of two tiers relevant to us, depending on type:

Core Capital (Tier 1). Tier 1 capital includes common equity, retained earnings, qualifying non cumulative perpetual preferred stock, a limited amount of qualifying cumulative perpetual stock at the holding company level, minority interests in equity accounts of consolidated subsidiaries, and qualifying trust preferred securities (subject to phase out as described under "-Basel III Capital Rules" below) minus goodwill, most intangible assets and certain other assets.

Supplementary Capital (Tier 2). Tier 2 capital includes, among other things, perpetual preferred stock and trust preferred securities not meeting the Tier 1 definition, qualifying mandatory convertible debt securities, qualifying subordinated debt, and allowances for possible credit losses, subject to limitations.

As a bank holding company, the Company currently is required to maintain Tier 1 capital and total capital equal to at least 4.0% and 8.0%, respectively, of its total risk weighted assets (including various off balance sheet items, such as letters of credit). The Bank is required to maintain equivalent capital levels under the FDIC's capital adequacy guidelines. In addition, as a depository institution, the Bank is subject to minimum capital ratios under the regulatory framework for prompt corrective action discussed under "-Prompt Corrective Action."

The Company and the Bank are also required to comply with minimum leverage ratio requirements. The leverage ratio is the ratio of a banking organization's Tier 1 capital to its total adjusted quarterly average assets (as defined for regulatory purposes). Bank holding companies and FDIC supervised banks, such as the Company and the Bank, respectively, are required to maintain a minimum leverage ratio of 4.0%, unless a different minimum is specified by an appropriate regulatory authority. In addition, for a depository institution to be considered "well capitalized" under the regulatory framework for prompt corrective action, its leverage ratio must be at least 5.0%.

Regulatory capital requirements limit the amount of deferred tax assets that may be included when determining the amount of regulatory capital. Deferred tax asset amounts in excess of the calculated limit are deducted from regulatory capital. See "Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations-Capital Resources-Capital" for further information on regulatory capital requirements, capital ratios, and deferred tax asset limits as of December 31, 2014 for Pacific Western Bank and the Company.

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The Company issued subordinated debentures to trusts that were established by us or entities we have acquired, which, in turn, issued trust preferred securities. The amount of subordinated debentures totaled $433.6 million at December 31, 2014 and includes $300.4 million of debentures assumed in connection with the CapitalSource Inc. merger. The Company includes in Tier 1 capital an amount of trust preferred securities equal to no more than 25% of the sum of all core capital elements, which is generally defined as shareholders' equity less goodwill, net of any related deferred income tax liability. At December 31, 2014, the amount of trust preferred securities included in Tier I capital was $131.0 million. The acquired CapitalSource Inc. trust preferred securities are ineligible for inclusion in Tier 1 capital but are included in Tier 2 capital. The $131.0 million of trust preferred securities are currently grandfathered as Tier 1 capital under the Dodd-Frank Act. However, under new capital rules approved by the FRB and FDIC in July 2013, described below under "-Basel III Capital Rules," as a result of the Company having exceeded $15 billion in consolidated total assets, beginning in 2015 only 25% of the Company's $131.0 million of trust preferred securities currently outstanding will be included in Tier 1 capital, and in 2016, none of the Company's trust preferred securities will be included in Tier 1 capital. Further, under such rules, trust preferred securities no longer included in the Company's Tier 1 capital may be included as a component of Tier 2 capital on a permanent basis without phase-out. If the $131.0 million of trust preferred securities are excluded from regulatory capital, we remain "well capitalized" at December 31, 2014.

Basel III Capital Rules. In July 2013, the Company's primary federal regulator, the FRB, and the Bank's primary federal regulator, the FDIC, approved final rules (the "New Capital Rules") establishing a new comprehensive capital framework for U.S. banking organizations. The New Capital Rules generally implement the Basel Committee's December 2010 final capital framework referred to as "Basel III" for strengthening international capital standards. The New Capital Rules substantially revise the risk based capital requirements applicable to bank holding companies and their depository institution subsidiaries, including the Company and the Bank, as compared to the current U.S. general risk based capital rules. The New Capital Rules revise the definitions and the components of regulatory capital, as well as address other issues affecting the numerator in banking institutions' regulatory capital ratio calculations. The New Capital Rules also address asset risk weights and other matters affecting the denominator in banking institutions' regulatory capital ratio calculations and replace the existing general risk weighting approach, which was derived from the Basel Committee's 1988 "Basel I" capital accords, with a more risk sensitive approach based, in part, on the "standardized approach" in the Basel Committee's 2004 "Basel II" capital accords. The New Capital Rules also implement the requirements of Section 939A of the Dodd Frank Act to remove references to credit ratings from the federal regulators' rules. The New Capital Rules were effective for the Company and the Bank as of January 1, 2015, subject to phase in periods for certain of their components and other provisions.

The New Capital Rules, among other things, (i) introduce a new capital measure called Common Equity Tier 1 ("CET1") and related regulatory capital ratio of CET1 to risk weighted assets, (ii) specify that Tier 1 capital consists of CET1 and "Additional Tier 1 capital" instruments meeting certain revised requirements, (iii) mandate that most deductions/adjustments to regulatory capital measures be made to CET1 and not to the other components of capital, and (iv) expand the scope of the deductions from and adjustments to capital as compared to existing regulations.

Under the New Capital Rules, for most banking organizations the most common form of Additional Tier 1 capital is non cumulative perpetual preferred stock and the most common form of Tier 2 capital is subordinated notes and a portion of the allowance for loan and lease losses, in each case, subject to the New Capital Rules' specific requirements.

Pursuant to the New Capital Rules, the minimum capital ratios as of January 1, 2015 are as follows:

- 4.5% CET1 to risk weighted assets;
- 6.0% Tier 1 capital (that is, CET1 plus Additional Tier 1 capital) to risk weighted assets;
- 8.0% Total capital (that is, Tier 1 capital plus Tier 2 capital) to risk weighted assets; and
- 4% Tier 1 capital to average consolidated assets as reported on regulatory financial statements (known as the "leverage ratio").

The New Capital Rules also introduce a new "capital conservation buffer", composed entirely of CET1, on top of these minimum risk weighted asset ratios. The capital conservation buffer is designed to absorb losses during periods of economic stress. Banking institutions with a ratio of CET1 to risk weighted assets above the minimum but below the capital conservation buffer will face constraints on dividends, equity repurchases and compensation based on the amount of the shortfall. The implementation of the capital conservation buffer will begin on January 1, 2016 at a 0.625% level and increase by 0.625% on each subsequent January 1, until it reaches 2.5% on January 1, 2019. When fully phased in, the Company and the Bank will be required to maintain such additional capital conservation buffer of 2.5% of CET1, effectively resulting in minimum ratios of (i) CET1 to risk weighted assets of at least 7%, (ii) Tier 1 capital to risk weighted assets of at least 8.5%, and (iii) Total capital to risk weighted assets of at least 10.5%.

The New Capital Rules provide for a number of deductions from and adjustments to CET1. These include, for example, the requirement that mortgage servicing rights, deferred tax assets arising from temporary differences that could not be realized through net operating loss carrybacks and significant investments in non consolidated financial entities be deducted from CET1 to the extent that any one such category exceeds 10% of CET1 or all such items, in the aggregate, exceed 15% of CET1.

