A-Mark Precious Metals, Inc.
Form 10-Q
November 12, 2015
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended September 30, 2015
OR

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

For the transition period from ________ to ________

Commission File Number: 001-36347

A-MARK PRECIOUS METALS, INC.
(Exact name of registrant as specified in its charter)

Delaware	11-2464169
(State of Incorporation)	(IRS Employer I.D. No.)

429 Santa Monica Blvd.
Suite 230
Santa Monica, CA 90401
(Address of principal executive offices)(Zip Code)
(310) 587-1477
(Registrant's Telephone Number, Including Area Code)

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

Title of each class	Name of each exchange on which registered
Common Stock, $0.01 par value	NASDAQ Global Select Market

Securities registered under Section 12 (g) of the Exchange Act: None

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Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.	Yes. þ No. o
Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).	Yes. þ No. 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:

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

As of November 9, 2015, the registrant had 6,973,549 shares of common stock outstanding, par value $0.01 per share.

A-MARK PRECIOUS METALS, INC.

QUARTERLY REPORT ON FORM 10-Q
For the Quarter Ended September 30, 2015

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PART I — FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

Index to the Condensed Consolidated Financial Statements

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A-MARK PRECIOUS METALS, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS
(amounts in thousands, except share data)
(unaudited)

	September 30, 2015	June 30, 2015
ASSETS		
Current assets:		
Cash	$5,044	$20,927
Receivables, net	47,899	30,025
Derivative assets	10,626	11,364
Secured loans receivables	49,766	48,666
Inventories:		
Inventories	204,476	152,076
Restricted inventories	50,030	39,425
	254,506	191,501
Income taxes receivable	6,024	7,846
Income taxes receivable from Former Parent	1,095	1,095
Prepaid expenses and other assets	1,074	1,202
Total current assets	376,034	312,626
Property and equipment, net	2,832	2,850
Goodwill	4,884	4,884
Intangibles, net	2,273	2,369
Long-term secured loans receivables	650	650
Long-term investments	2,500	2,500
Deferred tax assets - non-current	23	23
Total assets	$389,196	$325,902
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Lines of credit	$176,900	$147,000
Liability on borrowed metals	4,009	9,500
Product financing arrangement	50,030	39,425
Accounts payable	78,499	50,639
Derivative liabilities	12,893	17,897
Accrued liabilities	4,242	5,330
Deferred tax liability - current	1,593	149
Total current liabilities	328,166	269,940
Commitments and contingencies	—	—
Stockholders' equity:		
Preferred stock, $0.01 par value, authorized 10,000,000 shares; issued and outstanding: none as of September 30, 2015 and June 30, 2015	—	—
Common Stock, par value $0.01; 40,000,000 authorized; 6,973,549 and 6,973,549 issued and outstanding as of September 30, 2015 and June 30, 2015, respectively	70	70

Additional paid-in capital	22,523	22,470
Retaining earnings	38,437	33,422
Total stockholders’ equity	61,030	55,962
Total liabilities and stockholders’ equity	$389,196	$325,902

See accompanying Notes to Condensed Consolidated Financial Statements

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A-MARK PRECIOUS METALS, INC.
CONDENSED CONSOLIDATED STATEMENTS OF INCOME
(in thousands, except for share and per share data)
(unaudited)

	Three Months Ended	
	September 30, 2015	September 30, 2014
Revenues	$2,006,936	$1,453,466
Cost of sales	1,992,512	1,447,736
Gross profit	14,424	5,730
Selling, general and administrative expenses	(6,408)	(4,219)
Interest income	1,933	1,477
Interest expense	(1,234)	(1,063)
Unrealized losses on foreign exchange	(39)	(9)
Net income before provision for income taxes	8,676	1,916
Provision for income taxes	(3,312)	(778)
Net income	$5,364	$1,138
Basic and diluted income per share:		
Basic - net income	$0.77	$0.16
Diluted - net income	$0.76	$0.16
Weighted average shares outstanding:		
Basic	6,973,500	6,962,742
Diluted	7,058,700	7,065,700

See accompanying Notes to Condensed Consolidated Financial Statements

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A-MARK PRECIOUS METALS, INC.
CONDENSED CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY
(in thousands, except for share data)
(unaudited)

	Common Stock (Shares)	Common Stock	Additional Paid-in Capital	Retained Earnings	Total Stockholders' Equity
Balance, June 30, 2015	6,973,549	$70	$22,470	$33,422	$55,962
Net income	—	—	—	5,364	5,364
Share-based compensation	—	—	53	—	53
Dividends declared	—	—	—	(349)	(349)
Balance, September 30, 2015	6,973,549	$70	$22,523	$38,437	$61,030

See accompanying Notes to Condensed Consolidated Financial Statements

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A-MARK PRECIOUS METALS, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(amounts in thousands)
(unaudited)

Three Months Ended	September 30, 2015	September 30, 2014
Cash flows from operating activities:		
Net Income	$5,364	$1,138
Adjustments to reconcile net income to net cash provided by (used in) operating activities:		
Depreciation and amortization	303	228
Deferred income taxes	1,444	—
Interest added to principal of secured loans	(26)	(91)
Share-based compensation	53	62
Changes in assets and liabilities:		
Receivables	(17,223)	(19,286)
Secured loans	340	1,992
Secured loans to Former Parent	(710)	2,562
Derivative assets	738	(24,026)
Income tax receivable	1,822	—
Inventories	(63,005)	16,314
Prepaid expenses and other current assets	128	(115)
Accounts payable	27,860	5,816
Derivative liabilities	(5,004)	21,680
Liabilities on borrowed metals	(5,491)	3,289
Accrued liabilities	(1,088)	(2,135)
Income taxes payable	—	(1,794)
Net cash (used in) provided by operating activities	(54,495)	5,634
Cash flows from investing activities:		
Capital expenditures for property and equipment	(189)	(53)
Purchase of cost method investment	—	(1,111)
Secured loans, net	(1,355)	(1,809)
Net cash used in investing activities	(1,544)	(2,973)
Cash flows from financing activities:		
Product financing arrangement, net	10,605	(3,997)
Dividends paid	(349)	—
Borrowings under lines of credit, net	29,900	(7,200)
Net cash provided by (used in) financing activities	40,156	(11,197)
Net decrease in cash and cash equivalents	(15,883)	(8,536)
Cash and cash equivalents, beginning of period	20,927	13,193
Cash and cash equivalents, end of period	$5,044	$4,657
Supplemental disclosures of cash flow information:		
Cash paid during the period for:		
Interest expense	$1,134	$1,003
Income taxes	$—	$2,572
Non-cash investing and financing activities:		

Interest added to principal of secured loans	$26	$91

See accompanying Notes to Condensed Consolidated Financial Statements

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A-MARK PRECIOUS METALS, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

1. DESCRIPTION OF BUSINESS

A-Mark Precious Metals, Inc. and its subsidiaries (“A-Mark” or the “Company”) is a full-service precious metals trading company. Its products include gold, silver, platinum and palladium for storage and delivery primarily in the form of coins, bars, wafers and grain. The Company's trading-related services include financing, consignment, logistics, hedging and various customized financial programs.

Through its wholly owned subsidiary, Collateral Finance Corporation (“CFC”), a licensed California Finance Lender, the Company offers loans on precious metals, rare coins and other collectibles collateral to coin dealers, collectors and investors. Through its wholly owned subsidiary, A-Mark Trading AG (“AMTAG”), the Company promotes A-Mark bullion products throughout the European continent. Transcontinental Depository Services (“TDS”), also a wholly owned subsidiary of the Company, offers worldwide storage solutions to institutions, dealers and consumers.

The Company's wholly-owned subsidiary, A-M Global Logistics, LLC ("Logistics"), operates the Company's logistics fulfillment center based in Las Vegas, Nevada, which began operations in July 2015. Logistics provides our customers an array of complementary services, including storage, shipping, handling, receiving, processing, and inventorying of precious metals and custom coins on a secure basis.

Spinoff from Spectrum Group International, Inc.

On March 14, 2014, the Company's former parent, Spectrum Group International, Inc. ("SGI" or the "Former Parent"), effected a spinoff (the "spinoff" or the "Distribution") of the Company from SGI. As a result of the Distribution, the Company became a publicly traded company independent from SGI. On March 17, 2014, A-Mark’s shares of common stock commenced trading on the NASDAQ Global Select Market under the symbol "AMRK."

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation and Principles of Consolidation

The condensed consolidated financial statements reflect the financial condition, results of operations, and cash flows of the Company, and were prepared using accounting principles generally accepted in the United States (“U.S. GAAP”). The Company operated in one segment for all periods presented.

These condensed consolidated financial statements include the accounts of A-Mark, and its wholly owned subsidiaries, CFC, AMTAG, Logistics and TDS (collectively the “Company”). All significant inter-company accounts and transactions have been eliminated in consolidation.

Unaudited Interim Financial Information

The accompanying interim condensed consolidated financial statements have been prepared by the Company pursuant to the rules and regulations of the Securities and Exchange Commission (the “SEC”) for interim financial reporting. These interim condensed consolidated financial statements are unaudited and, in the opinion of management, include all adjustments (consisting of normal recurring adjustments and accruals) necessary to present fairly the condensed consolidated balance sheets, condensed consolidated statements of income, condensed consolidated statements of stockholders’ equity, and condensed consolidated statements of cash flows for the periods presented in accordance with U.S. GAAP. Operating results for the three months ended September 30, 2015 are not necessarily indicative of the results that may be expected for the year ending June 30, 2016 or for any other interim period during such fiscal year. Certain information and footnote disclosures normally included in annual consolidated financial statements prepared in accordance with U.S. GAAP have been omitted in accordance with the rules and regulations of the SEC. These interim condensed consolidated financial statements should be read in conjunction with the audited consolidated financial statements and notes thereto contained in the Company's Annual Report on Form 10-K for the fiscal year ended June 30, 2015 (the “2015 Annual Report”), as filed with the SEC. Amounts related to disclosure of June 30, 2015 balances within these interim condensed consolidated financial statements were derived from the aforementioned audited consolidated financial statements and notes thereto included in the 2015 Annual Report.

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Reclassifications

Certain previously reported amounts have been reclassified to conform to the current fiscal quarter's condensed consolidated financial statement presentation. In the previous reported periods, account receivables included secured loans and derivative assets; these components are shown as separate lines items on the condensed consolidated balance sheets and cash flow statements. Similarly, accounts payables included derivative liabilities; these components are shown as separate lines items on the condensed consolidated balance sheets and cash flow statements.

Use of Estimates

The preparation of condensed consolidated financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the condensed consolidated financial statements, and the reported amounts of revenue and expenses during the reporting periods. These estimates include, among others, determination of fair value, and allowances for doubtful accounts, impairment assessments of long-lived assets and intangible assets, valuation reserve determination on deferred tax assets, and revenue recognition judgments. Significant estimates also include the Company's fair value determination with respect to its financial instruments and precious metals materials. Actual results could materially differ from these estimates.

Concentration of Credit Risk

Cash is maintained at financial institutions and, at times, balances may exceed federally insured limits. The Company has never experienced any losses related to these balances.

Assets that potentially subject the Company to concentrations of credit risk consist principally of receivables, loans of inventory to customers, and inventory hedging transactions. Concentration of credit risk with respect to receivables is limited due to the large number of customers composing the Company's customer base, the geographic dispersion of the customers, and the collateralization of substantially all receivable balances. Based on an assessment of credit risk, the Company typically grants collateralized credit to its customers. The Company enters into inventory hedging transactions, principally utilizing metals commodity futures contracts traded on national futures exchanges or forward contracts with credit worthy financial institutions. Credit risk with respect to loans of inventory to customers is minimal; substantially all inventories loaned under consignment arrangements are collateralized for the benefit of the Company. All of our commodity derivative contracts are under master netting arrangements and include both asset and liability positions. Substantially all of these transactions are secured by the underlying metals positions.

Foreign Currency

The functional currency of the Company is the United States dollar ("USD"). Also, the functional currency of the Company's wholly-owned foreign subsidiary, AMTAG, is USD, but it maintains its books of record in Euros. The Company remeasures the financial statements of AMTAG into USD. The remeasurement of local currency amounts into USD creates remeasurement gains and losses, which are included in the condensed consolidated statements of income.

To manage the effect of foreign currency exchange fluctuations, the Company utilizes foreign currency forward contracts. These derivatives generate gains and losses when they are settled and/or when they are marked to market. The change in the value in the derivative instruments is shown on the face of the condensed consolidated statements of income as unrealized net gains (losses) on foreign exchange.

Cash Equivalents

The Company considers all highly liquid investments with original maturities of three months or less, when purchased, to be cash equivalents.

Inventories

Inventories principally include bullion and bullion coins and are acquired and initially recorded at fair market value. The fair market value of the bullion and bullion coins is comprised of two components: (1) published market values attributable to the costs of the raw precious metal, and (2) a published premium paid at acquisition of the metal. The premium is attributable to the additional value of the product in its finished goods form and the market value attributable solely to the premium may be readily determined, as it is published by multiple reputable sources.

The Company’s inventories, except for certain lower of cost or market basis products (as discussed below), are subsequently recorded at their fair market values, that is, "marked-to-market". The daily changes in the fair market value of our inventory are offset by daily changes in the fair market value of hedging derivatives that are taken with respect to our inventory positions; both the change in the fair market value of the inventory and the change in the fair market value of these derivative instruments are recorded in cost of sales in the condensed consolidated statements of income.

While the premium component included in inventories is marked-to-market, our commemorative coin inventory, including its premium component, is held at the lower of cost or market, because the value of commemorative coins is influenced more by supply and demand determinants than on the underlying spot price of the precious metal content of the commemorative coins. Unlike our bullion coins, the value of commemorative coins is not subject to the same level of volatility as bullion coins because our commemorative coins typically carry a substantially higher premium over the spot metal price than bullion coins. Neither the commemorative coin inventory nor the premium component of our inventory is hedged (see Note 6.)

Property and Equipment and Depreciation

Property and equipment is stated at cost less accumulated depreciation. Depreciation is calculated using a straight line method based on the estimated useful lives of the related assets, ranging from three years to five years.

Goodwill and Purchased Intangible Assets

Goodwill is recorded when the purchase price paid for an acquisition exceeds the estimated fair value of the net identified tangible and intangible assets acquired.

Goodwill and other indefinite life intangibles are evaluated for impairment annually in the fourth quarter of the fiscal year (or more frequently if indicators of potential impairment exist) in accordance with the Intangibles - Goodwill and Other Topic 350 of the Accounting Standards Codification ("ASC".) Other purchased intangible assets continue to be amortized over their useful lives and are evaluated for impairment when events or changes in business circumstances indicate that the carrying amount of the assets may not be recoverable. The Company may first qualitatively assess whether relevant events and circumstances make it more likely than not that the fair value of the reporting unit's goodwill is less than its carrying value. If, based on this qualitative assessment, management determines that goodwill is more likely than not to be impaired, the two-step impairment test is performed. This first step in this test includes comparing the fair value of each reporting unit to its carrying value, including goodwill. If the carrying amount of a reporting unit exceeds its fair value, the second step in the test is performed, which is measurement of the impairment loss. The impairment loss is calculated by comparing the implied fair value of goodwill, as if the reporting unit has been acquired in a business combination, to its carrying amount. As of September 30, 2015 and June 30, 2015, the Company had no impairments.

If the Company determines it will quantitatively assess impairment, the Company utilizes the discounted cash flow method to determine the fair value of each of its reporting units. In calculating the implied fair value of the reporting unit's goodwill, the present value of the reporting unit's expected future cash flows is allocated to all of the other assets and liabilities of that unit based on their fair values. The excess of the present value of the reporting unit's expected future cash flows over the amount assigned to its other assets and liabilities is the implied fair value of goodwill. In calculating the implied value of the Company's trade names, the Company uses the present value of the relief from royalty method.

Amortizable intangible assets are being amortized on a straight-line basis which approximates economic use, over periods ranging from four years to fifteen years. The Company considers the useful life of the trademarks to be indefinite. The Company tests the value of the trademarks and trade name annually for impairment.

Long-Lived Assets

Long-lived assets, other than goodwill and purchased intangible assets with indefinite lives are evaluated for impairment when events or changes in business circumstances indicate that the carrying amount of the assets may not be recoverable. In evaluating impairment, the carrying value of the asset is compared to the undiscounted estimated future cash flows expected to result from the use of the asset and its eventual disposition. An impairment loss is recognized when estimated future cash flows are less than the carrying amount. Estimates of future cash flows may be internally developed or based on independent appraisals and significant judgment is applied to make the estimates. Changes in the Company's strategy, assumptions and/or market conditions could significantly impact these judgments and require adjustments to recorded amounts of long-lived assets. As of September 30, 2015 and June 30, 2015, management concluded that an impairment was not required.

Investments

Investments into noncontrolled entities that do not have readily determinable fair values (i.e., non-marketable equity securities) under Cost Method Investments Topic 325-20 of the ASC are initially recorded at cost. Income is recorded for dividends received that are distributed from net accumulated earnings of the noncontrolled entity subsequent to the date of investment. Dividends received in excess of earnings subsequent to the date of investment are considered a return of investment and are recorded as reductions in the cost of the investment. Investments are written down only when there is clear evidence that a decline in value that is other than temporary has occurred. The Company assesses all cost-method investments for impairment quarterly. Below is a summary of the Company's cost-method investments.

On February 18, 2014, the Company purchased 2.5% of issued and outstanding Class A common stock of a nonpublic company, who is a customer of A-Mark, for $0.5 million. On September 19, 2014, the Company entered into an agreement with a separate nonpublic company, also a customer of A-Mark, to purchase up to 9% of its issued and outstanding common stock, on a fully diluted basis, in two tranches, for an aggregate purchase price of $2.0 million. The closing of the first tranche of the second transaction, for 5% of the retailer's issued and outstanding common stock at a purchase price equal to $1.1 million, took place on

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September 19, 2014. The closing of the second tranche of the second transaction, for 4% of this company's issued and outstanding common stock took place on April 1, 2015, at a purchase price equal to $0.9 million.

In connection with both transactions, the Company entered into exclusive supplier agreements, pursuant to which the customers will purchase all bullion products required for their respective businesses exclusively from A-Mark for a period of 5.0 years and 3.0 years, respectively (subject to renewal and earlier termination under certain circumstances). In the case of the second transaction, A-Mark will continue to provide fulfillment services to this customer under the terms of a previously existing fulfillment agreement. The Company initially had the right to appoint, and did appoint, a board member to each customer's boards of directors. During the fourth quarter of fiscal 2015, the operative agreements were amended to provide that the Company has the right instead to designate a board observer, who is entitled to attend, in a nonvoting observer capacity, all meetings of each company's board of directors and all committees thereof. Also during the fourth quarter of fiscal 2015, the Company's former board designee resigned as a member of both boards of directors.

As of September 30, 2015, the aggregate carrying amount of the Company’s cost-method investments was $2.5 million. There were no identifiable events or changes in circumstances that may have had a significant adverse effect on the fair value. As a result, no impairment loss was recorded, nor were any dividends received during the three months ended September 30, 2015 and 2014.

On October 26, 2015, the Company entered into an amended and restated agreement with one of its customers, an online retailer of generic gold and silver coins and bullion, to increase the Company's ownership of the retailer's outstanding common stock from 9% to up to 20% on a fully diluted basis (see Note 18.)

Fair Value Measurement

The Fair Value Measurements and Disclosures Topic 820 of the ASC ("ASC 820"), creates a single definition of fair value for financial reporting. The rules associated with ASC 820 state that valuation techniques consistent with the market approach, income approach and/or cost approach should be used to estimate fair value. Selection of a valuation technique, or multiple valuation techniques, depends on the nature of the asset or liability being valued, as well as the availability of data (see Note 3.)

Revenue Recognition

Revenues are recognized when persuasive evidence of an arrangement exists, delivery has occurred, the price is fixed or determinable, no obligations remain and collection is probable. The Company records sales of precious metals, which occurs upon receipt by the customer. The Company records revenues from its metal assaying and melting services after the related services are completed and the effects of forward sales contracts are reflected in revenue at the date the related precious metals are delivered or the contracts expire. The Company records revenues from its storage and logistics services after the related services are completed.

The Company accounts for its metals and sales contracts using settlement date accounting. Pursuant to such accounting, the Company recognizes the sale or purchase of the metals at settlement date. During the period between trade and settlement date, the Company has essentially entered into a forward contract that meets the definition of a derivative in accordance with the Derivatives and Hedging Topic 815 of the ASC. The Company records the derivative at the trade date with a corresponding unrealized gain (loss), which is reflected in the cost of sales in the condensed consolidated statements of income. The Company adjusts the derivatives to fair value on a daily basis until the transaction is physically settled. Sales which are physically settled are recognized at the gross amount in the condensed consolidated statements of income.

Interest Income

The Company uses the effective interest method to recognize interest income on its secured loans transactions. For these arrangements, the Company maintains a security interest in the precious metals and records interest income over the terms of the receivable. Recognition of interest income is suspended and the loan is placed on non-accrual status when management determines that collection of future interest income is not probable. The interest income accrual is resumed, and previously suspended interest income is recognized, when the loan becomes contractually current and/or collection doubts are removed. Cash receipts on impaired loans are recorded first against the receivable and then to any unrecognized interest income (see Note 5.)

Interest Expense

The Company incurs interest expense and related fees as a result of usage under its lines of credit, product financing arrangements and liability on borrowed metals.

The Company incurs interest expense based on usage under its Trading Credit Facility recording interest expense using the effective interest method.

The Company incurs financing fees (classified as interest expense) as a result of its product financing arrangements for the transfer and subsequent re-acquisition of gold and silver at a fixed price to a third party finance company. During the term of this type of financing agreement, a third party finance company holds the Company's inventory as collateral, with the intent to return the inventory to the Company at an agreed-upon price based on the spot price on the finance arrangement termination date, pursuant to the guidance in Product Financing Arrangements Topic 470-40 of the ASC. The third party charges a monthly fee as a percentage of the market value of the outstanding obligation. In addition, the Company incurs a financing fee related to custodial storage facility charges related to the transferred collateral inventory; this collateral is classified as restricted inventory on our condensed consolidated balance sheets.

Additionally, the Company incurs interest expense when we borrow precious metals from our suppliers under short-term arrangements, which bear interest at a designated rate. Amounts under these arrangements are due at maturity and require repayment either in the form of precious metals or cash. This liability is reflected in the condensed consolidated balance sheet as a liability on borrowed metals.

Derivative Instruments

The Company’s inventory, purchase and sale commitments transactions consist of precious metals bearing products. The value of our inventory and these commitments is intimately linked to the prevailing price of the underlying precious metal commodity. The Company seeks to minimize the effect of price changes of the underlying commodity and enters into inventory hedging transactions, principally utilizing metals commodity futures contracts traded on national futures exchanges or forward contracts with only major credit worthy financial institutions. All of our commodity derivative contracts are under master netting arrangements and include both asset and liability positions. Substantially all of these transactions are secured by the underlying metals positions. Notional balances of the Company's derivative instruments, consisting of contractual metal quantities, are expressed at current spot prices of the underlying precious metal commodity.

Commodity futures and forward contract transactions are recorded at fair value on the trade date. The difference between the original contract value and the market value of the open futures and forward contracts are reflected in derivative assets or derivative liabilities in the condensed consolidated balance sheet at fair value.

The Company records the change between market value and trade value of the underlying open commodity contracts as a derivative asset or liability, and the Company correspondingly records the related unrealized gains or losses. The change in unrealized gain (loss) on open commodity contracts from one period to the next is reflected in net gain (loss) on derivative instruments. These unrealized gains and losses are included as a component of cost of sales on the condensed consolidated statements of income. Gains or losses resulting from the termination of commodity contracts are reported as realized gains or losses on commodity contracts, which is recorded as a component of cost of sales on the condensed consolidated statements of income.

The Company enters into derivative transactions solely for the purpose of hedging our inventory holding risk, and not for speculative market purposes. The Company’s gains (losses) on derivative instruments are substantially offset by the changes in the fair market value of the underlying precious metals inventory, which is also recorded in cost of sales in the condensed consolidated statements of income (see Note 10.)

Advertising

Advertising costs are expensed as incurred, and are included in selling, general and administrative expenses in the condensed consolidated statements of income. Advertising expense was $0.2 million and $0.1 million, respectively, for the three months ended September 30, 2015 and 2014.

Shipping and Handling Costs

Shipping and handling costs represent costs associated with shipping product to customers, and receiving product from vendors and are included in cost of sales in the condensed consolidated statements of income. Shipping and handling costs incurred totaled $2.3 million and $1.5 million, respectively, for the three months ended September 30, 2015 and 2014.

Share-Based Compensation

The Company accounts for equity awards under the provisions of the Compensation - Stock Compensation Topic 718 of the ASC ("ASC 718"), which establishes fair value-based accounting requirements for share-based compensation to employees. ASC 718 requires the Company to recognize the grant-date fair value of stock options and other equity-based compensation issued to employees as expense over the service period in the Company's condensed consolidated financial statements.

Income Taxes

As part of the process of preparing its condensed consolidated financial statements, the Company is required to estimate its provision for income taxes in each of the tax jurisdictions in which it conducts business, in accordance with the Income Taxes Topic 740 of the ASC ("ASC 740"). The Company computes its annual tax rate based on the statutory tax rates and tax planning opportunities available to it in the various jurisdictions in which it earns income. Significant judgment is required in determining the Company's annual tax rate and in evaluating uncertainty in its tax positions. The Company recognizes a benefit for tax positions that it believes will more likely than not be sustained upon examination. The amount of benefit recognized is the largest amount of benefit that the Company believes has more than a 50% probability of being realized upon settlement. The Company regularly monitors its tax positions and adjusts the amount of recognized tax benefit based on its evaluation of information that has become available since the end of its last financial reporting period. The annual tax rate includes the impact of these changes in recognized tax benefits. When adjusting the amount of recognized tax benefits, the Company does not consider information that has become

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available after the balance sheet date, but does disclose the effects of new information whenever those effects would be material to the Company's condensed consolidated financial statements. The difference between the amount of benefit taken or expected to be taken in a tax return and the amount of benefit recognized for financial reporting represents unrecognized tax benefits. These unrecognized tax benefits are presented in the condensed consolidated balance sheet principally within accrued liabilities.

The Company records valuation allowances to reduce deferred tax assets to the amount that is more likely than not to be realized. Significant judgment is applied when assessing the need for valuation allowances. Areas of estimation include the Company's consideration of future taxable income and ongoing prudent and feasible tax planning strategies. Should a change in circumstances lead to a change in judgment about the utilization of deferred tax assets in future years, the Company would adjust related valuation allowances in the period that the change in circumstances occurs, along with a corresponding increase or charge to income. Changes in recognized tax benefits and changes in valuation allowances could be material to the Company's results of operations for any period, but is not expected to be material to the Company's condensed consolidated financial position.

The Company accounts for uncertainty in income taxes under the provisions of ASC 740. These provisions clarify the accounting for uncertainty in income taxes recognized in an enterprise's financial statements, and prescribe a recognition threshold and measurement criteria for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. The provisions also provide guidance on de-recognition, classification, interest, and penalties, accounting in interim periods, disclosure, and transition. The potential interest and/or penalties associated with an uncertain tax position are recorded in provision for income taxes on the condensed consolidated statements of income. Please refer to Note 11 for further discussion regarding these provisions.

Income taxes are accounted for using an asset and liability approach that requires the recognition of deferred tax assets and liabilities for the expected future tax consequences of events that have been included in the financial statements. Under this method, deferred tax assets and liabilities are determined based on the differences between the financial statement and tax basis of assets and liabilities using enacted tax rates in effect for the year in which the differences are expected to reverse. The effect of a change in tax rates on deferred tax assets and liabilities is recognized in income in the period that includes the enactment date. A valuation allowance is provided when it is more likely than not that some portion or all of the net deferred tax assets will not be realized. The factors used to assess the likelihood of realization include the Company's forecast of the reversal of temporary differences, future taxable income and available tax planning strategies that could be implemented to realize the net deferred tax assets. Failure to achieve forecasted taxable income in applicable tax jurisdictions could affect the ultimate realization of deferred tax assets and could result in an increase in the Company's effective tax rate on future earnings.

Based on our assessment it appears more likely than not that most of the net deferred tax assets will be realized through future taxable income. Management has established a valuation allowance against the deferred taxes related to certain state net operating loss carryovers. Management believes the utilization of these losses may be limited. We will continue to assess the need for a valuation allowance for our remaining deferred tax assets in the future.

The Company's condensed consolidated financial statements recognized the current and deferred income tax consequences that result from the Company's activities during the current and preceding periods, as if the Company were a separate taxpayer prior to the date of the Distribution rather than a member of the consolidated income tax return group of its former parent, Spectrum Group International, Inc. Following its spin-off, the Company files federal and state income tax filings that are separate from the Former Parent's tax filings. The Company recognizes current and deferred income taxes as a separate taxpayer for periods ending after the date of Distribution.

Income taxes receivable from Former Parent reflects balances due from the Former Parent for the Company's share of the income tax assets of the group, net of amounts related to federal and state jurisdictions due to taxable income generated as if the Company were a separate taxpaying entity prior to the Distribution.

Earnings per Share ("EPS")

The Company computes and reports both basic EPS and diluted EPS. Basic EPS is computed by dividing net earnings by the weighted average number of common shares outstanding for the period. Diluted EPS is computed by dividing net earnings by the sum of the weighted average number of common shares and dilutive common stock equivalents outstanding during the period. Diluted EPS reflects the total potential dilution that could occur from outstanding equity awards, including unexercised stock options, utilizing the treasury stock method.

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A reconciliation of shares used in calculating basic and diluted earnings per common shares follows. There is no dilutive effect of stock appreciation rights ("SARs"), as such obligations are not settled and were out of the money for the three months ended September 30, 2015 and 2014.
in thousands

	Three Months Ended	
	September 30, 2015	September 30, 2014
Basic weighted average shares outstanding [(1)]	6,974	6,963
Effect of common stock equivalents — stock issuable under outstanding equity awards	85	103
Diluted weighted average shares outstanding	7,059	7,066

(1) Basic weighted average shares outstanding include the effect of vested but unissued restricted stock grants.

Recent Accounting Pronouncements

In February 2015, the FASB issued Accounting Standards Update ("ASU") No. 2015-2, Consolidation (Topic 820): Amendments to the Consolidation Analysis. ASU 2015-2 provides a revised consolidation model for all reporting entities to use in evaluating whether they should consolidate certain legal entities. All legal entities will be subject to reevaluation under this revised consolidation model. The revised consolidation model, among other things, (i) modifies the evaluation of whether limited partnerships and similar legal entities are VIEs or voting interest entities, (ii) eliminates the presumption that a general partner should consolidate a limited partnership, and (iii) modifies the consolidation analysis of reporting entities that are involved with VIEs through fee arrangements and related party relationships. ASU 2015-2 is effective for fiscal years, and interim reporting periods within those fiscal years, beginning after December 15, 2015, which will be our fiscal year 2017 (or July 1, 2016). We are still evaluating what impact, if any, this ASU will have on the Company’s consolidated financial position, results of operations or cash flows.

In November 2014, the FASB issued ASU No. 2014-16, Derivatives and Hedging (Topic 815): Determining Whether the Host Contract in a Hybrid Financial Instrument Issued in the Form of a Share is More Akin to Debt or to Equity. ASU No. 2014-16 clarifies how current guidance should be interpreted in evaluating the economic characteristics and risks of a host contract in a hybrid financial instrument that is issued in the form of a share. In addition, ASU No. 2014-16 clarifies that in evaluating the nature of a host contract, an entity should assess the substance of the relevant terms and features (that is, the relative strength of the debt-like or equity-like terms and features given the facts and circumstances) when considering how to weight those terms and features. The effects of initially adopting ASU No. 2014-16 should be applied on a modified retrospective basis to existing hybrid financial instruments issued in a form of a share as of the beginning of the fiscal year for which the amendments are effective. Retrospective application is permitted to all relevant prior periods. ASU No. 2014-16 is effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2015, which will be our fiscal year 2017 (or July 1, 2016). Early adoption is permitted. We are still evaluating what impact, if any, this ASU will have on the Company’s consolidated financial position, results of operations or cash flows and related disclosures.

In May 2014, the FASB issued ASU No. 2014-09, Revenue from Contracts with Customers (Topic 606), which supersedes nearly all existing revenue recognition guidance under U.S. GAAP. The core principle of ASU No. 2014-09 is to recognize revenues when promised goods or services are transferred to customers in an amount that reflects the consideration to which an entity expects to be entitled for those goods or services. ASU No. 2014-09 defines a five step process to achieve this core principle and, in doing so, more judgment and estimates may be required within the revenue recognition process than are required under existing U.S. GAAP. In August 2015, the FASB issued ASU No. 2015-14, Revenue from Contracts with Customers (Topic 606): Deferral of the Effective Date, which defers the effective date of ASU 2014-09 for one year. With the deferral, the new standard is effective for the Company, on July 1, 2018, with early adoption permitted one year prior. The standard permits the use of either the retrospective or cumulative effect transition method. We are still evaluating what impact this standard will have on the

Company's consolidated financial position, results of operations or cash flows and related disclosures.

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3. ASSETS AND LIABILITIES, AT FAIR VALUE

Fair Value of Financial Instruments

The following table presents the carrying amounts and estimated fair values of the Company's financial instruments as of September 30, 2015 and June 30, 2015.

in thousands

	September 30, 2015		June 30, 2015	
	Carrying Amount	Fair value	Carrying Amount	Fair value
Financial assets:				
Cash	$5,044	$5,044	$20,927	$20,927
Receivables, and advances, net	47,899	47,899	30,025	30,025
Secured loans	50,416	50,416	49,316	49,316
Derivative assets - open sale and purchase commitments, net	7,508	7,508	1,722	1,722
Derivative assets - futures contracts	2,842	2,842	5,363	5,363
Derivative assets - forward contracts	276	276	4,279	4,279
Income taxes receivable from Former Parent	1,095	1,095	1,095	1,095
Financial liabilities:				
Lines of credit	$176,900	$176,900	$147,000	$147,000
Liability for borrowed metals	4,009	4,009	9,500	9,500
Product financing obligation	50,030	50,030	39,425	39,425
Derivative liabilities - liability on margin accounts	6,367	6,367	6,908	6,908
Derivative liabilities - open sale and purchase commitments, net	6,183	6,183	10,989	10,989
Derivative liabilities - forward contracts	343	343	—	—
Accounts payable, advances and other payables	78,499	78,499	50,639	50,639
Accrued liabilities	4,242	4,242	5,330	5,330

The fair values of the financial instruments shown in the above table as of September 30, 2015 and June 30, 2015 represent the amounts that would be received to sell those assets or that would be paid to transfer those liabilities in an orderly transaction between market participants at that date. Those fair value measurements maximize the use of observable inputs. However, in situations where there is little, if any, market activity for the asset or liability at the measurement date, the fair value measurement reflects the Company's own judgments about the assumptions that market participants would use in pricing the asset or liability. Those judgments are developed by the Company based on the best information available in the circumstances, including expected cash flows and appropriately risk adjusted discount rates, available observable and unobservable inputs.

The carrying amounts of cash and cash equivalents, secured loans, accounts receivable, consignor advances, accounts payable and accrued liabilities approximated fair value due to their short-term nature. The carrying amounts of derivative assets and derivative liabilities are marked-to-market on a daily basis to fair value. The carrying amounts of lines of credit approximate fair value based on the borrowing rates currently available to the Company for bank loans with similar terms and average maturities.

Valuation Hierarchy

Topic 820 of the ASC established a three-level valuation hierarchy for disclosure of fair value measurements. The valuation hierarchy is based upon the transparency of inputs to the valuation of an asset or liability as of the measurement date. The three levels are defined as follows:

- Level 1 - inputs to the valuation methodology are quoted prices (unadjusted) for identical assets or liabilities in active markets.
- Level 2 - inputs to the valuation methodology include quoted prices for similar assets and liabilities in active markets, and inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the financial instrument.
- Level 3 - inputs to the valuation methodology are unobservable and significant to the fair value measurement.

The significant assumptions used to determine the carrying value and the related fair value of the financial instruments are described below:

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Inventory. Inventories principally include bullion and bullion coins and are acquired and initially recorded at fair market value. The fair market value of the bullion and bullion coins is comprised of two components: 1) published market values attributable to the costs of the raw precious metal, and 2) a published premium paid at acquisition of the metal. The premium is attributable to the additional value of the product in its finished goods form and the market value attributable solely to the premium is readily determined, as it is published by multiple reputable sources. Except for commemorative coin inventory, which are included in inventory at the lower of cost or market, the Company's inventories are subsequently recorded at their fair market values on a daily basis. The fair value for commodities inventory (i.e., inventory excluding commemorative coins) is determined using pricing and data derived from the markets on which the underlying commodities are traded. Precious metals commodities inventory are classified in Level 1 of the valuation hierarchy.

Derivatives. Futures contracts, forward contracts and open sale and purchase commitments are valued at their fair values, based on the difference between the quoted market price and the contractual price (i.e., intrinsic value,) and are included within Level 1 of the valuation hierarchy.

Margin and Borrowed Metals Liabilities. Margin and borrowed metals liabilities consist of the Company's commodity obligations to margin customers and suppliers, respectively. Margin liabilities and borrowed metals liabilities are carried at fair value, which is determined using quoted market pricing and data derived from the markets on which the underlying commodities are traded. Margin and borrowed metals liabilities are classified in Level 1 of the valuation hierarchy.

Product Financing Obligations. Product financing obligations consist of financing agreements for the transfer and subsequent re-acquisition of the sale of gold and silver at a fixed price to a third party. Such transactions allow the Company to repurchase this inventory at an agreed-upon price based on the spot price on the repurchase date. The third party charges monthly interest as a percentage of the market value of the outstanding obligation, which is carried at fair value. The obligation is stated at the amount required to repurchase the outstanding inventory. Fair value is determined using quoted market pricing and data derived from the markets on which the underlying commodities are traded. Product financing obligations are classified in Level 1 of the valuation hierarchy.

The following tables present information about the Company's assets and liabilities measured at fair value on a recurring basis as of September 30, 2015 and June 30, 2015 aggregated by the level in the fair value hierarchy within which the measurements fall:

	September 30, 2015			
in thousands	Quoted Price in Active Markets for Identical Instruments (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total Balance
Assets:				
Inventory [1]	$254,343	$—	$—	$254,343
Derivative assets — open sale and purchase commitments, net	7,508	—	—	7,508
Derivative assets — futures contracts	2,842	—	—	2,842
Derivative assets — forward contracts	276	—	—	276
Total assets valued at fair value	$264,969	$—	$—	$264,969
Liabilities:				
Liability on borrowed metals	$4,009	$—	$—	$4,009
Product financing arrangement	50,030	—	—	50,030
Derivative liabilities — Liability on margin accounts	6,367	—	—	6,367
Derivative liabilities — open sales and purchase commitments, net	6,183	—	—	6,183
Derivative liabilities — forward contracts	343	—	—	343

Total liabilities, valued at fair value	$66,932	$—	$—	$66,932

(1) Commemorative coin inventory totaling $0.2 million is held at lower of cost or market and is thus excluded from this table.

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in thousands	June 30, 2015 Quoted Price in Active Markets for Identical Instruments (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total Balance
Assets:				
Inventory [(1)]	$189,983	$—	$—	$189,983
Derivative assets — open sale and purchase commitments, net	1,722	—	—	1,722
Derivative assets — futures contracts	5,363	—	—	5,363
Derivative assets — forward contracts	4,279	—	—	4,279
Total assets, valued at fair value	$201,347	$—	$—	$201,347
Liabilities:				
Liability on borrowed metals	$9,500	$—	$—	$9,500
Product financing arrangement	39,425	—	—	39,425
Derivative liabilities — Liability on margin accounts	6,908	—	—	6,908
Derivative liabilities — open sale and purchase commitments, net	10,989	—	—	10,989
Total liabilities valued at fair value	$66,822	$—	$—	$66,822

[(1)] Commemorative coin inventory totaling $1.5 million is held at lower of cost or market and is thus excluded from this table.

There were no transfers in or out of Level 2 or 3 during the three months ended September 30, 2015.

Assets Measured at Fair Value on a Non-Recurring Basis

Certain assets are measured at fair value on a nonrecurring basis. These assets are not measured at fair value on an ongoing basis but are subject to fair value adjustments only under certain circumstances. These include cost method investments that are written down to fair value when their declines are determined to be other-than-temporary, and long-lived assets or goodwill that are written down to fair value when they are held for sale or determined to be impaired.

The Company uses level-three inputs to measure the fair value of its cost method investments on a non-recurring basis. The Company's investments in ownership interests in noncontrolled entities do not have readily determinable fair values and were recorded at cost, $2.5 million, in aggregate. Quoted prices of the investments are not available, and the cost of obtaining an independent valuation appears excessive considering the materiality of the instruments to the Company. There were no gains or losses recognized in earnings associated with the Company's ownership interests in these noncontrolled entities during the three months ended September 30, 2015.

The Company uses level-three inputs to measure the fair value of goodwill and other intangibles on a non-recurring basis. These assets are measured at cost and are written down to fair value on the annual measurement dates or on the date of a triggering event, if impaired. As of September 30, 2015, there were no indications present that the Company's goodwill or other purchased intangibles were impaired, and therefore were not measured at fair value. There were no gains or losses recognized in earnings associated with the above purchased intangibles during the three months ended September 30, 2015.

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4. RECEIVABLES

Receivables consist of the following as of September 30, 2015 and June 30, 2015:
in thousands

	September 30, 2015	June 30, 2015
Customer trade receivables	$11,194	$11,835
Wholesale trade advances	26,810	12,164
Due from brokers	9,925	6,056
Subtotal	47,929	30,055
Less: allowance for doubtful accounts	(30)	(30)
Receivables, net	$47,899	$30,025

Customer trade receivables. Customer trade receivables represent short-term, non-interest bearing amounts due from precious metal sales and are secured by the related precious metals stored with the Company, a letter of credit issued on behalf of the customer, or other secured interests in assets of the customer.

Wholesale trade advances. Wholesale trade advances represent advances of various bullion products and cash advances to customers. Typically, these advances are: unsecured, short-term, and non-interest bearing, which are made to wholesale metals dealers and government mints.

Due from brokers. Due from brokers principally consists of the margin requirements held at brokers related to open futures contracts (see Note 10).

Allowance for Doubtful Accounts

Allowances for doubtful accounts are recorded based on specifically identified receivables, which the Company has identified as potentially uncollectible. A summary of the activity in the allowance for doubtful accounts is as follows:
in thousands

Period ended:	Beginning Balance	Provision	Charge-off	Ending Balance
Quarter Ended September 30, 2015	$30	$—	$—	$30
Year Ended June 30, 2015	$30	$—	$—	$30

5. SECURED LOANS RECEIVABLES

Below is a summary of the carrying-value of our secured loans as of September 30, 2015 and June 30, 2015:
in thousands

	September 30, 2015		June 30, 2015	
Secured loans originated	$35,564		$36,778	
Secured loans originated - with a related party	716		—	
	36,280		36,778	
Secured loans acquired	14,136	(1)	12,538	(2)
Secured loans, total	$50,416		$49,316	

(1) Includes $99,000 of amortized loan premium as of September 30, 2015.

(2) Includes $99,000 of amortized loan premium as of June 30, 2015.

Secured loans - originated: Secured loans include short-term loans, which include a combination of on-demand lines and short term facilities, and long-term loans that are made to our customers (i.e., originated secured loans). These loans are fully secured by the customers' assets that include bullion, numismatic and semi-numismatic material, which are typically held in safekeeping by the Company. (See Note 12, for further information regarding our secured loans made to related parties.)

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Secured loans - acquired: Secured loans also include short-term loans, which include a combination of on-demand lines and short term facilities that are purchased from our customers. The Company acquires a portfolio of their loan receivables at price that approximates the aggregate carrying-value of the each loan in the portfolio, as determined on the effective transaction date. Each loan in the portfolio is fully secured by the borrowers' assets, which include bullion, numismatic and semi-numismatic material that are held in safekeeping by the Company. Typically, our customer retains the responsibility for the servicing and administration of the loans.

As of September 30, 2015 and June 30, 2015, our secured loans carried weighted-average effective interest rates of 8.4% and 8.5%, respectively, and mature in periods generally ranging from on-demand to two years.

The secured loans that the Company generates with active customers of A-Mark are reflected as an operating activity on the condensed consolidated statements of cash flows. The secured loans that the Company generates with borrowers who are not active customers of A-Mark are reflected as an investing activity on the condensed consolidated statements of cash flows as secured loans, net. For the secured loans that are reflected as an investing activity and have terms that allow the borrower to increase their loan balance (at the discretion of the Company) based on the excess value of their collateral compared to their aggregate principal balance of loan and are repayable on demand or in the short-term, the borrowings and repayments are netted on the condensed consolidated statements of cash flows. In contrast, for the secured loans that are reflected as an investing activity and do not contain a revolving credit-line feature or have long-term maturities, the borrowed funds are shown at gross as other originated secured loans, segregated from the repayments of the principal, which are shown as principal collections on other originated secured loans on the condensed consolidated statements of cash flows.

Credit Quality of Secured Loans Receivables and Allowance for Credit Losses

The Company applies a systematic methodology to determine the allowance for credit losses for secured loan receivables. The secured loan receivables portfolio is comprised solely of secured loans with similar risk profiles. This similarity allows the Company to apply a standard methodology to determine the credit quality for each loan. The credit quality of each loan is generally determined by the secured material, the initial and ongoing collateral value determination and the assessment of loan to value determination. Typically, the Company's secured loan receivables within its portfolio have similar credit risk profiles and methods for assessing and monitoring credit risk.

The Company evaluates its loan portfolio in one of three classes of secured loan receivables: those loans secured by: 1) bullion 2) numismatic items and 3) customers' pledged assets, which may include bullion and numismatic items. The Company's secured loans by portfolio class, which align with management reporting, are as follows:

in thousands

	September 30, 2015			June 30, 2015		
Bullion	$17,121	34.0	%	$16,250	33.0	%
Numismatic and semi numismatic	32,445	64.3		32,216	65.3	
Subtotal	49,566	98.3		48,466	98.3	
Other pledged assets[1]	850	1.7		850	1.7	
Total secured loans	$50,416	100.0	%	$49,316	100.0	%

(1) Includes secured loans that are collateralized by borrower's assets, which are not exclusively precious metal products.

Each of the three classes of receivables have the same initial measurement attribute and a similar method for assessing and monitoring credit risk. The methodology of assessing the credit quality of the secured loans acquired by the Company is similar to the secured loans originated loans by the Company; they are administered using the same internal reporting system, collateralized by precious metals or other pledged assets, for which a loan to value determination procedures are applied.

Credit Quality of Loans and Non Performing Status

Generally, interest is due and payable within 30 days. A loan is considered past due if interest is not paid in 30 days or collateral calls are not met timely. Typically, loans do not achieve the threshold of non performing status due to the fact that customers are generally put into default for any interest past due over 30 days and for unsatisfied collateral calls. When this occurs the loan collateral is typically liquidated within 90 days.

For certain secured loans, interest is billed monthly and, if not paid, is added to the outstanding loan balance. These secured loans are considered past due if their current loan-to-value ratio fails to meet established minimum equity levels, and the borrower fails to meet the collateral call required to reestablish the appropriate loan to value ratio. Non-performing loans have the highest probability for credit loss. The allowance for credit losses attributable to non-performing loans is based on the most probable source of repayment, which is normally the liquidation of collateral. In determining collateral value, the Company estimates the current market value of the collateral and considers credit enhancements such as

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additional collateral and third-party guarantees. Due to the accelerated liquidation terms of the Company's loan portfolio, all past due loans are generally liquidated within 90 days of default.

Further information about the Company's credit quality indicators includes differentiating by categories of current loan-to-value ratios. The Company disaggregates its secured loans that are collateralized by precious metal products, as follows:

in thousands

	September 30, 2015			June 30, 2015		
Loan-to-value of 75% or more [1]	$27,418	55.3	%	$17,153	35.4	%
Loan-to-value of less than 75% [1]	22,148	44.7		31,313	64.6	
Secured loans collateralized by precious metal products [1]	$49,566	100.0	%	$48,466	100.0	%

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(1) Excludes secured loans that are collateralized by borrower's assets, which are not exclusively precious metal products.

The Company had three loans with a loan-to-value ratio in excess of 100% at September 30, 2015; the aggregate balance of these loans totaled $227,000 or 0.5% of the secured loan balance. At June 30, 2015, the Company had one loan with a loan-to-value ratio in excess of 100%, the aggregate balance of this loan totaled $175,600 or 0.4% of the secured loan balance. The primary reason for the increase in the loan-to-value ratio of 75% or more from June 30, 2015 to September 30, 2015 was the decline in the value of the underlying precious metal products.

For the Company's secured loans where the loan-to-value ratio is not a valid indicator (because the loans are collateralized by other assets of the borrower in addition to their precious metal inventory) the Company uses other indicators to measure the quality of this type of loan. For this type of loan, the Company uses the following credit quality indicators: accounts receivable-to-loan ratios and inventory-to-loan ratios and delinquency status of the loan.

Impaired loans

A loan is considered impaired if it is probable, based on current information and events, that the Company will be unable to collect all amounts due according to the contractual terms of the loan. Customer loans are reviewed for impairment and include loans that are past due, non-performing or in bankruptcy. Recognition of interest income is suspended and the loan is placed on non-accrual status when management determines that collection of future interest income is not probable. Accrual is resumed, and previously suspended interest income is recognized, when the loan becomes contractually current and/or collection doubts are removed. Cash receipts on impaired loans are recorded first against the receivable and then to any unrecognized interest income.

All loans are contractually subject to margin call. As a result, loans typically do not become impaired due to the fact the Company has the ability to require margin calls which are due upon receipt. Per the terms of the loan agreement, the Company has the right to rapidly liquidate the loan collateral in the event of a default. The material is highly liquid and easily sold to pay off the loan. Such circumstances would result in a short term impairment that would typically result in full repayment of the loan and fees due to the Company.

For the three months ended September 30, 2015 and 2014, the Company incurred no loan impairment costs.

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6. INVENTORIES

Our inventory consists of the precious metals that the Company has physically received, and inventory held by third-parties, which at the Company's option may or may not receive. Below, our inventory is summarized by classification at September 30, 2015 and June 30, 2015:

in thousands

	September 30, 2015	June 30, 2015
Inventory held for sale	$118,796	$86,353
Repurchase arrangements with customers	75,910	49,117
Consignment arrangements with customers	5,598	5,588
Commemorative coins, held at lower of cost or market	163	1,518
Borrowed precious metals from suppliers	4,009	9,500
Product financing arrangements, restricted	50,030	39,425
	$254,506	$191,501

Inventory held for sale. Inventory held for sale represents precious metals, excluding commemorative coin inventory, that have been received by the Company that is not subject to repurchase or consignment arrangements with third parties. As of September 30, 2015 and June 30, 2015, the inventory held for sale totaled $118.8 million and 86.4 million, respectively.

Repurchase Arrangements with Customers. The Company enters into arrangements with certain customers under which A-Mark purchases precious metals products that are subject to repurchase by the customer at the fair value of the product on the repurchase date. The Company or the counterparty may typically terminate any such arrangement with 14 days' notice. Upon termination the customer's rights to repurchase any remaining inventory is forfeited. As of September 30, 2015 and June 30, 2015, included within inventory is $75.9 million and $49.1 million, respectively, of precious metals products subject to repurchase.

Consignment Arrangements with Customers. The Company periodically loans metals to customers on a short-term consignment basis, charging interest fees based on the value of the metal loaned. Inventories loaned under consignment arrangements to customers as of September 30, 2015 and June 30, 2015 totaled $5.6 million and $5.6 million, respectively. Such inventories are removed at the time the customer elects to price and purchase the precious metals, and the Company records a corresponding sale and receivable. Substantially all inventories loaned under consignment arrangements are collateralized for the benefit of the Company.

Commemorative Coins. Our commemorative coin inventory, including its premium component, is held at the lower of cost or market, because the value of commemorative coins is influenced more by supply and demand determinants than on the underlying spot price of the precious metal content of the commemorative coins. Unlike our bullion coins, the value of commemorative coins is not subject to the same level of volatility as bullion coins because our commemorative coins typically carry a substantially higher premium over the spot metal price than bullion coins. Our commemorative coins are not hedged, are included in inventory at the lower of cost or market and totaled $0.2 million and $1.5 million as of September 30, 2015 and June 30, 2015, respectively.

Borrowed Precious Metals from Suppliers. Inventories include amounts borrowed from suppliers under arrangements to purchase precious metals on an unallocated basis that are held by the supplier. Unallocated or pool metal represents an unsegregated inventory position that is due on demand, in a specified physical form, based on the total ounces of metal held in the position. Amounts under these arrangements require delivery either in the form of precious metals or cash. Corresponding obligations related to liabilities on borrowed metals are reflected on the condensed consolidated balance sheets and totaled $4.0 million and $9.5 million as of September 30, 2015 and June 30, 2015, respectively.

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Product Financing Arrangements. Inventories include amounts for obligations under product financing arrangements. The Company enters into a product financing agreement for the transfer and subsequent re-acquisition of gold and silver at a fixed price to a third party finance company. This inventory is restricted and is held at a custodial storage facility in exchange for a financing fee, by the third party finance company. During the term of the financing, the third party finance company holds the inventory as collateral, and both parties intend to return the inventory to the Company at an agreed-upon price based on the spot price on the finance arrangement termination date. The third party charges a monthly fee as percentage of the market value of the outstanding obligation; such monthly charge is classified in interest expense. Pursuant to the guidance in ASC 470-40 Product Financing Arrangements, these transactions do not qualify as sales and therefore have been accounted for as financing arrangements and reflected in the condensed consolidated balance sheet within product financing arrangement. The obligation is stated at the amount required to repurchase the outstanding inventory. Both the product financing and the underlying inventory are carried at fair value, with changes in fair value included in cost of sales in the condensed consolidated statements of income. Such obligation totaled $50.0 million and $39.4 million as of September 30, 2015 and June 30, 2015, respectively.

The Company mitigates market risk of its physical inventories and open commitments through commodity hedge transactions (see Note 10.)

Premium component of inventory

The Company's inventories primarily include bullion and bullion coins and are acquired and initially recorded at fair market value. The fair market value of the bullion and bullion coins is comprised of two components: (1) published market values attributable to the cost of the raw precious metal, and (2) a published premium paid at acquisition of the metal. The premium is attributable to the additional value of the product in its finished goods form and the market value attributable solely to the premium is readily determined, as it is published by multiple reputable sources. The premium is included in the cost of the inventory, paid at acquisition, and is a component of the total fair market value of the inventory. The precious metal component of the inventory may be hedged through the use of precious metal commodity positions, while the premium component of our inventory is not a commodity that may be hedged.

The Company’s inventories are subsequently recorded at their fair market values, that is, "marked-to-market", except for our commemorative coin inventory. The daily changes in the fair market value of our inventory are offset by daily changes in fair market value of hedging derivatives that are taken with respects to our inventory positions; both the change in the fair market value of the inventory and the change in the fair market value of these derivative instruments are recorded in cost of sales in the condensed consolidated statements of income.

The premium component, at market value, included in the inventories as of September 30, 2015 and June 30, 2015 totaled $3.5 million and $3.3 million, respectively. As of September 30, 2015 and June 30, 2015, the unrealized gains (losses) resulting from the difference between market value and cost of physical inventories were $(5.2) million and $(3.9) million, respectively.

7. PROPERTY AND EQUIPMENT

Property and equipment consists of the following at September 30, 2015 and June 30, 2015:
in thousands

	September 30, 2015	June 30, 2015
Office furniture, fixtures and equipment	$844	$616
Computer equipment	368	368
Computer software	2,376	2,376
Leasehold improvements	1,661	1,700
Subtotal	5,249	5,060
Less: accumulated depreciation	(2,417)	(2,210)
Property and equipment, net	$2,832	$2,850

Depreciation expense for the three months ended September 30, 2015 and 2014 was $0.2 million and $0.1 million, respectively.

8. GOODWILL AND INTANGIBLE ASSETS

On July 1, 2005, all of the outstanding common stock of A-Mark was acquired by Spectrum PMI, Inc. Spectrum PMI was a holding company whose outstanding common stock was owned 80% by SGI, and 20% by Auctentia, S.L. In September 2012, SGI purchased from Auctentia its 20% interest in Spectrum PMI. On September 30, 2013, Spectrum PMI was merged with and into SGI, as a result of which all of the outstanding shares of A Mark were then owned directly by SGI.

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In connection with the acquisition of A-Mark by Spectrum PMI on July 1, 2005, the accounts of the Company were adjusted using the push down basis of accounting to recognize the allocation of the consideration paid to the respective net assets acquired. In accordance with the push down basis of accounting, the Company's net assets were adjusted to their fair values as of the date of the acquisition based upon an independent appraisal, which resulted in goodwill of $4.9 million and identifiable purchased intangible assets of $8.4 million. Goodwill represents the excess of the purchase price and related costs over the value assigned to intangible assets of businesses acquired and accounted for under the purchase method.

The carrying value of other purchased intangibles as of September 30, 2015 and June 30, 2015 is as described below:

dollar amounts in thousands

		September 30, 2015			June 30, 2015		
	Estimated Useful Lives (Years)	Gross Carrying Amount	Accumulated Amortization	Net Book Value	Gross Carrying Amount	Accumulated Amortization	Net Book Value
Trade-name	Indefinite	$454	$—	$454	$454	$—	$454
Existing customer relationships	5 - 15	5,747	(3,928)	1,819	5,747	(3,832)	1,915
Non-compete and other	4	2,000	(2,000)	—	2,000	(2,000)	—
Employment agreement	3	195	(195)	—	195	(195)	—
Purchased intangibles subject to amortization		7,942	(6,123)	1,819	7,942	(6,027)	1,915
		$8,396	$(6,123)	$2,273	$8,396	$(6,027)	$2,369

The Company's other purchased intangible assets are subject to amortization except for trademarks, which have an indefinite life. Intangible assets subject to amortization are amortized using the straight-line method over their useful lives, which are estimated to be four to fifteen years. Amortization expense related to the Company's intangible assets for the three months ended September 30, 2015 and 2014 was $0.1 million and $0.1 million, respectively.

Estimated amortization expense on an annual basis for the succeeding five years is as follows (in thousands):

Fiscal year ending June 30,	Amount
Fiscal 2016 (9 months remaining)	$289
2017	385
2018	385
2019	385
2020	375
Thereafter	—
Total	$1,819

9. ACCOUNTS PAYABLE

Accounts payable consist of the following:

in thousands

	September 30, 2015	June 30, 2015
Trade payable to customers payables	$1,026	$128
Advances from customers	59,877	38,039
Liability on deferred revenue	15,069	11,039
Other accounts payable	2,527	1,433
	$78,499	$50,639

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10. DERIVATIVE INSTRUMENTS AND HEDGING TRANSACTIONS

The Company is exposed to market risk, such as change in commodity prices, and foreign exchange rates. To manage the volatility relating to these exposures, the Company enters into various derivative products, such as forwards and futures contracts. By policy, the Company historically has entered into derivative financial instruments for the purpose hedging substantially all of Company's market exposure to precious metals prices, and not for speculation reasons.

Commodity Price Management

The Company manages the value of certain specific assets and liabilities of its trading business, including trading inventories, by employing a variety of hedging strategies. These strategies include the management of exposure to changes in the market values of the Company's trading inventories through the purchase and sale of a variety of derivative instruments, such as, forwards and futures contracts.

The Company's trading inventories and purchase and sale transactions consist primarily of precious metal bearing products. The value of these assets and liabilities are marked-to-market daily to the prevailing closing price of the underlying precious metals.

The Company's precious metals inventories are subject to market value changes, created by changes in the underlying commodity market prices. Inventories purchased or borrowed by the Company are subject to price changes. Inventories borrowed are considered natural hedges, since changes in value of the metal held are offset by the obligation to return the metal to the supplier.

Open sale and purchase commitments are subject to changes in value between the date the purchase or sale price is fixed (the trade date) and the date the metal is received or delivered (the settlement date). The Company seeks to minimize the effect of price changes of the underlying commodity through the use of forward and futures contracts.

The Company's policy is to substantially hedge its inventory position, net of open sale and purchase commitments that is subject to price risk. The Company regularly enters into precious metals commodity forward and futures contracts with major financial institutions to hedge price changes that would cause changes in the value of its physical metals positions and purchase commitments and sale commitments. The Company has access to all of the precious metals markets, allowing it to place hedges. However, the Company also maintains relationships with major market makers in every major precious metals dealing center.

The Company enters into these derivative transactions solely for the purpose of hedging our inventory subject to price risk, and not for speculative market purposes. Due to the nature of the Company's global hedging strategy, the Company is not using hedge accounting as defined under Topic 815 of the ASC, whereby the gains or losses would be deferred and included as a component of other comprehensive income. Instead, gains or losses resulting from the Company's futures and forward contracts and open sale and purchase commitments are reported as unrealized gains or losses on commodity contracts (a component of cost of sales) with the related unrealized amounts due from or to counterparties reflected as a derivative asset or liability.

Derivative Assets and Liabilities

The Company's derivative assets and liabilities represent the net fair value of the difference (or intrinsic value) between market values and trade values at the trade date for open precious metals sale and purchase contracts, as adjusted on a daily basis for changes in market values of the underlying metals, until settled. The Company's derivative assets and liabilities represent the net fair value of open precious metals forwards and futures contracts. The precious metals forwards and futures contracts are settled at the contract settlement date.

All of our commodity derivative contracts are under master netting arrangements and include both asset and liability positions (i.e., offsetting derivative instruments). Substantially all of these transactions are secured by the underlying metals positions. As such, the Company's derivative contracts with the same counterparty, the receivables and payables have been netted on the condensed consolidated balance sheets. Such derivative contracts include open sale and purchase commitments, futures, forwards and margin accounts. In the table below, the aggregate gross and net derivative receivables and payables balances are presented by contract type and type of hedge, as of September 30, 2015 and June 30, 2015.

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in thousands	September 30, 2015 Gross Derivative	Amounts Netted	Cash Collateral Pledge	Net Derivative	June 30, 2015 Gross Derivative	Amounts Netted	Cash Collateral Pledge	Net Derivative
Nettable derivative assets:								
Open sale and purchase commitments	$10,624	$(3,116)	$—	$7,508	$2,815	$(1,093)	$—	$1,722
Future contracts	9,917	(7,075)	—	2,842	11,159	(5,796)	—	5,363
Forward contracts	670	(394)	—	276	4,279	—	—	4,279
	$21,211	$(10,585)	$—	$10,626	$18,253	$(6,889)	$—	$11,364
Nettable derivative liabilities:								
Open sale and purchase commitments	$7,562	$(1,379)	$—	$6,183	$11,723	$(734)	$—	$10,989
Margin commitments	11,436	—	(5,069)	6,367	12,430	—	(5,522)	6,908
Future contracts	—	—		—	—	—		—
Forward contracts	348	(5)	—	343	—	—	—	—
	$19,346	$(1,384)	$(5,069)	$12,893	$24,153	$(734)	$(5,522)	$17,897

The Company’s management sets credit and position risk limits. These limits include gross position limits for counterparties engaged in sales and purchase transactions with the Company. They also include collateral limits for different types of sale and purchase transactions that counterparties may engage in from time to time.

Gain or Loss on Derivative Instruments

The Company records the derivative at the trade date with a corresponding unrealized gain (loss), which is reflected in the cost of sales in the condensed consolidated statements of income. The Company adjusts the derivatives to fair value on a daily basis until the transaction is physically settled. Sales which are physically settled are recognized at the gross amount in the consolidated statements of income. Below, is a summary of the net losses on derivative instruments for the three months ended September 30, 2015 and 2014.

in thousands

	Three Months Ended September 30, 2015	September 30, 2014
Gain (loss) on derivative instruments:		
Unrealized loss on open future commodity and forward contracts and open sale and purchase commitments, net	$(3,816)	$ 1,278
Realized loss on future commodity contracts, net	(10,592)	(7,634)
Total	$(14,408)	$ (6,356)

The Company’s open sale and purchase commitments typically settle within 2 business days, and for those commitments that do not have stated settlement dates, the Company has the right to settle the positions upon demand. Futures and forwards contracts open at quarter-end typically settle within 30 days.

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Summary of Hedging Activity

In a hedging relationship, the change in the value of the derivative financial instrument is offset to a great extent by the change in the value of the underlying hedged item. The following table summarizes the results of our hedging activities, which shows the precious metal commodity inventory position, net of open sale and purchase commitments, that is subject to price risk as of September 30, 2015 and at June 30, 2015.

in thousands

	September 30, 2015	June 30, 2015
Inventory	$254,506	$191,501
Less unhedgable inventory:		
Commemorative coin inventory, held at lower of cost or market	(163)	(1,518)
Premium on metals position	(3,529)	(3,255)
Inventory value not hedged	(3,692)	(4,773)
Subtotal	250,814	186,728
Commitments at market:		
Open inventory purchase commitments	556,388	444,023
Open inventory sales commitments	(477,089)	(249,081)
Margin sale commitments	(11,436)	(12,430)
In-transit inventory no longer subject to market risk	(16,625)	(13,807)
Unhedgable premiums on open commitment positions	6,356	528
Inventory borrowed from suppliers	(4,009)	(9,500)
Product financing obligation	(50,030)	(39,425)
Advances on industrial metals	3,709	3,340
Inventory subject to price risk	258,078	310,376
Inventory subject to derivative financial instruments:		
Precious metals forward contracts at market values	123,658	202,323
Precious metals futures contracts at market values	134,367	107,993
Total market value of derivative financial instruments	258,025	310,316
Net inventory subject to commodity price risk	$53	$60

Notional Balances of Derivatives

The notional balances of the Company's derivative instruments, consisting of contractual metal quantities, are expressed at current spot prices of the underlying precious metal commodity. As of September 30, 2015 and June 30, 2015, the Company had the following outstanding commitments and open forward and future contracts:

in thousands

	September 30, 2015	June 30, 2015
Purchase commitments	$556,388	$444,023
Sales commitments	(477,089)	(249,081)
Margin sales commitments	(11,436)	(12,430)
Open forward contracts	123,658	202,323
Open futures contracts	134,367	107,993

The contract amounts (i.e., notional balances) of the Company's forward and futures contracts and the open sales and purchase orders are not reflected in the accompanying condensed consolidated balance sheet; as required, the Company records the difference between the market price of the underlying metal or contract and the trade amount at fair value.

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The Company is exposed to the risk of failure of the counterparties to its derivative contracts. Significant judgment is applied by the Company when evaluating the fair value implications. The Company regularly reviews the creditworthiness of its major counterparties and monitors its exposure to concentrations. At September 30, 2015, the Company believes its risk of counterparty default is mitigated as a result of such evaluation and the short-term duration of these arrangements.

Foreign Currency Exchange Rate Management

The Company utilizes foreign currency forward contracts to manage the effect of foreign currency exchange fluctuations of its sale and purchase transactions. These contracts generally have maturities of less than one week. The accounting treatment of our foreign currency exchange derivative instruments is similar to the accounting treatment of our commodity derivative instruments, that is, the change in the value in the financial instrument is immediately recognized as a component of cost of sales. Unrealized net gains (losses) on foreign exchange derivative instruments shown on the face of the condensed consolidated statements of income totaled $(39,000) and $(9,000) for the three months ended September 30, 2015 and 2014, respectively. The market values (fair values) of the Company’s foreign exchange forward contracts and the net open sale and purchase commitment transactions, denominated in foreign currencies, outstanding at September 30, 2015 was $1.2 million and $4.1 million, respectively. The market values (fair values) of the Company’s foreign exchange forward contracts and the net open sale and purchase commitment transactions, denominated in foreign currencies, outstanding at June 30, 2015 was $6.2 million and $9.9 million, respectively.

11. INCOME TAXES

The Company files a consolidated federal income tax return based on a June 30th tax year end. The provision for income taxes for the three months ended September 30, 2015 and 2014 consists of the following:

in thousands

	Three Months Ended	
	September 30, 2015	September 30, 2014
Federal	$3,052	$680
State and local	260	98
Provision for income taxes	$3,312	$778

The effective tax rate for the three months ended September 30, 2015 and 2014 is as follows:

in thousands

	Three Months Ended	
	September 30, 2015	September 30, 2014
Effective tax rate	38.2 %	40.6 %

The Company uses an estimated annual effective tax rate, which is based on expected annual income, statutory tax rates and tax planning opportunities available in the various jurisdictions in which the Company operates, to determine its quarterly provision for income taxes. Certain significant or unusual items are separately recognized in the quarter in which they occur and can be a source of variability in the effective tax rates from quarter to quarter. The effective tax rate varies significantly from the federal statutory rate due to permanent adjustments for nondeductible items and state taxes.

In assessing the realizability of deferred tax assets, management considers whether it is more likely than not that some portion or all of the deferred tax assets will be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income during the periods in which those temporary differences become deductible. During the three months ended September 30, 2015, management concluded that with the exception of certain state net operating losses, it was more likely than not that the Company would be able to realize the benefit of the U.S. federal and state deferred tax assets in the future. We based this conclusion on historical and projected operating performance, as well as our expectation that our operations will generate sufficient taxable income in future periods to realize the tax benefits associated with the deferred tax assets. As of September 30, 2015 and 2014, the

Company had $0.1 million and $0.3 million, respectively, of valuation allowance for its realizability of deferred tax assets. The Company will continue to assess the need for a valuation allowance in the future by evaluating both positive and negative evidence that may exist.

The Company's condensed consolidated financial statements recognized the current and deferred income tax consequences that result from the Company's activities during the current and preceding periods, as if the Company were a separate taxpayer during the period prior to the Distribution rather than a member of the Former Parent's consolidated income tax return group. Current tax receivable from Former Parent reflects balances due from the Former Parent to A-Mark for its share of the income tax

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assets of the group. Income taxes receivable represents amounts paid to federal and state jurisdictions due to taxable income generated following the close of the transaction.

As of September 30, 2015, the Company has state and city net operating loss carryforwards of approximately $16.0 million, which expire beginning with the year ending June 30, 2030. The tax effect of the state and city net operating loss carryforwards included in the Company's deferred tax assets is $16.0 million. Due to limitations on the ability to use certain state and city net operating loss carryforwards, the Company has recorded a valuation allowance of $0.1 million against these assets as the Company believes that it is not more likely than not that they will realize the benefit of these carryforwards.

As of September 30, 2015, the Company had $243,000 of unrecognized tax benefits and $105,000 of liabilities for interest expense related to uncertain tax positions. Of the total unrecognized tax benefits, $243,000 would reduce the Company's effective tax rate, if recognized. For the three months ended September 30, 2015 and 2014, the Company recognized approximately $5,000 of interest expense and $0 of interest expense related to uncertain tax positions, respectively. For the three months ended September 30, 2015 and 2014, the Company had no additional accruals for tax penalties.