In addition, under the current general risk based capital rules, the effects of accumulated other comprehensive income or loss ("AOCI") items included in shareholders' equity (for example, unrealized gains and losses of securities held in the available-for-sale portfolio) under U.S. GAAP are reversed for the purposes of determining regulatory capital ratios. Pursuant to the New Capital Rules, the effects of certain AOCI items are not excluded; however, non advanced approaches banking organizations, including the Company and the Bank, may make a one time permanent election to continue to exclude these items. This election must be made concurrently with the first filing of certain of the Company's and the Bank's periodic regulatory reports in the beginning of 2015. The Company and the Bank expect to make this election in order to avoid significant variations in the level of capital depending upon the impact of interest rate fluctuations on the fair value of our securities portfolio.

Implementation of the deductions and other adjustments to CET1 commenced on January 1, 2015 and will be phased in over a 4 year period (beginning at 40% on January 1, 2015 and an additional 20% per year thereafter).

With respect to the Bank, the New Capital Rules revised the prompt corrective action regulations as described below under "-Prompt Corrective Action".

The New Capital Rules prescribe a new standardized approach for risk weightings that expand the risk weighting categories from the current four Basel I derived categories (0%, 20%, 50% and 100%) to a larger and more risk sensitive number of categories, depending on the nature of the assets, generally ranging from 0% for U.S. government and agency securities, to 600% for certain equity exposures, resulting in higher risk weights for a variety of asset classes.

We are continuing to evaluate the impact of the New Capital Rules on our capital ratios and related calculations. We believe that, as of December 31, 2014, the Company and the Bank would remain "well-capitalized" under the New Capital Rules as if such requirements had been in effect.

Liquidity Requirements. Historically, regulation and monitoring of bank and bank holding company liquidity has been addressed as a supervisory matter, both in the U.S. and internationally, without required formulaic measures. The Basel III framework requires banks and bank holding companies to measure their liquidity against specific liquidity tests that, although similar in some respects to liquidity measures historically applied by banks and regulators for management and supervisory purposes, going forward will be required by regulation. One test, referred to as the liquidity coverage ratio ("LCR"), is designed to ensure that the banking entity maintains an adequate level of unencumbered high quality liquid assets equal to the entity's expected net cash outflow for a 30 day time horizon (or, if greater, then 25% of its expected total cash outflow) under an acute liquidity stress scenario. The other test, referred to as the net stable funding ratio ("NSFR"), is designed to promote more medium and long term funding of the assets and activities of banking entities over a one year time horizon. These requirements will incentivize banking entities to increase their holdings of U.S. Treasury securities and other sovereign debt as a component of assets and increase the use of long term debt as a funding source.

In September 2014, the federal banking agencies approved final rules implementing the LCR for advanced approaches banking organizations (i.e., banking organizations with $250 billion or more in total consolidated assets or $10 billion or more in total on-balance sheet foreign exposure) and a modified version of the LCR for bank holding companies with at least $50 billion in total consolidated assets that are not advanced approach banking organizations, neither of which apply to the Company or the Bank. The federal banking agencies have not yet proposed rules to implement the NSFR.

Prompt Corrective Action

The Federal Deposit Insurance Corporation Improvement Act, or FDICIA, requires each federal banking agency to take prompt corrective action to resolve the problems of insured depository institutions, including but not limited to those that fall below one or more prescribed minimum capital ratios. Pursuant to FDICIA, the FDIC promulgated regulations defining the following five categories in which an insured depository institution will be placed, based on the level of its capital ratios: well capitalized, adequately capitalized, undercapitalized, significantly undercapitalized and critically undercapitalized. A bank's category is determined solely for the purpose of applying prompt corrective action regulations, and the capital category may not constitute an accurate representation of the bank's overall financial condition or prospects for other purposes.

Under the prompt corrective action provisions of FDICIA ("PCA"), an insured depository institution generally will be classified as undercapitalized if its total risk based capital is less than 8% or its Tier 1 risk based capital or leverage ratio is less than 4%. The New Capital Rules revise the PCA regulations by: (i) introducing a CET1 ratio requirement at each PCA category (other than critically undercapitalized), with the required CET1 ratio being 6.5% for well capitalized status; (ii) increasing the minimum Tier 1 capital ratio requirement for each category, with the minimum Tier 1 capital ratio for well capitalized status being 8% (as compared to the current 6%); and (iii) eliminating the current provision that provides that a bank with a composite supervisory rating of 1 may have a 3% leverage ratio and still be adequately capitalized (under the New Capital Rules a 5% leverage ratio is required for an institution to be well capitalized and a 4% leverage ratio is required to be adequately capitalized). The New Capital Rules do not change the total risk based capital requirement for any PCA category. An institution that, based upon its capital levels, is classified as "well capitalized", "adequately capitalized" or "undercapitalized" may be treated as though it were in the next lower capital category if the appropriate federal banking agency, after notice and opportunity for hearing, determines that an unsafe or unsound condition or an unsafe or unsound practice warrants such treatment. At each successive lower capital category, an insured depository institution is subject to more restrictions and prohibitions, including restrictions on growth, restrictions on interest rates paid on deposits, prohibitions on payment of dividends and restrictions on the acceptance of brokered deposits. Furthermore, if a bank is classified in one of the undercapitalized categories, it is required to submit a capital restoration plan to its federal bank regulator, and the holding company must guarantee the performance of that plan. The obligation of a controlling bank holding company to fund a capital restoration plan is limited to the lesser of 5% of an undercapitalized subsidiary's assets or the amount required to meet regulatory capital requirements.

In addition to measures taken under the prompt corrective action provisions, commercial banking organizations, such as the Bank, may be subject to potential enforcement actions by the federal or state banking agencies for unsafe or unsound practices in conducting their businesses or for violations of any law, rule, regulation or any condition imposed in writing by the agency or any written agreement with the agency. Enforcement actions may include the imposition of a conservator or receiver, the issuance of a cease and desist order that can be judicially enforced, the termination of insurance for deposits (in the case of a depository institution), the imposition of civil money penalties, the issuance of directives to increase capital, the issuance of formal and informal agreements, the issuance of removal and prohibition orders against institution affiliated parties. The enforcement of such actions through injunctions or restraining orders may be based upon a judicial determination that the agency would be harmed if such equitable relief was not granted.

Safety and Soundness Standards

The FDIA requires the federal bank regulators to prescribe standards, by regulations or guidelines, relating to internal controls, information systems and internal audit systems, loan documentation, credit underwriting, interest rate risk exposure, asset growth, asset quality, earnings, stock valuation and compensation, fees and benefits, and such other operational and managerial standards as the agencies deem appropriate. Guidelines adopted by the federal bank regulatory agencies establish general standards relating to internal controls and information systems, internal audit systems, loan documentation, credit underwriting, interest rate exposure, asset growth and compensation, fees and benefits. In general, these guidelines require, among other things, appropriate systems and practices to identify and manage the risk and exposures specified in the guidelines. These guidelines also prohibit excessive compensation as an unsafe and unsound practice and describe compensation as excessive when the amounts paid are unreasonable or disproportionate to the services performed by an executive officer, employee, director or principal stockholder. In addition, the agencies adopted regulations that authorize, but do not require, an agency to order an institution that has been given notice by an agency that it is not satisfying any of such safety and soundness standards to submit a compliance plan. If, after being so notified, an institution fails to submit an acceptable compliance plan or fails in any material respect to implement an acceptable compliance plan, the bank regulator must issue an order directing action to correct the deficiency and may issue an order directing other actions of the types to which an undercapitalized institution may be subject under the FDIA. If an institution fails to comply with such an order, the bank regulator may seek to enforce such order in judicial proceedings and to impose civil money penalties.