The Company files income tax returns in the U.S. and various states. Prior to the Distribution, the Company was included in the consolidated federal and state tax filing of the Former Parent. The Former Parent has been under examination by the IRS for the years ended June 30, 2004 through 2013; however, during the year ended June 30, 2015, the Former Parent was notified that it had successfully resolved the June 30, 2004 through June 30, 2007 tax years. As a result of the IRS exam, the Former Parent amended the state tax filings for the applicable periods. The amended state tax filings resulted in a tax benefit of approximately $0.6 million related to state net operating loss apportioned to the Company under intrastate apportionment rules. The Former Parent remains in appeals with the IRS for the years ended June 30, 2008 through 2013 and in examination with other taxing jurisdictions on certain tax matters, including challenges to certain positions the Former Parent has taken. The Former Parent is unable to determine the outcome of these audits at this time. With few exceptions, either prior federal, state or local examinations have been completed by the tax authorities or the statute of limitations have expired for U.S. federal, state and local income tax returns filed by the Former Parent for the years through 2003.

In connection with the spinoff, the Company entered into a tax separation agreement with SGI (the "Tax Separation Agreement"). The Tax Separation Agreement governs the respective rights, responsibilities and obligations of SGI and us with respect to, among other things, liabilities for U.S. federal, state, local and other taxes. In addition to the allocation of tax liabilities, the Tax Separation Agreement addresses the preparation and filing of tax returns for such taxes and disputes with taxing authorities regarding such taxes. Pursuant to the Tax Separation Agreement, A-Mark may be responsible for any tax amount related to A-Mark that is incurred as the result of adjustments made during the Internal Revenue Service examination or other tax jurisdictions' examinations of the Former Parent. Under the terms of the Tax Separation Agreement, SGI will have the responsibility to prepare and file tax returns for tax periods ending prior to the Distribution date and for tax periods which include the Distribution date but end after the Distribution date, which will include A-Mark and its subsidiaries.

These tax returns will be prepared on a basis consistent with past practices. The Company will cooperate in the preparation of these tax returns and have an opportunity to review and comment on these returns prior to filing. A-Mark will pay all taxes attributable to A-Mark and its subsidiaries, and will be entitled to any refund with respect to taxes it has paid.

The amounts receivable under the Company's income tax sharing obligation due from SGI totaled $1.1 million, and $1.1 million as of September 30, 2015 and June 30, 2015, respectively, and is shown on the face of the condensed consolidated balance sheets as income taxes receivable from Former Parent. Based on the terms to the Tax Separation Agreement, payment is due to the Company after SGI files its tax return and is in receipt of its tax refund from the IRS. Furthermore, pursuant to the terms of the Tax Separation Agreement, the Company has been allocated approximately $15.7 million of state net operating losses. These net operating losses resulted in a deferred tax asset of $0.5 million.

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12. RELATED PARTY TRANSACTIONS

Sales and Purchases Made to Affiliated Companies

During the three months ended September 30, 2015 and 2014, the Company made sales and purchases to various companies that had been under common control with A-Mark through the date of Distribution, and which have been deemed to be related parties.

in thousands

	Three Months Ended			
	September 30, 2015		September 30, 2014	
	Sales	Purchases	Sales	Purchases
Related Party Company				
Calzona Ventures, LLC	$—	$—	$157	$—
Stack's Bowers Numismatics, LLC	10,482 (1)	27,004	1,395	2,921
Related party, total	$10,482	$27,004	$1,552	$2,921

(1) Excludes $156,000 of fees related to finance charges earned in connection with purchase-sale transactions, which was recorded as interest income.

As of September 30, 2015 and June 30, 2015, the Company's had related party receivables and payables balance as set forth below:

in thousands

	September 30, 2015		June 30, 2015	
	Receivables	Payable	Receivables	Payable
Related Party Company				
Stack's Bowers Numismatics, LLC	$854	$28	$2	$10
SGI (Former Parent)	1,095	—	1,095	—
Related party, total	$1,949	$28	$1,097	$10

Secured Loans to Related Parties

On June 18, 2014, CFC assumed the rights to a secured portfolio of short-term loan receivables totaling $2.6 million from Stack's Bowers Numismatics, LLC (Stack's Bowers), a related party. The Company reflects this transaction as a financing arrangement with the related party, secured by the portfolio of short-term loan receivables collateralized by numismatic and semi numismatic products, and bearing interest at 5.5% per annum. This secured loan was paid off in full, plus accrued interest, on August 19, 2014. As of September 30, 2015, the aggregate carrying value of this loan was $0.0 million.

On October 9, 2014, CFC entered into a loan agreement with Stack's Bowers providing for a secured line of credit in the maximum principal amount of up to $16.0 million, bearing interest at a competitive rate per annum. Advances under the line of credit were secured by numismatic and semi-numismatic products. This secured loan was paid off in full, plus accrued interest, on April 15, 2015. As of September 30, 2015, the aggregate carrying value of this loan was $0.0 million.

On July 23, 2015, CFC entered into a loan agreement with Stack's Bowers providing a secured line of credit in the maximum principal amount of up to $2.5 million, bearing interest at a competitive rate per annum. The loan is secured by numismatic and semi-numismatic products. As of September 30, 2015, the aggregate carrying value of this loan was $0.7 million.

During the three months ended September 30, 2015 and 2014, the Company earned approximately $21,000 and $23,000 in interest income related to loans that we made to Stack's Bowers.

Secondment Agreement Fees and Reimbursements

In connection with the Distribution, SGI and the Company entered into a secondment agreement (the "Secondment Agreement"). Under the terms of the Secondment Agreement, A-Mark has agreed to make Gregory N. Roberts, our Chief Executive Officer, and Carol Meltzer, our Executive Vice President, General Counsel and Secretary, available

to SGI for the performance of specified management and professional services following the spinoff in exchange for an annual secondment fee of $150,000 (payable monthly) and reimbursement of certain bonus payments.
Neither Mr. Roberts nor Ms. Meltzer will devote more than 20% of their professional working time on a monthly basis to SGI and in no event will the performance of services for SGI interfere with the performance of the duties and responsibilities of Mr. Roberts and Ms. Meltzer to A-Mark. In addition, to the services to be provided under the Secondment Agreement, both Mr. Roberts and Ms. Meltzer continue to serve as officers and directors of SGI. The Secondment Agreement will terminate on June 30, 2016 and is subject to earlier termination under certain circumstances. Under the Secondment Agreement, SGI will be obligated

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to reimburse A-Mark for the portion of the performance bonus payable under Mr. Roberts' employment agreement with A-Mark attributable to pre-tax profits of SGI.

The Company records the accrual of secondment fees as a reduction to selling, general and administration expense. During the three months ended September 30, 2015 and 2014 the Company did not accrue any secondment fees. As of September 30, 2015 and June 30, 2015 the outstanding balance of secondment fees due from SGI was $0 and $150,000, respectively.

Income Tax Sharing Obligations

The amounts receivable under the Company's income tax sharing obligation due from SGI, totaled $1.1 million, and $1.1 million as of September 30, 2015 and June 30, 2015, respectively, and is shown on the face of the condensed consolidated balance sheets as income taxes receivable from Former Parent (see Note 11.)

Transaction with Affiliate of Board Member

In February 2015, A-M Global Logistics, LLC ("Logistics"), a wholly owned subsidiary of the Company that was formed to operate the Company's logistics fulfillment center in Las Vegas, Nevada, entered into various agreements with W. A. Richardson Builders, LLC ("WAR"), for the buildout of and improvements to the Las Vegas premises. The amount involved under the WAR contract was approximately $1.2 million, and Logistics paid WAR a fee equal to 5.0% of the contract work. The spouse of the Chairman of the Company's Audit Committee, Ellis Landau, is an owner and a managing member of WAR.

Royalties to Former Owner

As part of the sales agreement dated July 1, 2005, a former owner of the Company receives a portion of the finance income earned with a specific customer through July 2015. The Company incurred $20,000 and $73,000 in selling, general and administrative expenses (royalty expense) during the three months ended September 30, 2015 and 2014, respectively. The total amount due to the former owner of $274,000 and $254,000 are included in accrued liabilities as of September 30, 2015 and June 30, 2015, respectively.

13. FINANCING AGREEMENTS

Lines of Credit

The Company has a borrowing facility ("Trading Credit Facility") with a group of financial institutions under an inter-creditor agreement, which provides for lines of credit up to the maximum of the credit facility. All lenders have a perfected, first security interest in all assets of the Company presented as collateral. Loan advances will be available against a borrowing base report of eligible assets in accordance with the inter-creditor agreement currently in place. Pledged collateral comprises assigned and confirmed inventory, trade receivables, trade advances, derivatives, equity and pledged non bullion and bullion loans.

As of September 30, 2015, the maximum of the Trading Credit Facility was $205.0 million. The Company routinely uses the Trading Credit Facility to purchase precious metals from suppliers and for operating cash flow purposes. Amounts under the Trading Credit Facility bear interest based on London Interbank Offered Rate ("LIBOR") plus a margin. The one-month LIBOR rate was approximately 0.19% and 0.19% as of September 30, 2015 and June 30, 2015, respectively. Borrowings are due on demand and totaled $176.9 million and $147.0 million at September 30, 2015 and at June 30, 2015, respectively. The amounts available under the Trading Credit Facility are determined at the end of each week following a specified borrowing base formula. The Company is able to access additional credit as needed to finance operations, subject to the overall limits of the Trading Credit Facility and lender approval of the revised borrowing base calculation. The amounts available under the Trading Credit Facility after taking into consideration current borrowings, based upon the latest approved borrowing bases in effect, totaled $34.3 million and $20.9 million at September 30, 2015 and June 30, 2015, respectively.

The Trading Credit Facility has certain restrictive financial covenants, which require the Company to maintain a minimum tangible net worth. As of September 30, 2015 the minimum tangible net worth financial covenant under the Trading Credit Facility was $35.0 million. The Company is in compliance with all restrictive financial covenants as of September 30, 2015. The Company's ability to pay dividends, if it were to elect to do so, could be limited as a result of these restrictions. Each lender has the right to cancel its credit line upon written notice.

Interest expense related to the Company's borrowing arrangements totaled $1.1 million and $0.9 million, which represents 92.1% and 87.8% of the total interest expense recognized, for the three months ended September 30, 2015 and 2014, respectively. Our borrowing arrangements carried a daily weighted average effective interest rate of 2.83% and 3.06%, respectively, for the three months ended September 30, 2015 and 2014.

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Liability on Borrowed Metals

The Company borrows precious metals from its suppliers under short-term agreements, which bear interest at a designated rate. Amounts under these agreements are due at maturity and require repayment either in the form of precious metals or cash. The Company's inventories included borrowed metals with market values totaling $4.0 million and $9.5 million as of September 30, 2015 and June 30, 2015, respectively.

Product Financing Arrangement

The Company has an agreement with a financial institution (a third party) that allows the Company to transfer its gold and silver inventory at a fixed price to this third party. Such agreement allows the Company to repurchase this inventory at an agreed-upon price based on the spot price on the repurchase date. The third party charges a monthly fee as percentage of the market value of the outstanding obligation; such monthly charges are classified in interest expense. These transactions do not qualify as sales, and therefore have been accounted for as financing arrangements and reflected in the condensed consolidated balance sheet within product financing obligation. The obligation is stated at the amount required to repurchase the outstanding inventory. Both the product financing obligation and the underlying inventory (which is entirely restricted) are carried at fair value, with changes in fair value recorded as a component of cost of sales in the condensed consolidated statements of income. Such obligation totaled $50.0 million and $39.4 million as of September 30, 2015 and June 30, 2015, respectively.

14. COMMITMENTS AND CONTINGENCIES

Refer to Note 13 of the Notes to Consolidated Financial Statements in the 2015 Annual Report for information relating to minimum rental payments under operating and capital leases, consulting and employment contracts, and other commitments. Other than the following item, there has been no material changes to those scheduled commitments as of the filing of that report.

On October 25, 2015, the Company received notification from the City of Santa Monica that the City was challenging the Company's classification as an "agent/broker" for purposes of computing the business license fee due to the City. Historically, A-Mark has paid its business license fee on net receipts, consistent with the "agent/broker" classification. The City of Santa Monica has asserted that the Company should have instead paid the fee based on gross receipts and has made a preliminary assessment against the Company seeking a material amount of what it believes to be underreported fees, together with a material amount of penalties and interest. The Company intends to meet with the City of Santa Monica shortly to discuss the preliminary assessment and the position taken by the Company with respect to the calculation of the fee. Neither the outcome of this administrative matter nor the amount or range of a potential impact to the Company in the event of an unfavorable outcome can be determined at this time.

15. STOCKHOLDERS' EQUITY

Payment of Dividends

Fiscal 2015. In fiscal 2015, the Board of Directors of the Company initiated a cash dividend policy that calls for the payment of a quarterly cash dividend of $0.05 per common share. On February 6, 2015, the Board of Directors declared a quarterly cash dividend of $0.05 per common share that was paid on March 20, 2015 to stockholders of record at the close of business on March 12, 2015. On May 1, 2015, the Board of Directors declared a quarterly cash dividend of $0.05 per common share that was paid on May 25, 2015 to stockholders of record at the close of business on May 14, 2015.

Fiscal 2016. On September 11, 2015, the Board of Directors of the Company declared a quarterly cash dividend of $0.05 per common share to stockholders of record at the close of business on September 24, 2015 that was paid on October 5, 2015. On October 30, 2015, the Board of Directors of the Company declared a quarterly cash dividend of $0.05 per common share to stockholders of record at the close of business on November 13, 2015, which is scheduled to be paid on November 25, 2015.

2014 Stock Award and Incentive Plan

Prior to the Distribution, the Company's Board of Directors ("Board") adopted and the Company's then sole stockholder approved the 2014 Stock Award and Incentive Plan ("2014 Plan"). Under the 2014 Plan, the Company may grant options and other equity awards as a means of attracting and retaining officers, employees, non-employee directors and consultants, to provide incentives to such persons, and to align the interests of such persons with the interests of stockholders by providing compensation based on the value of the Company's stock. Awards under the

2014 Plan may be granted in the form of incentive or non-qualified stock options, stock appreciation rights ("SARs"), restricted stock, restricted stock units, dividend equivalent rights and other stock-based awards (which may include outright grants of shares). The 2014 Plan also authorizes grants of performance-based cash incentive awards. The 2014 Plan is administered by the Compensation Committee of the Board of Directors, which, in its discretion, may select officers and other employees, directors (including non-employee directors) and consultants to the Company and its subsidiaries to receive grants of awards. The Board of Directors itself may perform any of the functions of the Compensation Committee under the 2014 Plan.

Under the 2014 Plan, the exercise price of options and base price of SARs may be set at the discretion of the Committee, but generally may not be less than the fair market value of the shares on the date of grant, and the maximum term of stock options

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and SARs is 10 years. The 2014 Plan limits the number of share-denominated awards that may be granted to any one eligible person to 250,000 shares in any fiscal year. Also, in the case of non-employee directors, the 2014 Plan limits the maximum grant-date fair value at $300,000 of stock-denominated awards granted to a director in a given fiscal year, except for a non-employee Chairman of the Board whose grant-date fair value maximum is $600,000 per fiscal year. The 2014 Plan will terminate when no shares remain available for issuance and no awards remain outstanding; however, the authority to grant new awards will terminate on December 13, 2022.

As of September 30, 2015, 622,000 shares were available for grant under the 2014 Plan.

Valuation and Significant Assumptions of Equity Awards Issued

The Company uses the Black-Scholes option pricing model, which has various inputs such as the estimated common share price, the risk-free interest rate, volatility, expected life and dividend yield, all of which are estimates. The Company also records share-based compensation expense net of expected forfeitures. Valuation models and significant assumptions for share-based compensation are as follows:

- Determining Fair Values. For all equity grants granted, the primary factor in the valuation of equity awards was the fair value of the underlying common stock at the time of grant.
- Expected Volatility. The Company has limited data regarding company-specific historical or implied volatility of its share price. Consequently, the Company estimates its volatility based on the average of the historical volatilities of peer group companies from publicly available data for sequential periods approximately equal to the expected terms of its option grants. Management considers factors such as stage of life cycle, competitors, size, market capitalization and financial leverage in the selection of similar entities.
- Expected Term. The expected term represents the period of time in which the options granted are expected to be outstanding. The Company estimates the expected term of options granted based on the midpoint between the vesting date and the end of the contractual term under the “short-cut” or simplified method permitted by the SEC implementation guidance for “plain vanilla” options. The Company will continue to use the short-cut method, as permitted, until we have developed sufficient historical data for employee exercise and post-vesting employment termination behavior after our common stock has been publicly traded for a reasonable period of time.
- Forfeitures. The Company estimates forfeitures at the time of grant and revises those estimates in subsequent periods if actual experience differs from those estimates. For the current fiscal year, the Company estimated an average overall forfeiture rate of 0%, based on the historical forfeitures rates of executives of our Former Parent prior to the spinoff transaction. Share-based compensation is recorded net of expected forfeitures. The Company will periodically assess the forfeiture rate and the amount of expense recognized based on estimated historical forfeitures as compared to actual forfeitures. Changes in estimates are recorded in the period they are identified.
- Risk-Free Rate. The risk-free interest rate is selected based upon the implied yields in effect at the time of the option grant on U.S. Treasury zero-coupon issues with a term approximately equal to the expected life of the option being valued.
- Dividends. The Company anticipates on paying quarterly cash dividends 5% of outstanding shares of common stock in the foreseeable future.

The Company did not grant any share-based awards during the three months ended September 30, 2015 and 2014. There are no awards with performance conditions nor awards with market conditions.

Stock Options

During the three months ended September 30, 2015 and 2014, the Company incurred $37,944 and $39,575 of compensation expense related to stock options, respectively. As of September 30, 2015, there was total remaining compensation expense of $0.3 million related to employee stock options, which will be recorded over a weighted average period of approximately 2.3 years.

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The following table summarizes the stock option activity for the three months ended September 30, 2015.

	Options	Weighted Average Exercise Price Per Share	Aggregate Intrinsic Value (in thousands)	Weighted Average Grant Date Fair Value Per Award (1)
Outstanding at June 30, 2015	233,127	$9.89	$283	$5.96
Granted through stock option plan	—	—		
Exercised	—	—		
Cancellations, expirations and forfeitures	—	—		
Outstanding at September 30, 2015	233,127	9.89	$485	$5.96
Shares exercisable at September 30, 2015	158,213	10.60	$249	$5.87

(1) For awards held by A-Mark employees, the fair value of the awards assumed in Distribution was based on the awards' fair value at grant date, which were determined by SGI prior to the Distribution. Since the Company does not recognize compensation costs for the awards assumed in the Distribution held by employees of SGI, the calculation of the weighted average fair value per share price at grant date was solely based on the awards' fair value at grant date that were awarded to employees of A-Mark.

Following is a summary of the status of stock options outstanding at September 30, 2015:

Exercise Price Ranges		Options Outstanding			Options Exercisable		
From	To	Number of Shares Outstanding	Weighted Average Remaining Contractual Life (Years)	Weighted Average Exercise Price	Number of Shares Exercisable	Weighted Average Remaining Contractual Life (Years)	Weighted Average Exercise Price
$—	$10.00	134,239	7.11	$8.39	62,325	7.14	$8.44
10.01	15.00	98,888	7.03	11.94	95,888	6.96	12.00
		233,127	7.07	9.89	158,213	7.03	10.60

Restricted Stock Units

During the three months ended September 30, 2015 and 2014, the Company incurred $15,530 and $22,561 of compensation expense related to RSUs, respectively. The remaining compensation expense that will be recorded under restricted stock grants totals $46,556, which will be recorded over a weighted average period of approximately 0.6 years.

The following table summarizes the RSU activity for the three months ended September 30, 2015:

	Shares	Weighted Average Share Price at Grant Date (1)
Outstanding at June 30, 2015	86,298	$2.34
Shares granted	—	—
Shares released	—	—
Shares surrendered to cover employee minimum withholding taxes	—	—
Shares forfeited	—	—
Outstanding at September 30, 2015	86,298	$2.34
Vested but unissued at September 30, 2015	35,957	$—

(1) For awards held by A-Mark employees, the fair value of the awards assumed in Distribution was based on the awards' fair value at grant date, which were determined by SGI prior to the Distribution. Since, the Company does not recognize compensation costs for the awards assumed in the Distribution held by employees of SGI, the calculation of the weighted average share price at grant date was solely based on the awards' fair value at

grant date that were awarded to employees of A-Mark.

No tax benefit was recognized in the condensed consolidated statements of income related to share-based compensation for the three months ended September 30, 2015. No share-based compensation was capitalized for the three months ended September 30, 2015 and 2014.

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Stock Appreciation Rights
The Company, from time to time, may grant SARs to certain key employees and executive officers. The number of shares to be received under these awards ultimately depends on the appreciation in the Company's common stock over a specified period of time, generally 3.0 years. At the end of the stated appreciation period, the number of shares of common stock issued will be equal in value to the appreciation in the shares of the Company's common stock, as measured from the stock's closing price on the date of grant to the average price in the last month of the third year of vesting. As of September 30, 2015 and June 30, 2015, the Company had zero and 8,990 SARs issued and outstanding, respectively. The Company did not recognize any compensation expense related to these awards during the three months ended September 30, 2015 and 2014.
Certain Anti-Takeover Provisions
The Company's Certificate of Incorporation and by-laws contain certain anti-takeover provisions that could have the effect of making it more difficult for a third party to acquire, or of discouraging a third party from attempting to acquire, control of the Company without negotiating with its Board. Such provisions could limit the price that certain investors might be willing to pay in the future for the Company's securities. Certain of such provisions provide for a Board with staggered terms, allow the Company to issue preferred stock with rights senior to those of the common stock, or impose various procedural and other requirements which could make it more difficult for stockholders to effect certain corporate actions.
16. CUSTOMER AND SUPPLIER CONCENTRATION
Customer Concentration
Customers providing 10 percent or more of the Company's revenues for the three months ended September 30, 2015 and 2014 are listed below:
in thousands

	Three Months Ended					
	September 30, 2015			September 30, 2014		
	Amount	Percent		Amount	Percent	
Total revenue	$2,006,936	100.0	%	$1,453,466	100.0	%
Customer concentrations						
HSBC Bank USA	$333,553	16.6	%	$534,538	36.8	%
JM Bullion	246,869	12.3		66,565	4.6	
Total	$580,422	28.9	%	$601,103	41.4	%

Customers providing 10 percent or more of the Company's accounts receivable as of September 30, 2015 and June 30, 2015, respectively, are listed below:
in thousands

	September 30, 2015			June 30, 2015		
	Amount	Percent		Amount	Percent	
Total accounts receivable, net	$47,899	100.0	%	$30,025	100.0	%
Customer concentrations						
ABN AMRO	$9,967	20.8	%	$—	—	%
Total	$9,967	20.8	%	$—	—	%

No single customer provided 10 percent or more of the Company's secured loans as of September 30, 2015 and June 30, 2015.
The loss of any of the above listed customers could have a material adverse effect on the operations of the Company.
Supplier Concentration
A-Mark buys precious metals from a variety of sources, including through brokers and dealers, from sovereign and private mints, from refiners and directly from customers. The Company believes that no one or small group of suppliers is critical to its business, since other sources of supply are available that provide similar products on comparable terms.

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17. GEOGRAPHIC INFORMATION

Revenue are attributed to geographic location based on customer location. The Company's geographic operations are as follows:

in thousands

	Three Months Ended	
	September 30, 2015	September 30, 2014
Revenue by geographic region:		
United States	$1,853,272	$1,313,486
Europe	52,132	54,950
North America, excluding United States	86,785	71,779
Asia Pacific	13,266	11,312
Africa	45	—
Australia	1,404	1,939
South America	32	—
Total revenue	$2,006,936	$1,453,466

in thousands

	September 30, 2015	June 30, 2015
Inventories by geographic region:		
United States	$241,114	$173,939
Europe	6,148	4,374
North America, excluding United States	5,842	12,287
Asia	1,402	901
Total inventories	$254,506	$191,501

in thousands

	September 30, 2015	June 30, 2015
Assets by geographic region:		
United States	$373,785	$302,046
Europe	8,167	10,668
North America, excluding United States	5,842	12,287
Asia	1,402	901
Total assets	$389,196	$325,902

in thousands

	September 30, 2015	June 30, 2015
Long term assets by geographic region:		
United States	$13,093	$13,204
Europe	69	72
Total long-term assets	$13,162	$13,276

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18. SUBSEQUENT EVENTS
Additional Investment in a Noncontrolled Entity
On October 26, 2015, the Company entered into an amended and restated agreement with one of its customers, an online retailer of generic gold and silver coins and bullion, to increase the Company's ownership of the retailer's outstanding common stock from 9% to up to 20% on a fully diluted basis. The additional investment is to be made in two tranches, for an aggregate purchase price of $4.7 million. The closing of the first tranche, for 6.2% of the retailer's issued and outstanding common stock at a purchase price equal to $2.3 million, took place on October 28, 2015. The closing of the second tranche, for 5.8% of the retailer's issued and outstanding common stock at a purchase price equal to $2.3 million, will take place on or prior to January 15, 2016; provided that A-Mark’s obligation to close the second tranche will be subject to the condition, among others, that the retailer's gross profit for the quarter ending December 31, 2015 shall be not less than $3.0 million. The parties also entered into an amendment to the existing exclusive supplier agreement which, among other provisions, extended the term of that agreement to 2020 (subject to renewal and earlier termination under certain circumstances). A-Mark will continue to provide fulfillment services to the retailer under the terms of a previously existing fulfillment agreement. A-Mark has the right to designate a board observer, who is entitled to attend, in a nonvoting observer capacity, all meetings of the company's board of directors and all committees thereof, and so long as it owns at least 15% of the outstanding stock of the retailer, the Company has the right to appoint a board member to the retailer's board of directors.
Dividend Declaration
On October 30, 2015, the Board of Directors of the Company declared a quarterly cash dividend of $0.05 per common share to stockholders of record at the close of business on November 13, 2015, which is scheduled to be paid on November 25, 2015.
ITEM 2. MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Cautionary Statement Pursuant to the Private Securities Litigation Reform Act of 1995
This Quarterly Report on Form 10-Q ("Form 10-Q") contains statements that are considered forward-looking statements. Forward-looking statements give the Company's current expectations and forecasts of future events. All statements other than statements of current or historical fact contained in this Quarterly Report, including statements regarding the Company's future financial position, business strategy, budgets, projected costs and plans and objectives of management for future operations, are forward-looking statements. The words “anticipate,” “believe,” “continue,” “estimate,” “expect,” “intend,” “may,” “plan,” and similar expressions, as they relate to the Company, are intended to identify forward-looking statements. These statements are based on the Company's current plans, and the Company's actual future activities and results of operations may be materially different from those set forth in the forward-looking statements. These forward-looking statements are subject to risks and uncertainties that could cause actual results to differ materially from the statements made. Any or all of the forward-looking statements in this Quarterly Report may turn out to be inaccurate. The Company has based these forward-looking statements largely on its current expectations and projections about future events and financial trends that it believes may affect its financial condition, results of operations, business strategy and financial needs. The forward-looking statements can be affected by inaccurate assumptions or by known or unknown risks, uncertainties and assumptions. The Company undertakes no obligation to publicly revise these forward-looking statements to reflect events occurring after the date hereof. All subsequent written and oral forward-looking statements attributable to the Company or persons acting on its behalf are expressly qualified in their entirety by the cautionary statements contained in this Form 10-Q.
The following discussion and analysis of our financial condition and results of operations should be read in conjunction with the condensed consolidated financial statements and notes contained elsewhere in this Form 10-Q. This discussion contains forward-looking statements that reflect our plans, estimates and beliefs. Our actual results could differ materially from those discussed in these forward-looking statements. Factors that could cause or contribute to these differences include those factors discussed below and elsewhere in this Quarterly Report, particularly in “Risk Factors.”
Introduction

Management's discussion and analysis of financial condition and results of operations is provided as a supplement to the accompanying condensed consolidated financial statements and related notes to help provide an understanding of our results of operations and financial condition. Our discussion is organized as follows:

- Executive overview. This section provides a general description of our business, as well as significant transactions and events that we believe are important in understanding the results of operations.

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- Results of operations. This section provides an analysis of our results of operations presented in the accompanying condensed consolidated statements of income by comparing the results for the respective years. Included in our analysis is a discussion of five performance metrics: (i) inventory turnover ratio and (ii) number of secured loans at quarter-end. Our inventory turnover ratio is a measure of how quickly inventory has moved during the period; higher turnover ratios are generally associated with periods of higher volatility. The majority of the Company's trading activities involve two-day value trades that produce low gross margin percentages. The inventory turnover ratio measures the efficiency of our trading activity and the liquidity of our inventory. The number of secured loans at quarter-end, together with the aggregate of secured loans outstanding, are indicators of the size of our finance lending business.
- Financial condition and liquidity and capital resources. This section provides an analysis of our cash flows, as well as a discussion of our outstanding debt that existed as of September 30, 2015. Included in the discussion of outstanding debt is a discussion of the amount of financial capacity available to fund our future commitments, as well as a discussion of other financing arrangements.
- Critical accounting estimates. This section discusses those accounting policies that both are considered important to our financial condition and results, and require significant judgment and estimates on the part of management in their application. In addition, all of our policies, including critical accounting policies, are summarized in Note 2 to the accompanying condensed consolidated financial statements.
- Recent accounting pronouncements. This section discusses new accounting pronouncements, dates of implementation and impact on our accompanying condensed consolidated financial statements, if any.

Executive Overview

Our Business

A-Mark is a full-service precious metals trading company, and an official distributor for many government mints throughout the world. We offer gold, silver, platinum and palladium in the form of bars, plates, powder, wafers, grain, ingots and coins. Our Industrial unit services manufacturers and fabricators of products utilizing or incorporating precious metals. Our Coin & Bar unit deals in over 200 coin and bar products in a variety of weights, shapes and sizes for distribution to dealers and other qualified purchasers. We have trading centers in Santa Monica, California and Vienna, Austria for buying and selling precious metals. In addition to wholesale trading activity, A-Mark offers its customers a variety of services, including financing, consignment, logistics and various customized financial programs. As a U.S. Mint-authorized purchaser of gold, silver and platinum coins, A-Mark purchases product directly from the U.S. Mint and other sovereign mints for sale to its customers.

Through our subsidiary Collateral Finance Corporation, referred to as CFC, a licensed California Finance Lender, we offer loans collateralized by numismatic and semi-numismatic coins and bullion to coin and precious metal dealers, investors and collectors. Through our Transcontinental Depository Services subsidiary, referred to as TDS, we offer a variety of managed storage options for precious metals products to financial institutions, dealers, investors and collectors around the world. TDS started doing business in 2012. Our financing business generates interest income that is not classified as revenues. If interest income generated by the financing business were classified as revenues, it would represent less than 1% of our total revenues for each of the periods presented. Our storage business generates less than 1% of total revenues for each of the periods presented.

In July 2015, the Company formed a wholly-owned subsidiary, A-M Global Logistics, LLC, referred to as Logistics, which operates the Company's logistics fulfillment center based in Las Vegas, Nevada. Logistics provides our customers an array of complementary services, including storage, shipping, handling, receiving, processing, and inventorying of precious metals and custom coins on a secure basis. Our logistics business generates less than 1% of the total revenues for each of the periods presented.

Our Strategy

The Company has grown from a small numismatics firm in 1965 to a significant participant in the bullion and coin markets, with approximately $6.0 billion in revenues for the year ended June 30, 2015. Our strategy continues to focus on growth, including the volume of our business, our geographic presence, particularly in Europe, and the scope of complementary products and services that we offer to our customers. We intend to promote our growth by leveraging off of our existing, integrated operations; the depth of our customer relations; our access to market makers, suppliers and government mints and other mints; our trading offices in the U.S. and Europe, which are open 17 hours a day 5 days a week; our expansive precious metals dealer network; our depository relationships around the world; our knowledge of secured lending; our logistics capabilities; our trading expertise; and the quality and experience of our management team.

Our Customers

The Company sells gold, silver, platinum and palladium products to a wide array of customers, including financial institutions, bullion retailers, industrial manufacturers, and sovereign mints. The Company makes a two way market, which results

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in many customers also operating as our suppliers. This diverse base of customers purchases a variety of products from the Company in a multitude of grades primarily in the form of coins and bars.

Factors Affecting Revenues and Gross Profits

The Company operates in a high volume/low margin industry. Revenues are impacted by three primary factors: product volume, market prices and market volatility. A material change in any one or more of these factors may result in a significant change in the Company's revenues. A significant increase or decrease in revenues can occur simply based on changes in the underlying commodity prices and may not be reflective of an increase or decrease in the volume of products sold.

Gross profit is the difference between our revenues and the cost of our products. Since we quote prices based on the current commodity market prices for precious metals, we enter into a combination of forward and futures contracts to effect a hedge position equal to the underlying precious metal commodity value, which substantially represents inventory subject to price risk. We enter into these derivative transactions solely for the purpose of hedging our inventory, and not for speculative purposes. Our gross profit includes the gains and losses resulting from these derivative instruments. However, the gains and losses on the derivative instruments are substantially offset by the gains and losses on the corresponding changes in the market value of our precious metals inventory. As a result, our results of operations generally are not materially impacted solely by changes in commodity prices.

Volatility also affects our gross profits. Greater volatility typically causes the trading spreads to widen resulting in an increase in the gross profit. Product supply constraints during extended periods of higher volatility has historically resulted in a heightening of wider trading spreads resulting in further improvement in the gross profit.

The Company has also been able recently to increase incremental margins, with corresponding positive contributions to gross profits, through certain distribution contracts and strategic partnerships. Under these arrangements, the Company sells unique bullion products to distributors for marketing to the retail public, under its standard trading terms with no right of return. The related distribution contracts provide the Company with higher margins than its ordinary trading activities.

Fiscal Year

Our fiscal year end is June 30 each year. Unless otherwise stated, references to years in this report relate to fiscal years rather than to calendar years.

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RESULTS OF OPERATIONS

Overview of Results of Operations for the Three Months Ended September 30, 2015 and 2014

Condensed Consolidated Results of Operations

The operating results of our business for the three months ended September 30, 2015 and 2014 are as follows:

in thousands, except per share data and performance metrics

Three Months Ended September 30,	2015		2014		$	%
	$	% of revenue	$	% of revenue	Increase/(decrease)	Increase/(decrease)
Revenues	$2,006,936	100.000 %	$1,453,466	100.000 %	$ 553,470	38.1 %
Gross profit	14,424	0.719 %	5,730	0.394 %	$ 8,694	151.7 %
Selling, general and administrative expenses	(6,408)	(0.320)%	(4,219)	(0.290)%	$ 2,189	51.9 %
Interest income	1,933	0.096 %	1,477	0.102 %	$ 456	30.9 %
Interest expense	(1,234)	(0.061)%	(1,063)	(0.073)%	$ 171	16.1 %
Unrealized losses on foreign exchange	(39)	(0.002)%	(9)	(0.001)%	$ 30	NM
Net income before provision for income taxes	8,676	0.432 %	1,916	0.132 %	$ 6,760	352.8 %
Provision for income taxes	(3,312)	(0.165)%	(778)	(0.054)%	$ 2,534	325.7 %
Net income	$5,364	0.267 %	$1,138	0.078 %	$ 4,226	371.4 %
Per Share Data:						
Basic	$0.77		$0.16		$ 0.61	381.3 %
Diluted	$0.76		$0.16		$ 0.60	375.0 %
Performance Metrics:						
Inventory turnover ratio(1)	8.9		8.6		0.3	3.5 %
Number of secured loans at quarter end(2)	470		120		350	291.7 %

NM Not meaningful.

(1) Inventory turnover ratio is the cost of sales divided by average inventory, measured at recorded fair value.

(2) Number of outstanding secured loans to customers at quarter end.

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Revenues

Three Months Ended September 30,	2015		2014		$	%
in thousands	$	% of revenue	$	% of revenue	Increase/(decrease)	Increase/(decrease)
Revenues	$2,006,936	100.000 %	$1,453,466	100.000 %	$ 553,470	38.1 %

Revenues for the three months ended September 30, 2015 increased $553.5 million, or 38.1%, to $2.007 billion from $1.453 billion in 2014. Our revenues increased primarily due to an increase in the total amount of gold ounces and silver ounces sold during the three months ended September 30, 2015 as compared to 2014. A key factor contributing to the increase in demand was the volatility and the decrease in commodity prices; the average spot prices for gold declined 11.8% and average spot prices for silver declined 22.2% during the three months ended September 30, 2015 as compared to 2014. The increase in volatility was due in part to macro-economic factors which created an increase in demand at lower price levels. The combination of higher volatility and demand for product that exceeds supply historically results in higher revenues, but is not representative of normal market conditions.

Gross Profit

Three Months Ended September 30,	2015		2014		$	%
in thousands, except performance metrics	$	% of revenue	$	% of revenue	Increase/(decrease)	Increase/(decrease)
Gross profit	$14,424	0.719 %	$5,730	0.394 %	$ 8,694	151.7 %
Inventory turnover ratio	8.9		8.6		0.3	3.5 %

Gross profit for the three months ended September 30, 2015 increased by $8.7 million, or 151.7%, to $14.4 million from $5.7 million in 2014. The Company's profit margin increased 84.6% to 0.72% from 0.39% in 2014, primarily due to higher premium spreads on the Company's primary products. The Company experienced higher volatility and greater supply constraints, compared to 2014, which resulted in a widening of trading spreads. Our inventory turnover rate increased by 3.5% to 8.9 from 8.6 as compared to 2014. This increase in the inventory turnover rate was primarily due to higher demand for our primary products; offset by an increase in the carry length associated with the Company's development of foreign markets and the longer carry periods associated with higher margin value added products, which resulted in the Company carrying higher inventory levels in foreign and domestic locations at lower turnover rates, compared to 2014.

Selling, General and Administrative Expenses

Three Months Ended September 30,	2015		2014		$	%
in thousands	$	% of revenue	$	% of revenue	Increase/(decrease)	Increase/(decrease)
Selling, general and administrative expenses	$(6,408)	(0.320)%	$(4,219)	(0.290)%	$ 2,189	51.9 %

Selling, general and administrative expenses for the three months ended September 30, 2015 increased $2.2 million, or 51.9%, to $6.4 million from $4.2 million in 2014. The increase is primarily due to performance-based compensation accruals and the operational cost of a logistics center established to provide fulfillment services to our customers.

In fiscal 2015, the Company expanded its logistics capabilities by relocating to a new facility in Las Vegas, Nevada. The Company began to receive and ship inventory from this facility shortly after June 30, 2015. The Company is proceeding with its plans to reduce the volume of business it does with third-party storage providers during this fiscal year.

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Interest Income
The Company enters into secured loans and secured financing structures with its customers under which it charges interest income. The Company offers a number of secured financing options to its customers to finance their precious metals purchases including consignments and other structured inventory finance products. Through its wholly owned subsidiary, CFC, the Company also enters into loans secured by precious metals and numismatic material owned by the borrowers and held by the Company for the term of the loan.

Three Months Ended September 30,	2015			2014			$	%	
in thousands, except performance metrics	$	% of revenue		$	% of revenue		Increase/(decrease)	Increase/(decrease)	
Interest income	$1,933	0.096	%	$1,477	0.102	%	$ 456	30.9	%
Number of secured loans at quarter-end	470			120			350	291.7	%

Interest income for the three months ended September 30, 2015 increased $0.5 million, or 30.9%, to $1.9 million from $1.5 million in 2014. Interest income increased primarily due to an increase in the size of the CFC loan portfolio as well as improvement in certain A-Mark finance products. The improvement in the value of loans outstanding at CFC, which resulted in higher interest income, was due primarily to an increase in the number of CFC borrowers. The number of CFC borrowers increase by 291.7% to 470 from 120 in 2014. This 291.7% increase in the number of secured loans was primarily due to acquisitions of bullion based loan portfolios from a retail customer.
Interest Expense
The Company incurs interest expense as a result of usage under its lines of credit, product financing arrangements and liability on borrowed metals. Also, the Company incurs interest expense as a result of its product financing agreements for the transfer and subsequent re-acquisition of gold and silver at a fixed price to a third-party finance company. Additionally, the Company incurs interest expense when we borrow precious metals from our suppliers under short-term arrangements, which bear interest at a designated rate.

Three Months Ended September 30,	2015			2014			$	%	
in thousands	$	% of revenue		$	% of revenue		Increase/(decrease)	Increase/(decrease)	
Interest expense	$(1,234)	(0.061	)%	$(1,063)	(0.073	)%	$ 171	16.1	%

Interest expense for the three months ended September 30, 2015 increased $0.2 million, or 16.1% to $1.2 million from $1.1 million in 2014. The increase was related primarily to usage of our lines of credit. We believe the interest rates paid on borrowings under our Trading Credit Facility are consistent with current market interest rates for first lien demand loans secured by inventory and receivables. We utilize our lines of credit extensively for working capital requirements.
Provision for Income Taxes
Our effective rate could be adversely affected by the relative proportions of revenue and income before taxes in the various domestic and international jurisdictions in which we operate. We are also subject to changing tax laws, regulations and interpretations in multiple jurisdictions in which we operate. Our effective rate can also be influenced by the tax effects of purchase accounting for acquisitions and non-recurring charges, which may cause fluctuations between reporting periods.

Three Months Ended September 30,	2015			2014			$	%	
in thousands	$	% of revenue		$	% of revenue		Increase/(decrease)	Increase/(decrease)	
Provision for income taxes	(3,312)	(0.165	)%	(778)	(0.054	)%	2,534	325.7	%

Our provision for income taxes was $3.3 million and $0.8 million for the three months ended September 30, 2015 and 2014, respectively. Our effective tax rate was approximately 38.2% and 40.6% for the three months ended September 30, 2015 and 2014, respectively. Our effective tax rate differs from the federal statutory rate due to permanent adjustments for nondeductible items. In addition, the Company accrues for income tax due in state and foreign jurisdictions in which it operates. Our estimate of the annual effective tax rate ("blended rate") changed primarily due to the mix of states that we operate and a decrease in non-deductible tax expense (as a percentage of taxable income), compared to 2014.

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LIQUIDITY AND FINANCIAL CONDITION
Primary Sources and Uses of Cash
Overview
Liquidity is defined as our ability to generate sufficient amounts of cash to meet all of our cash needs. Liquidity is of critical importance to us and imperative to maintain our operations on a daily basis.
A substantial portion of our assets are liquid. As of September 30, 2015, approximately 94% of our assets consisted of cash, customer receivables, and precious metals inventory, measured at fair value. Cash generated from the sales of our precious metals products is our primary source of operating liquidity.
Typically, we acquire our inventory by: (1) purchasing inventory from our suppliers by utilizing our own capital and lines of credit; (2) borrowing precious metals from our suppliers under short-term arrangements which bear interest at a designated rate, and (3) repurchasing inventory at an agreed-upon price based on the spot price on the specified repurchase date.
In addition, the Company generates cash from earned interest income. Through CFC, the Company enters into secured loans and secured financing structures with its customers under which it charges interest income. The Company offers a number of secured financing options to its customers to finance their precious metals purchases including consignments and other structured inventory finance products. The loans are secured by precious metals and numismatic material owned by the borrowers and held by the Company as security for the term of the loan. Furthermore, our customers may enter into purchase agreements whereby the customer agrees to purchase our inventory at the prevailing spot price for delivery of the product at a specific point in time in the future; interest income is earned from contract date until the material is delivered and paid for in full.
We continually review our overall credit and capital needs to ensure that our capital base, both stockholders' equity and available credit facilities, can appropriately support our anticipated financing needs. The Company also continually monitors its current and forecasted cash requirements, and draw upon and pays down its lines of credit so as to minimize interest expense.
Lines of Credit
in thousands

	September 30, 2015	June 30, 2015	September 30, 2015 Compared to June 30, 2015
Lines of credit	$176,900	$147,000	$29,900

A-Mark has a borrowing facility ("Trading Credit Facility") with a group of financial institutions under an inter-creditor agreement, which provides for lines of credit up to the maximum of the credit facility. All lenders have a perfected, first security interest in all assets of the Company presented as collateral. Loan advances will be available against a borrowing base report of eligible assets in accordance with the inter-creditor agreement currently in place. Pledged collateral comprises assigned and confirmed inventory, trade receivable, trade advances, derivatives, equity and pledged non bullion and bullion loans.
As of September 30, 2015, the maximum of the Trading Credit Facility was $205.0 million. The Company routinely uses the Trading Credit Facility to purchase precious metals from suppliers and for operating cash flow purposes. Amounts under the Trading Credit Facility bear interest based on London Interbank Offered Rate ("LIBOR") plus a margin. The one-month LIBOR rate was approximately 0.19% and 0.19% as of September 30, 2015 and June 30, 2015, respectively. Borrowings are due on demand and totaled $176.9 million and $147.0 million at September 30, 2015 and at June 30, 2015, respectively. The Company is able to access additional credit as needed to finance operations, subject to the overall limits of the Trading Credit Facility and lender approval of the revised borrowing base calculation. The amounts available under the Trading Credit Facility are determined at the end of each week following a specified borrowing base formula. The amounts available under the Trading Credit Facility after taking into consideration current borrowings, based upon the latest approved borrowing bases in effect, totaled $34.3 million and $20.9 million at September 30, 2015 and June 30, 2015, respectively.
The Trading Credit Facility has certain restrictive financial covenants, which require the Company to maintain a minimum tangible net worth. As of September 30, 2015, the minimum tangible net worth financial covenant under the

Trading Credit Facility was $35.0 million. The Company is in compliance with all restrictive financial covenants as of September 30, 2015. The Company's ability to pay dividends, if it were to elect to do so, could be limited as a result of these restrictions. Each lender has the right to cancel its credit line upon written notice.

Liability on Borrowed Metals

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in thousands

	September 30, 2015	June 30, 2015	September 30, 2015 Compared to June 30, 2015
Liability on borrowed metals	$4,009	$9,500	$(5,491)

We borrow precious metals from our suppliers under short-term arrangements which bear interest at a designated rate. Amounts under these arrangements are due at maturity and require repayment either in the form of precious metals or cash. Our inventories included borrowed metals with market values totaling $4.0 million and $9.5 million at September 30, 2015 and at June 30, 2015, respectively.

Product Financing Agreement

in thousands

	September 30, 2015	June 30, 2015	September 30, 2015 Compared to June 30, 2015
Product financing agreement	$50,030	$39,425	$10,605

The Company has an agreement with a financial institution (a third party) that allows the Company to transfer its gold and silver inventory at a fixed price to this third party. Such agreement allows the Company to repurchase this inventory at an agreed-upon price based on the spot price on the repurchase date. The third party charges monthly interest as a percentage of the market value of the outstanding obligation; such monthly charges are classified in interest expense. These transactions do not qualify as sales and therefore have been accounted for as financing arrangements and reflected in the condensed consolidated balance sheet within product financing obligation. The obligation is stated at the amount required to repurchase the outstanding inventory. Both the product financing arrangement and the underlying inventory (which is entirely restricted) are carried at fair value, with changes in fair value included as component of cost of sales. Such obligation totaled $50.0 million and $39.4 million as of September 30, 2015 and June 30, 2015, respectively.

Secured Loans

in thousands

	September 30, 2015	June 30, 2015	September 30, 2015 Compared to June 30, 2015
Secured loans	$50,416	$49,316	$1,100

The Company is a California license finance lender that makes and acquires commercial loans secured by numismatic and semi-numismatic coins and bullion that affords our customers a convenient means of financing their inventory or collections. Predominantly, most of the Company's secured loans are short-term in nature and do not represent a long term obligation of the Company. The renewal of these instruments is at the discretion of the Company and, as such, provides us with some flexibility in regards to our capital deployment strategies.

Dividends

in thousands

	September 30, 2015	June 30, 2015	September 30, 2015 Compared to June 30, 2015
Dividends, declared	$349	$698	$(349)

In fiscal 2015, the Board of Directors of the Company initiated a cash dividend policy that calls for the payment of a quarterly cash dividend of $0.05 per common share. Two quarterly dividends of $0.05 per common share were paid by the Company in fiscal 2015.

In fiscal 2016, on September 11, 2015, the Board of Directors of the Company declared a quarterly cash dividend of $0.05 per common share to stockholders of record at the close of business on September 24, 2015, which was paid on October 5, 2015. On October 30, 2015, the Board of Directors of the Company declared a quarterly cash dividend of $0.05 per common share to stockholders of record at the close of business on November 13, 2015, which is scheduled to be paid on November 25, 2015.

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Cash Flows

The majority of the Company’s trading activities involve two day value trades under which payment is made in advance of delivery or product is received in advance of payment. The high volume, rapid rate of inventory turn, and high average value per trade can cause material changes in the sources of cash used in or provided by operating activities on a daily basis. The Company manages these variances through its liquidity forecasts and counterparty limits maintaining a liquidity reserve to meet the Company’s cash needs. The Company uses various short-term financial instruments to manage the rapid cycle of our trading activities from customer purchase order to cash collections and product delivery, which can cause material changes in the of cash used in or provided by financing activities on a daily basis.

The following summarizes components of our condensed consolidated statements of cash flows for the three months ended September 30, 2015 and 2014:

in thousands

Three Months Ended	September 30, 2015	September 30, 2014	Three Months Ended September 30, 2015 Compared to Three Months Ended September 30, 2014
Net cash (used in) provided by operating activities	$(54,495)	$5,634	(60,129)
Net cash used in investing activities	$(1,544)	$(2,973)	1,429
Net cash provided by (used in) financing activities	$40,156	$(11,197)	51,353

Our principal capital requirements have been to fund (i) working capital and (ii) capital expenditures. Our working capital requirements fluctuate with market conditions, the availability of precious metals and the volatility of precious metals commodity pricing.

Net cash (used in) provided by operating activities

Operating activities used $54.5 million and provided $5.6 million in cash for the three months ended September 30, 2015 and 2014, respectively, representing an increase of $60.1 million in the use of cash compared to three months ended September 30, 2014. This period over period increase in the of use of funds in operating activities was primarily due changes in the balances of inventory, derivative liabilities and liabilities on borrowed metals, offset by the change in net income, and changes in the balances of derivative assets, and accounts payables.

Net cash used in investing activities

Investing activities used $1.5 million and used $3.0 million in cash for the three months ended September 30, 2015 and 2014, respectively, representing an increase of $1.4 million in the source of cash compared to three months ended September 30, 2014. This period over period increase is the result of the change in balance of secured loans of $0.5 million that was primarily due to fewer acquisitions of loan portfolios, and a fewer investments of $1.1 million made in the current comparable period.

Net cash provided by (used in) financing activities

Financing activities provided $40.2 million and used $11.2 million in cash for the three months ended September 30, 2015 and 2014, respectively, representing an increase of $51.4 million in the source of cash compared to three months ended September 30, 2014. This period over period increase in the source of funds provided by financing activities was primarily due to changes in the balance of product financing arrangements of $14.6 million, and by the change in the balance of our lines of credit of $37.1 million.

CAPITAL RESOURCES

We believe that our current cash and cash equivalents, availability under the Trading Credit Facility, and cash we anticipate to generate from operating activities will provide us with sufficient liquidity to satisfy our working capital needs, capital expenditures, investment requirements and commitments through at least the next twelve months.

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CONTRACTUAL OBLIGATIONS, CONTINGENT LIABILITIES AND COMMITMENTS

Counterparty Risk

We manage our counterparty risk by setting credit and position risk limits with our trading counterparties. These limits include gross position limits for counterparties engaged in sales and purchase transactions with us. They also include collateral limits for different types of sale and purchase transactions that counter parties may engage in from time to time.

Commodities Risk and Derivatives

We use a variety of strategies to manage our risk including fluctuations in commodity prices for precious metals. See Note 10 in the accompanying condensed consolidated financial statements. Our inventories consist of, and our trading activities involve, precious metals and precious metal products, whose prices are linked to the corresponding precious metals prices. Inventories purchased or borrowed by us are subject to price changes. Inventories borrowed are considered natural hedges, since changes in value of the metal held are offset by the obligation to return the metal to the supplier.

Open sale and purchase commitments in our trading activities are subject to changes in value between the date the purchase or sale price is fixed (the trade date) and the date the metal is received or delivered (the settlement date). We seek to minimize the effect of price changes of the underlying commodity through the use of forward and futures contracts. Our open sale and purchase commitments generally settle within 2 business days, and for those commitments that do not have stated settlement dates, we have the right to settle the positions upon demand.

Our policy is to substantially hedge our underlying precious metal commodity inventory position. We regularly enter into metals commodity forward and futures contracts with major financial institutions to hedge price changes that would cause changes in the value of our physical metals positions and purchase commitments and sale commitments. We have access to all of the precious metals markets, allowing us to place hedges. However, we also maintain relationships with major market makers in every major precious metals dealing center, which allows us to enter into contracts with market makers. Futures and forwards contracts open at September 30, 2015 are scheduled to settle within 30 days.

The Company enters into these derivative transactions solely for the purpose of hedging our inventory holding risk, and not for speculative market purposes. Due to the nature of our hedging strategy, we are not using hedge accounting as defined under, Derivatives and Hedging Topic 815 of the Accounting Standards Codification ("ASC".) Gains or losses resulting from our futures and forward contracts are reported as cost of sales with the related amounts due from or to counterparties reflected as a derivative asset or liability (see Notes 10 to the accompanying condensed consolidated financial statements.) Gains or losses resulting from the termination of hedge contracts are reported as cost of sales. The Company’s gains (losses) on derivative instruments are substantially offset by the changes in fair market value underlying precious metals inventory and open sale and purchase commitments, which is also recorded in cost of sales in the condensed consolidated statements of income.

Net gains (losses) on derivative instruments in the condensed consolidated statements of income totaled \$(14.4) million and \$(6.4) million for the three months ended September 30, 2015 and 2014, respectively (see Note 10.)

Commitments and Contingencies

Refer to Note 13 of the Notes to Consolidated Financial Statements in the 2015 Annual Report for information relating to minimum rental payments under operating and capital leases, consulting and employment contracts, and other commitments. Other than the following item, there has been no material changes to those scheduled commitments as of the filing of that report.

On October 25, 2015, the Company received notification from the City of Santa Monica that the City was challenging the Company's classification as an "agent/broker" for purposes of computing the business license fee due to the City. Historically, A-Mark has paid its business license fee on net receipts, consistent with the "agent/broker" classification. The City of Santa Monica has asserted that the Company should have instead paid the fee based on gross receipts and has made a preliminary assessment against the Company seeking a material amount of what it believes to be underreported fees, together with a material amount of penalties and interest. The Company intends to meet with the City of Santa Monica shortly to discuss the preliminary assessment and the position taken by the Company with respect to the calculation of the fee. Neither the outcome of this administrative matter nor the amount or range of a potential impact to the Company in the event of an unfavorable outcome can be determined at this time.

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In a hedging relationship, the change in the value of the derivative financial instrument is offset to a great extent by the change in the value of the underlying hedged item. The following table summarizes the results of our hedging activities as follows at September 30, 2015 and at June 30, 2015, showing the precious metal commodity inventory position, net of open sale and purchase commitments, which is subject to price risk:

	September 30, 2015	June 30, 2015
Inventory	$254,506	$191,501
Less unhedgable inventory:		
Commemorative coin inventory, held at lower of cost or market	(163)	(1,518)
Premium on metals position	(3,529)	(3,255)
Inventory value not hedged	(3,692)	(4,773)
Subtotal	250,814	186,728
Commitments at market:		
Open inventory purchase commitments	556,388	444,023
Open inventory sales commitments	(477,089)	(249,081)
Margin sale commitments	(11,436)	(12,430)
In-transit inventory no longer subject to market risk	(16,625)	(13,807)
Unhedgable premiums on open commitment positions	6,356	528
Inventory borrowed from suppliers	(4,009)	(9,500)
Product financing obligation	(50,030)	(39,425)
Advances on industrial metals	3,709	3,340
Inventory subject to price risk	258,078	310,376
Inventory subject to derivative financial instruments:		
Precious metals forward contracts at market values	123,658	202,323
Precious metals futures contracts at market values	134,367	107,993
Total market value of derivative financial instruments	258,025	310,316
Net inventory subject to commodity price risk	$53	$60

We are exposed to the risk of default of the counter parties to our derivative contracts. Significant judgment is applied by us when evaluating the fair value implications. We regularly review the creditworthiness of our major counterparties and monitor our exposure to concentrations. At September 30, 2015, we believe our risk of counterparty default is mitigated based on our evaluation, the strong financial condition of our counterparties, and the short-term duration of these arrangements.

OFF-BALANCE SHEET ARRANGEMENTS

As of September 30, 2015 and June 30, 2015, we had the following outstanding sale and purchase commitments and open forward and future contracts, which are normal and recurring, in nature:

in thousands	September 30, 2015	June 30, 2015
Purchase commitments	$556,388	$444,023
Sales commitments	$(477,089)	$(249,081)
Margin sale commitments	$(11,436)	$(12,430)
Open forward contracts	$123,658	$202,323
Open futures contracts	$134,367	$107,993
Foreign exchange forward contracts	$1,211	$6,242

The notional amounts of the commodity forward and futures contracts and the open sales and purchase orders, as shown in the table above, are not reflected at the notional amounts in the condensed consolidated balance sheets. The Company records commodity forward and futures contracts at the fair value, which is the difference between the market price of the underlying metal or contract measured on the reporting date and at fair value of trade amount measured on the date the contract was transacted. The fair value of the open derivative contracts are shown as a component of receivables or payables in the accompanying condensed consolidated balance sheets (see Note 10.) The Company enters into the derivative forward and future transactions solely for the purpose of hedging its inventory holding risk, and not for speculative market purposes. The Company's gains (losses) on derivative instruments are substantially offset by the changes in fair market value underlying precious metals inventory position, including our open sale and purchase commitments (see Note 10). The Company records the derivatives at the trade date, and the corresponding unrealized gains or losses are shown as a component of cost of sales in the condensed consolidated statements of income. We adjust the carrying value of the derivatives to fair value on a daily basis until the transactions are physically settled.

CRITICAL ACCOUNTING ESTIMATES

Our condensed consolidated financial statements are prepared in accordance with accounting principles generally accepted in the United States ("U.S. GAAP"). In connection with the preparation of our financial statements, we are required to make estimates and assumptions about future events and apply judgments that affect the reported amounts of assets, liabilities, revenue, expenses and related disclosures. We base our assumptions, estimates and judgments on historical experience, current trends and other factors that we believe to be relevant at the time our condensed consolidated financial statements are prepared. On a regular basis, we review our accounting policies, assumptions, estimates and judgments to ensure that our condensed consolidated financial statements are presented fairly and in accordance with U.S. GAAP. However, because future events and their effects cannot be determined with certainty, actual results could materially differ from our estimates.

Our significant accounting policies are discussed in Note 1 and Note 2, Description of Business and Summary of Significant Accounting Policies, respectively, of the Notes to the accompanying condensed consolidated financial statements that are included in Item 1, Financial Statements, of this Quarterly Report. We believe that the following accounting policies are the most critical to aid in fully understanding and evaluating our reported financial results, and they require our most difficult, subjective or complex judgments, resulting from the need to make estimates about the effect of matters that are inherently uncertain. We have reviewed these critical accounting estimates and related disclosures with the Audit Committee of our Board of Directors.

Revenue Recognition

Revenues are recognized when persuasive evidence of an arrangement exists, delivery has occurred, the price is fixed or determinable, no obligations remain and collection is probable. We record sales of precious metals upon the transfer of title, which occurs upon receipt by customer. We record revenues from our metal assaying and melting services after the related services are completed and the effects of forward sales contracts are reflected in revenue at the date the related precious metals are delivered or the contracts expire. The Company records revenues from its storage and logistics services after the related services are completed.

We account for our metals and sales contracts using settlement date accounting. Pursuant to such accounting, we recognize the sales or purchases of the metals at the settlement date. During the period between trade and settlement dates, we have essentially entered into a forward contract that meets the definition of a derivative in accordance with the Derivatives and Hedging Topic 815 of the Accounting Standards Codification ("ASC".). We record the derivatives at the trade date; the fair value of the open derivative contracts are shown as a component of receivables or payables in the accompanying condensed consolidated balance sheets. The corresponding unrealized gains or losses are shown as a component of cost of sales in the condensed consolidated statements of income. We adjust the carrying value of the derivatives to fair value on a daily basis until the transactions are physically settled. Sales which are physically settled are recognized at the gross amount in the condensed consolidated statements of income.

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Inventories
The Company's inventories primarily include bullion and bullion coins and are acquired and initially recorded at fair market value. The fair market value of the bullion and bullion coins is comprised of two components: (1) published market values attributable to the cost of the raw precious metal, and (2) a published premium paid at acquisition of the metal. The premium is attributable to the additional value of the product in its finished goods form and the market value attributable solely to the premium may be readily determined, as it is published by multiple reputable sources. The premium is included in the cost of the inventory, paid at acquisition, and is a component of the total fair market value of the inventory. The precious metal component of the inventory may be hedged through the use of precious metal commodity positions, while the premium component of our inventory is not a commodity that may be hedged.
The Company’s inventories, except for certain lower of cost or market basis products (as described below), are subsequently recorded at their fair market values. The daily changes in the fair market value of our inventory are offset by daily changes in the fair market value of hedging derivatives that are taken with respect to our inventory positions; both the change in the fair market value of the inventory and the change in the fair market value of these derivative instruments are recorded in cost of sales in the condensed consolidated statements of income.
As of September 30, 2015 and June 30, 2015, the unrealized gains (losses) resulting from the difference between market value and cost of physical inventories were $(5.2) million and $(3.9) million, respectively. The premium component of market value included in the inventories as of September 30, 2015 and June 30, 2015 totaled $3.5 million and $3.3 million, respectively.
While the premium component included in inventories is marked-to-market, our commemorative coin inventory, including its premium component, is held at the lower of cost or market, because the value of commemorative coins is influenced more by supply and demand determinants than on the underlying spot price of the precious metal content of the commemorative coins. Unlike our bullion coins, the value of commemorative coins is not subject to the same level of volatility as bullion coins because our commemorative coins typically carry a substantially higher premium over the spot metal price than bullion coins. Additionally, neither the commemorative coin inventory nor the premium component of our inventory is hedged. As of September 30, 2015 and June 30, 2015, our commemorative coin inventory totaled $0.2 million and $1.5 million, respectively.
Inventories include amounts borrowed from suppliers under arrangements to purchase precious metals on an unallocated basis. Unallocated or pool metal represents an unsegregated inventory position that is due on demand, in a specified physical form, based on the total ounces of metal held in the position. Amounts under these arrangements require delivery either in the form of precious metals or cash. Corresponding obligations related to liabilities on borrowed metals are reflected on the condensed consolidated balance sheets and totaled $4.0 million and $9.5 million as of September 30, 2015 and June 30, 2015, respectively. The Company mitigates market risk of its physical inventories and open commitments through commodity hedge transactions (see Note 10.)
Inventory includes amounts for obligations under product financing arrangements. A-Mark entered into a product financing agreement for the transfer and subsequent re-acquisition of gold and silver at a fixed price to a third party finance company. This inventory is restricted and is held at a custodial storage facility in exchange for a financing fee, by the third party finance company. During the term of the financing, the third party finance company holds the inventory as collateral, and both parties intend to return the inventory to A-Mark at an agreed-upon price based on the spot price on the finance arrangement termination date, pursuant to the guidance in ASC 470-40 Product Financing Arrangements. The third party charges a monthly fee as percentage of the market value of the outstanding obligation; such monthly charge is classified in interest expense. These transactions do not qualify as sales and therefore have been accounted for as financing arrangements and reflected in the condensed consolidated balance sheet within product financing arrangement. The obligation is stated at the amount required to repurchase the outstanding inventory. Both the product financing and the underlying inventory are carried at fair value, with changes in fair value included in cost of sales in the condensed consolidated statements of income. Such obligation totaled $50.0 million and $39.4 million as of September 30, 2015 and June 30, 2015, respectively.
The Company periodically loans metals to customers on a short-term consignment basis, charging interest fees based on the value of the metal loaned. Inventories loaned under consignment arrangements to customers as of September 30, 2015 and June 30, 2015 totaled $5.6 million and $5.6 million, respectively. Such inventories are

removed at the time the customer elects to price and purchase the metals, and the Company records a corresponding sale and receivable. Substantially all inventory loaned under consignment arrangements are collateralized for benefit of the Company.

The Company enters into arrangements with certain customers under which A-Mark purchases precious metals products that are subject to repurchase by the customer at the fair value of the of the product on the repurchase date. The Company or the counterparty may typically terminate any such arrangement with 14 days' notice. Upon termination the customer's rights to repurchase any remaining inventory is forfeited. As of September 30, 2015 and June 30, 2015, included within inventory is $75.9 million and $49.1 million of precious metals products subject to repurchase.

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Goodwill and Other Purchased Intangible Assets

We evaluate goodwill and other indefinite life intangibles for impairment annually in the fourth quarter of the fiscal year (or more frequently if indicators of potential impairment exist) in accordance with the Intangibles - Goodwill and Other Topic 350 of the ASC. Other finite life intangible assets are evaluated for impairment when events or changes in business circumstances indicate that the carrying amount of the assets may not be recoverable. We may first qualitatively assess whether relevant events and circumstances make it more likely than not that the fair value of the reporting unit's goodwill is less than its carrying value. If, based on this qualitative assessment, we determine that goodwill is more likely than not to be impaired, a two-step impairment test is performed. This first step in this test involves comparing the fair value of each reporting unit to its carrying value, including goodwill. If the carrying amount of a reporting unit exceeds its fair value, the second step in the test is performed, which is measurement of the impairment loss. The impairment loss is calculated by comparing the implied fair value of goodwill, as if the reporting unit has been acquired in a business combination, to its carrying amount. In accordance with ASU No. 2011-08, we performed a qualitative assessment on our goodwill, totaling $4.9 million, and determined no impairment was necessary as of June 30, 2015.

We utilize the discounted cash flow method to determine the fair value of the Company. In calculating the implied fair value of the Company's goodwill, the present value of the Company's expected future cash flows is allocated to all of the other assets and liabilities of the Company based on their fair values. The excess of the present value of the Company's expected future cash flows over the amount assigned to its other assets and liabilities is the implied fair value of goodwill.

Estimates critical to these calculations include projected future cash flows, discount rates, royalty rates, customer attrition rates and foreign exchange rates. Imprecision in estimating unobservable market inputs can impact the carrying amount of assets on the balance sheet. Furthermore, while we believe our valuation methods are appropriate, the use of different methodologies or assumptions to determine the fair value of certain assets could result in a different estimate of fair value at the reporting date.

Income Taxes

As part of the process of preparing our condensed consolidated financial statements, we are required to estimate our provision for income taxes in each of the tax jurisdictions in which we conduct business, in accordance with the Income Taxes Topic 740 of the ASC. We compute our annual tax rate based on the statutory tax rates and tax planning opportunities available to us in the various jurisdictions in which we earn income. Significant judgment is required in determining our annual tax rate and in evaluating uncertainty in its tax positions. We recognize a benefit for tax positions that we believe will more likely than not be sustained upon examination. The amount of benefit recognized is the largest amount of benefit that we believe has more than a 50% probability of being realized upon settlement. We regularly monitor our tax positions and adjust the amount of recognized tax benefit based on our evaluation of information that has become available since the end of our last financial reporting period. The annual tax rate includes the impact of these changes in recognized tax benefits. The difference between the amount of benefit taken or expected to be taken in a tax return and the amount of benefit recognized for financial reporting represents unrecognized tax benefits. These unrecognized tax benefits are presented in the condensed consolidated balance sheet principally within accrued liabilities. We record valuation allowances to reduce deferred tax assets to the amount that is more likely than not to be realized. Significant judgment is applied when assessing the need for valuation allowances. Areas of estimation include our consideration of future taxable income and ongoing prudent and feasible tax planning strategies.

Should a change in circumstances lead to a change in judgment about the utilization of deferred tax assets in future years, we would adjust related valuation allowances in the period that the change in circumstances occurs, along with a corresponding increase or charge to income. Changes in recognized tax benefits and changes in valuation allowances could be material to our results of operations for any period, but is not expected to be material to our condensed consolidated financial position.

We account for uncertainty in income taxes under the provisions of Topic 740 of the ASC. These provisions clarify the accounting for uncertainty in income taxes recognized in an enterprise's financial statements, and prescribe a recognition threshold and measurement criteria for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. The provisions also provide guidance on de-recognition, classification, interest, and penalties, accounting in interim periods, disclosure, and transition. The potential interest and/or penalties associated with an uncertain tax position are recorded in provision for income taxes on the condensed consolidated statements of income. Please refer to Note 11 to the accompanying condensed consolidated financial statements for further discussion regarding these provisions.

Income taxes are accounted for using an asset and liability approach that requires the recognition of deferred tax assets and liabilities for the expected future tax consequences of events that have been included in the financial statements. Under this method, deferred tax assets and liabilities are determined based on the differences between the financial statement and tax basis of assets and liabilities using enacted tax rates in effect for the year in which the differences are expected to reverse. The effect of a change in tax rates on deferred tax assets and liabilities is recognized in income in the period that includes the enactment date. A valuation allowance is provided when it is more likely than not that some portion or all of the net deferred tax assets will not be realized. The factors used to assess the likelihood of realization include our forecast of the reversal of temporary differences, future taxable income and available tax planning strategies that could be implemented to realize the net deferred tax assets. Failure to achieve forecasted taxable income in applicable tax jurisdictions could affect the ultimate realization of deferred tax assets and

could result in an increase in our effective tax rate on future earnings.
Based on our assessment it appears more likely than not that most of the net deferred tax assets will be realized through future taxable income. Management has established a valuation allowance against the deferred taxes related to certain net operating loss carryovers. Management believes the utilization of these losses may be limited. We will continue to assess the need for a valuation allowance for our remaining deferred tax assets in the future.
The Company's condensed consolidated financial statements recognized the current and deferred income tax consequences that result from the Company's activities during the current and preceding periods, as if the Company were a separate taxpayer prior to the date of the Distribution rather than a member of the Former Parent's condensed consolidated income tax return group. Current tax receivable reflects balances due from the Former Parent for the Company's share of the income tax assets of the group.
Following the Distribution, the Company files federal and state income tax filings that are separate from the Former Parent's tax filings. The Company recognizes current and deferred income taxes as a separate taxpayer for periods ending after the date of Distribution.

RECENT ACCOUNTING PRONOUNCEMENTS

For a description of accounting changes and recent accounting standards, including the expected dates of adoption and estimated effects, if any, on our consolidated financial statements, see Note 2 – Summary of Significant Accounting Policies in Part I, Item 1 of this Form 10-Q.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Not applicable.

ITEM 4. CONTROLS AND PROCEDURES

Disclosure Controls and Procedures

Under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Accounting Officer, which position constitutes our principal financial officer within the meaning of SEC regulations (together, the “Certifying Officers”), we carried out an evaluation of the effectiveness of the design and operation of our disclosure controls and procedures as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the “Exchange Act”). Based on the foregoing, our Certifying Officers concluded that our disclosure controls and procedures were effective as of the end of the period covered by this Annual Report.
Disclosure controls and procedures are controls and other procedures designed to ensure that information required to be disclosed in our reports filed or submitted under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC’s rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed in our reports filed or submitted under the Exchange Act is accumulated and communicated to management, including our Certifying Officers, or persons performing similar functions, as appropriate, to allow timely decisions regarding required disclosure.

Changes in Internal Control over Financial Reporting

There were no changes in our internal control over financial reporting (as such term is defined in Rules 13a-15(f) and 15d-15(f) of the Exchange Act) during the most recent fiscal quarter that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

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PART II — OTHER INFORMATION

ITEM 3. LEGAL PROCEEDINGS

We are party to various legal proceedings arising in the ordinary course of its business. Based on the information currently available, we are not currently a party to any legal proceeding that management believes would have a material adverse effect on our condensed consolidated financial position, cash flows or operations.