Deposit Insurance

The Bank is a state chartered, “non member” bank and therefore is regulated by the DBO and the FDIC. Pacific Western accepts deposits, and those deposits have the benefit of FDIC insurance up to the applicable limits. The applicable limit for FDIC insurance for most types of accounts is $250,000.

Pursuant to the Dodd Frank Act, the FDIC amended its regulations to determine insurance assessments based on the average consolidated assets less the average tangible equity of the insured depository institution during the assessment period. In addition, in October 2010, the FDIC adopted a new Deposit Insurance Fund restoration plan to ensure that the fund reserve ratio reaches 1.35% by September 30, 2020. The FDIC has established a long-term target for the reserve ratio of 2.0%. At least semi annually, the FDIC will update its loss and income projections for the fund and, if needed, will increase or decrease assessment rates, following notice and comment rulemaking if required.

The Bank, as is the case with all FDIC insured banks, is subject to deposit insurance assessments as determined by the FDIC. Each institution's assessments are based on the average consolidated total assets less the average tangible equity of the insured depository institution during the assessment period (the "assessment base"). As a result of the April 7, 2014 CapitalSource Inc. merger, the Bank's total consolidated assets exceeded $15 billion, which categorizes the Bank as a "large institution" under the FDIC's deposit assessment rules. For large institutions, such as the Bank, the FDIC uses a performance score and a loss-severity score that are used to calculate an initial assessment rate. In calculating these scores, the FDIC uses a bank's capital level and supervisory ratings (its "CAMELS ratings") and certain financial measures to assess an institution's ability to withstand asset-related stress and funding-related stress. The FDIC has the ability to make discretionary adjustments to the total score based upon significant risk factors that are not adequately captured in the calculations.

Under the FDIA, the FDIC may terminate deposit insurance upon a finding that the institution has engaged in unsafe and unsound practices, is in an unsafe or unsound condition to continue operations, or has violated any applicable law, regulation, rule, order or condition imposed by the FDIC.

Incentive Compensation

The Dodd Frank Act requires the federal bank regulatory agencies and the SEC to establish joint regulations or guidelines prohibiting incentive based payment arrangements at specified regulated entities having at least $1 billion in total assets, such as the Company and the Bank, that encourage inappropriate risks by providing an executive officer, employee, director or principal stockholder with excessive compensation, fees, or benefits that could lead to material financial loss to the entity. In addition, these regulators must establish regulations or guidelines requiring enhanced disclosure of incentive based compensation arrangements to regulators. The agencies proposed such regulations in April 2011, but these regulations have not yet been finalized. If the regulations are adopted in the form initially proposed, they will impose limitations on the manner in which we may structure compensation for our executives.

In addition to the proposed rules, in June 2010, the FRB and the FDIC issued comprehensive final guidance on incentive compensation policies intended to ensure that the incentive compensation policies of banking organizations do not undermine the safety and soundness of such organizations by encouraging excessive risk taking. The guidance, which covers all employees that have the ability to materially affect the risk profile of an organization, either individually or as part of a group, is based upon the key principles that a banking organization's incentive compensation arrangements should (i) provide incentives that do not encourage risk taking beyond the organization's ability to effectively identify and manage risks, (ii) be compatible with effective internal controls and risk management, and (iii) be supported by strong corporate governance, including active and effective oversight by the organization's board of directors. These three principles are incorporated into the proposed joint compensation regulations under Dodd Frank, discussed above.

The FRB will review, as part of its regular, risk focused examination process, the incentive compensation arrangements of banking organizations, such as the Company, that are not "large, complex banking organizations." These reviews will be tailored to each organization based on the scope and complexity of the organization's activities and the prevalence of incentive compensation arrangements. The findings of the supervisory initiatives will be included in reports of examination. Deficiencies will be incorporated into the organization's supervisory ratings, which can affect the organization's ability to make acquisitions and take other actions. Enforcement actions may be taken against a banking organization if its incentive compensation arrangements, or related risk management control or governance processes, pose a risk to the organization's safety and soundness and the organization is not taking prompt and effective measures to correct the deficiency.

Consumer Regulation

We are subject to a number of federal and state consumer protection laws that extensively govern our relationship with our customers. These laws include the Equal Credit Opportunity Act, the Fair Credit Reporting Act, the Truth in Lending Act, the Truth in Savings Act, the Electronic Fund Transfer Act, the Expedited Funds Availability Act, the Home Mortgage Disclosure Act, the Fair Housing Act, the Real Estate Settlement Procedures Act, the Fair Debt Collection Practices Act, the Service Members Civil Relief Act and these laws' respective state-law counterparts, as well as state usury laws and laws regarding unfair and deceptive acts and practices. These and other federal laws, among other things, require disclosures of the cost of credit and terms of deposit accounts, provide substantive consumer rights, prohibit discrimination in credit transactions, regulate the use of credit report information, provide financial privacy protections, prohibit unfair, deceptive and abusive acts and practices, restrict our ability to raise interest rates and subject us to substantial regulatory oversight. Violations of applicable consumer protection laws can result in significant potential liability from litigation brought by customers, including actual damages, restitution and attorneys' fees. Federal bank regulators, state attorneys general and state and local consumer protection agencies may also seek to enforce consumer protection requirements and obtain these and other remedies, including regulatory sanctions, customer rescission rights, action by the state and local attorneys general in each jurisdiction in which we operate and civil money penalties. Failure to comply with consumer protection requirements may also result in our failure to obtain any required bank regulatory approval for merger or acquisition transactions we may wish to pursue or our prohibition from engaging in such transactions even if approval is not required.

The Dodd Frank Act established the CFPB with broad rulemaking, supervisory and enforcement powers under various federal consumer financial protection laws. The CFPB is also authorized to engage in consumer financial education, track consumer complaints, request data and promote the availability of financial services to underserved consumers and communities. Banking organizations with more than $10 billion in assets, such as the Bank, are subject to direct oversight and examination by the CFPB.

The consumer protection provisions of the Dodd-Frank Act and the examination, supervision and enforcement of those laws and implementing regulations by the CFPB have created a more intense and complex environment for consumer finance regulation. The CFPB has significant authority to implement and enforce federal consumer finance laws, including the Truth in Lending Act, the Equal Credit Opportunity Act and new requirements for financial services products provided for in the Dodd-Frank Act, as well as the authority to identify and prohibit unfair, deceptive or abusive acts and practices. The review of products and practices to prevent such acts and practices is a continuing focus of the CFPB, and of banking regulators more broadly. The ultimate impact of this heightened scrutiny is uncertain but could result in changes to pricing, practices, products and procedures. It could also result in increased costs related to regulatory oversight, supervision and examination, additional remediation efforts and possible penalties. In addition, the Dodd-Frank Act provides the CFPB with broad supervisory, examination and enforcement authority over various consumer financial products and services, including the ability to require reimbursements and other payments to customers for alleged legal violations and to impose significant penalties, as well as injunctive relief that prohibits lenders from engaging in allegedly unlawful practices. The CFPB also has the authority to obtain cease and desist orders providing for affirmative relief or monetary penalties. The Dodd-Frank Act does not prevent states from adopting stricter consumer protection standards. State regulation of financial products and potential enforcement actions could also adversely affect our business, financial condition or results of operations.