ITEM 1A. RISK FACTORS

Risks Relating to Our Business Generally

Our business is heavily dependent on our credit facility.

Our business depends substantially on our ability to obtain financing for our operations. A-Mark's borrowing facility, which we refer to as the Trading Credit Facility, provides A-Mark and CFC with the liquidity to buy and sell billions of dollars of precious metals annually. The Trading Credit Facility is a demand facility with a variable interest rate in which five lending institutions currently participate. A-Mark routinely uses the Trading Credit Facility to purchase metals from its suppliers and for operating cash flow purposes. Our CFC subsidiary also uses the facility to finance its lending activities.

An institutional participant in the Trading Credit facility can withdraw at any time on written notice to the Company. The loss of one or more of the lines under the Trading Credit Facility, and the failure of A-Mark to replace those lines, would reduce the financing available to the Company and could limit our ability to conduct our business, including the lending activity of our CFC subsidiary. There can be no assurance that we could procure replacement financing if all or part of the Trading Credit Facility were terminated, on commercially acceptable terms and on a timely basis, or at all.

Because the Trading Credit Facility is a demand facility, the lenders may require us to repay the indebtedness outstanding under the facility at any time. They may require repayment of the indebtedness even if we are in compliance with the financial and other covenants under the Trading Credit Facility. If the lenders were to demand repayment, we may not at the time have the financial resources to comply.

Because interest under the Trading Credit Facility is variable, we are subject to fluctuations in interest rates and we may not be able to pass along to our customers and borrowers some or any part of an increase in the interest that we are required to pay under the facility. Amounts under the Trading Credit Facility bear interest based on one month LIBOR plus a margin and vary by financial institution. The LIBOR rate was approximately 0.19% and 0.19% as of September 30, 2015 and June 30, 2015, respectively.

A change in the rates of interest charged by the lenders could adversely impact our profitability in a number of ways.

- The prices that we charge our trading customers include an interest carrying factor that reflects our cost of funds. The trading business is highly price competitive, and characterized by narrow margins. If our cost of funds increases and we cannot pass on the increase to our customers, our gross profit will decrease.
- We borrow to finance, in part, our inventory of precious metals and coins. If our interest costs increase, we would either have to absorb the increased costs, cutting into our margins, or reduce our inventory levels, which could adversely impact our ability to service our customers.
- In certain cases, our ability to offer customers financing for their purchases of precious metals and coins at competitive rates is an important factor the customers' decision to transact with us. The financing we provide to our customers is funded, in part, through the borrowings under our credit facility. If our borrowing costs increase, and our customers are unwilling to finance their purchases at the higher rates, we would lose sales.

We could suffer losses with our financing operations.

We engage in a variety of financing activities with our customers:

- Receivables from our customers with whom we trade in precious metal products are effectively short-term, non-interest bearing extensions of credit that are, in most cases, secured by the related products maintained in the Company's possession or by a letter of credit issued on behalf of the customer. On average, these receivables are outstanding for periods of between 8 and 9 days.
- The Company operates a financing business through CFC that makes secured loans at loan to value ratios—principal loan amount divided by the "liquidation value", as conservatively estimated by management, of the

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collateral—of, in most cases, 50% to 80%. These loans are both variable and fixed interest rate loans, with maturities from six to twelve months.

- We make advances to our customers on unrefined metals secured by materials received from the customer. These advances are limited to a portion of the materials received.
- The Company makes unsecured, short-term, non-interest bearing advances to wholesale metals dealers and government mints.
- The Company periodically extends short-term credit through the issuance of notes receivable to approved customers at interest rates determined on a customer-by-customer basis.

Our ability to minimize losses on the credit that we extend to our customers depends on a variety of factors, including:

- our loan underwriting and other credit policies and controls designed to assure repayment, which may prove inadequate to prevent losses;
- our ability to sell collateral upon customer defaults for amounts sufficient to offset credit losses, which can be affected by a number of factors outside of our control, including (i) changes in economic conditions, (ii) increases in market rates of interest and (iii) changes in the condition or value of the collateral; and
- the reserves we establish for loan losses, which may prove inadequate.

Our business is dependent on a concentrated customer base.

One of A-Mark's key assets is its customer base. This customer base provides deep distribution of product and makes A-Mark a desirable trading partner for precious metals product manufacturers, including sovereign mints seeking to distribute precious metals coinage or large refiners seeking to sell large volumes of physical precious metals. Two customers represented 28.9% of A-Mark's revenues for the three months ended September 30, 2015. A single customer represented 30.9% of A-Mark's revenues for the year ended June 30, 2015. If our relationship with these customers deteriorated, or if we were to lose these customers, our business would be materially adversely affected.

The loss of a government purchaser/distributorship arrangement could materially adversely affect our business.

A-Mark’s business is heavily dependent on its purchaser/distributorship arrangements with various governmental mints. Our ability to offer numismatic coins and bars to our customers on a competitive basis is based on the ability to purchase products directly from a government source. The arrangements with the governmental mints may be discontinued by them at any time. The loss of an authorized purchaser/distributor relationship, including with the U.S. Mint could have a materially adverse effect on our business.

The materials held by A-Mark are subject to loss, damage, theft or restriction on access.

A-Mark has significant quantities of high-value precious metals on site, at third-party depositories and in transit. There is a risk that part or all of the gold and other precious metals held by A-Mark, whether on its own behalf or on behalf of its customers, could be lost, damaged or stolen. In addition, access to A-Mark’s precious metals could be restricted by natural events (such as an earthquake) or human actions (such as a terrorist attack). Although we maintain insurance on terms and conditions that we consider appropriate, we may not have adequate sources of recovery if our precious metals inventory is lost, damaged, stolen or destroyed, and recovery may be limited. Among other things, our insurance policies exclude coverage in the event of loss as a result of terrorist attacks or civil unrest. In addition, with the establishment of our Logistics facility and the transfer of our wholesale storage operations from third party depositories to that facility, we are assuming greater potential liability for any loss suffered in connection with the stored inventory. Among other things, our insurance, rather than the third-party depository’s, is now the primary risk policy. While we believe we have adequate insurance coverage covering these operations, in the event of any loss in excess of our coverage, we may be held liable for that excess.

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Our business is subject to the risk of fraud and counterfeiting.

The precious metals (particularly bullion) business is exposed to the risk of loss as a result of "materials fraud" in its various forms. We seek to minimize our exposure to this type of fraud through a number of means, including third-party authentication and verification, reliance on our internal experts and the establishment of procedures designed to detect fraud. However, there can be no assurance that we will be successful in preventing or identifying this type of fraud, or in obtaining redress in the event such fraud is detected.

Our business is influenced by political conditions and world events.

The precious metals business is especially subject to global political conditions and world events. Precious metals are viewed by some as a secure financial investment in times of political upheaval or unrest, particularly in developing economies, which may drive up pricing. The volatility of the commodity prices for precious metals is also likely to increase in politically uncertain times. Conversely, during periods of relative international calm precious metal volatility is likely to decrease, along with demand, and the prices of precious metals may retreat. Because our business is dependent on the volatility and pricing of precious metals, we are likely to be influenced by world events more than businesses in other economic sectors.

We have significant operations outside the United States.

We derive over 10% of our revenues from business outside the United States, including from customers in developing countries. Business operations outside the U.S. are subject to political, economic and other risks inherent in operating in foreign countries. These include risks of general applicability, such as the need to comply with multiple regulatory regimes; trade protection measures and import or export licensing requirements; and fluctuations in equity, revenues and profits due to changes in foreign currency exchange rates. Currently, we do not conduct substantial business with customers in developing countries. However, if our business in these areas of the world were to increase, we would also face risks that are particular to developing countries, including the difficulty of enforcing agreements, collecting receivables; protecting inventory and other assets through foreign legal systems; limitations on the repatriation of earnings; currency devaluation and manipulation of exchange rates; and high levels of inflation.

We try to manage these risks by monitoring current and anticipated political, economic, legal and regulatory developments in the countries outside the United States in which we operate or have customers and adjusting operations as appropriate, but there can be no assurance that the measures we adopt will be successful in protecting the Company's business interests.

We are dependent on our key management personnel and our trading experts.

Our performance is dependent on our senior management and certain other key employees. We have employment agreements with Greg Roberts, our CEO; Thor Gjerdrum, our COO; and our senior vice president. These employment agreements all expire at the end of fiscal 2016. These and other employees have expertise in the trading markets, have industry-wide reputations, and perform critical functions for our business. We cannot offer assurance that we will be able to negotiate acceptable terms for the renewal of the employment agreements or otherwise retain our key employees. Also, there is significant competition for skilled precious metals traders and other industry professionals. The loss of our current key officers and employees, without the ability to replace them, would materially and adversely affect our business.

We are focused on growing our business, but there is no assurance that we will be successful.

We expect to grow both organically and through opportunistic acquisitions. We have devoted considerable time, resources and efforts over the past few years to our growth strategy. We may not be successful in implementing our growth initiatives, which could adversely affect our business.

With the establishment of our Logistics facility, we are undertaking direct responsibility for comprehensive inventory and depository services to support our wholesale operations beyond that which we have provided in the past. We may not have the expertise to perform such services successfully. In addition, we have no prior experience offering the type of turn-key logistics services to our retail customers that Logistics intends to provide. The efforts to establish and operate Logistics have placed, and are expected to continue to place, demands on our management and other personnel and resources, and have required, and will continue to require, timely and continued investment in facilities, personnel and financial and management systems and controls. If we are not successful with our Logistics operations, our operations as a whole could be adversely affected.

Our bank group has approved our Logistics facility as an authorized depository. If that approval were to be withdrawn for any reason, we would no longer be able to keep inventory at that location, which would substantially limit our ability to conduct business from that facility.

Liquidity constraints may limit our ability to grow our business.

To accomplish our growth strategy, we will require adequate sources of liquidity to fund both our existing business and our expansion activity. Currently, our sources of liquidity are the cash that we generate from operations and our borrowing availability under the Trading Credit Facility. There can be no assurance that these sources will be adequate to support the growth

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that we are hoping to achieve or that additional sources of financing for this purpose, in the form of additional debt or equity financing, will be available to us, on satisfactory terms or at all. Also, the Trading Credit Facility contains, and any future debt financing is likely to contain, various financial and other restrictive covenants. The need to comply with these covenants may limit our ability to implement our growth initiatives.

We expect to grow in part through acquisitions, but an acquisition strategy entails risks.

We expect to grow in part through acquisitions. We will consider potential acquisitions of varying sizes and may, on a selective basis, pursue acquisitions or consolidation opportunities involving other public companies or privately held companies. However, it is possible that we will not realize the expected benefits from our acquisitions or that our existing operations will be adversely affected as a result of acquisitions. Acquisitions entails certain risks, including: unrecorded liabilities of acquired companies that we fail to discover during our due diligence investigations; difficulty in assimilating the operations and personnel of the acquired company within our existing operations or in maintaining uniform standards; loss of key employees of the acquired company; and strains on management and other personnel time and resources both to research and integrate acquisitions.

We expect to pay for future acquisitions using cash, capital stock, notes and/or assumption of indebtedness. To the extent that our existing sources of cash are not sufficient to fund future acquisitions, we will require additional debt or equity financing and, consequently, our indebtedness may increase or shareholders may be diluted as we implement our growth strategy.

We are subject to laws and regulations

We are subject to various laws, litigation, regulatory matters and ethical standards, and our failure to comply with or adequately address developments as they arise could adversely affect our reputation and operations. Our policies, procedures and practices and the technology we implement are designed to comply with federal, state, local and foreign laws, rules and regulations, including those imposed by the SEC and other regulatory agencies, the marketplace, the banking industry and foreign countries, as well as responsible business, social and environmental practices, all of which may change from time to time. Significant legislative changes, including those that relate to employment matters and health care reform, could impact our relationship with our workforce, which could increase our expenses and adversely affect our operations. In addition, if we fail to comply with applicable laws and regulations or implement responsible business, social and environmental practices, we could be subject to damage to our reputation, class action lawsuits, legal and settlement costs, civil and criminal liability, increased cost of regulatory compliance, restatements of our financial statements, disruption of our business and loss of customers. Any required changes to our employment practices could result in the loss of employees, reduced sales, increased employment costs, low employee morale and harm to our business and results of operations. In addition, political and economic factors could lead to unfavorable changes in federal and state tax laws, which may increase our tax liabilities. An increase in our tax liabilities could adversely affect our results of operations. We are also regularly involved in various litigation matters that arise in the ordinary course of business. Litigation or regulatory developments could adversely affect our business and financial condition.

There are various federal, state, local and foreign laws, ordinances and regulations that affect our trading business. For example, we are required to comply with a variety of anti-money laundering and know-your-customer rules in response to the USA Patriot Act.

The SEC has promulgated final rules mandated by the Dodd-Frank Act regarding disclosure, on an annual basis, of the use of tin, tantalum, tungsten and gold, known as conflict minerals, in products manufactured by public companies. These new rules require due diligence to determine whether such minerals originated from the Democratic Republic of Congo (the DRC) or an adjoining country and whether such minerals helped finance the armed conflict in the DRC.

The Company has concluded that it is not currently subject to the conflict minerals rules because it is not a manufacturer of conflict minerals under the definitions set forth in the rules. Depending on developments in the Company’s business, it could become subject to the rules at some point in the future. In that event, there will be costs associated with complying with these disclosure requirements, including costs to determine the origin of gold used in our products. In addition, the implementation of these rules could adversely affect the sourcing, supply and pricing of gold used in our products. Also, we may face disqualification as a supplier for customers and reputational challenges if the due diligence procedures we implement do not enable us to verify the origins for the gold used in our products or to determine that the gold is conflict free.

CFC operates under a California Finance Lenders License issued by the California Department of Corporations. CFC is required to submit a finance lender law annual report to the state which summarizes certain loan portfolio and financial information regarding CFC. The Department of Corporations may audit the books and records of CFC to determine whether CFC is in compliance with the terms of its lending license.

There can be no assurance that the regulation of our trading and lending businesses will not increase or that compliance with the applicable regulations will not become more costly or require us to modify our business practices.

On October 25, 2015, the Company received notification from the City of Santa Monica that the City was challenging the Company's classification as an "agent/broker" for purposes of computing the business license fee due to the City. Historically,

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A Mark has paid its business license fee on net receipts, consistent with the "agent/broker" classification. The City of Santa Monica has asserted that the Company should have instead paid the fee based on gross receipts and has made a preliminary assessment against the Company seeking a material amount of what it believes to be underreported fees, together with a material amount of penalties and interest. The Company intends to meet with the City of Santa Monica shortly to discuss the preliminary assessment and the position taken by the Company with respect to the calculation of the fee. Neither the outcome of this administrative matter nor the amount or range of a potential impact to the Company in the event of an unfavorable outcome can be determined at this time.

We operate in a highly competitive industry.

The business of buying and selling precious metals is global and highly competitive. The Company competes with precious metals trading firms and banks throughout North America, Europe and elsewhere in the world, some of whom have greater financial and other resources, and greater name recognition, than the Company. We believe that, as a full service firm devoted exclusively to precious metals trading, we offer pricing, product availability, execution, financing alternatives and storage options that are attractive to our customers and allow us to compete effectively. We also believe that our purchaser/distributorship arrangements with various governmental mints give us a competitive advantage in our coin distribution business. However, given the global reach of the precious metals trading business, the absence of intellectual property protections and the availability of numerous, evolving platforms for trading in precious metals, we cannot assure you that A-Mark will be able to continue to compete successfully or that future developments in the industry will not create additional competitive challenges.

We rely extensively on computer systems to execute trades and process transactions, and we could suffer substantial damages if the operation of these systems were interrupted.

We rely on our computer and communications hardware and software systems to execute a large volume of trading transactions each year. It is therefore critical that we maintain uninterrupted operation of these systems, and we have invested considerable resources to protect our systems from physical compromise and security breaches and to maintain backup and redundancy. Nevertheless, our systems are subject to damage or interruption from power outages, computer and telecommunications failures, computer viruses, security breaches, including breaches of our transaction processing or other systems, catastrophic events such as fires, tornadoes and hurricanes, and usage errors by our employees. If our systems are breached, damaged or cease to function properly, we may have to make a significant investment to fix or replace them, we may suffer interruptions in our ability to provide quotations or trading services in the interim, and we may face costly litigation.

If our customer data were breached, we could suffer damages and loss of reputation.

By the nature of our business, we maintain significant amounts of customer data on our systems. Moreover, certain third party providers have access to confidential data concerning the Company in the ordinary course of their business relationships with the Company. In recent years, various companies, including companies that are significantly larger than us, have reported breaches of their computer systems that have resulted in the compromise of customer data. Any significant compromise or breach of customer or company data held or maintained by either the Company or our third party providers could significantly damage our reputation and result in costs, lost trades, fines and lawsuits. The regulatory environment related to information security and privacy is increasingly rigorous, with new and constantly changing requirements applicable to our business, and compliance with those requirements could result in additional costs. There is no guarantee that the procedures that we have implemented to protect against unauthorized access to secured data are adequate to safeguard against all data security breaches.

Risks Relating to Commodities

A-Mark’s business is heavily influenced by volatility in commodities prices.

A primary driver of A-Mark’s profitability is volatility in commodities prices, which leads to wider bid and ask spreads. Among the factors that can impact the price of precious metals are supply and demand of precious metals; political, economic, and global financial events; movement of the U.S. dollar versus other currencies; and the activity of large speculators such as hedge funds. If commodity prices were to stagnate, there would likely be a reduction in trading activity, resulting in less demand for the services A-Mark provides, which could materially adversely affect our business, liquidity and results of operations.

This volatility may drive fluctuation of our revenues, as a consequence of which our results for any one period may not be indicative of the results to be expected for any other period. See "Management's Discussion and Analysis of Financial Condition and Results of Operations."

Our business is exposed to commodity price risks, and our hedging activity to protect our inventory is subject to risks of default by our counterparties.

A-Mark's precious metals inventories are subject to market value changes created by change in the underlying commodity price, as well as supply and demand of the individual products the Company trades. In addition, open sale and purchase commitments are subject to changes in value between the date the purchase or sale is fixed (the trade date) and the date metal is delivered or received (the settlement date). A-Mark seeks to minimize the effect of price changes of the underlying commodity through the

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use of financial derivative instruments, such as forward and futures contracts. A-Mark's policy is to remain substantially hedged as to its inventory position and its individual sale and purchase commitments. A-Mark's management monitors its hedged exposure daily. However, there can be no assurance that these hedging activities will be adequate to protect the Company against commodity price risks associated with A-Mark's business activities. Furthermore, even if we are fully hedged as to any given position, there is the risk of default by our counterparties to the hedge. Any such default could have a material adverse effect on our financial position and results of operations.

Increased commodity pricing could limit the inventory that we are able to carry.

We maintain a large and varied inventory of precious metal products, including bullion and coins, in order to support our trading activities and provide our customers with superior service. The amount of inventory that we are able to carry is constrained by the borrowing limitations and working capital covenants under our credit facility. If commodity prices were to rise substantially, and we were unable to modify the terms of our credit facility to compensate for the increase, the quantity of product that we could finance, and hence maintain in our inventory, would fall. This would likely have a material adverse effect on our operations.

The Dodd-Frank Act could adversely impact our use of derivative instruments to hedge precious metal prices and may have other adverse effects on our business.

On July 21, 2010, President Obama signed into law the Dodd-Frank Wall Street Reform and Consumer Protection Act, which requires the Commodity Futures Trading Commission to promulgate rules and regulations implementing the new legislation, including with respect to derivative contracts on commodities. This legislation and any implementing regulations could significantly increase the cost of some commodity derivative contracts (including through requirements to post collateral, which could adversely affect our available liquidity), materially alter the terms of some commodity derivative contracts, reduce the availability of some derivatives to protect against risks, reduce our ability to monetize or restructure our existing commodity derivative contracts and potentially increase our exposure to less creditworthy counterparties. If we reduce our use of derivatives as a result of the Dodd-Frank legislation and regulations, we would be exposed to inventory and other risks associated with fluctuations in commodity prices. Also, if the Dodd-Frank legislation and regulations result in less volatility in commodity prices, our revenues could be adversely affected.

We rely on the efficient functioning of commodity exchanges around the world, and disruptions on these exchanges could adversely affect our business.

The Company buys and sells precious metals contracts on commodity exchanges around the world, both in support of its customer operations and to hedge its inventory and transactional exposure against fluctuations in commodity prices. The Company's ability to engage in these activities would be compromised if the exchanges on which the Company trades or any of their clearinghouses were to discontinue operations or to experience disruptions in trading, due to computer problems, unsettled markets or other factors. The Company may also experience risk of loss if futures commission merchants or commodity brokers with whom the Company deals were to become insolvent or bankrupt.

Risks Relating to Our Common Stock

Public company costs have increased our expenses and administrative burden, in particular in order to bring our Company into compliance with certain provisions of the Sarbanes Oxley Act of 2002.

As a public company, we are incurring significant legal, accounting and other expenses that we did not incur as a private company. These increased costs and expenses may arise from various factors, including financial reporting costs associated with complying with federal securities laws (including compliance with the Sarbanes-Oxley Act of 2002).

Changing laws, regulations and standards relating to corporate governance and public disclosure, including the Sarbanes-Oxley Act of 2002, and related regulations implemented by the SEC and NASDAQ have created uncertainty for public companies, increasing legal and financial compliance costs and making some activities more time consuming. We are currently evaluating and monitoring developments with respect to new and proposed rules and cannot predict or estimate the amount of the additional costs we may incur or the timing of such costs. Applicable laws, regulations and standards are subject to varying interpretations, in many cases due to their lack of specificity, and, as a result, their application in practice may evolve over time as new guidance is provided by regulatory and governing bodies. This could result in continuing uncertainty regarding compliance matters and higher costs necessitated by ongoing revisions to disclosure and governance practices. We intend to invest resources to comply with evolving laws, regulations and standards, and this investment may result in increased selling, general and administrative expenses and a diversion of management’s time and attention from revenue-generating activities to compliance activities. If our efforts to comply with new laws, regulations and standards differ from the activities intended by regulatory or governing bodies due to ambiguities related to practice, regulatory authorities may initiate legal proceedings against us and our business may be harmed.

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Failure to achieve and maintain effective internal controls in accordance with Section 404 of Sarbanes-Oxley could have a material adverse effect on our business.

As a public company, we are required to document and test our internal control over financial reporting in order to satisfy the requirements of Section 404 of Sarbanes-Oxley, which requires annual management assessments of the effectiveness of our internal control over financial reporting.

We are required to implement standalone policies and procedures to comply with the requirements of Section 404. During the course of our testing of our internal controls and procedures, we may identify deficiencies which we may not be able to remediate in time to meet our deadline for compliance with Section 404. Testing and maintaining internal controls can divert our management's attention from other matters that are also important to the operation of our business. We also expect that the imposition of these regulations will increase our legal and financial compliance costs and make some activities more difficult, time consuming and costly. We may not be able to conclude on an ongoing basis that we have effective internal controls over financial reporting in accordance with Section 404. If we are unable to conclude that we have effective internal controls over financial reporting, then investors could lose confidence in our reported financial information, which would likely have a negative effect on the trading price of our common stock. In addition, if we do not maintain effective internal controls, we may not be able to accurately report our financial information on a timely basis, which could harm the trading price of our common stock, impair our ability to raise additional capital, or jeopardize our continued listing on the NASDAQ Global Select Market or any other stock exchange on which common stock may be listed.

The Company has determined that it qualifies as a smaller reporting company as of December 31, 2014. As such, it is not categorized as an accelerated filer for the fiscal year ended June 30, 2015. Therefore, the Company is not required to obtain a report by our independent registered public accounting firm that addresses the effectiveness of internal control over financial reporting for that year. The Company will continue to be exempt from the requirement of obtaining such a report unless and until it meets the definition of an accelerated filer.

We may not be able to continue to pay dividends.

Effective March 2, 2015, the Board of Directors approved a cash dividend policy calling for the payment of a quarterly cash dividend of $0.05 per common share. Under the approved cash dividend policy, the declaration of cash dividends in the future is subject to the determination each quarter by the Board of Directors, based on a number of factors, including the Company's financial performance, available cash resources, cash requirements, bank covenants, and alternative uses of cash that the Board of Directors may conclude would represent an opportunity to generate a greater return on investment for the Company. Accordingly, there can be no assurance that the Company will continue to pay dividends on a regular basis. If the Board of Directors were to determine not to pay dividends in the future, shareholders would not receive any further return on an investment in our capital stock in the form of dividends, and may only obtain an economic benefit from the common stock only after an increase in its trading price and only by selling the common stock.

Provisions in our Certificate of Incorporation and Bylaws and of Delaware law may prevent or delay an acquisition of the Company, which could decrease the trading price of our common stock.

Our amended and restated certificate of incorporation and amended and restated bylaws and Delaware law contain certain anti-takeover provisions that could have the effect of making it more difficult for a third party to acquire, or of discouraging a third party from attempting to acquire, control of the Company without negotiating with our board of directors. Such provisions could limit the price that certain investors might be willing to pay in the future for the Company's securities. Certain of such provisions allow the Company to issue preferred stock with rights senior to those of the common stock, impose various procedural and other requirements which could make it more difficult for shareholders to effect certain corporate actions and set forth rules regarding how shareholders may present proposals or nominate directors for election at shareholder meetings.

We believe these provisions protect our shareholders from coercive or otherwise unfair takeover tactics by requiring potential acquirers to negotiate with our board and by providing our board with more time to assess any acquisition proposal. However, these provisions apply even if an acquisition offer may be considered beneficial by some shareholders and could delay or prevent an acquisition that our board determines is not in the best interests of our company and our shareholders. Accordingly, in the event that our board determines that a potential business combination transaction is not in the best interests of our Company and our shareholders, but certain shareholders believe that such a transaction would be beneficial to the Company and its shareholders, such shareholders may elect to sell their shares in the Company and the trading price of our common stock could decrease.

Your percentage ownership in the Company could be diluted in the future.

Your percentage ownership in A-Mark potentially will be diluted in the future because of additional equity awards that we expect will be granted to our directors, officers and employees in the future. We have established an equity incentive plan that provides for the grant of common stock-based equity awards to our directors, officers and other employees. In addition, we may

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issue equity in order to raise capital or in connection with future acquisitions and strategic investments, which would dilute your percentage ownership.

Our board and management beneficially own a sizeable percentage of our common stock and therefore have the ability to exert substantial influence as shareholders.

Members of our board and management beneficially own over 45% of our outstanding common stock. Acting together in their capacity as shareholders, the board members and management could exert substantial influence over matters on which a shareholder vote is required, such as the approval of business combination transactions. Also because of the size of their beneficial ownership, the board members and management may be in a position effectively to determine the outcome of the election of directors and the vote on shareholder proposals. The concentration of beneficial ownership in the hands of our board and management may therefore limit the ability of our public shareholders to influence the affairs of the Company.

If the Company's spinoff from SGI is determined to be taxable for U.S. federal income tax purposes, our shareholders could incur significant U.S. federal income tax liabilities.

In connection with the spinoff, SGI received the written opinion of Kramer Levin Naftalis & Frankel LLP (Kramer Levin)to the effect that the spinoff qualified as a tax-free transaction under Section 355 of the Internal Revenue Code, and that for U.S. federal income tax purposes (i) no gain or loss was recognized by SGI upon the distribution of our common stock in the spinoff, and (ii) no gain or loss was recognized by, and no amount was included in the income of, holders of SGI common stock upon the receipt of shares of our common stock in the spinoff. The opinion of tax counsel is not binding on the Internal Revenue Service or the courts, and there is no assurance that the IRS or a court will not take a contrary position. In addition, the opinion of Kramer Levin relied on certain representations and covenants delivered by SGI and us. If, notwithstanding the conclusions included in the opinion, it is ultimately determined that the distribution does not qualify as tax-free for U.S. federal income tax purposes, each SGI shareholder that is subject to U.S. federal income tax and that received shares of our common stock in the distribution could be treated as receiving a taxable distribution in an amount equal to the fair market value of such shares. In addition, if the distribution were not to qualify as tax-free for U.S. federal income tax purposes, then SGI would recognize gain in an amount equal to the excess of the fair market value of our common stock distributed to SGI shareholders on the date of the distribution over SGI’s tax basis in such shares. Also, we could have an indemnification obligation to SGI related to its tax liability.

We might not be able to engage in desirable strategic transactions and equity issuances because of restrictions relating to U.S. federal income tax requirements for tax-free distributions.

Our ability to engage in significant equity transactions is restricted in order to preserve for U.S. federal income tax purposes the tax-free nature of the distribution by SGI. Even if the distribution otherwise qualifies for tax-free treatment under Section 355 of the Internal Revenue Code, it may be taxable to SGI if 50% or more, by vote or value, of shares of our common stock or SGI’s common stock are acquired or issued as part of a plan or series of related transactions that includes the distribution. For this purpose, any acquisitions or issuances of SGI’s common stock within two years before the distribution, and any acquisitions or issuances of our or SGI’s common stock within two years after the distribution, generally are presumed to be part of such a plan, although we or SGI may be able to rebut that presumption. If an acquisition or issuance of shares of our common stock or SGI’s common stock triggers the application of Section 355(e) of the Code, SGI would recognize a taxable gain to the extent the fair market value of our common stock immediately prior to the distribution exceeds SGI’s tax basis in our common stock at such time. Under the tax separation agreement, there are restrictions on our ability to take actions that could cause the distribution to fail to qualify for favorable treatment under the Internal Revenue Code. These restrictions may prevent us from entering into transactions which might be advantageous to us or our shareholders.

There can be no assurance that SGI will not enter insolvency proceedings.

There is no assurance that, in the future, SGI will not be subject to bankruptcy or other insolvency proceedings. If that were the case, SGI creditors may allege that SGI was insolvent at the time of the distribution, or was rendered insolvent as a result of the distribution, such that the distribution constituted a fraudulent conveyance, and such creditors could seek to recover the A-Mark shares distributed in the spinoff or their value.

As disclosed in SGI's Annual Report on Form 10-K, in May 2006, Spanish judicial authorities shut down the operations of Afinsa and began an investigation related to alleged criminal wrongdoing, including money laundering, fraud, tax evasion and criminal insolvency. The Spanish criminal investigation initially focused on Afinsa and certain of its executives and was later expanded to include several former officers and directors of SGI and Central de Compras, including Greg Manning, a former chief executive officer of SGI. The allegations against Afinsa and the certain named individuals relate to the central claim that Afinsa's business operations constituted a fraudulent "Ponzi scheme," whereby funds received from later investors were used to pay interest to earlier investors, and that the stamps that were the subject of the investment contracts were highly overvalued. Spanish authorities have alleged that Mr. Manning knew Afinsa's business, and aided and abetted in its activity by, among other things, causing SGI to supply allegedly overvalued stamps to Afinsa.

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The Company understands that under Spanish law, if any of the former officers or directors of SGI or its subsidiary were ultimately found guilty, then, under the principle of secondary civil liability, SGI could be held liable for certain associated damages.
Mr. Manning, other former directors and officers of SGI, and SGI itself, on a secondary civil liability basis, are parties to the proceedings. The charges include a civil demand for substantial monetary damages.
We cannot predict the outcome of the proceedings, and we cannot assure you that the solvency of SGI could not be deemed to be affected by the proceedings.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

None.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

ITEM 4. MINE SAFETY DISCLOSURES

None.

ITEM 5. OTHER INFORMATION

None.

ITEM 6. EXHIBITS

Regulation S-K Exhibit Table Item No.		Description of Exhibit					
31.1	*	Certification Under Section 302 of the Sarbanes-Oxley Act of 2002.					
31.2	*	$	(12,174)	$ (12,875)	$ (15,406)	$ (10,898)	
Year-to-date change percentage				-27%	-28%	-34%	-24%

Umpqua Holdings Corporation

The following table presents the remaining non-covered performing residential development loans by size and geographic distribution as of December 31, 2010:

Non-Covered Residential Development Performing Loans

(dollars in thousands)

	$250k and less	$250k to $1 million	$1 million to $3 million	$3 million to $5 million	$5 million to $10 million	$10 million and greater	Total
Northwest Oregon	$ 1,955	$ 5,646	$ 8,189	$ 10,277	$ 13,541	$ 14,464	$ 54,072
Central Oregon	384	718	2,417				3,519
Southern Oregon	1,174	1,860	1,100				4,134
Washington	601	344	5,330				6,275
Greater Sacramento	3,308	3,905	1,894	4,780	11,455	13,226	38,568
Northern California	1,489	1,026	4,144				6,659
Total	$ 8,911	$ 13,499	$ 23,074	$ 15,057	$ 24,996	$ 27,690	$ 113,227

At December 31, 2010 and December 31, 2009, impaired loans of $84.4 million and $134.4 million were classified as non-covered performing restructured loans, respectively. The restructurings were granted in response to borrower financial difficulty, and generally provide for a temporary modification of loan repayment terms. The non-covered performing restructured loans on accrual status represent the only impaired loans accruing interest at each respective date. In order for a restructured loan to be considered performing and on accrual status, the loan s collateral coverage generally will be greater than or equal to 100% of the loan balance, the loan is current on payments, and the borrower must either prefund an interest reserve or demonstrate the ability to make payments from a verified source of cash flow. The Company had no obligations to lend additional funds on the restructured loans as of December 31, 2010.

The following tables summarize our non-covered performing restructured loans by loan type and region as of December 31, 2010 and December 31, 2009:

Non-Covered Restructured Loans by Type and Region

(in thousands)

							December 31, 2010
	Northwest Oregon	Central Oregon	Southern Oregon	Washington	Greater Sacramento	Northern California	Total
Commercial real estate							
Term & multifamily	$ 9,446	$	$ 3,888	$	$ 11,820	$ 3,543	$ 28,697
Construction & development					5,434		5,434
Residential development	22,277			5,330	21,322		48,929
Commercial						904	904
Term							
LOC & other						298	298
Residential	179						179
Mortgage							
Home equity loans & lines							
Consumer & other							
Total	$ 31,902	$	$ 3,888	$ 5,330	$ 38,576	$ 4,745	$ 84,441

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	Northwest Oregon	Central Oregon	Southern Oregon	Washington	Greater Sacramento	Northern California	December 31, 2009 Total
Commercial real estate							
Term & multifamily	$ 18,349	$	$ 5,790	$	$ 9,742	$ 7,866	$ 41,747
Construction & development							
Residential development	26,994		306	7,985	33,103		68,388
Commercial							
Term	315					1,785	2,100
LOC & other	400				279	16,843	17,522
Residential	4,597						4,597
Mortgage							
Home equity loans & lines	31				35		66
Consumer & other	6				13		19
Total	$ 50,692	$	$ 6,096	$ 7,985	$ 43,172	$ 26,494	$ 134,439

The following table presents a distribution of our non-covered performing restructured loans by year of maturity, according to the restructured terms, as of December 31, 2010:

(in thousands)

Year	Amount
2011	$ 58,519
2012	16,356
2013	
2014	1,631
2015	5,293
Thereafter	2,642
Total	$ 84,441

A further decline in the economic conditions in our general market areas or other factors could adversely impact individual borrowers or the loan portfolio in general. Accordingly, there can be no assurance that loans will not become 90 days or more past due, become impaired or placed on non-accrual status, restructured or transferred to other real estate owned in the future. Additional information about the loan portfolio is provided in Note 5 of the *Notes to Consolidated Financial Statements* in Item 8 below.

Covered non-performing assets

Covered non-performing assets, which include covered other real estate owned (covered OREO) totaled $29.9 million, representing 0.26% of total assets at December 31, 2010. These covered non-performing assets are subject to shared-loss agreements with the FDIC.