Depositor Preference

The Federal Deposit Insurance Act provides that, in the event of the "liquidation or other resolution" of an insured depository institution, the claims of depositors of the institution, including the claims of the FDIC as subrogee of insured depositors, and certain claims for administrative expenses of the FDIC as a receiver, will have priority over other general unsecured claims against the institution. If an insured depository institution fails, insured and uninsured depositors, along with the FDIC, will have priority in payment ahead of unsecured, non deposit creditors, including the parent bank holding company, with respect to any extensions of credit they have made to such insured depository institution.

USA PATRIOT Act

The Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act of 2001, or "PATRIOT Act," designed to deny terrorists and others the ability to obtain access to the United States financial system, has significant implications for depository institutions, brokers, dealers and other businesses involved in the transfer of money. The PATRIOT Act, as implemented by various federal regulatory agencies, requires financial institutions, including the Company, to establish and implement policies and procedures with respect to, among other matters, anti money laundering, compliance, suspicious activity and currency transaction reporting and due diligence on customers and prospective customers. The PATRIOT Act and its underlying regulations permit information sharing for counter terrorist purposes between federal law enforcement agencies and financial institutions, as well as among financial institutions, subject to certain conditions, and require the FRB, the FDIC and other federal banking agencies to evaluate the effectiveness of an applicant in combating money laundering activities when considering applications filed under Section 3 of the BHCA or the Bank Merger Act.

We regularly evaluate and continue to enhance our systems and procedures to continue to comply with the PATRIOT Act and other anti money laundering initiatives. We believe that the ongoing cost of compliance with the PATRIOT Act is not likely to be material to the Company. Failure of a financial institution to maintain and implement adequate programs to combat money laundering and terrorist financing, or to comply with all of the relevant laws or regulations, could have serious legal, strategic, and reputational consequences for the institution and result in material fines and sanctions.

Bank Secrecy Act/Anti-Money Laundering

The Bank Secrecy Act, which applies to all financial institutions, was enacted on October 26, 1970, as a means to detect incidents of money laundering for any of a multitude of illegal, illicit and suspicious activities. Money laundering is the process of making illegally-gained funds (i.e. "dirty money") appear legal (i.e. "clean"). There are a variety of ways this can take place and against which the Bank must guard. Money laundering can facilitate crimes such as drug trafficking and terrorism, and can adversely impact the global economy. We regularly monitor account activities of all customers to ensure they are not using the Bank for these activities and take appropriate steps as we detect such activities.

Office of Foreign Assets Control Regulation

The United States has imposed economic sanctions that affect transactions with designated foreign countries, designated nationals and others. These are typically known as the “OFAC” rules based on their administration by the U.S. Treasury Department Office of Foreign Assets Control (“OFAC”). The OFAC administered sanctions targeting designated countries take many different forms. Generally, however, they contain one or more of the following elements: (i) restrictions on trade with or investment in a sanctioned country, including prohibitions against direct or indirect imports from and exports to a sanctioned country and prohibitions on “U.S. persons” engaging in financial transactions relating to making investments in, or providing investment related advice or assistance to, a sanctioned country; and (ii) a blocking of assets in which the government or specially designated nationals of the sanctioned country have an interest, by prohibiting transfers of property subject to U.S. jurisdiction (including property in the possession or control of U.S. persons). Blocked assets (e.g., property and bank deposits) cannot be paid out, withdrawn, set off or transferred in any manner without a license from OFAC. Failure to comply with these sanctions could have serious legal, strategic, and reputational consequences, and result in civil money penalties on the Bank.

Community Reinvestment Act

The CRA generally requires insured depository institutions to identify the communities they serve and to make loans and investments, offer products, make donations in, and provide services designed to meet the credit needs of these communities. The CRA also requires banks to maintain comprehensive records of its CRA activities to demonstrate how it is meeting the credit needs of their communities; these documents are subject to periodic examination by the FDIC. During these examinations, the FDIC rates such institutions’ compliance with CRA as “Outstanding,” “Satisfactory,” “Needs to Improve” or “Substantial Noncompliance.” The CRA requires the FDIC to take into account the record of a bank in meeting the credit needs of all of the communities served, including low and moderate income neighborhoods, in determining such rating. Failure of an institution to receive at least a “Satisfactory” rating could inhibit such institution or its holding company from undertaking certain activities, including acquisitions. The Bank received a CRA rating of “Satisfactory” as of its most recent examination. In the case of a bank holding company, such as the Company, when applying to acquire a bank, savings association, or a bank holding company, the FRB will assess the CRA record of each depository institution of the applicant bank holding company in considering the application.

Customer Information Security

The FRB and other bank regulatory agencies have adopted guidelines for safeguarding confidential, personal, non public customer information. These guidelines require each financial institution, under the supervision and ongoing oversight of its board of directors or an appropriate committee thereof, to create, implement and maintain a comprehensive written information security program designed to ensure the security and confidentiality of customer information, protect against any anticipated threats or hazard to the security or integrity of such information and protect against unauthorized access to or use of such information that could result in substantial harm or inconvenience to any customer. We have adopted a customer information security program to comply with such requirements.

Privacy

The Gramm Leach Bliley Act of 1999 and the California Financial Information Privacy Act require financial institutions to implement policies and procedures regarding the disclosure of non-public personal information about consumers to non affiliated third parties. In general, the statutes require explanations to consumers on policies and procedures regarding the disclosure of such non-public personal information and, except as otherwise required by law, prohibit disclosing such information except as provided in the Bank's policies and procedures. Pacific Western has implemented privacy policies addressing these restrictions, which are distributed regularly to all existing and new customers of the Bank.

Legislative and Regulatory Initiatives

From time to time, various legislative and regulatory initiatives are introduced in the U.S. Congress and state legislatures, as well as by regulatory agencies. Such initiatives may include proposals to expand or contract the powers of bank holding companies and depository institutions or proposals to substantially change the financial institution regulatory system. Such legislation could change banking statutes and our operating environment in substantial and unpredictable ways. If enacted, such legislation could increase or decrease the cost of doing business, limit or expand permissible activities or affect the competitive balance among banks, savings associations, credit unions, and other financial institutions. We cannot predict whether any such legislation will be enacted, and, if enacted, the effect that it, or any implementing regulations, would have on our financial condition, results of operations or cash flows. A change in statutes, regulations or regulatory policies applicable to the Company or any of its subsidiaries could have a material effect on our business.

Hazardous Waste Clean Up and Climate Related Risk

Our primary exposure to environmental laws is through our lending activities and through properties or businesses we may own, lease or acquire, or which are collateral for our loans, since we are not involved in any business that manufactures, uses or transports chemicals, waste, pollutants or toxins that might have a material adverse effect on the environment. Based on a general survey of the Bank's loan portfolio, conversations with local appraisers and the type of lending currently and historically done by the Bank, we are not presently aware of any actual liability for hazardous waste contamination that would be reasonably likely to have a material adverse effect on the Company as of February 20, 2015. Finally, we are not aware of any physical or regulatory consequence resulting from climate change that would have a material adverse effect upon the Company.