Total non-performing loans and leases

The following tables summarize our total (including covered and non-covered) nonperforming assets at December 31:

	2010	2009	2008	2007	2006
Loans on non-accrual status	$ 138,177	$ 193,118	$ 127,914	$ 81,317	$ 8,629
Loans past due 90 days or more and accruing	7,071	5,909	5,452	9,782	429
Total non-performing loans	145,248	199,027	133,366	91,099	9,058
Other real estate owned	62,654	24,566	27,898	6,943	
Total non-performing assets	$ 207,902	$ 223,593	$ 161,264	$ 98,042	$ 9,058

ALLOWANCE FOR LOAN AND LEASE LOSSES AND RESERVE FOR UNFUNDED COMMITMENTS

The allowance for non-covered loan and lease losses (ALLL) totaled $101.9 million and $107.7 million at December 31, 2010 and 2009, respectively. The decrease in the allowance for loan and lease losses as of December 31, 2010 as compared to prior year is principally attributable to a decrease in provision for non-covered loan and lease losses at a level below net charge offs for the year, as a result of the improving conditions of the non-covered loan portfolio.

The following table sets forth the allocation of the allowance for non-covered loan and lease losses:

Allowance for loan and lease losses Composition

As of December 31,

(in thousands)

	2010	2009	2008	2007	2006
Commercial real estate	$ 64,405	$ 67,281	$ 57,907	$ 57,433	$ 41,135
Commercial	22,146	24,583	23,104	19,514	14,094
Residential	5,926	5,811	5,778	3,406	3,111
Consumer & other	803	455	484	504	603
Unallocated	8,641	9,527	8,592	4,047	1,147
Allowance for loan and lease losses	$ 101,921	$ 107,657	$ 95,865	$ 84,904	$ 60,090

The unallocated portion of ALLL provides for coverage of credit losses inherent in the loan portfolio but not captured in the credit loss factors that are utilized in the risk rating-based component, or in the specific impairment reserve component of the allowance for loan and lease losses, and acknowledges the inherent imprecision of all loss prediction models. As of December 31, 2010, the unallocated allowance amount represented 8% of the allowance for loan and lease losses, compared to 9% at December 31, 2009. The level in unallocated ALLL in the current year reflects management s evaluation of the existing general business and economic conditions, and declining credit quality and collateral values of real estate in our markets. The ALLL composition should not be interpreted as an indication of specific amounts or loan categories in which future charge-offs may occur.

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The following table provides a summary of activity in the ALLL by major loan type for each of the five years ended December 31:

Activity in the Allowance for loan and lease losses

Years Ended December 31,

(dollars in thousands)

	2010	2009	2008	2007	2006
Balance at beginning of year	$ 107,657	$ 95,865	$ 84,904	$ 60,090	$ 43,885
Loans charged off:					
Commercial real estate	(71,030)	(136,382)	(82,919)	(20,632)	(300)
Commercial	(50,242)	(57,932)	(14,614)	(2,208)	(2,353)
Residential	(5,168)	(4,331)	(1,597)	(547)	(213)
Consumer & other	(2,061)	(2,222)	(1,922)	(1,343)	(1,339)
Total loans charged off	(128,501)	(200,867)	(101,052)	(24,730)	(4,205)
Recoveries:					
Commercial real estate	6,980	1,334	2,571	1,022	739
Commercial	1,318	1,549	1,021	819	1,996
Residential	334	126	148	241	108
Consumer & other	465	526	595	654	788
Total recoveries	9,097	3,535	4,335	2,736	3,631
Net charge-offs	(119,404)	(197,332)	(96,717)	(21,994)	(574)
Addition incident to mergers				5,078	14,227
Provision charged to operations	113,668	209,124	107,678	41,730	2,552
Balance at end of year	$ 101,921	$ 107,657	$ 95,865	$ 84,904	$ 60,090
Ratio of net charge-offs to average non-covered loans	2.06%	3.23%	1.58%	0.38%	0.01%
Ratio of provision to average non-covered loans	1.97%	3.43%	1.76%	0.72%	0.05%
Recoveries as a percentage of charge-offs	7.08%	1.76%	4.29%	11.06%	86.35%

The decrease in the ALLL as of December 31, 2010 is primarily a result of the decrease in the provision for loan and lease losses in 2010. The decrease in the provision for loan and lease losses is due to improving credit quality of the loan portfolio.

All impaired loans are individually evaluated for impairment. If the measurement of each impaired loans value is less than the recorded investment in the loan, we recognize this impairment and adjust the carrying value of the loan to fair value through the allowance for loan and lease losses. This can be accomplished by charging-off the impaired portion of the loan or establishing a specific component within the allowance for loan and lease losses. If in management s assessment the sources of repayment will not result in a reasonable probability that the carrying value of a loan can be recovered, the amount of a loan s specific impairment is charged-off against the allowance for loan and lease losses. Prior to the second quarter of 2008, the Company established specific reserves within the allowance for loan and leases losses for loan impairments and recognized the charge-off of the impairment reserve when the loan was resolved, sold, or foreclosed and transferred to other real estate owned. Due to declining real estate values in our markets and the deterioration of the U.S. economy in general, it became increasingly likely that impairment reserves on collateral dependent loans, particularly those relating to real estate, would not be recoverable and represented a confirmed loss. As a result, beginning in the second quarter of 2008, the Company began recognizing the charge-off of impairment reserves on impaired loans in the period they arise for collateral dependent loans. This process has effectively accelerated the recognition of charge-offs recognized since the second quarter of 2008. The change in our assessment of the possible recoverability of our collateral dependent impaired loans carrying values has ultimately had no impact on our impairment valuation procedures or the amount of provision for loan and leases losses included within the

Consolidated Statements of Operations. Impairment reserves on non-collateral dependent restructured loans are measured by comparing the present value of expected future cash flows on the restructured loans discounted at the interest rate of the original loan agreement to the loan s carrying value. These impairment reserves are recognized as a specific component to be provided for in the allowance for loan and lease losses.

At December 31, 2010, the recorded investment in non-covered loans classified as impaired totaled $222.6 million, with a corresponding valuation allowance (included in the allowance for loan and lease losses) of $5.2 million. The valuation allowance on impaired loans represents the impairment reserves on performing restructured loans and nonaccrual loans. At December 31, 2009, the total recorded investment in impaired loans was $328.0 million, with a corresponding valuation allowance (included in the allowance for loan and lease losses) of $2.7 million.

The majority of loan charge-offs in the current year relate to real estate related credits. In the current year we experienced decreased charge-offs in all categories except for residential. These charge-offs were largely driven by economic conditions coupled with falling real estate values in our markets. The majority of all charge-offs taken in the current year relate to borrowers that were directly affected by the housing market downturn or indirectly impacted from the contraction of real estate dependent businesses.

The following table presents a summary of activity in the reserve for unfunded commitments (RUC):

Summary of Reserve for Unfunded Commitments Activity

Years Ended December 31,

(in thousands)

					December 31, 2010
	Commercial Real Estate	Commercial	Residential	Consumer & Other	Total
Balance, beginning of year	$ 57	$ 484	$ 144	$ 46	$ 731
Net change to other expense	(24)	91	14	6	87
Balance, end of year	$ 33	$ 575	$ 158	$ 52	$ 818
Unfunded commitments	$ 33,326	$ 548,920	$ 210,574	$ 45,556	$ 838,376

					December 31, 2009
	Commercial Real Estate	Commercial	Residential	Consumer & Other	Total
Balance, beginning of year	$ 151	$ 625	$ 161	$ 46	$ 983
Net change to other expense	(94)	(141)	(17)		(252)
Balance, end of year	$ 57	$ 484	$ 144	$ 46	$ 731
Unfunded commitments	$ 58,206	$ 479,153	$ 220,697	$ 39,354	$ 797,410

					December 31, 2008
	Commercial Real Estate	Commercial	Residential	Consumer & Other	Total

Balance, beginning of year	$ 247	$ 728	$ 159	$ 48	$ 1,182
Net change to other expense	(96)	(103)	2	(2)	(199)
Balance, end of year	$ 151	$ 625	$ 161	$ 46	$ 983
Unfunded commitments	$ 154,906	$ 617,759	$ 245,706	$ 38,832	$ 1,057,203

We believe that the ALLL and RUC at December 31, 2010 are sufficient to absorb losses inherent in the loan portfolio and credit commitments outstanding as of that date, respectively, based on the best information available. This assessment, based in part

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on historical levels of net charge-offs, loan growth, and a detailed review of the quality of the loan portfolio, involves uncertainty and judgment. Therefore, the adequacy of the ALLL and RUC cannot be determined with precision and may be subject to change in future periods. In addition, bank regulatory authorities, as part of their periodic examination of the Bank, may require additional charges to the provision for loan and lease losses in future periods if warranted as a result of their review.

MORTGAGE SERVICING RIGHTS

The following table presents the key elements of our mortgage servicing rights asset as of December 31, 2010, 2009 and 2008:

Summary of Mortgage Servicing Rights

Years Ended December 31,

(dollars in thousands)

	2010	2009	2008
Balance, beginning of year	$ 12,625	$ 8,205	$ 10,088
Additions for new mortgage servicing rights capitalized	5,645	7,570	2,694
Acquired mortgage servicing rights	62		
Changes in fair value:			
Due to changes in model inputs or assumptions(1)	(1,598)	(3,469)	(1,270)
Other(2)	(2,280)	319	(3,307)
Balance, end of year	$ 14,454	$ 12,625	$ 8,205
Balance of loans serviced for others	$ 1,603,414	$ 1,277,832	$ 955,494
MSR as a percentage of serviced loans	0.90%	0.99%	0.86%

(1) Principally reflects changes in discount rates and prepayment speed assumptions, which are primarily affected by changes in interest rates.
(2) Represents changes due to collection/realization of expected cash flows over time.

Mortgage servicing rights are adjusted to fair value quarterly with the change recorded in mortgage banking revenue. The value of mortgage servicing rights is impacted by market rates for mortgage loans. Historically low market rates can cause prepayments to increase as a result of refinancing activity. To the extent loans are prepaid sooner than estimated at the time servicing assets are originally recorded, it is possible that certain mortgage servicing rights assets may decrease in value. Generally, the fair value of our mortgage servicing rights will increase as market rates for mortgage loans rise and decrease if market rates fall.

In the fourth quarter of 2007, the Company began using derivative instruments to hedge the risk of changes in the fair value of MSR due to changes in interest rates. Starting in late February 2008 and continuing into March 2008, the bond markets experienced extraordinary volatility. This volatility resulted in widening spreads and price declines on the derivative instruments that were not offset by corresponding gains in the MSR asset. As a result, a $2.4 million charge was recognized within mortgage banking revenue in the first quarter of 2008. In March 2008, the Company indefinitely suspended the MSR hedge, given the continued volatility. Additional information about the Company s mortgage servicing rights is provided in Note 10 of the *Notes to Consolidated Financial Statements* in Item 8 below.

GOODWILL AND OTHER INTANGIBLE ASSETS

At December 31, 2010, we had recognized goodwill of $655.9 million, as compared to $610.0 million at December 31, 2009. The increase of $45.9 million is due to the acquisition of Rainier and Nevada Security. The goodwill recorded in connection with acquisitions represents the excess of the purchase price over the estimated fair value of the net assets acquired. Goodwill and other intangible assets with indefinite lives are not amortized but instead are periodically tested for impairment. Management evaluates goodwill and intangible assets with indefinite lives on an annual basis as of December 31. Additionally, we perform impairment evaluations on an interim basis when events or circumstances indicate impairment potentially exists. A significant amount of judgment is involved in determining if an indicator of impairment has occurred. Such indicators may include, among others, a significant decline in our expected future cash flows; a sustained, significant decline in our stock price and market capitalization; a significant adverse change in legal factors or in the business climate; adverse action or assessment by a regulator; and unanticipated competition.

The goodwill impairment test involves a two-step process. The first step compares the fair value of a reporting unit (e.g. Retail Brokerage and Community Banking) to its carrying value. If the reporting unit s fair value is less than its carrying value, the Company would be required to proceed to the second step. In the second step the Company calculates the implied fair value of the reporting unit s goodwill. The implied fair value of goodwill is determined in the same manner as goodwill recognized in a business combination. The estimated fair value of the Company is allocated to all of the Company s assets and liabilities, including any unrecognized identifiable intangible assets, as if the Company had been acquired in a business combination and the estimated fair value of the reporting unit is the price paid to acquire it. The allocation process is performed only for purposes of determining the amount of goodwill impairment. No assets or liabilities are written up or down, nor are any additional unrecognized identifiable intangible assets recorded as a part of this process. Any excess of the estimated purchase price over the fair value of the reporting unit s net assets represents the implied fair value of goodwill. If the carrying amount of the goodwill is greater than the implied fair value of that goodwill, an impairment loss would be recognized as a charge to earnings in an amount equal to that excess.

Substantially all of the Company s goodwill is associated with our community banking operations. Due to a decline in the Company s market capitalization below book value of equity and continued weakness in the banking industry, the Company performed a goodwill impairment evaluation of the Community Banking operating segment as of June 30, 2009. The Company engaged an independent valuation consultant to assist us in determining whether and to what extent our goodwill asset was impaired. We utilized a variety of valuation techniques to analyze and measure the estimated fair value of reporting units under both the income and market valuation approach. Under the income approach, the fair value of the reporting unit is determined by projecting future earnings for five years, utilizing a terminal value based on expected future growth rates, and applying a discount rate reflective of current market conditions. The estimation of forecasted earnings uses management s best estimate of economic and market conditions over the projected periods and considers estimated growth rates in loans and deposits and future expected changes in net interest margins. Various market-based valuation approaches are utilized and include applying market price to earnings, core deposit premium, and tangible book value multiples as observed from relevant, comparable peer companies of the reporting unit. We also valued the reporting unit by applying an estimated control premium to the market capitalization. Weightings are assigned to each of the aforementioned model results, judgmentally allocated based on the observability and reliability of the inputs, to arrive at a final fair value estimate of the reporting unit. The results of the Company s and valuation specialist s step one impairment test indicated that the reporting unit s fair value was less than its carrying value. As a result, the Company performed a step two analysis. The external valuation specialist assisted management s analysis under step two of the goodwill impairment test. Under this approach, we calculated the fair value for the reporting unit s assets and liabilities, as well as its unrecognized identifiable intangible assets, such as the core deposit intangible and trade name. Fair value adjustments to items on the balance sheet primarily related to investment securities held to maturity, loans, other real estate owned, Visa Class B common stock, deferred taxes, deposits, term debt, and junior subordinated debentures carried at amortized cost. The external valuation specialist assisted management to estimate the fair value of our unrecognized identifiable assets, such as the core deposit intangible and trade name.

The most significant fair value adjustment made in this analysis was to adjust the carrying value of the Company s loans receivable portfolio to fair value. The fair value of the Company s loan receivable portfolio at June 30, 2009 was estimated in a manner similar to methodology utilized as part of the December 31, 2008 goodwill impairment evaluation. As part of the December 31, 2008 loan valuation, the loan portfolio was stratified into sixty-eight loan pools that shared common characteristics, namely loan type, payment terms, and whether the loans were performing or non-performing. Each loan pool was discounted at a rate that considers current market interest rates, credit risk, and assumed liquidity premiums required based upon the nature of the underlying pool. Due to the disruption in the financial markets experienced during 2008 and continuing through 2009, the liquidity premium reflects the reduction in demand in the secondary markets for all grades of non-conforming credit, including those that are performing. Liquidity premiums for individual loan categories generally ranged from 4.6% for performing loans to 30% for construction and non-performing loans. At December 31, 2008, the fair value of the overall loan portfolio was calculated to be at a 9% discount relative to its book value. The composition of the loan portfolio at June 30, 2009, including loan type and performance indicators, was substantially similar to the loan portfolio at December 31, 2008. At June 30, 2009, the fair value of the loan portfolio was estimated to be at a 12% discount relative to its carrying value. The additional discount is primarily attributed to the additional liquidity premium required as of the measurement date associated with the Company s concentration of commercial real estate loans.

Other significant fair value adjustments utilized in this goodwill impairment analysis included the value of the core deposit intangible asset which was calculated as 0.53% of core deposits, and includes all deposits except certificates of deposit. The carrying value of other real estate owned was discounted by 25%, representing a liquidity adjustment given the current market conditions. The fair value of our trade name, which represents the competitive advantage associated with our brand recognition and ability to attract and retain relationships, was estimated to be $19.3 million. The fair value of our junior subordinated debentures carried at amortized cost was determined in a manner and utilized inputs, primarily the credit risk adjusted spread, consistent with our methodology for determining the fair value of junior subordinated debentures recorded at fair value. Information relating to our methodologies for estimating the fair value of financial instruments that were adjusted to fair value as part of this analysis, including the Visa Class B common stock, deposits, term debt, and junior subordinated debentures, is included in Note 24 of the *Notes to Consolidated Financial Statements*.

Based on the results of the step two analysis, the Company determined that the implied fair value of the goodwill was less than its carrying amount on the Company s balance sheet, and as a result, we recognized a goodwill impairment loss of $112.0 million in the second quarter of 2009. This write-down of goodwill is a non-cash charge that does not affect the Company s or the Bank s liquidity or operations. In addition, because goodwill is excluded in the calculation of regulatory capital, the Company s well-capitalized regulatory capital ratios are not affected by this charge.

The Company also conducted its annual evaluation of goodwill for impairment as of December 31, 2010. In the first step of the goodwill impairment test the Company determined that the fair value of the Community Banking reporting unit exceeded its carrying amount. This determination is consistent with the events occurring after the Company recognized the $112.0 million impairment of goodwill second quarter of 2009. First, the market capitalization and estimated fair value of the Company increased significantly subsequent to the recognition of the impairment charge as the fair value of the Company s stock increased 57% from June 30, 2009 to December 31, 2010. Secondly, the Company s successful public common stock offerings in the third quarter of 2009 and first quarter of 2010 diluted the carrying value of the reporting book equity on a per share basis, against which the fair value of the reporting unit is measured. The significant assumptions and methodology utilized to test for goodwill impairment as of December 31, 2010 were consistent with these used at December 31, 2009.

If the Company s common stock price declines further or continues to trade below book value per common share, or should general economic conditions deteriorate further or remain depressed for a prolonged period of time, particularly in the financial industry, the Company may be required to recognize additional impairment of all, or some portion of, its goodwill. It is possible that changes in circumstances, existing at the measurement date or at other times in the future, or changes in the numerous estimates associated with management s judgments, assumptions and estimates made in assessing the fair value of our goodwill, such as valuation multiples, discount rates, or projected earnings, could result in an impairment charge in future periods. Additional impairment charges, if any, may be material to the Company s results of operations and financial position. However, any potential future impairment charge will have no effect on the Company s or the Bank s cash balances, liquidity, or regulatory capital ratios.

The inputs management utilizes to estimate the fair value of a reporting unit in step one of the goodwill impairment test, and estimating the fair values of the underlying assets and liabilities of a reporting unit in the second step of the goodwill impairment test, require management to make significant judgments, assumptions and estimates where observable market may not readily exist. Such inputs include, but are not limited to, trading multiples from comparable transactions, control premiums, the value that may arise from synergies and other benefits that would accrue from control over an entity, and the appropriate rates to discount projected cash flows. Additionally, there may be limited current market inputs to value certain assets or liabilities, particularly loans and junior subordinated debentures. These valuation inputs are considered to be Level 3 inputs.

Management will continue to monitor the relationship of the Company s market capitalization to both its book value and tangible book value, which management attributes to both financial services industry-wide and Company specific factors, and to evaluate the carrying value of goodwill and other intangible assets.

As a result of the December 31, 2008 goodwill impairment evaluation related to the Retail Brokerage reporting segment, management determined that there was a $1.0 million impairment following the departure of certain Umpqua Investments financial advisors. The valuation of the impairment at the Retail Brokerage operating segment was determined using an income approach by discounting cash flows of forecasted earnings. The key assumptions used to estimate the fair value of each reporting unit include earnings forecasts for five years, a terminal value based on expected future growth rates, and a discount rate reflective of current market conditions. The Company evaluated the Retail Brokerage reporting segment s goodwill for impairment as of December 31, 2010. The first step of the goodwill impairment test indicated that the reporting unit s fair value exceeded its carrying value. As of December 31, 2010, the ending carrying value of the Retail Brokerage segment s goodwill was $2.7 million.

At December 31, 2010, we had other intangible assets of $26.1 million, as compared to $29.6 million at December 31, 2009. As part of a business acquisition, a portion of the purchase price is allocated to the other value of intangible assets such as the merchant servicing portfolio or core deposits, which includes all deposits except certificates of deposit. The value of these other intangible assets were determined by a third party based on the net present value of future cash flows for the merchant servicing portfolio and an analysis of the cost differential between the core deposits and alternative funding sources for the core deposit intangible. Intangible assets with definite useful lives are amortized to their estimated residual values over their respective estimated useful lives, and are also reviewed for impairment. We amortize other intangible assets on an accelerated or straight-line basis over an estimated ten to fifteen year life. In the fourth quarter of 2009, the Company recognized an $804,000 impairment related to the merchant servicing portfolio obtained through a prior acquisition. The remaining decrease in other intangible assets resulted from scheduled amortization. No other impairment losses were recognized in connection with other intangible assets since their initial recognition.

Additional information regarding our accounting for goodwill and other intangible assets is included in Notes 1, 2 and 9 of the *Notes to Consolidated Financial Statements* in Item 8 below.

DEPOSITS

Total deposits were $9.4 billion at December 31, 2010, an increase of $2.0 billion, or 26.8%, as compared to year-end 2009. Excluding the deposits acquired through the FDIC-assisted purchase and assumption of Evergreen, Rainier, and Nevada Security, the annualized organic deposit growth rate was 13.3%. Of the total change in deposit balances during the current year, deposits from consumers and businesses increased $1.9 billion, and deposits from public entities increased $46.8 million. Despite the increased competitive pressures to build deposits in light of the current recessionary economic climate, management attributes the ability to maintain our overall deposit base and grow certain lines of business to ongoing business development and marketing efforts in our service markets. Information on average deposit balances and average rates paid is included under the *Net Interest Income* section of this report. Additional information regarding interest bearing deposits is included in Note 14 of the *Notes to Consolidated Financial Statements* in Item 8 below.

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The following table presents the deposit balances by major category as of December 31:

Deposits

As of December 31,

(dollars in thousands)

	2010 Amount	2010 Percentage	2009 Amount	2009 Percentage
Noninterest bearing	$ 1,616,687	17%	$ 1,398,332	19%
Interest bearing demand	927,224	10%	872,184	12%
Savings and money market	3,817,245	41%	2,813,805	37%
Time, $100,000 or greater	2,191,055	23%	1,603,410	22%
Time, less than $100,000	881,594	9%	752,703	10%
Total	$ 9,433,805	100%	$ 7,440,434	100%

The following table presents the scheduled maturities of time deposits of $100,000 and greater as of December 31, 2010:

Maturities of Time Deposits of $100,000 and Greater

(in thousands)

Three months or less	$ 642,060
Over three months through six months	325,706
Over six months through twelve months	839,661
Over twelve months	383,628
Time, $100,000 and over	$ 2,191,055

The Company has an agreement with Promontory Interfinancial Network LLC (Promontory) that makes it possible to provide FDIC deposit insurance to balances in excess of current deposit insurance limits. Promontory s Certificate of Deposit Account Registry Service (CDARS) uses a deposit-matching program to exchange Bank deposits in excess of the current deposit insurance limits for excess balances at other participating banks, on a dollar-for-dollar basis, that would be fully insured at the Bank. This product is designed to enhance our ability to attract and retain customers and increase deposits, by providing additional FDIC coverage to customers. CDARS deposits can be reciprocal or one-way. All of the Bank s CDARS deposits are reciprocal. At December 31, 2010 and December 31, 2009, the Company s CDARS balances totaled $323.2 million and $290.3 million, respectively. Of these totals, at December 31, 2010 and December 31, 2009, $300.6 million and $245.6 million, respectively, represented time deposits equal to or greater than $100,000 but were fully insured under current deposit insurance limits.

On November 21, 2008, the FDIC approved the final ruling establishing the Transaction Account Guarantee Program (TAGP) as part of the Temporary Liquidity Guarantee Program (TLGP). Under this program, all non-interest bearing transaction accounts are fully guaranteed by the FDIC for the entire amount in the account. This unlimited coverage also extends to NOW (interest bearing deposit accounts) earning an interest rate no greater than 0.50% and all IOLTAs (lawyers trust accounts). Coverage under the TAGP, funded through insurance premiums paid by participating financial institutions, is in addition to and separate from the additional coverage announced under EESA. On August 26, 2009, the FDIC extended the TAGP portion of the TLGP through June 30, 2010. On June 22, 2010, the FDIC extended the TAGP portion of the TLGP for an additional six months, from July 1, 2010 to December 31, 2010. The rule requires that interest rates on qualifying NOW accounts offered by banks participating in the program be reduced to 0.25% from 0.50%. The rule provides for an additional extension of the program, without further rulemaking, for a period of time not to exceed December 31, 2011. Umpqua has elected to participate in the TAGP program through the extended period. The Dodd-Frank Act provides for unlimited deposit insurance for noninterest bearing transactions accounts (excluding NOW) beginning December 31, 2010 for a period of two years.

Also, the Dodd-Frank Act permanently raises the current standard maximum federal deposit insurance amount from $100,000 to $250,000 per qualified account.

BORROWINGS

At December 31, 2010, the Bank had outstanding $73.8 million of securities sold under agreements to repurchase and no outstanding federal funds purchased balances. Additional information regarding securities sold under agreements to repurchase and federal funds purchased is provided in Notes 15 and 16 of *Notes to Consolidated Financial Statements* in Item 8 below.

At December 31, 2010, the Bank had outstanding term debt of $262.8 million primarily with the Federal Home Loan Bank (FHLB). Term debt outstanding as of December 31, 2010 increased $186.5 million since December 31, 2009 primarily as a result of term debt assumed in the Evergreen and Rainier acquisitions, partially offset by repayment of FHLB borrowings. Management expects continued use of FHLB advances as a source of short and long-term funding. The following table summarizes the maturity dates of FHLB advances outstanding (excluding the remaining purchase accounting adjustments relating to the Rainier acquisition of $12.2 million at December 31, 2010) and weighted average contractual interest rate (excluding the accretion of purchase accounting adjustments) at December 31, 2010:

	Amount	Wtd Avg. Rate
2011	$ 5,000	2.19%
2012		
2013		
2014		
2015		
Thereafter	245,016	4.56%
Total	$ 250,016	4.51%

Additional information regarding term debt is provided in Note 17 of *Notes to Consolidated Financial Statements* in Item 8 below.

JUNIOR SUBORDINATED DEBENTURES

We had junior subordinated debentures with carrying values of $183.6 million and $188.9 million, respectively, at December 31, 2010 and 2009.

At December 31, 2010, approximately $219.6 million, or 95% of the total issued amount, had interest rates that are adjustable on a quarterly basis based on a spread over three month LIBOR. Interest expense for junior subordinated debentures decreased in 2010 as compared to 2009 and in 2009 as compared to 2008, primarily resulting from decreases in short-term market interest rates and LIBOR. Although increases in short-term market interest rates will increase the interest expense for junior subordinated debentures, we believe that other attributes of our balance sheet will serve to mitigate the impact to net interest income on a consolidated basis.

On January 1, 2007, the Company elected the fair value measurement option for certain pre-existing junior subordinated debentures of $97.9 million (the Umpqua Statutory Trusts). The remaining junior subordinated debentures as of the adoption date were acquired through business combinations and were measured at fair value at the time of acquisition. In 2007, the Company issued two series of trust preferred securities and elected to measure each instrument at fair value. Accounting for junior subordinated debentures originally issued by the Company at fair value enables us to more closely align our financial performance with the economic value of those liabilities. Additionally, we believe it improves our ability to manage the market and interest rate risks associated with the junior subordinated debentures. The junior subordinated debentures measured at fair value and amortized cost have been presented as separate line items on the balance sheet. The ending carrying (fair) value of the junior subordinated debentures measured at fair value represents the estimated amount that would be paid to transfer these liabilities in an orderly transaction amongst market participants under current market conditions as of the measurement date.

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Prior to the second quarter of 2009, we estimated the fair value of junior subordinated debentures using an internal discounted cash flow model. The future cash flows of these instruments were extended to the next available redemption date or maturity date as appropriate based upon the spreads of recent issuances or quotes from brokers for comparable bank holding companies, as available, compared to the contractual spread of each junior subordinated debenture measured at fair value. The significant inputs utilized in the estimation of fair value of these instruments is the credit risk adjusted spread and three month LIBOR. The credit risk adjusted spread represents the nonperformance risk of the liability, contemplating both the inherent risk of the obligation and the Company s entity-specific credit risk. Generally, an increase in the credit risk adjusted spread and/or a decrease in the three month LIBOR will result in positive fair value adjustments. Conversely, a decrease in the credit risk adjusted spread and/or an increase in the three month LIBOR will result in negative fair value adjustments. For additional assurance, we obtained valuations from a third party pricing service to validate the results of our model. Prior to the third quarter of 2008, we utilized a credit risk adjusted spread that was based upon recent issuances or quotes from brokers for comparable bank holding companies as of the date of valuation, and we considered this to be a Level 2 input. Due to the increasing credit concerns in the capital markets and inactivity in the trust preferred markets that have limited the observability of credit risk adjusted market spreads, we classified this as a Level 3 fair value measure in the third quarter of 2008.

In the second quarter of 2009, due to continued inactivity in the junior subordinated debenture and related markets and clarified guidance relating to the determination of fair value when the volume and level of activity for an asset or liability have significantly decreased or where transactions are not orderly, management evaluated and determined to rely on a third-party pricing service to estimate the fair value of these liabilities. The pricing service utilized an income approach valuation technique, specifically an option-adjusted spread (OAS) valuation model. This OAS model values the cash flows over multiple interest rate scenarios and discounts these cash flows using a credit risk adjustment spread over the three month LIBOR swap curve. The OAS model utilized is more sophisticated and computationally intensive than the model previously used; however, the models react similarly to changes in the underlying inputs, and the results are considered comparable. With the assistance of a third-party pricing service, we determined that a credit risk adjusted spread of 725 basis points (an effective yield of approximately 11.6%) is representative of the nonperformance risk premium a market participant would require under current market conditions as of March 31, 2010. Generally, an increase in the credit risk adjusted spread and/or a decrease in the swap curve will result in positive fair value adjustments. Conversely, a decrease in the credit risk adjusted spread and/or an increase in the swap curve will result in negative fair value adjustments.

In July 2010, the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act) was signed into law which, among other things, limits the ability of certain bank holding companies to treat trust preferred security debt issuances as Tier 1 capital. This law may require many banks to raise new Tier 1 capital and will effectively close the trust-preferred securities markets from offering new issuances in the future. As a result of this legislation, our third-party pricing service noted that they were no longer to able to provide reliable fair value estimates related to these liabilities given the absence of observable or comparable transactions in the market place in recent history or as anticipated into the future. As a result, management evaluated current market conditions and determined that the 11.6% effective yield utilized to discount the junior subordinated debentures, and the related prices, to determine fair value as of March 31, 2010 continued to represent appropriate estimates of the fair value of these liabilities. Since the Company had less than $15 billion in assets at December 31, 2009, under the Dodd-Frank Act, the Company will be able to continue to include its existing trust preferred securities in Tier 1 capital.

In the third quarter of 2010, the Company began utilizing a discounted cash flow model to measure these instruments at fair value each reporting period, which will have the long-term effect of amortizing the cumulative fair value discount of $53.3 million, as of December 31, 2010, over each junior subordinated debentures expected term, to eventually return the carrying value of these instruments to their notional values at their expected redemption dates. This will result in recognizing losses on junior subordinated debentures carried at fair value on a quarterly basis within non-interest income. For additional assurance, we obtained a valuation from a third-party to validate the results of our model at December 31, 2010. The results of the valuation were consistent with the results of our internal model. The Company will continue to monitor activity in the trust preferred markets. Observable activity in the junior subordinated debenture and related markets in future periods may change the effective rate used to discount these liabilities, and could result in additional fair value adjustments (gains or losses on junior subordinated debentures measured at fair value) above the periodic change in fair value under the effective yield method.

For the years ended December 31, 2010, 2009 and 2008, we recorded gains of $5.0 million, $6.5 million and $38.9 million, respectively, resulting from the change in fair value of the junior subordinated debentures recorded at fair value. The change in fair value of the junior subordinated debentures carried at fair value during these periods primarily result from the widening of the credit risk adjusted spread. Management believes that the credit risk adjusted spread being utilized is indicative of the nonperformance risk premium a willing market participant would require under current market conditions, that is, the inactive market. In management s estimation, the change in fair value of the junior subordinated debentures during the periods represent changes in the market s nonperformance risk expectations and pricing of this type of debt, and not as a result of changes to our entity-specific credit risk. Any gains recognized are recorded in gain on junior subordinated debentures carried at fair value within non-interest income. The contractual interest expense on junior subordinated debentures continues to be recorded on an accrual basis and is reported in interest expense. The junior subordinated debentures recorded at fair value of $80.7 million had contractual unpaid principal amounts of $134.0 million outstanding as of December 31, 2010. The junior subordinated debentures recorded at fair value of $85.7 million had contractual unpaid principal amounts of $134.0 million outstanding as of December 31, 2009.

Additional information regarding junior subordinated debentures measured at fair value is included in Note 24 of the *Notes to Consolidated Financial Statements* in Item 8 below.

All of the debentures issued to the Trusts, less the common stock of the Trusts, qualified as Tier 1 capital as of December 31, 2010, under guidance issued by the Board of Governors of the Federal Reserve System. Additional information regarding the terms of the junior subordinated debentures, including maturity/redemption dates, interest rates and the fair value election, is included in Note 18 of the *Notes to Consolidated Financial Statements* in Item 8 below.

LIQUIDITY AND CASH FLOW

The principal objective of our liquidity management program is to maintain the Bank s ability to meet the day-to-day cash flow requirements of our customers who either wish to withdraw funds or to draw upon credit facilities to meet their cash needs.

We monitor the sources and uses of funds on a daily basis to maintain an acceptable liquidity position. One source of funds includes public deposits. Individual state laws require banks to collateralize public deposits, typically as a percentage of their public deposit balance in excess of FDIC insurance. Public deposits represent 10.3% of total deposits at December 31, 2010 and 12.4% at December 31, 2009. The amount of collateral required varies by state and may also vary by institution within each state, depending on the individual state s risk assessment of depository institutions. Changes in the pledging requirements for uninsured public deposits may require pledging additional collateral to secure these deposits, drawing on other sources of funds to finance the purchase of assets that would be available to be pledged to satisfy a pledging requirement, or could lead to the withdrawal of certain public deposits from the Bank. In addition to liquidity from core deposits and the repayments and maturities of loans and investment securities, the Bank can utilize established uncommitted federal funds lines of credit, sell securities under agreements to repurchase, borrow on a secured basis from the FHLB or issue brokered certificates of deposit.

The Bank had available lines of credit with the FHLB totaling $1.9 billion at December 31, 2010 subject to certain collateral requirements, namely the amount of pledged loans and investment securities. The Bank had available lines of credit with the Federal Reserve totaling $289.4 million subject to certain collateral requirements, namely the amount of certain pledged loans at December 31, 2010. The Bank had uncommitted federal funds line of credit agreements with additional financial institutions totaling $125.0 million at December 31, 2010. Availability of the lines is subject to federal funds balances available for loan and continued borrower eligibility. These lines are intended to support short-term liquidity needs, and the agreements may restrict the consecutive day usage.