Available Information

We maintain an Internet website at www.pacwestbancorp.com, and a website for Pacific Western at www.pacificwesternbank.com. At www.pacwestbancorp.com and via the “Investor Relations” link at the Bank’s website, our Annual Report on Form 10 K, quarterly reports on Form 10 Q, current reports on Form 8 K and amendments to such reports filed or furnished pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended (the "Exchange Act") are available, free of charge, as soon as reasonably practicable after such forms are electronically filed with, or furnished to, the SEC. The public may read and copy any materials we file with the SEC at the SEC’s Public Reference Room, located at 100 F Street, NE, Washington, D.C. 20549. The public may obtain information on the operation of the Public Reference Room by calling the SEC at 1 800 SEC 0330. The SEC also maintains an Internet website at http://www.sec.gov that contains reports, proxy and information statements, and other information regarding issuers that file electronically with the SEC. You may obtain copies of the Company’s filings on the SEC website. These documents may also be obtained in print upon request by our stockholders to our Investor Relations Department.

We have adopted a written code of ethics that applies to all directors, officers and employees of the Company, including our principal executive officer and senior financial officers, in accordance with Section 406 of the Sarbanes Oxley Act of 2002 and the rules of the SEC promulgated thereunder. The code of ethics, which we call our Code of Business Conduct and Ethics, is available on our corporate website, www.pacwestbancorp.com in the section entitled “Corporate Governance.” In the event that we make changes in, or provide waivers from, the provisions of this code of ethics that the SEC requires us to disclose, we intend to disclose these events on our corporate website in such section. In the Corporate Governance section of our corporate website, we have also posted the charters for our Audit Committee, our Compensation, Nominating and Governance Committee, and our Risk Committee, as well as our Corporate Governance Guidelines. In addition, information concerning purchases and sales of our equity securities by our executive officers and directors is posted on our website.

Our Investor Relations Department can be contacted at PacWest Bancorp, 130 S. State College Blvd., Brea, CA 92821, Attention: Investor Relations, telephone (714) 671 6800, or via e mail to investor relations@pacwestbancorp.com.

All website addresses given in this document are for information only and are not intended to be an active link or to incorporate any website information into this document.

Forward-Looking Information

This Form 10-K contains certain "forward-looking statements" about the Company and its subsidiaries within the meaning of the Private Securities Litigation Reform Act of 1995, including certain plans, strategies, goals, and projections and including statements about our expectations regarding our operating expenses, profitability, allowance for loan and lease losses, net interest margin, deposit growth, loan and lease portfolio growth and production, future acquisitions, maintaining capital adequacy, liquidity, goodwill, interest rate risk management, and realization of our deferred tax asset. All statements contained in this Form 10-K that are not clearly historical in nature are forward-looking, and the words "anticipate," "assume," "intend," "believe," "forecast," "expect," "estimate," "plan," "continue "should," "look forward" and similar expressions are generally intended to identify forward-looking statements. All forward-looking statements involve risks, uncertainties and contingencies, many of which are beyond our control, which may cause actual results, performance, or achievements to differ materially from results, performance or achievements expressed or implied by these forward-looking statements. Actual results could differ materially from those contained or implied by such forward-looking statements for a variety of factors, including without limitation:

- change in interest rates and lending spreads;
- compression of interest rate spreads on newly originated loans or due to changes in our loan product mix;
- unfavorable changes in asset mix;
- changes in economic or competitive market conditions could negatively impact investment or lending opportunities or product pricing and services;
- credit quality deterioration or pronounced and sustained reduction in market values or other economic factors which adversely affect our borrowers' ability to repay loans and leases;
- continued, worsening or higher than anticipated credit losses or charge-offs;
- higher than anticipated increases in operating expenses;
- higher compensation costs and professional fees;
- increased costs to manage and sell foreclosed assets;
- the Company's ability to complete future acquisitions and to successfully integrate such acquired entities or achieve expected benefits, synergies and/or operating efficiencies within expected time frames or at all;
- higher than anticipated delinquencies and reserves;
- a change in the interest rate environment reduces interest margins;
- asset/liability repricing risks and liquidity risks reduce interest margins and the value of investments;
- pending legal matters may take longer or cost more to resolve or may be resolved adversely to the Company;
- a deterioration in the overall macroeconomic conditions or the state of the banking industry that could warrant further analysis of the carrying value of goodwill and could result in an adjustment to its carrying value resulting in a non-cash charge to net income;
- general economic conditions, either nationally or in the market areas in which the Company does or anticipates doing business, are less favorable than expected;
- our inability to grow deposits and access wholesale funding sources;
- legislative or regulatory requirements or changes adversely affecting the Company's business, including an increase to capital requirements;
- loan repayments higher than expected;
- reduced demand for our services due to strategic or regulatory reasons;
- the success and timing of other business strategies and asset sales;
- lower than expected taxable income which adversely affects the value of deferred tax assets;
- lower than expected dividends paid from Pacific Western Bank to the holding company;
- changes in tax laws or regulations affecting our business;
- our inability to generate sufficient earnings;
- tax planning or disallowance of tax benefits by tax authorities;
- changes in the forward yield curve;
- changes in the relationship between yields on investments and loans repaid and yields on assets reinvested; and

- other risk factors described in our audited consolidated financial statements, and other risk factors described in this Form 10-K and other documents filed or furnished by PacWest with the SEC.

All forward-looking statements included in this Form 10-K are based on information available at the time the statement is made. We are under no obligation to (and expressly disclaim any such obligation to) update or alter our forward-looking statements, whether as a result of new information, future events or otherwise except as required by law.

ITEM 1A. RISK FACTORS
Ownership of our common stock involves risk. You should carefully consider, in addition to the other information set forth herein, the following risk factors.
Risks Related to Our Business
Our business has been and may continue to be adversely affected by current conditions in the financial markets and economic conditions generally.
The U.S. economic recession in 2007 through 2009, and the sluggish economic recovery since then, has had an adverse effect on our business. In addition, the global financial markets have undergone and may continue to experience pervasive and fundamental disruptions, which also have an adverse effect on our business. In some cases, the markets have produced downward pressure on stock prices and credit availability for certain issuers without regard to those issuers' underlying financial strength. While economic conditions have shown signs of improvement, the sustainability of an economic recovery is uncertain as economic activity continues to face difficulties due to cautious business spending, the variable rate of U.S. economic growth, weak commodity prices, low wage growth offsetting the improved levels of unemployment, currency exchange rate volatility and its effect on export growth, and the slowing and negative economic growth and other continuing economic developments in Europe and Asia.
A sustained weakness or further weakening in business and economic conditions generally or specifically in the principal markets in which we do business could have one or more of the following adverse effects on our business:

- a decrease in the demand for loans and other products and services offered by us;
- a decrease in deposit balances due to overall reductions in the accounts of customers;
- a decrease in the value of our loans or other assets secured by real estate;
- a decrease in net interest income derived from our lending and deposit gathering activities;
- an impairment of certain intangible assets; or
- an increase in the number of borrowers who become delinquent, file for protection under bankruptcy laws or default on their loans or other obligations to us. An increase in the number delinquencies, bankruptcies or defaults could result in a higher level of nonperforming assets, net charge-offs and provisions for credit losses.

Unfavorable changes in economic conditions generally have an adverse effect on our business, and there can be no assurance that the economic recovery will be sustainable in the near term. If economic conditions worsen or remain volatile, we expect our business, financial condition and results of operations to be adversely affected.
Our concentration of loans to privately owned small and medium-sized companies and to a limited number of clients within a particular industry or region could expose us to greater lending risk if the market sector, industry or region were to experience economic difficulties or changes in the regulatory environment.
Our portfolio consists primarily of commercial loans to small and medium-sized, privately owned businesses in a limited number of industries and regions primarily throughout the United States.
As of December 31, 2014, real estate mortgage loans (which are predominately commercial real estate loans) comprised 47.1% of our total portfolio. At December 31, 2014, our largest property type concentration was healthcare property, totaling 18.4% of real estate mortgage loans. Other significant real estate mortgage loan property type concentrations were office properties at 13.9% and multi-family properties at 13.8% at December 31, 2014. In addition, 52.7% of our loans secured by real estate were in California at December 31, 2014.
Commercial loans and leases comprised 49.4% of our total portfolio at December 31, 2014. At December 31, 2014, our largest commercial loan type concentration was cash flow loans, totaling 20.9% of our total portfolio. Cash flow secured loans are provided to sophisticated buyers and private equity groups, financial investors, strategic companies and sponsors to finance the acquisition or recapitalization of a business. Other significant commercial concentrations were asset-based loans at 15.1% and equipment finance at 8.2% of the total portfolio at December 31, 2014.
If any particular industry or geographic region were to experience economic difficulties, the overall timing and amount of collections on our loans to clients operating in those industries or geographic regions may differ from what we expected, which could have a material adverse impact on our financial condition or results of operations.

Additionally, compared to larger, publicly owned firms, privately owned small and medium-sized companies generally have limited access to capital and higher funding costs, may be in a weaker financial position and therefore more susceptible to economic downturns or volatility and may need more capital to expand or compete. These financial challenges may make it difficult for our clients to make scheduled payments of interest or principal on our loans. Accordingly, loans made to these types of clients entail higher risks than loans made to companies that are able to access a broader array of credit sources. The concentration of our portfolio in loans to these types of clients could amplify these risks.

Further, there is generally no publicly available information about the small and medium-sized privately owned companies to which we lend. Therefore, we underwrite our loans based on detailed financial information and projections provided to us by our clients and we must rely on our clients and the due diligence efforts of our employees to obtain the information relevant to making our credit decisions. We rely upon the management of these companies to provide full and accurate disclosure of material information concerning their business, financial condition and prospects. We may not have access to all of the material information about a particular client's business, financial condition and prospects, or a client's accounting records may be poorly maintained or organized. The client's business, financial condition and prospects may also change rapidly in the current economic environment. In such instances, we may not make a fully informed credit decision which may lead, ultimately, to a failure or inability to recover our loan in its entirety.

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

Changes in the interest rate environment may reduce our profits. It is expected that we will continue to realize income from the differential or "spread" between the interest earned on loans, securities and other interest-earning assets, and interest paid on deposits, borrowings and other interest-bearing liabilities. Net interest spreads are affected by the difference between the maturities and repricing characteristics of interest-earning assets and interest-bearing liabilities. Changes in market interest rates generally affect loan volume, loan yields, funding sources and funding costs. Our net interest spread depends on many factors that are partly or completely out of our control, including competition, federal economic monetary and fiscal policies, and general economic conditions.

While an increase in the general level of interest rates may increase our loan yield, it may adversely affect the ability of certain borrowers with variable-rate loans to pay the interest on and principal of their obligations. In addition, an increase in market interest rates on loans is generally associated with a lower volume of loan originations, which may reduce earnings. Following an increase in the general level of interest rates, our ability to maintain a positive net interest spread is dependent on our ability to increase our loan offering rates, replace loan maturities with new originations, minimize increases on our deposit rates, and maintain an acceptable level and mix of funding. We cannot provide assurances that we will be able to increase our loan offering rates and continue to originate loans due to the competitive landscape in which we operate. Additionally, we cannot provide assurances that we can minimize the increases in our deposit rates while maintaining an acceptable level of deposits. Finally, we cannot provide any assurances that we can maintain our current levels of noninterest-bearing deposits as customers may seek higher yielding products when rates increase.

Following a decline in the general level of interest rates, our ability to maintain a positive net interest spread is dependent on our ability to reduce the interest paid on deposits, borrowings, and other interest-bearing liabilities. We cannot provide assurance that we would be able to lower the rates paid on deposit accounts to support our liquidity requirements as lower rates may result in deposit outflows.

Accordingly, changes in levels of market interest rates could materially and adversely affect our net interest spread, asset quality, loan origination volume, liquidity, and overall profitability. We cannot assure you that we can minimize our interest rate risk.

Liquidity risk would impair our ability to fund operations and jeopardize our financial condition.

Liquidity is essential to our business. An inability to raise funds through deposits, borrowings, the sale of loans and other sources could have a material adverse effect on our liquidity. Our access to funding sources in amounts adequate to finance our activities could be impaired by factors that affect us specifically or the financial services industry in general. Factors that could detrimentally impact our access to liquidity sources include a decrease in the level of our business activity due to a market downturn or adverse regulatory action against us. Our ability to acquire deposits or borrow could also be impaired by factors that are not specific to us, such as a severe disruption of the financial markets or negative views and expectations about the prospects for the financial services industry as a whole as a result of conditions faced by banking organizations in the domestic and worldwide credit markets.

We face strong competition from financial services companies and other companies that offer banking services, which could materially and adversely affect our business.

We conduct our community banking operations primarily in Southern California. Increased competition in our market may result in reduced loans and deposits or less favorable loan and deposit terms. Ultimately, we may not be able to compete successfully against current and future competitors. Many competitors offer the same banking services that we offer in our service areas. These competitors include national banks, regional banks and other community banks. We also face competition from many other types of financial institutions, including without limitation, savings and loan institutions, finance companies, brokerage firms, insurance companies, credit unions, mortgage banks and other financial intermediaries. In particular, our competitors include several major financial companies whose greater resources may afford them a marketplace advantage by enabling them to maintain numerous banking locations and ATMs and conduct extensive promotional and advertising campaigns.

Additionally, banks and other financial institutions with larger capitalization and financial intermediaries not subject to bank regulatory restrictions have larger or no lending limits and are thereby able to serve the credit needs of larger customers. Areas of competition include interest rates for loans and deposits, efforts to obtain deposits, and the range and quality of products and services provided, including new technology driven products and services. Technological innovation continues to contribute to greater competition in domestic and international financial services markets as technological advances enable more companies to provide financial services. We also face competition from out-of-state financial intermediaries that have opened production offices or that solicit deposits in our market areas. Should competition in the financial services industry intensify, our ability to market our products and services may be adversely affected. If we are unable to attract and retain banking customers, we may be unable to grow or maintain the levels of our loans and deposits and our results of operations and financial condition may be adversely affected as a result.