The Company is a separate entity from the Bank and must provide for its own liquidity. Substantially all of the Company s revenues are obtained from dividends declared and paid by the Bank. In 2010, there were no dividends paid by the Bank to the Company. There are statutory and regulatory provisions that could limit the ability of the Bank to pay dividends to the Company. We believe that such restrictions will not have an adverse impact on the ability of the Company to fund its quarterly cash dividend distributions to shareholders, when approved, and meet its ongoing cash obligations, which consist principally of

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debt service on the $230.1 million (issued amount) of outstanding junior subordinated debentures. As of December 31, 2010, the Company did not have any borrowing arrangements of its own.

Additional discussion related to liquidity related risks given the current economic climate is provided in Item 1A *Risk Factors* above.

As disclosed in the *Consolidated Statements of Cash Flows* in Item 8 of this report, net cash provided by operating activities was $198.6 million during 2010. The difference between cash provided by operating activities and net income largely consisted of non-cash items including a $113.7 million provision for non-covered loan and lease losses. Net cash of $556.4 million used by investing activities consisted principally of $1.5 billion of purchases of investment securities available for sale and $47.6 million of purchases of premises and equipment, partially offset by net non-covered loan paydowns and maturities of $146.3 million, net covered loan paydowns of $119.9 million, proceeds from investment securities available for sale of $408.7 million, cash acquired in FDIC-assisted acquisitions of $179.0 million, proceeds from the FDIC indemnification asset of $48.4 million, proceeds from the sale of loans of $38.7 million, proceeds from the sale of non-covered other real estate owned of $25.1 million, and proceeds from the sale of covered other real estate owned of $14.6 million. The $756.5 million of cash provided by financing activities primarily consisted of $847.9 million increase in net deposits, $28.6 million increase in net securities sold under agreements to repurchase, $89.8 million in net proceeds from the issuance of common stock and $198.3 million in net proceeds from the issuance of preferred stock, partially offset by $165.8 million repayment of term debt, $214.2 million of redemption of preferred stock, $4.5 million of redemption of warrants, $20.6 million of dividends paid on common stock and $3.7 million of dividends paid on preferred stock.

Although we expect the Bank s and the Company s liquidity positions to remain satisfactory during 2011, it is possible that our deposit growth for 2011 may not be maintained at previous levels due to pricing pressure or, in order to generate deposit growth, our pricing may need to be adjusted in a manner that results in increased interest expense on deposits.

OFF-BALANCE-SHEET ARRANGEMENTS

Information regarding Off-Balance-Sheet Arrangements is included in Note 20 and Note 21 of the *Notes to Consolidated Financial Statements in Item 8 below.*

The following table presents a summary of significant contractual obligations extending beyond one year as of December 31, 2010 and maturing as indicated:

Future Contractual Obligations

As of December 31, 2010:

(in thousands)

	Less than 1 Year	1 to 3 Years	3 to 5 Years	More than 5 Years	Total
Deposits(1)	$ 8,865,806	$ 511,172	$ 54,398	$ 2,429	$ 9,433,805
Term debt	5,000			245,528	250,528
Junior subordinated debentures(2)				230,061	230,061
Operating leases	14,814	24,705	18,061	24,855	82,435
Other long-term liabilities(3)	2,019	3,501	3,199	35,311	44,030
Total contractual obligations	$ 8,887,352	$ 538,663	$ 74,899	$ 537,827	$ 10,038,741

(1) Deposits with indeterminate maturities, such as demand, savings and money market accounts, are reflected as obligations due in less than one year.
(2) Represents the issued amount of all junior subordinated debentures.
(3) Includes maximum payments related to employee benefit plans, assuming all future vesting conditions are met. Additional information about employee benefit plans is provided in Note 19 of the *Notes to Consolidated Financial Statements* in Item 8 below.

The table above does not include interest payments or purchase accounting adjustments related to deposits, term debt or junior subordinated debentures.

As of December 31, 2010, the Company has a liability for unrecognized tax benefits relating to California tax incentives and temporary differences in the amount of $762,000, which includes accrued interest of $172,000. As the Company is not able to estimate the period in which this liability will be paid in the future, this amount is not included in the future contractual obligations table above.

CONCENTRATIONS OF CREDIT RISK

Information regarding Concentrations of Credit Risk is included in Notes 3, 5, and 20 of the *Notes to Consolidated Financial Statements.*

CAPITAL RESOURCES

Shareholders equity at December 31, 2010 was $1.6 billion, an increase of $76.1 million, or 5%, from December 31, 2009. The increase in shareholders equity during 2010 was principally due to the $288.1 million in net proceeds from the public stock offering in February 2010, net income of $28.3 million, offset by the redemption of preferred stock under the Troubled Asset Relief Program (TARP) Capital Purchase Program (CPP) of $214.2 million, repurchase of warrants issued to the United States Department of Treasury (U.S. Treasury) for $4.5 million, common stock dividends of $22.0 million, and preferred stock dividends of $3.7 million.

The Federal Reserve Board has in place guidelines for risk-based capital requirements applicable to U.S. banks and bank/financial holding companies. These risk-based capital guidelines take into consideration risk factors, as defined by regulation, associated with various categories of assets, both on and off-balance sheet. Under the guidelines, capital strength is measured in two tiers, which are used in conjunction with risk-adjusted assets to determine the risk-based capital ratios. The guidelines require an 8% total risk-based capital ratio, of which 4% must be Tier I capital. Our consolidated Tier I capital, which consists of shareholders equity and qualifying trust-preferred securities, less other comprehensive income, goodwill, other intangible assets, disallowed servicing assets and disallowed deferred tax assets, totaled $1.2 billion at December 31, 2010. Tier II capital components include all, or a portion of, the allowance for loan and lease losses and the portion of trust preferred securities in excess of Tier I statutory limits. The total of Tier I capital plus Tier II capital components is referred to as Total Risk-Based Capital, and was $1.3 billion at December 31, 2010. The percentage ratios, as calculated under the guidelines, were 16.36% and 17.62% for Tier I and Total Risk-Based Capital, respectively, at December 31, 2010. The Tier 1 and Total Risk-Based Capital ratios at December 31, 2009 were 15.91% and 17.16%, respectively.

A minimum leverage ratio is required in addition to the risk-based capital standards and is defined as period-end shareholders equity and qualifying trust preferred securities, less other comprehensive income, goodwill and deposit-based intangibles, divided by average assets as adjusted for goodwill and other intangible assets. Although a minimum leverage ratio of 4% is required for the highest-rated financial holding companies that are not undertaking significant expansion programs, the Federal Reserve Board may require a financial holding company to maintain a leverage ratio greater than 4% if it is experiencing or anticipating significant growth or is operating with less than well-diversified risks in the opinion of the Federal Reserve Board. The Federal Reserve Board uses the leverage and risk-based capital ratios to assess capital adequacy of banks and financial holding companies. Our consolidated leverage ratios at December 31, 2010 and 2009 were 10.56% and 12.79%, respectively. As of December 31, 2010, the most recent notification from the FDIC categorized the Bank as well-capitalized under the regulatory framework for prompt corrective action. There are no conditions or events since that notification that management believes have changed the Bank s regulatory capital category.

During the year ended December 31, 2010, the Company made no contributions to the Bank. At December 31, 2010, all three of the capital ratios of the Bank exceeded the minimum ratios required by federal regulation. Management monitors these ratios on a regular basis to ensure that the Bank remains within regulatory guidelines. Further information regarding the actual and required capital ratios is provided in Note 23 of the *Notes to Consolidated Financial Statements* in Item 8 below.

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On August 13, 2009, the Company raised $258.7 million through a public offering by issuing 26,538,461 shares of the Company s common stock, including 3,461,538 shares pursuant to the underwriters over-allotment option, at a share price of $9.75 per share. The net proceeds to the Company after deducting underwriting discounts and commissions and offering expenses were $245.7 million. The net proceeds from the offering qualified as Tier 1 capital and were to be used for general corporate purposes, which included capital to support growth and acquisition opportunities and positioned the Company for redemption of preferred stock and warrants issued to the U.S. Treasury under the CPP. In connection with the public offering, the number of shares of common stock underlying the warrant held by the U.S. Treasury was reduced by 50%, to 1,110,898 shares. In connection with the company s public offering in February 2010, Umpqua repurchased the preferred stock. See Note 22 of the *Notes to the Consolidated Financial Statement* in Item 8 below.

On February 3, 2010, the Company raised $303.6 million through a public offering by issuing 8,625,000 shares of the Company s common stock, including 1,125,000 shares pursuant to the underwriters over-allotment option, at a share price of $11.00 per share and 18,975,000 depository shares, including 2,475,000 depository shares pursuant to the underwriter s over-allotment option, also at a price of $11.00 per share. Fractional interests (1/100th) in each share of the Series B Common Stock Equivalent were represented by the 18,975,000 depositary shares; as a result, each depositary share would convert into one share of common stock. The net proceeds to the Company after deducting underwriting discounts and commissions and offering expenses were $288.1 million. The net proceeds from the offering were used to redeem the preferred stock issued to the United States Department of the Treasury (U.S. Treasury) under the Troubled Asset Relief Program (TARP) Capital Purchase Program (CPP), to fund FDIC-assisted acquisition opportunities and for general corporate purposes.

On February 17, 2010, the Company redeemed all of the outstanding Fixed Rate Cumulative Perpetual Preferred Stock, Series A, issued to the U.S. Treasury under the TARP CPP for an aggregate purchase price of $214.2 million. As a result of the repurchase of the Series A preferred stock, the Company incurred a one-time deemed dividend of $9.7 million due to the accelerated amortization of the remaining issuance discount on the preferred stock.

On March 31, 2010, the Company repurchased the common stock warrant issued to the U.S. Treasury pursuant to the TARP CPP, for $4.5 million. The warrant repurchase, together with the Company s redemption in February 2010 of the entire amount of Fixed Rate Cumulative Perpetual Preferred Stock, Series A, issued to the U.S. Treasury, represents full repayment of all TARP obligations and cancellation of all equity interests in the Company held by the U.S. Treasury.

On April 20, 2010, shareholders of the Company approved an amendment to the Company s Restated Articles of Incorporation. The amendment, which became effective on April 21, 2010, increased the number of authorized shares of common stock to 200,000,000 (from 100,000,000). As a result of the effectiveness of the amendment, as of the close of business on April 21, 2010, the Company s Series B Common Stock Equivalent preferred stock automatically converted into newly issued shares of common stock at a conversion rate of 100 shares of common stock for each share of Series B Common Stock Equivalent preferred stock. All shares of Series B Common Stock Equivalent preferred stock and representative depositary shares ceased to exist upon the conversion. Trading in the depositary shares on NASDAQ (ticker symbol UMPQP) ceased and the UMPQP symbol voluntarily delisted effective as of the close of business on April 21, 2010.

During 2010, Umpqua s Board of Directors declared a quarterly cash dividend of $0.05 per common share per quarter. These dividends were made pursuant to our existing dividend policy and in consideration of, among other things, earnings, regulatory capital levels, the overall payout ratio and expected asset growth. We expect that the dividend rate will be reassessed on a quarterly basis by the Board of Directors in accordance with the dividend policy. The payment of cash dividends is subject to regulatory limitations as described under the *Supervision and Regulation* section of Part I of this report.

There is no assurance that future cash dividends on common shares will be declared or increased. The following table presents cash dividends declared and dividend payout ratios (dividends declared per common share divided by basic earnings per common share) for the years ended December 31, 2010, 2009 and 2008:

Cash Dividends and Payout Ratios per Common Share

	2010	2009	2008
Dividend declared per common share	$ 0.20	$ 0.20	$ 0.62
Dividend payout ratio	133%	-8%	76%

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The Company s share repurchase plan, which was approved by the Board and announced in August 2003, originally authorized the repurchase of up to 1.0 million shares. Prior to 2008, the authorization was amended to increase the repurchase limit to 6.0 million shares. On April 21, 2009, the Board of Directors approved an extension to the expiration date of the common stock repurchase plan to June 30, 2011. As of December 31, 2010, a total of 1.5 million shares remained available for repurchase. The Company repurchased no shares under the repurchase plan in 2010 or 2009. The timing and amount of future repurchases will depend upon the market price for our common stock, securities laws restricting repurchases, asset growth, earnings, and our capital plan. In addition, our stock plans provide that option and award holders may pay for the exercise price and tax withholdings in part or whole by tendering previously held shares.

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ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The absolute level and volatility of interest rates can have a significant impact on our profitability. The objective of interest rate risk management is to identify and manage the sensitivity of net interest income to changing interest rates to achieve our overall financial objectives. Based on economic conditions, asset quality and various other considerations, management establishes tolerance ranges for interest rate sensitivity and manages within these ranges. Net interest income and the fair value of financial instruments are greatly influenced by changes in the level of interest rates. We manage exposure to fluctuations in interest rates through policies that are established by the Asset/Liability Management Committee (ALCO). The ALCO meets monthly and has responsibility for developing asset/liability management policy, formulating and implementing strategies to improve balance sheet positioning and earnings and reviewing interest rate sensitivity. The Board of Directors Loan and Investment Committee provides oversight of the asset/liability management process, reviews the results of the interest rate risk analyses prepared for the ALCO and approves the asset/liability policy on an annual basis.

Management utilizes an interest rate simulation model to estimate the sensitivity of net interest income to changes in market interest rates. Such estimates are based upon a number of assumptions for each scenario, including the level of balance sheet growth, deposit repricing characteristics and the rate of prepayments. Interest rate sensitivity is a function of the repricing characteristics of our interest earnings assets and interest bearing liabilities. These repricing characteristics are the time frames within which the interest bearing assets and liabilities are subject to change in interest rates either at replacement, repricing or maturity during the life of the instruments. Interest rate sensitivity management focuses on the maturity structure of assets and liabilities and their repricing characteristics during periods of changes in market interest rates. Effective interest rate sensitivity management seeks to ensure that both assets and liabilities respond to changes in interest rates within an acceptable timeframe, thereby minimizing the impact of interest rate changes on net interest income. Interest rate sensitivity is measured as the difference between the volumes of assets and liabilities at a point in time that are subject to repricing at various time horizons: immediate to three months, four to twelve months, one to five years, over five years, and on a cumulative basis. The differences are known as interest sensitivity gaps. The table below sets forth interest sensitivity gaps for these different intervals as of December 31, 2010.

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Umpqua Holdings Corporation

Interest Sensitivity Gap

(dollars in thousands)

	By Repricing Interval					
	0-3 Months	4-12 Months	1-5 Years	Over 5 Years	Non-Rate-Sensitive	Total
ASSETS						
Interest bearing deposits	$ 891,634	$	$	$	$	$ 891,634
Temporary Investments	545					545
Trading account assets	3,024					3,024
Securities available for sale	300,430	666,451	1,419,266	400,118	132,915	2,919,180
Securities held to maturity	2,073	1,569	1,000	119	1	4,762
Total loans and loans held for sale	1,971,725	1,239,800	2,945,943	243,975	119,068	6,520,511
Non-interest earning assets					1,329,054	1,329,054
Total assets	3,169,431	1,907,820	4,366,209	644,212	1,581,038	$ 11,668,710
LIABILITIES AND SHAREHOLDERS EQUITY						
Interest bearing demand deposits	927,224					$ 927,224
Savings and money market deposits	3,817,245					3,817,245
Time deposits	811,631	1,692,233	565,164	2,430	1,191	3,072,649
Securities sold under agreements to repurchase	73,759					73,759
Term debt	5,009	26	137	245,358	12,230	262,760
Junior subordinated debentures	166,260			10,465	6,829	183,554
Non-interest bearing liabilities and shareholders equity					3,331,519	3,331,519
Total liabilities and shareholders equity	5,801,128	1,692,259	565,301	258,253	3,351,769	$ 11,668,710
Interest rate sensitivity gap	(2,631,697)	215,561	3,800,908	385,959	(1,770,731)	
Cumulative interest rate sensitivity gap	$ (2,631,697)	$ (2,416,136)	$ 1,384,772	$ 1,770,731	$	
Cumulative gap as a % of earning assets	-25.5%	-23.4%	13.4%	17.1%		

Changes in the mix of earning assets or supporting liabilities can either increase or decrease the net interest margin without affecting interest rate sensitivity. In addition, the interest rate spread between an asset and its supporting liability can vary significantly, while the timing of repricing for both the asset and the liability remains the same, thus impacting net interest income. This characteristic is referred to as basis risk and generally relates to the possibility that the repricing characteristics of short-term assets tied to the prime rate are different from those of short-term funding sources such as certificates of deposit. Varying interest rate environments can create unexpected changes in prepayment levels of assets and liabilities that are not reflected in the interest rate sensitivity analysis. These prepayments may have a significant impact on our net interest margin. Because of these factors, an interest sensitivity gap analysis may not provide an accurate assessment of our exposure to changes in interest rates.

We utilize an interest rate simulation model to monitor and evaluate the impact of changing interest rates on net interest income. The estimated impact on our net interest income over a time horizon of one year as of December 31, 2010 is indicated in the table below. For the scenarios shown, the interest rate simulation assumes a parallel and sustained shift in market interest rates ratably over a twelve-month period and no change in the composition or size of the balance sheet. For example, the up 200 basis points scenario is based on a theoretical increase in market rates of 16.7 basis points per month for twelve months applied to the balance sheet of December 31 for each respective year.

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Interest Rate Simulation Impact on Net Interest Income

As of December 31,

(dollars in thousands)

	2010		2009		2008	
	Increase (Decrease) in Net Interest Income from Base Scenario	Percentage Change	Decrease in Net Interest Income from Base Scenario	Percentage Change	Increase (Decrease) in Net Interest Income from Base Scenario	Percentage Change
Up 200 basis points	$ 9,115	2.4%	$ (2,118)	-0.6%	$ (9,539)	-3.6%
Up 100 basis points	$ 6,464	1.7%	$ (3,033)	-0.9%	$ (4,824)	-1.8%
Down 100 basis points	$ (12,478)	-3.3%	$ (290)	-0.1%	$ 1,370	0.5%
Down 200 basis points	$ (21,512)	-5.7%	$ (7,609)	-2.2%	$ (2,304)	-0.9%

At December 31, 2008, we believe our balance sheet was in a liability-sensitive position, as the repricing characteristics were such that an increase in market interest rates would have a negative effect on net interest income and a decrease in market interest rates would have positive effect on net interest income. At December 31, 2009, we were liability-sensitive in an increased market interest rate scenario, and asset-sensitive in a decreased interest rate scenario. At December 31, 2010, we were asset-sensitive. Some of the assumptions made in the simulation model may not materialize and unanticipated events and circumstances will occur. In addition, the simulation model does not take into account any future actions which we could undertake to mitigate an adverse impact due to changes in interest rates from those expected, in the actual level of market interest rates or competitive influences on our deposit base.

A second interest rate sensitivity measure we utilize is the quantification of market value changes for all financial assets and liabilities, given an increase or decrease in market interest rates. This approach provides a longer-term view of interest rate risk, capturing all future expected cash flows. Assets and liabilities with option characteristics are measured based on different interest rate path valuations using statistical rate simulation techniques.

The table below illustrates the effects of various market interest rate changes on the fair values of financial assets and liabilities (excluding mortgage servicing rights) as compared to the corresponding carrying values and fair values:

Interest Rate Simulation Impact on Fair Value of Financial Assets and Liabilities

As of December 31,

(dollars in thousands)

	2010		2009	
	Decrease in Estimated Fair Value of Equity	Percentage Change	Increase (Decrease) in Estimated Fair Value of Equity	Percentage Change
Up 200 basis points	$ (114,667)	-5.0%	$ (93,095)	-4.3%
Up 100 basis points	$ (59,857)	-2.6%	$ (49,027)	-2.3%
Down 100 basis points	$ (55,141)	-2.4%	$ 19,874	0.9%
Down 200 basis points	$ (126,830)	-5.5%	$ 6,007	0.3%

Consistent with the results in the interest rate simulation impact on net interest income, our overall sensitivity to market interest rate changes as of December 31, 2010 has increased compared to December 31, 2009.

IMPACT OF INFLATION AND CHANGING PRICES

A financial institution s asset and liability structure is substantially different from that of an industrial firm in that primarily all assets and liabilities of a bank are monetary in nature, with relatively little investment in fixed assets or inventories. Inflation has an important impact on the growth of total assets and the resulting need to increase equity capital at higher than normal rates in order to maintain appropriate capital ratios. We believe that the impact of inflation on financial results depends on management s ability to react to changes in interest rates and, by such reaction, reduce the inflationary impact on performance. We have an asset/liability management program which attempts to manage interest rate sensitivity. In addition, periodic reviews of banking services and products are conducted to adjust pricing in view of current and expected costs.

Our financial statements included in Item 8 below have been prepared in accordance with accounting principles generally accepted in the United States, which requires us to measure financial position and operating results principally in terms of historic dollars. Changes in the relative value of money due to inflation or recession are generally not considered. The primary effect of inflation on our results of operations is through increased operating costs, such as compensation, occupancy and business development expenses. In management s opinion, changes in interest rates affect the financial condition of a financial institution to a far greater degree than changes in the rate of inflation. Although interest rates are greatly influenced by changes in the inflation rate, they do not necessarily change at the same rate or in the same magnitude as the inflation rate. Interest rates are highly sensitive to many factors that are beyond our control, including U.S. fiscal and monetary policy and general national and global economic conditions.

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ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA.

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Shareholders

Umpqua Holdings Corporation and Subsidiaries

We have audited the accompanying consolidated balance sheets of Umpqua Holdings Corporation and Subsidiaries (the Company) as of December 31, 2010 and 2009, and the related consolidated statements of operations, changes in shareholders equity, comprehensive income (loss), and cash flows for each of the years in the three-year period ended December 31, 2010. We also have audited the Company s internal control over financial reporting as of December 31, 2010, based on criteria established in Internal Control Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The Company s management is responsible for these financial statements, for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting included in the accompanying Report of Management on Internal Control over Financial Reporting. Our responsibility is to express an opinion on these financial statements and an opinion on the effectiveness of the Company s internal control over financial reporting based on our audits.

We conducted our audits in accordance with auditing standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement and whether effective internal control over financial reporting was maintained in all material respects. Our audit of the financial statements included examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risks. Our audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

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

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

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Umpqua Holdings Corporation and Subsidiaries as of December 31, 2010 and 2009, and the results of their operations and their cash flows for each of the years in the three-year period ended December 31, 2010, in conformity with accounting principles generally accepted in the United States of America. Also in our opinion, Umpqua Holdings Corporation maintained, in all material respects, effective internal control over financial reporting as of December 31, 2010 based on criteria established in Internal Control Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

/s/ Moss Adams LLP

Portland, Oregon

February 17, 2011

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Umpqua Holdings Corporation

UMPQUA HOLDINGS CORPORATION AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

December 31, 2010 and 2009

(in thousands, except shares)

	December 31, 2010	December 31, 2009
ASSETS		
Cash and due from banks	$ 111,946	$ 113,353
Interest bearing deposits	891,634	491,462
Temporary investments	545	598
Total cash and cash equivalents	1,004,125	605,413
Investment securities		
Trading, at fair value	3,024	2,273
Available for sale, at fair value	2,919,180	1,795,616
Held to maturity, at amortized cost	4,762	6,061
Loans held for sale	75,626	33,715
Non-covered loans and leases	5,658,987	5,999,267
Allowance for loan and lease losses	(101,921)	(107,657)
Net non-covered loans and leases	5,557,066	5,891,610
Covered loans and leases, net	785,898	
Restricted equity securities	34,475	15,211
Premises and equipment, net	136,599	103,266
Goodwill and other intangible assets, net	681,969	639,634
Mortgage servicing rights, at fair value	14,454	12,625
Non-covered other real estate owned	32,791	24,566
Covered other real estate owned	29,863	
FDIC indemnification asset	146,413	
Other assets	242,465	251,382
Total assets	$ 11,668,710	$ 9,381,372
LIABILITIES AND SHAREHOLDERS EQUITY		
Deposits		
Noninterest bearing	$ 1,616,687	$ 1,398,332
Interest bearing	7,817,118	6,042,102
Total deposits	9,433,805	7,440,434
Securities sold under agreements to repurchase	73,759	45,180
Term debt	262,760	76,274
Junior subordinated debentures, at fair value	80,688	85,666
Junior subordinated debentures, at amortized cost	102,866	103,188
Other liabilities	72,258	64,113
Total liabilities	10,026,136	7,814,855
COMMITMENTS AND CONTINGENCIES (NOTE 20)		
SHAREHOLDERS EQUITY		

Preferred stock, no par value, 4,000,000 shares authorized; Series A (liquidation preference $1,000 per share) issued and outstanding: none in 2010 and 214,181 in 2009		204,335
Common stock, no par value, 200,000,000 shares authorized; issued and outstanding: 114,536,814 in 2010 and 86,785,588 in 2009	1,540,928	1,253,288
Retained earnings	76,701	83,939
Accumulated other comprehensive income	24,945	24,955
Total shareholders equity	1,642,574	1,566,517
Total liabilities and shareholders equity	$ 11,668,710	$ 9,381,372

See notes to condensed consolidated financial statements

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UMPQUA HOLDINGS CORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF OPERATIONS

For the Years Ended December 31, 2010, 2009 and 2008

(in thousands, except per share amounts)

	2010	2009	2008
INTEREST INCOME			
Interest and fees on loans	$ 410,132	$ 355,195	$ 393,927
Interest and dividends on investment securities			
Taxable	67,388	60,195	41,189
Exempt from federal income tax	8,839	7,794	6,653
Dividends	14	22	334
Interest on temporary investments and interest bearing deposits	2,223	526	443
Total interest income	488,596	423,732	442,546
INTEREST EXPENSE			
Interest on deposits	76,241	88,742	129,370
Interest on securities sold under agreements to repurchase and federal funds purchased	517	680	2,220
Interest on term debt	9,229	4,576	6,994
Interest on junior subordinated debentures	7,825	9,026	13,655
Total interest expense	93,812	103,024	152,239
Net interest income	394,784	320,708	290,307
PROVISION FOR NON-COVERED LOAN AND LEASE LOSSES	113,668	209,124	107,678
PROVISION FOR COVERED LOAN AND LEASE LOSSES	5,151		
Net interest income after provision for loan and lease losses	275,965	111,584	182,629
NON-INTEREST INCOME			
Service charges on deposit accounts	34,874	32,957	34,775
Brokerage commissions and fees	11,661	7,597	8,948
Mortgage banking revenue, net	21,214	18,688	2,436
Gain (loss) on investment securities, net			
Gain on sale of investment securities, net	2,326	8,896	5,529
Total other-than-temporary impairment losses	(93)	(12,556)	(4,180)
Portion of other-than-temporary impairment losses (transferred from) recognized in other comprehensive income	(321)	1,983	
Total gain (loss) on investment securities, net	1,912	(1,677)	1,349
Gain on junior subordinated debentures carried at fair value	4,980	6,482	38,903
Bargain purchase gain on acquisition	6,437		
Change in FDIC indemnification asset	(16,445)		
Proceeds from Visa mandatory partial redemption			12,633
Other income	11,271	9,469	8,074
Total non-interest income	75,904	73,516	107,118
NON-INTEREST EXPENSE			
Salaries and employee benefits	162,875	126,850	114,600
Net occupancy and equipment	45,940	39,673	37,047
Communications	10,464	7,671	7,063
Marketing	6,225	4,529	4,573
Services	22,576	21,918	18,792
Supplies	3,998	3,257	2,908
FDIC assessments	15,095	15,825	5,182
Net loss on other real estate owned	5,925	23,204	8,313

Intangible amortization and impairment	5,389	6,165	5,857
Goodwill impairment		111,952	982
Merger related expenses	6,675	273	
Visa litigation			(5,183)
Other expenses	32,576	18,086	16,436
Total non-interest expense	317,738	379,403	216,570
Income (loss) before provision for (benefit from) income taxes	34,131	(194,303)	73,177
Provision for (benefit from) income taxes	5,805	(40,937)	22,133
Net income (loss)	$ 28,326	$ (153,366)	$ 51,044

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Umpqua Holdings Corporation

UMPQUA HOLDINGS CORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF OPERATIONS (Continued)

For the Years Ended December 31, 2010, 2009 and 2008

(in thousands, except per share amounts)

	2010	2009	2008
Net income (loss)	$ 28,326	$ (153,366)	$ 51,044
Preferred stock dividends	12,192	12,866	1,620
Dividends and undistributed earnings allocated to participating securities	67	30	154
Net earnings (loss) available to common shareholders	$ 16,067	$ (166,262)	$ 49,270
Earnings (loss) per common share:			
Basic	$ 0.15	$ (2.36)	$ 0.82
Diluted	$ 0.15	$ (2.36)	$ 0.82
Weighted average number of common shares outstanding:			
Basic	107,922	70,399	60,084
Diluted	108,153	70,399	60,424

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UMPQUA HOLDINGS CORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS EQUITY

For the Years Ended December 31, 2010, 2009 and 2008

(in thousands, except shares)

	Preferred Stock	Common Stock Shares	Common Stock Amount	Retained Earnings	Accumulated Other Comprehensive (Loss) Income	Total
BALANCE AT JANUARY 1, 2008	$	59,980,161	$ 988,780	$ 251,545	$ (387)	$ 1,239,938
Net income				51,044		51,044
Other comprehensive income, net of tax					14,459	14,459
Comprehensive income						$ 65,503
Stock-based compensation			3,893			3,893
Stock repurchased and retired		(8,199)	(129)			(129)
Issuances of common stock under stock plans and related tax benefit		174,438	1,022			1,022
Issuance of preferred stock to U.S. Treasury	201,927					201,927
Issuance of warrants to U.S. Treasury			12,254			12,254
Amortization of discount on preferred stock	251			(251)		
Cash dividends on common stock ($0.62 per share)				(37,400)		(37,400)
Balance at December 31, 2008	$ 202,178	60,146,400	$ 1,005,820	$ 264,938	$ 14,072	$ 1,487,008
BALANCE AT JANUARY 1, 2009	$ 202,178	60,146,400	$ 1,005,820	$ 264,938	$ 14,072	$ 1,487,008
Net loss				(153,366)		(153,366)
Other comprehensive income, net of tax					10,883	10,883
Comprehensive loss						$ (142,483)
Issuance of common stock		26,538,461	245,697			245,697
Stock-based compensation			2,188			2,188
Stock repurchased and retired		(19,516)	(174)			(174)
Issuances of common stock under stock plans and related net tax deficiencies		120,243	(243)			(243)
Amortization of discount on preferred stock	2,157			(2,157)		
Dividends declared on preferred stock				(10,739)		(10,739)
Cash dividends on common stock ($0.20 per share)				(14,737)		(14,737)
Balance at December 31, 2009	$ 204,335	86,785,588	$ 1,253,288	$ 83,939	$ 24,955	$ 1,566,517
BALANCE AT JANUARY 1, 2010	$ 204,335	86,785,588	$ 1,253,288	$ 83,939	$ 24,955	$ 1,566,517
Net income				28,326		28,326
Other comprehensive (loss) income, net of tax					(10)	(10)
Comprehensive income						$ 28,316

Issuance of common stock		8,625,000	89,786			89,786
Stock-based compensation			3,505			3,505
Stock repurchased and retired		(22,541)	(284)			(284)
Issuances of common stock under stock plans and related net tax benefit		173,767	844			844
Redemption of preferred stock issued to U.S. Treasury	(214,181)					(214,181)
Issuance of preferred stock	198,289					198,289
Conversion of preferred stock to common stock	(198,289)	18,975,000	198,289			
Amortization of discount on preferred stock	9,846			(9,846)		
Dividends declared on preferred stock				(3,686)		(3,686)
Repurchase of warrants issued to U.S. Treasury			(4,500)			(4,500)
Cash dividends on common stock ($0.20 per share)				(22,032)		(22,032)
Balance at December 31, 2010	$	114,536,814	$ 1,540,928	$ 76,701	$ 24,945	$ 1,642,574

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Umpqua Holdings Corporation

UMPQUA HOLDINGS CORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)

For the Years Ended December 31, 2010, 2009 and 2008

(in thousands)

	2010	2009	2008
Net income (loss)	$ 28,326	$ (153,366)	$ 51,044
Available for sale securities:			
Unrealized gains arising during the year	1,305	23,888	33,950
Reclassification adjustment for gains realized in net income (net of tax expense of $930, $3,431, and $2,156 in 2010, 2009, and 2008, respectively)	(1,396)	(5,147)	(3,234)
Income tax expense related to unrealized gains	(522)	(9,555)	(13,580)
Net change in unrealized gains	(613)	9,186	17,136
Held to maturity securities:			
Unrealized losses on investment securities available for sale transferred to investment securities held to maturity (net of tax benefit of $2,988 in 2008)			(4,482)
Reclassification adjustment for impairments realized in net income (net of tax benefit of $1,716 and $1,146 in 2009 and 2008, respectively)		2,574	1,718
Amortization of unrealized losses on investment securities transferred to held to maturity (net of tax benefit of $70 and $58 for 2009 and 2008, respectively)		103	87
Net change in unrealized losses on investment securities transferred to held to maturity		2,677	(2,677)
Unrealized gain (losses) related to factors other than credit (net of tax benefit of $150 and tax expense of $1,080 in 2010 and 2009, respectively)	225	(1,620)	
Reclassification adjustment for impairments realized in net income (net of tax benefit of $137 and $307 in 2010 and 2009, respectively)	205	460	
Accretion of unrealized losses related to factors other than credit to investment securities held to maturity (net of tax benefit of $115 and $120 in 2010 and 2009, respectively)	173	180	
Net change in unrealized losses related to factors other than credit	603	(980)	
Other comprehensive (loss) income, net of tax	(10)	10,883	14,459
Comprehensive income (loss)	$ 28,316	$ (142,483)	$ 65,503

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UMPQUA HOLDINGS CORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

For the Years Ended December 31, 2010, 2009 and 2008

(in thousands)

	2010	2009	2008
CASH FLOWS FROM OPERATING ACTIVITIES:			
Net income (loss)	$ 28,326	$ (153,366)	$ 51,044
Adjustments to reconcile net income (loss) to net cash provided by operating activities:			
Restricted equity securities stock dividends			(198)
Deferred income tax expense (benefit)	4,393	(18,360)	9,889
Amortization of investment premiums, net	20,464	9,301	1,898
Gain on sale of investment securities, net	(2,326)	(8,896)	(5,529)
Other-than-temporary impairment on investment securities available for sale		239	139
Other-than-temporary impairment on investment securities held to maturity	414	10,334	4,041
Loss on sale of non-covered other real estate owned	4,023	10,957	3,229
Gain on sale of covered other real estate owned	(4,113)		
Valuation adjustment on non-covered other real estate owned	4,074	12,247	5,084
Valuation adjustment on covered other real estate owned	1,941		
Provision for non-covered loan and lease losses	113,668	209,124	107,678
Provision for covered loan and lease losses	5,151		
Bargain purchase gain on acquisition	(6,437)		
Change in FDIC indemnification asset	16,445		
Depreciation, amortization and accretion	9,199	11,649	7,085
Goodwill impairment		111,952	982
Increase in mortgage servicing rights	(5,645)	(7,570)	(2,694)
Change in mortgage servicing rights carried at fair value	3,878	3,150	4,577
Change in junior subordinated debentures carried at fair value	(4,978)	(6,854)	(39,166)
Stock-based compensation	3,505	2,188	3,893
Net (increase) decrease in trading account assets	(751)	(286)	850
Gain on sale of loans	(10,923)	(6,649)	(790)
Origination of loans held for sale	(702,449)	(682,535)	(250,439)
Proceeds from sales of loans held for sale	670,872	677,598	241,481
Excess tax benefits from the exercise of stock options	(7)	(1)	(5)
Change in other assets and liabilities			
Net decrease (increase) in other assets	47,011	(72,570)	18,032
Net increase (decrease) in other liabilities	2,914	(8,426)	(14,535)
Net cash provided by operating activities	198,649	93,226	146,546
CASH FLOWS FROM INVESTING ACTIVITIES:			
Purchases of investment securities available for sale	(1,498,224)	(1,002,490)	(811,868)
Proceeds from investment securities available for sale	408,670	464,376	635,883
Proceeds from investment securities held to maturity	1,675	2,282	1,705
Purchases of restricted equity securities			(4,415)
Redemption of restricted equity securities	472	1,280	3,395
Net non-covered loan and lease paydowns (originations)	146,252	(121,257)	(230,098)
Net covered loan and lease paydowns	119,941		
Proceeds from sales of loans	38,744	12,519	22,952
Proceeds from disposals of furniture and equipment	1,237	270	357
Purchases of premises and equipment	(47,559)	(11,239)	(10,737)
Net proceeds from FDIC indemnification asset	48,443		
Proceeds from sales of non-covered other real estate owned	25,124	26,167	15,319
Proceeds from sales of covered other real estate owned	14,598		
Proceeds from sale of acquired insurance portfolio	5,150		
Cash acquired in merger, net of cash consideration paid	179,046	178,905	

Net cash used by investing activities	(556,431)	(449,187)	(377,507)

Umpqua Holdings Corporation

UMPQUA HOLDINGS CORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS (Continued)

For the Years Ended December 31, 2010, 2009 and 2008

(in thousands)

	2010	2009	2008
CASH FLOWS FROM FINANCING ACTIVITIES:			
Net increase (decrease) in deposit liabilities	$ 847,895	$ 667,610	$ (437)
Net decrease in federal funds purchased			(69,500)
Net increase (decrease) in securities sold under agreements to repurchase	28,579	(2,408)	11,294
Proceeds from term debt borrowings			345,000
Repayment of term debt	(165,789)	(130,191)	(212,284)
Proceeds from issuance of preferred stock	198,289		201,927
Redemption of preferred stock	(214,181)		
Proceeds from issuance of warrants			12,254
Repurchase of warrants issued to U.S. Treasury	(4,500)		
Net proceeds from issuance of common stock	89,786	245,697	
Dividends paid on preferred stock	(3,686)	(10,739)	
Dividends paid on common stock	(20,626)	(13,399)	(45,796)
Excess tax benefits from the exercise of stock options	7	1	5
Proceeds from stock options exercised	1,004	301	1,233
Retirement of common stock	(284)	(174)	(129)
Net cash provided by financing activities	756,494	756,698	243,567
Net increase in cash and cash equivalents	398,712	400,737	12,606
Cash and cash equivalents, beginning of year	605,413	204,676	192,070
Cash and cash equivalents, end of year	$ 1,004,125	$ 605,413	$ 204,676
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:			
Cash paid during the year for:			
Interest	$ 99,556	$ 106,541	$ 156,686
Income taxes	$ 285	$ 48	$ 6,092
SUPPLEMENTAL DISCLOSURE OF NONCASH INVESTING AND FINANCING ACTIVITIES:			
Change in unrealized gains on investment securities available for sale, net of taxes	$ (613)	$ 9,186	$ 17,136
Change in unrealized loss on investment securities transferred to held to maturity, net of taxes	$	$ 2,677	$ (2,677)
Change in unrealized losses on investment securities held to maturity related to factors other than credit, net of taxes	$ 603	$ (980)	$
Cash dividend declared on common and preferred stock and payable after period-end	$ 5,745	$ 4,346	$ 3,016
Transfer of investment securities available for sale to held to maturity	$	$	$ 12,580
Transfer of non-covered loans to non-covered other real estate owned	$ 41,491	$ 50,914	$ 44,587
Transfer of covered loans to covered other real estate owned	$ 15,350	$	$
Conversion of preferred stock to common stock	$ 198,289	$	$
Receivable from sales of noncovered other real estate owned and loans	$ 45	$ 4,875	$
Acquisitions:			
Assets acquired	$ 1,512,048	$ 4,978	$
Liabilities assumed	$ 1,505,611	$ 183,883	$

See notes to consolidated financial statements

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Years Ended December 31, 2010, 2009 and 2008

NOTE 1. SIGNIFICANT ACCOUNTING POLICIES

Nature of Operations Umpqua Holdings Corporation (the Company) is a financial holding company headquartered in Portland, Oregon, that is engaged primarily in the business of commercial and retail banking and the delivery of retail brokerage services. The Company provides a wide range of banking, asset management, mortgage banking and other financial services to corporate, institutional and individual customers through its wholly-owned banking subsidiary Umpqua Bank (the Bank). The Company engages in the retail brokerage business through its wholly-owned subsidiary Umpqua Investments, Inc. (Umpqua Investments). Prior to July 2009, Umpqua Investments was known as Strand, Atkinson, Williams & York, Inc. The Company and its subsidiaries are subject to regulation by certain federal and state agencies and undergo periodic examination by these regulatory agencies.