Competition from financial institutions seeking to maintain adequate liquidity places upward pressure on the rates paid on certain deposit accounts relative to the level of market interest rates during times of both decreasing and increasing market liquidity. To maintain both attractive and adequate levels of liquidity, without exhausting secondary sources of liquidity, we may incur increased deposit costs.

Several rating agencies publish unsolicited ratings of the financial performance and relative financial health of many banks, including Pacific Western, based on publicly available data. As these ratings are publicly available, a decline in the Bank's ratings from these agencies may result in deposit outflows or the inability of the Bank to raise deposits in the secondary market as broker-dealers and depositors may use such ratings in deciding where to deposit their funds.

We may be adversely affected by changes in the actual or perceived soundness or condition of other financial institutions.

Financial services institutions that deal with each other are interconnected as a result of trading, investment, liquidity management, clearing, counterparty and other relationships. Within the financial services industry, loss of public confidence, including through default by any one institution, could lead to liquidity challenges or to defaults by other institutions. Concerns about, or a default by, one institution could lead to significant liquidity problems and losses or defaults by other institutions, as the commercial and financial soundness of many financial institutions is closely related as a result of these credit, trading, clearing and other relationships. Even the perceived lack of creditworthiness of, or questions about, a counterparty may lead to market-wide liquidity problems and losses or defaults by various institutions. This systemic risk may adversely affect financial intermediaries, such as clearing agencies, banks and exchanges with which we interact on a daily basis or key funding providers such as the Federal Home Loan Banks, any of which could have a material adverse effect on our access to liquidity or otherwise have a material adverse effect on our business, financial condition or results of operations.

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We may not recover all amounts that are contractually owed to us by our borrowers.
The Company is dependent primarily on loan and lease principal, interest, and fee collections to fund its operations. A shortfall in collections and proceeds may impair our ability to fund our operations or to repay our existing debt.
When we loan money, commit to loan money or enter into a letter of credit or other contract with a counterparty, we incur credit risk. The credit quality of our portfolio can have a significant impact on our earnings. We expect to experience charge-offs and delinquencies on our loans in the future. Our clients' actual operating results may be worse than our underwriting indicated when we originated the loans, and in this circumstance, if timely corrective action is not taken, we could incur a substantial impairment or loss of the value on such loans. We may fail to identify problems because our client did not report them in a timely manner or, even if the client did report the problem, we may fail to address it quickly enough or at all. Even if clients provide us with full and accurate disclosure of all material information concerning their businesses, we may misinterpret or incorrectly analyze this information. Mistakes may cause us to make loans that we otherwise would not have made, to fund advances that we otherwise would not have funded, result in losses on one or more of our loans, or necessitate that we significantly increase our allowance for loans losses. As a result, we could suffer loan losses and have nonperforming loans, which could have a material adverse effect on our revenues, net income and results of operations and financial condition, to the extent the losses exceed our allowance for loan and lease losses.
The collateral securing a loan or lease may not be sufficient to protect us if we have not properly obtained or perfected a lien on such collateral or if the collateral value does not cover the loan or lease.
Most of our loans are secured by a lien on specified collateral of the client and we may not obtain or properly perfect our liens or the value of the collateral securing any particular loan may not protect us from suffering a partial or complete loss if the loan becomes non-performing and we move to foreclose on the collateral. In such event, we could suffer loan losses, which could have a material adverse effect on our revenue, net income, financial condition and results of operations.
In particular, cash flow lending involves lending money to a client based primarily on the expected cash flow, profitability and enterprise value of a client rather than on the value of its assets. As of December 31, 2014, approximately 20.9% of our portfolio was comprised of cash flow loans. Although the value of the enterprise is significantly in excess of our loan balance, the value of the stand-alone assets which we hold as collateral for these loans is typically substantially less than the amount of money we advance to a client under these loans. When a cash flow loan becomes non-performing, our primary recourse to recover some or all of the principal of our loan is to force the sale of the entire company as a going concern or restructure the company in a way we believe would enable it to generate sufficient cash flow over time to repay our loan. Neither of these alternatives may be an available or viable option or generate enough proceeds to repay the loan.
We may need to raise additional capital in the future and such capital may not be available when needed or at all.
We may need to raise additional capital in the future to provide us with sufficient capital resources and liquidity to meet our commitments, regulatory requirements, and business needs. As a publicly traded company, a likely source of additional funds is the capital markets, accomplished generally through the issuance of equity, both common and preferred stock, and the issuance of subordinated debentures. Our ability to raise additional capital, if needed, will depend on, among other things, conditions in the capital markets at that time, which are outside of our control, and our financial performance. Deterioration in economic conditions and the loss of confidence in financial institutions may increase our cost of funding and limit our access to some of our customary sources of liquidity, including, but not limited to, the capital markets, inter-bank borrowings, repurchase agreements and borrowings from the discount window of the Federal Reserve Bank of San Francisco ("FRBSF").
We cannot assure you that access to such capital and liquidity will be available to us on acceptable terms or at all. Any occurrence that may limit our access to the capital markets, such as a decline in the confidence of debt purchasers, or depositors of the Bank or counterparties participating in the capital markets, may materially and adversely affect our capital costs and our ability to raise capital and, in turn, our liquidity. Further, if we need to raise capital in the future, we may have to do so when many other financial institutions are also seeking to raise capital and would then have to compete with those institutions for investors. An inability to raise additional capital on acceptable terms when needed could have a materially adverse effect on our business, financial condition or results of operations.

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The value of our securities in our investment portfolio may decline in the future.
As of December 31, 2014, we owned $1.6 billion of investment securities. The fair value of our investment securities may be adversely affected by market conditions, including changes in interest rates, and the occurrence of any events adversely affecting the issuer of particular securities in our investments portfolio. We analyze our securities on a quarterly basis to determine if an other-than-temporary impairment has occurred. The process for determining whether impairment is other-than-temporary usually requires complex, subjective judgments about the future financial performance of the issuer in order to assess the probability of receiving all contractual principal and interest payments on the security. Because of changing economic and market conditions affecting issuers, we may be required to recognize other-than-temporary impairment in future periods, which could have a material adverse effect on our business, financial condition or results of operations.
We are subject to extensive regulation, which could materially and adversely affect our business.
The banking industry is extensively regulated and supervised under both federal and state laws and regulations that are intended primarily for the protection of depositors, customers, federal deposit insurance funds and the banking system as a whole, not for the protection of our stockholders and creditors. The Company is subject to regulation and supervision by the FRB, and the Bank is subject to regulation and supervision by the FDIC, DBO and CFPB. The laws and regulations applicable to us govern a variety of matters, including permissible types, amounts and terms of loans and investments we make, the maximum interest rate that may be charged, consumer disclosures on the products and services we offer, the amount of reserves our bank must hold against deposits it takes, the types of deposits our bank may accept and the rates it may pay on such deposits, maintenance of adequate capital and liquidity, changes in control of us and the Bank, restrictions on dividends and establishment of new offices by the Bank. We must obtain approval from our regulators before engaging in certain activities, including certain acquisitions, and there can be no assurance that any regulatory approvals we may require will be obtained, or obtained without conditions, either in a timely manner or at all. Our regulators have the ability to compel us to, or restrict us from, taking certain actions entirely, such as actions that our regulators deem to constitute unsafe or unsound banking practice. Our failure to comply with any applicable laws or regulations, or regulatory policies and interpretations of such laws and regulations, could result in orders from our regulators, civil monetary penalties, or damage to our reputation, all of which could have a material adverse effect on our business, financial condition or results of operation.
The Dodd-Frank Act significantly revised and expanded the rulemaking, supervisory and enforcement authority of federal bank regulators. Regulations affecting banks and other financial institutions, such as the Dodd-Frank Act, are undergoing continuous review and change frequently; the ultimate effect of such changes cannot be predicted. Because our business is highly regulated, compliance with such regulations and laws may increase our costs and limit our ability to pursue business opportunities. Also, participation in any future specific government stabilization programs may subject us to additional restrictions. There can be no assurance that laws, rules and regulations will not be proposed or adopted in the future, which could (i) make compliance much more difficult or expensive, (ii) restrict our ability to originate, broker or sell loans or accept certain deposits, (iii) further limit or restrict the amount of commissions, interest or other charges earned on loans originated or sold by us, or (iv) otherwise materially and adversely affect our business or prospects for business.
The Dodd-Frank Act has had and will continue to have material implications for the Company and the entire financial services industry. Among other things it has, had, or will or potentially could have the following effects:

- together with regulations implementing Basel reforms, affect the levels of capital and liquidity with which we must operate and how we plan capital and liquidity levels;
- subject us to new and/or higher fees paid to various regulatory entities, including but not limited to deposit insurance fees to the FDIC;
- subject us to annual stress tests;
- impact our ability to invest in certain types of entities or engage in certain activities;
- restrict the nature of our incentive compensation programs for executive officers;
- subject us to the supervision of the CFPB, with its very broad rule-making and enforcement authorities; and
- subject us to new and different litigation and regulatory enforcement risks.

The full impact of the Dodd-Frank Act on us, our business strategies, and financial performance cannot be known at this time, and may not be known for a number of years, because this legislation requires many studies to be conducted and hundreds of regulations to be written in order for it to be fully implemented. However, these impacts are expected to be substantial and some of them may adversely affect us and our financial performance. The Dodd-Frank Act and related regulations may also require us to invest significant management attention and resources to make any necessary or desired changes, and could therefore also adversely affect our business, financial condition and results of operations.

Additionally, on December 10, 2013, five financial regulatory agencies, including our primary federal regulator, the FRB, adopted the final rules implementing the Volcker Rule embodied in Section 13 of the Bank Holding Company Act, which was added by Section 619 of the Dodd-Frank Act. The final rules prohibit banking entities from, among other things, (i) engaging in short-term proprietary trading for their own accounts, and (ii) having certain ownership interests in and relationships with hedge funds or private equity funds. The final rules are intended to provide greater clarity with respect to both the extent of those primary prohibitions and of the related exemptions and exclusions. The final rules also require each regulated entity to establish an internal compliance program that is consistent with the extent to which it engages in activities covered by the Volcker Rule, which must include (for the largest entities) making regular reports about those activities to regulators. The final rules are effective April 1, 2014, but the conformance period has been extended from its statutory end date of July 21, 2014 until July 21, 2016. Because many of the effects of the Volcker Rule may become apparent only over the next several years as the federal financial regulatory agencies apply the rules in practice, the precise financial impact of the rule on the Company, its customers, or the financial industry more generally cannot currently be determined.

We are subject to capital adequacy standards, and a failure to meet these standards could adversely affect our financial condition.

The Company and the Bank are each subject to capital adequacy and liquidity guidelines and other regulatory requirements specifying minimum amounts and types of capital that must be maintained. From time to time, the regulators implement changes to these regulatory capital adequacy and liquidity guidelines. If we fail to meet these minimum capital and liquidity guidelines and other regulatory requirements, we or our subsidiaries may be restricted in the types of activities we may conduct and may be prohibited from taking certain capital actions, such as paying dividends and repurchasing or redeeming capital securities.

In particular, the capital requirements applicable to the Company and the Bank under the recently adopted New Capital Rules are in the process of being phased-in. As a result of the New Capital Rules, we will be required to satisfy additional and more stringent capital adequacy and liquidity standards than we have in the past. Additionally, stress testing requirements may have the effect of requiring us to comply with the requirements of the New Capital Rules, or potentially even greater capital requirements, sooner than expected. While we expect to meet the requirements of the New Capital Rules, inclusive of the capital conservation buffer, as phased in by the FRB, these requirements could have a negative impact on our ability to lend, grow deposit balances, make acquisitions and make capital distributions in the form of dividends or share repurchases. Maintaining higher capital levels could also result in a lower return on equity, which may have a material adverse effect on our business, financial condition and results of operations.

Increases in or required prepayments of FDIC insurance premiums may adversely affect our earnings.

We are generally unable to control the amount of premiums that we are required to pay for FDIC insurance and premiums may be increased or accelerated in the future. Since 2008, higher levels of bank failures dramatically increased resolution costs of the FDIC and depleted the deposit insurance fund. In addition, the FDIC instituted temporary programs, some of which were made permanent by the Dodd-Frank Act, to further insure customer deposits at FDIC-insured banks, which have placed additional stress on the deposit insurance fund.

In order to maintain a strong funding position and restore reserve ratios of the deposit insurance fund, the FDIC increased assessment rates of insured institutions. In addition, on November 12, 2009, the FDIC adopted a rule requiring banks to prepay three years' worth of premiums to replenish the depleted insurance fund.

Historically, the FDIC utilized a risk-based assessment system that imposed insurance premiums based upon a risk matrix that takes into account several components including but not limited to the bank's capital level and supervisory ratings. Pursuant to the Dodd-Frank Act, the FDIC amended its regulations to base insurance assessments on average consolidated assets less average tangible equity of the insured depository institution during the assessment period. Any future increases in or required prepayments of FDIC insurance premiums may adversely affect our financial condition or results of operations.

Our ability to maintain, attract and retain customer relationships is highly dependent on our reputation.
Our customers expect us to deliver superior, personalized financial services with the highest standards of ethics, performance, professionalism and compliance. Damage to our reputation could undermine the confidence of our current and potential customers in our ability to provide high-quality financial services. Such damage could also impair the confidence of our counterparties and vendors and ultimately affect our ability to effect transactions. Maintenance of our reputation depends not only on our success in maintaining our service-focused culture and controlling and mitigating the various risks described herein, but also on our success in identifying and appropriately addressing issues that may arise in areas such as potential conflicts of interest, anti-money laundering, client personal information and privacy issues, customer and other third party fraud, record-keeping, technology-related issues including but not limited to cyber fraud, regulatory investigations and any litigation that may arise from the failure or perceived failure to comply with legal and regulatory requirements. Maintaining our reputation also depends on our ability to successfully prevent third parties from infringing on our brands and associated trademarks and our other intellectual property. Defense of our reputation, trademarks and other intellectual property, including through litigation, could result in costs that could have a material adverse effect on our business, financial condition or results of operations.
Our information and customer systems may experience an interruption or security breach.
Our communications, information, technology and customer systems supporting our operations are important to our efficiency and vulnerable to unforeseen problems. Our operations depend on our ability, as well as that of third party service provide