Basis of Financial Statement Presentation The consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States and with prevailing practices within the banking and securities industries. In preparing such financial statements, management is required to make certain estimates and judgments that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities as of the date of the balance sheet and the reported amounts of revenues and expenses for the reporting period. Actual results could differ significantly from those estimates. Material estimates that are particularly susceptible to significant change relate to the determination of the allowance for loan and lease losses, the valuation of mortgage servicing rights, the fair value of junior subordinated debentures, the valuation of covered loans and the FDIC indemnification asset, and the valuation of goodwill and other intangible assets.

Consolidation The accompanying consolidated financial statements include the accounts of the Company, the Bank and Umpqua Investments. All significant intercompany balances and transactions have been eliminated in consolidation. As of December 31, 2010, the Company had 14 wholly-owned trusts (Trusts) that were formed to issue trust preferred securities and related common securities of the Trusts. The Company has not consolidated the accounts of the Trusts in its consolidated financial statements in accordance with Financial Accounting Standards Board Accounting Standards Codification (FASB ASC) 810, Consolidation. As a result, the junior subordinated debentures issued by the Company to the Trusts are reflected on the Company s consolidated balance sheet as junior subordinated debentures.

Subsequent events The Company has evaluated events and transactions subsequent to December 31, 2010 for potential recognition or disclosure.

Cash and Cash Equivalents Cash and cash equivalents include cash and due from banks, and temporary investments which are federal funds sold and interest bearing balances due from other banks. Cash and cash equivalents generally have a maturity of 90 days or less at the time of purchase.

Trading Account Securities Debt and equity securities held for resale are classified as trading account securities and reported at fair value. Realized and unrealized gains or losses are recorded in non-interest income.

Investment Securities Debt securities are classified as *held to maturity* if the Company has both the intent and ability to hold those securities to maturity regardless of changes in market conditions, liquidity needs or changes in general economic conditions. These securities are carried at cost adjusted for amortization of premium and accretion of discount, computed by the effective interest method over their contractual lives.

Securities are classified as *available for sale* if the Company intends and has the ability to hold those securities for an indefinite period of time, but not necessarily to maturity. Any decision to sell a security classified as available for sale would be based on various factors, including significant movements in interest rates, changes in the maturity mix of assets and liabilities, liquidity needs, regulatory capital considerations and other similar factors. Securities available for sale are carried at fair value. Unrealized holding gains or losses are included in other comprehensive income as a separate component of shareholders equity, net of tax. Realized gains or losses, determined on the basis of the cost of specific securities sold, are included in earnings. Premiums and discounts are amortized or accreted over the life of the related investment security as an adjustment to yield using the effective interest method. Dividend and interest income are recognized when earned.

Prior to the second quarter of 2009, the Company would assess an other-than-temporary impairment (OTTI) or permanent impairment based on the nature of the decline and whether the Company has the ability and intent to hold the investments until a market price recovery. If the Company determined a security to be other-than-temporarily or permanently impaired, the full amount of impairment would be recognized through earnings in its entirety. New guidance related to the recognition and presentation of OTTI of debt securities became effective in the second quarter of 2009. Rather than asserting whether a Company has the ability and intent to hold an investment until a market price recovery, a Company must consider whether it intends to sell a security or if it is likely that they would be required to sell the security before recovery of the amortized cost basis of the investment, which may be maturity. For debt securities, if we intend to sell the security or it is likely that we will be required to sell the security before recovering its cost basis, the entire impairment loss would be recognized in earnings as an OTTI. If we do not intend to sell the security and it is not likely that we will be required to sell the security but we do not expect to recover the entire amortized cost basis of the security, only the portion of the impairment loss representing credit losses would be recognized in earnings. The credit loss on a security is measured as the difference between the amortized cost basis and the present value of the cash flows expected to be collected. Projected cash flows are discounted by the original or current effective interest rate depending on the nature of the security being measured for potential OTTI. The remaining impairment related to all other factors, the difference between the present value of the cash flows expected to be collected and fair value, is recognized as a charge to other comprehensive income (OCI). Impairment losses related to all other factors are presented as separate categories within OCI. For investment securities held to maturity, this amount is accreted over the remaining life of the debt security prospectively based on the amount and timing of future estimated cash flows. The accretion of the amount recorded in OCI increases the carrying value of the investment and does not affect earnings. If there is an indication of additional credit losses the security is re-evaluated according to the procedures described above. OTTI losses totaling $414,000, $10.6 million, and $4.2 million were recognized through earnings in the years ended December 31, 2010, 2009 and 2008, respectively, within total gain (loss) on investment securities, net.

Transfers of securities from available for sale to held to maturity are accounted for at fair value as of the date of the transfer. The difference between the fair value and the par value at the date of transfer is considered a premium or discount and is accounted for accordingly. Any unrealized gain or loss at the date of the transfer is reported in OCI, and is amortized over the remaining life of the security as an adjustment of yield in a manner consistent with the amortization of any premium or discount, and will offset or mitigate the effect on interest income of the amortization of the premium or discount for that held to maturity security.

Loans Held for Sale Loans held for sale includes mortgage loans and are reported at the lower of cost or market value. Cost generally approximates market value, given the short duration of these assets. Gains or losses on the sale of loans that are held for sale are recognized at the time of the sale and determined by the difference between net sale proceeds and the net book value of the loans less the estimated fair value of any retained mortgage servicing rights.

Non-Covered Loans Loans are stated at the amount of unpaid principal, net of unearned income and any deferred fees or costs. All discounts and premiums are recognized over the estimated life of the loan as yield adjustments. This estimated life is adjusted for prepayments.

Loans are classified as *impaired* when, based on current information and events, it is probable that the Bank will be unable to collect the scheduled payments of principal and interest when due, in accordance with the terms of the original loan agreement. The carrying value of impaired loans is based on the present value of expected future cash flows (discounted at each loan s effective interest rate) or, for collateral dependent loans, at fair value of the collateral, less selling costs. If the measurement of each impaired loans value is less than the recorded investment in the loan, we recognize this impairment and adjust the carrying value of the loan to fair value through the allowance for loan and lease losses. This can be accomplished by charging-off the impaired portion of the loan or establishing a specific component to be provided for in the allowance for loan and lease losses.

Covered Loans Loans acquired in a FDIC-assisted acquisition that are subject to a loss-share agreement are referred to as covered loans and reported separately in our consolidated balance sheets. Covered loans are reported exclusive of the expected cash flow reimbursements expected from the FDIC. Acquired loans are aggregated into pools based on individually evaluated common risk characteristics and aggregate expected cash flows were estimated for each pool. A pool is accounted for as a single asset with a single interest rate, cumulative loss rate and cash flow expectation. The Company aggregated all of the loans acquired in the FDIC-assisted acquisitions into different pools based on common risk characteristics such as risk rating, underlying collateral, type of interest rate (fixed or adjustable), types of amortization, and other similar factors. A loan will be removed from a pool of loans only if the loan is sold, foreclosed, assets are received in full satisfaction of the loan, and will be removed from the pool at its carrying value. If an individual loan is removed from a pool of loans, the difference between its relative carrying amount and its cash, fair value of the collateral, or other assets received will be recognized in income immediately as interest income on loans and would not affect the effective yield used to recognize the accretable yield on the remaining pool. Loans originally placed into a performing pool are not be reported individually as 30-89 days past due, non-performing (90+ days past due or nonaccrual), or accounted for as a troubled debt restructuring as the pool is the unit of accounting. Rather, these metrics related to the underlying loans within a performing pool will be considered in our ongoing assessment and estimates of future cash flows. If, at acquisition, the loans are collateral dependent and acquired primarily for the rewards of ownership of the underlying collateral, or if cash flows expected to be collected cannot be reasonably estimated, accrual of income is inappropriate. Such loans will be placed into nonperforming (nonaccrual) loan pools quarterly.

The cash flows expected to be received over the life of the pool were estimated by management with the assistance of a third party valuation specialist. These cash flows were input into a ASC 310-30 compliant loan accounting system which calculates the carrying values of the pools and underlying loans, book yields, effective interest income and impairment, if any, based on actual and projected events. Default rates, loss severity, and prepayment speeds assumptions will be periodically reassessed and updated within the accounting system to update our expectation of future cash flows. The excess of the cash flows expected to be collected over a pool s carrying value is considered to be the accretable yield and is recognized as interest income over the estimated life of the loan or pool using the effective yield method. The accretable yield may change due to changes in the timing and amounts of expected cash flows. Changes in the accretable yield are disclosed quarterly.

The excess of the undiscounted contractual balances due over the cash flows expected to be collected is considered to be the nonaccretable difference. The nonaccretable difference represents our estimate of the credit losses expected to occur and was considered in determining the fair value of the loans as of the acquisition date. Subsequent to the acquisition date, any increases in expected cash flows over those expected at purchase date in excess of fair value are adjusted through an increase to the accretable yield on a prospective basis. Any subsequent decreases in expected cash flows over those expected at the purchase date are recognized by recording a provision for covered loan losses.

The covered loans acquired are and will continue to be subject to the Company s internal and external credit review and monitoring. If credit deterioration is experienced subsequent to the initial acquisition fair value amount, such deterioration will be measured, and a provision for credit losses will be charged to earnings. These provisions will be mostly offset by an increase to the FDIC indemnification asset, and will be recognized in non-interest income.

The covered loan portfolio also includes revolving lines of credit with funded and unfunded commitments. Funds advanced at the time of acquisition are accounted for under FASB ASC 310-30, *Loans and Debt Securities Acquired with Deteriorated Credit Quality*. Any additional advances on these loans subsequent to the acquisition date are not accounted for under ASC 310-30.

FDIC Indemnification Asset The Company has elected to account for amounts receivable under the loss-share agreement as an indemnification asset in accordance with FASB ASC 805, *Business Combinations*. The FDIC indemnification asset is initially recorded at fair value, based on the discounted value of expected future cash flows under the loss-share agreement. The difference between the present value and the undiscounted cash flows the Company expects to collect from the FDIC will be accreted or amortized into non-interest income over the life of the FDIC indemnification asset.

Subsequent to initial recognition, the FDIC indemnification asset is reviewed quarterly and adjusted for any changes in expected cash flows based on recent performance and expectations for future performance of the covered portfolio. These adjustments are measured on the same basis as the related covered loans, at a pool level, and covered other real estate owned. Generally, any increases in cash flow of the covered assets over those previously expected will result in prospective increases in the loan pool yield and amortization of the FDIC indemnification asset. Any decreases in cash flow of the covered assets under those previously expected will trigger impairments on the underlying loan pools and will result in a corresponding gain of the

FDIC indemnification asset. Increases and decreases to the FDIC indemnification asset are recorded as adjustments to non-interest income. The resulting carrying value of the indemnification asset represents the present value of amounts recoverable from the FDIC for future expected losses and the amounts due from the FDIC for claims related to covered losses.

Income Recognition on Non-Covered, Non-Accrual and Impaired Loans Non-covered loans, including impaired non-covered loans, are classified as non-accrual if the collection of principal and interest is doubtful. Generally, this occurs when a non-covered loan is past due as to maturity or payment of principal or interest by 90 days or more, unless such non-covered loans are well-secured and in the process of collection. Generally, if a non-covered loan or portion thereof is partially charged-off, the non-covered loan is considered impaired and classified as non-accrual. Non-covered loans that are less than 90 days past due may also be classified as non-accrual if repayment in full of principal and/or interest is in doubt.

When a non-covered loan is classified as non-accrual, all uncollected accrued interest is reversed to interest income and the accrual of interest income is terminated. Generally, any cash payments are applied as a reduction of principal outstanding. In cases where the future collectability of the principal balance in full is expected, interest income may be recognized on a cash basis. A non-covered loan may be restored to accrual status when the borrower s financial condition improves so that full collection of future contractual payments is considered likely. For those non-covered loans placed on non-accrual status due to payment delinquency, this will generally not occur until the borrower demonstrates repayment ability over a period of not less than six months.

Non-covered loans are reported as restructured when the Bank grants a concession(s) to a borrower experiencing financial difficulties that it would not otherwise consider. Examples of such concessions include forgiveness of principal or accrued interest, extending the maturity date(s) or providing a lower interest rate than would be normally available for a transaction of similar risk. As a result of these concessions, restructured loans are impaired as the Bank will not collect all amounts due, both principal and interest, in accordance with the terms of the original loan agreement. Impairment reserves on non-collateral dependent restructured loans are measured by comparing the present value of expected future cash flows on the restructured loans discounted at the interest rate of the original loan agreement to the loan s carrying value. These impairment reserves are recognized as a specific component to be provided for in the allowance for loan and lease losses.

The decision to classify a non-covered loan as impaired is made by the Bank s Allowance for Loan and Lease Losses (ALLL) Committee. The ALLL Committee meets regularly to review the status of all problem and potential problem loans. If the ALLL Committee concludes a loan is impaired but recovery of the full principal and interest is expected, an impaired loan may remain on accrual status.

Allowance for Loan and Lease Losses The Bank performs regular credit reviews of the loan and lease portfolio to determine the credit quality of the portfolio and the adherence to underwriting standards. When loans and leases are originated, they are assigned a risk rating that is reassessed periodically during the term of the loan through the credit review process. The Company s risk rating methodology assigns risk ratings ranging from 1 to 10, where a higher rating represents higher risk. The 10 risk rating categories are a primary factor in determining an appropriate amount for the allowance for loan and lease losses. The Bank has a management ALLL Committee, which is responsible for, among other things, regularly reviewing the ALLL methodology, including loss factors, and ensuring that it is designed and applied in accordance with generally accepted accounting principles. The ALLL Committee reviews and approves loans and leases recommended for impaired status. The ALLL Committee also approves removing loans and leases from impaired status. The Bank s Audit and Compliance Committee provides board oversight of the ALLL process and reviews and approves the ALLL methodology on a quarterly basis.

Each risk rating is assessed an inherent credit loss factor that determines the amount of the allowance for loan and lease losses provided for that group of loans and leases with similar risk rating. Credit loss factors may vary by region based on management s belief that there may ultimately be different credit loss rates experienced in each region.

Regular credit reviews of the portfolio also identify loans that are considered potentially impaired. Potentially impaired loans are referred to the ALLL Committee which reviews and approves designated loans as impaired. A loan is considered impaired when based on current information and events, we determine that we will probably not be able to collect all amounts due according to the loan contract, including scheduled interest payments. When we identify a loan as impaired, we measure the impairment using discounted cash flows, except when the sole remaining source of the repayment for the loan is the liquidation of the collateral. In these cases, we use the current fair value of the collateral, less selling costs, instead of discounted cash flows. If we determine that the value of the impaired loan is less than the recorded investment in the loan, we either recognize this impairment reserve as a specific component to be provided for in the allowance for loan and lease losses or charge-off the impaired balance on collateral dependent loans if it is determined that such amount represents a confirmed loss. The combination of the risk rating-based allowance component and the impairment reserve allowance component lead to an allocated allowance for loan and lease losses.

The Bank may also maintain an unallocated allowance amount to provide for other credit losses inherent in a loan and lease portfolio that may not have been contemplated in the credit loss factors. This unallocated amount generally comprises less than 10% of the allowance, but may be maintained at higher levels during times of economic conditions characterized by falling real estate values. The unallocated amount is reviewed periodically based on trends in credit losses, the results of credit reviews and overall economic trends.

As adjustments become necessary, they are reported in earnings in the periods in which they become known as a change in the provision for loan and lease losses and a corresponding charge to the allowance. Loans, or portions thereof, deemed uncollectible are charged to the allowance. Provisions for losses, and recoveries on loans previously charged-off, are added to the allowance.

The adequacy of the ALLL is monitored on a regular basis and is based on management s evaluation of numerous factors. These factors include the quality of the current loan portfolio; the trend in the loan portfolio s risk ratings; current economic conditions; loan concentrations; loan growth rates; past-due and non-performing trends; evaluation of specific loss estimates for all significant problem loans; historical charge-off and recovery experience; and other pertinent information.

Management believes that the ALLL was adequate as of December 31, 2010. There is, however, no assurance that future loan losses will not exceed the levels provided for in the ALLL and could possibly result in additional charges to the provision for loan and lease losses. In addition, bank regulatory authorities, as part of their periodic examination of the Bank, may require additional charges to the provision for loan and lease losses in future periods if warranted as a result of their review. Approximately 82% of our loan portfolio is secured by real estate, and a significant decline in real estate market values may require an increase in the allowance for loan and lease losses. The U.S. recession, the housing market downturn, and declining real estate values in our markets have negatively impacted aspects of our residential development, commercial real estate, commercial construction and commercial loan portfolios, and have led to an increase in non-performing loans, charge-offs, and the allowance for loan and lease losses. A continued deterioration or prolonged delay in economic recovery in our markets may adversely affect our loan portfolio and may lead to additional charges to the provision for loan and lease losses.

Reserve for Unfunded Commitments A reserve for unfunded commitments is maintained at a level that, in the opinion of management, is adequate to absorb probable losses associated with the Bank s commitment to lend funds under existing agreements such as letters or lines of credit. Management determines the adequacy of the reserve for unfunded commitments based upon reviews of individual credit facilities, current economic conditions, the risk characteristics of the various categories of commitments and other relevant factors. The reserve is based on estimates, and ultimate losses may vary from the current estimates. These estimates are evaluated on a regular basis and, as adjustments become necessary, they are reported in earnings in the periods in which they become known. Draws on unfunded commitments that are considered uncollectible at the time funds are advanced are charged to the allowance. Provisions for unfunded commitment losses, and recoveries on loans commitments previously charged-off, are added to the reserve for unfunded commitments, which is included in the *Other Liabilities* section of the consolidated balance sheets.

Loan Fees and Direct Loan Origination Costs Loan origination and commitment fees and direct loan origination costs are deferred and recognized as an adjustment to the yield over the life of the related loans.

Restricted Equity Securities Restricted equity securities were $34.5 million and $15.2 million at December 31, 2010 and 2009, respectively. Federal Home Loan Bank stock amounted to $33.2 million and $14.3 million of the total restricted securities as of December 31, 2010 and 2009, respectively. Federal Home Loan Bank stock represents the Bank s investment in the

Federal Home Loan Banks of Seattle and San Francisco (FHLB) stock and is carried at par value, which reasonably approximates its fair value. Management periodically evaluates FHLB stock for other-than-temporary or permanent impairment. Management s determination of whether these investments are impaired is based on its assessment of the ultimate recoverability of cost rather than by recognizing temporary declines in value. The determination of whether a decline affects the ultimate recoverability of cost is influenced by criteria such as (1) the significance of any decline in net assets of the FHLB as compared to the capital stock amount for the FHLB and the length of time this situation has persisted, (2) commitments by the FHLB to make payments required by law or regulation and the level of such payments in relation to the operating performance of the FHLB, (3) the impact of legislative and regulatory changes on institutions and, accordingly, the customer base of the FHLB, and (4) the liquidity position of the FHLB.

As a member of the FHLB system, the Bank is required to maintain a minimum level of investment in FHLB stock based on specific percentages of its outstanding mortgages, total assets, or FHLB advances. At December 31, 2010, the Bank s minimum required investment in FHLB stock was $7.6 million. The Bank may request redemption at par value of any stock in excess of the minimum required investment. Stock redemptions are at the discretion of the FHLB. The remaining restricted equity securities balance primarily represents an investment in Pacific Coast Bankers Bancshares stock.

Premises and Equipment Premises and equipment are stated at cost less accumulated depreciation and amortization. Depreciation is provided over the estimated useful life of equipment, generally three to ten years, on a straight-line or accelerated basis. Depreciation is provided over the estimated useful life of premises, up to 39 years, on a straight-line or accelerated basis. Leasehold improvements are amortized over the life of the related lease, or the life of the related asset, whichever is shorter. Expenditures for major renovations and betterments of the Company s premises and equipment are capitalized.

Management reviews long-lived and intangible assets any time that a change in circumstance indicates that the carrying amount of these assets may not be recoverable. Recoverability of these assets is determined by comparing the carrying value of the asset to the forecasted undiscounted cash flows of the operation associated with the asset. If the evaluation of the forecasted cash flows indicates that the carrying value of the asset is not recoverable, the asset is written down to fair value.

Goodwill and Other Intangibles Intangible assets are comprised of goodwill and other intangibles acquired in business combinations. Goodwill and intangible assets with indefinite useful lives are not amortized. Intangible assets with definite useful lives are amortized to their estimated residual values over their respective estimated useful lives, and also reviewed for impairment. Amortization of intangible assets is included in other non-interest expense in the *Consolidated Statements of Operations*.

The Company performs a goodwill impairment analysis on an annual basis as of December 31. Additionally, the Company performs a goodwill impairment evaluation on an interim basis when events or circumstances indicate impairment potentially exists. A significant amount of judgment is involved in determining if an indicator of impairment has occurred. Such indicators may include, among others, a significant decline in our expected future cash flows; a sustained, significant decline in our stock price and market capitalization; a significant adverse change in legal factors or in the business climate; adverse action or assessment by a regulator; and unanticipated competition.

The goodwill impairment test involves a two-step process. The first step compares the fair value of a reporting unit to its carrying value. If the reporting unit s fair value is less than its carrying value, the Company would be required to proceed to the second step. In the second step the Company calculates the implied fair value of the reporting unit s goodwill. The implied fair value of goodwill is determined in the same manner as goodwill recognized in a business combination. The estimated fair value of the Company is allocated to all of the Company s assets and liabilities, including any unrecognized identifiable intangible assets, as if the Company had been acquired in a business combination and the estimated fair value of the reporting unit is the price paid to acquire it. The allocation process is performed only for purposes of determining the amount of goodwill impairment. No assets or liabilities are written up or down, nor are any additional unrecognized identifiable intangible assets recorded as a part of this process. Any excess of the estimated purchase price over the fair value of the reporting unit s net assets represents the implied fair value of goodwill. If the carrying amount of the goodwill is greater than the implied fair value of that goodwill, an impairment loss would be recognized as a charge to earnings in an amount equal to that excess.

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Mortgage Servicing Rights (MSR) The Company determines its classes of servicing assets based on the asset type being serviced along with the methods used to manage the risk inherent in the servicing assets, which includes the market inputs used to value the servicing assets. The Company measures its residential mortgage servicing assets at fair value and reports changes in fair value through earnings. Fair value adjustments that encompass market-driven valuation changes and the runoff in value that occurs from the passage of time, are each separately reported. Under the fair value method, the MSR is carried in the balance sheet at fair value and the changes in fair value are reported in earnings under the caption mortgage banking revenue in the period in which the change occurs.

Retained mortgage servicing rights are measured at fair value as of the date of sale. We use quoted market prices when available. Subsequent fair value measurements are determined using a discounted cash flow model. In order to determine the fair value of the MSR, the present value of expected future cash flows is estimated. Assumptions used include market discount rates, anticipated prepayment speeds, delinquency and foreclosure rates, and ancillary fee income. This model is periodically validated by an independent external model validation group. The model assumptions and the MSR fair value estimates are also compared to observable trades of similar portfolios as well as to MSR broker valuations and industry surveys, as available. Key assumptions used in measuring the fair value of MSR as of December 31, 2010 were as follows:

	2010	2009	2008
Constant prepayment rate	18.54%	18.35%	13.69%
Discount rate	8.62%	8.70%	8.85%
Weighted average life (years)	4.5	4.5	5.0

The expected life of the loan can vary from management s estimates due to prepayments by borrowers, especially when rates fall. Prepayments in excess of management s estimates would negatively impact the recorded value of the mortgage servicing rights. The value of the mortgage servicing rights is also dependent upon the discount rate used in the model, which we base on current market rates. Management reviews this rate on an ongoing basis based on current market rates. A significant increase in the discount rate would reduce the value of mortgage servicing rights.

SBA/USDA Loans Sales and Servicing The Bank, on a limited basis, sells or transfers loans, including the guaranteed portion of Small Business Administration (SBA) and Department of Agriculture (USDA) loans (with servicing retained) for cash proceeds equal to the principal amount of loans, as adjusted to yield interest to the investor based upon the current market rates. The Bank records an asset representing the right to service loans for others when it sells a loan and retains the servicing rights. The carrying value of loans is allocated between the loan and the servicing rights, based on their relative fair values. The fair value of servicing rights is estimated by discounting estimated future cash flows from servicing using discount rates that approximate current market rates and using estimated prepayment rates. The servicing rights are carried at the lower of cost or market and are amortized in proportion to, and over the period of, the estimated net servicing income, assuming prepayments.

For purposes of evaluating and measuring impairment, servicing rights are based on a discounted cash flow methodology, current prepayment speeds and market discount rates. Any impairment is measured as the amount by which the carrying value of servicing rights for a stratum exceeds its fair value. The carrying value of SBA/USDA servicing rights at December 31, 2010 and 2009 were $721,000 and $728,000, respectively. No impairment charges were recorded for the years ended December 31, 2010, 2009 or 2008 related to SBA/USDA servicing assets.

A premium over the adjusted carrying value is received upon the sale of the guaranteed portion of an SBA or USDA loan. The Bank s investment in an SBA or USDA loan is allocated among the sold and retained portions of the loan based on the relative fair value of each portion at the time of loan origination, adjusted for payments and other activities. Because the portion retained does not carry an SBA or USDA guarantee, part of the gain recognized on the sold portion of the loan may be deferred and amortized as a yield enhancement on the retained portion in order to obtain a market equivalent yield.

Non-Covered Other Real Estate Owned Non-covered other real estate owned (non-covered OREO) represents real estate which the Bank has taken control of in partial or full satisfaction of loans. At the time of foreclosure, other real estate owned is recorded at the lower of the carrying amount of the loan or fair value less costs to sell, which becomes the property s new basis. Any write-downs based on the asset s fair value at the date of acquisition are charged to the allowance for loan and lease losses. After foreclosure, management periodically performs valuations such that the real estate is carried at the lower of its new cost basis or fair value, net of estimated costs to sell. Subsequent valuation adjustments are recognized within net loss on non-covered OREO. Revenue and expenses from operations and subsequent adjustments to the carrying amount of the property are included in other non-interest expense in the *Consolidated Statements of Operations*.

In some instances, the Bank may make loans to facilitate the sales of other real estate owned. Management reviews all sales for which it is the lending institution for compliance with sales treatment under provisions established within FASB ASC 360-20, *Real Estate Sales*. Any gains related to sales of other real estate owned may be deferred until the buyer has a sufficient initial and continuing investment in the property.

Covered Other Real Estate Owned All OREO acquired in FDIC-assisted acquisitions that are subject to a FDIC loss-share agreement are referred to as covered OREO and reported separately in our statements of financial position. Covered OREO is reported exclusive of expected reimbursement cash flows from the FDIC. Foreclosed covered loan collateral is transferred into covered OREO at the collateral s net realizable value, less selling costs.

Covered OREO was initially recorded at its estimated fair value on the acquisition date based on similar market comparable valuations less estimated selling costs. Any subsequent valuation adjustments due to declines in fair value will be charged to non-interest expense, and will be mostly offset by non-interest income representing the corresponding increase to the FDIC indemnification asset for the offsetting loss reimbursement amount. Any recoveries of previous valuation adjustments will be credited to non-interest expense with a corresponding charge to non-interest income for the portion of the recovery that is due to the FDIC.

Income Taxes Income taxes are accounted for using the asset and liability method. Under this method a deferred tax asset or liability is determined based on the enacted tax rates which will be in effect when the differences between the financial statement carrying amounts and tax basis of existing assets and liabilities are expected to be reported in the Company s income tax returns. The effect on deferred taxes of a change in tax rates is recognized in income in the period that includes the enactment date. Valuation allowances are established to reduce the net carrying amount of deferred tax assets if it is determined to be more likely than not, that all or some portion of the potential deferred tax asset will not be realized.

Derivative Loan Commitments The Bank enters into forward delivery contracts to sell residential mortgage loans or mortgage-backed securities to broker/dealers at specific prices and dates in order to hedge the interest rate risk in its portfolio of mortgage loans held for sale and its residential mortgage loan commitments. The commitments to originate mortgage loans held for sale and the related forward delivery contracts are considered derivatives. The Company recognizes all derivatives as either assets or liabilities in the balance sheet and requires measurement of those instruments at fair value through adjustments to accumulated other comprehensive income and/or current earnings, as appropriate. None of the Company s derivatives are designated as hedging instruments. Rather, they are accounted for as free-standing derivatives, or economic hedges, and the Company reports changes in fair values of its derivatives in current period net income.

The fair value of the derivative loan commitments is estimated using the present value of expected future cash flows. Assumptions used include pull-through rate assumption based on historical information, current mortgage interest rates, the stage of completion of the underlying application and underwriting process, the time remaining until the expiration of the derivative loan commitment, and the expected net future cash flows related to the associated servicing of the loan.

Operating Segments Public enterprises are required to report certain information about their operating segments in a complete set of financial statements to shareholders. They are also required to report certain enterprise-wide information about the Company s products and services, its activities in different geographic areas, and its reliance on major customers. The basis for determining the Company s operating segments is the manner in which management operates the business. Management has identified three primary business segments, Community Banking, Retail Brokerage and Mortgage Banking.

Share-Based Payment The Company has two active stock-based compensation plans that provide for the granting of stock options and restricted stock to eligible employees and directors. In accordance with FASB ASC 718, *Stock Compensation,* we recognize in the income statement the grant-date fair value of stock options and other equity-based forms of compensation issued to employees over the employees requisite service period (generally the vesting period). The requisite service period may be subject to performance conditions.

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The Company s 2003 Stock Incentive Plan provides for granting of stock options and restricted stock awards. Stock options and restricted stock awards generally vest ratably over 5 years and are recognized as expense over that same period of time.

The fair value of each option grant is estimated as of the grant date using the Black-Scholes option-pricing model using assumptions noted in the following table. Expected volatility is based on the historical volatility of the price of the Company s common stock. The Company uses historical data to estimate option exercise and stock option forfeiture rates within the valuation model. The expected term of options granted is determined based on historical experience with similar options, giving consideration to the contractual terms and vesting schedules, and represents the period of time that options granted are expected to be outstanding. The expected dividend yield is based on dividend trends and the market value of the Company s common stock at the time of grant. The risk-free rate is based on the U.S. Treasury yield curve in effect at the time of grant corresponding to the estimated expected term of the options granted. The following weighted average assumptions were used to determine the fair value of stock option grants as of the grant date to determine compensation cost for the years ended December 31, 2010, 2009 and 2008:

	2010	2009	2008
Dividend yield	2.72%	2.23%	4.39%
Expected life (years)	7.1	7.3	7.3
Expected volatility	52%	46%	34%
Risk-free rate	2.69%	2.18%	3.29%
Weighted average grant date fair value of options granted	$ 5.24	$ 3.65	$ 3.32

The Company s 2007 Long Term Incentive Plan provides for granting of restricted stock units for the benefit of certain executive officers. Restricted stock unit grants are subject to performance-based vesting as well as other approved vesting conditions. The current restricted stock units outstanding cliff vest after three years based on performance and service conditions. Compensation expense is recognized over the service period to the extent restricted stock units are expected to vest.

Earnings per Share According to the revised provisions of FASB ASC 260, *Earnings Per Share*, which became effective January 1, 2009, nonvested share-based payment awards that contain nonforfeitable rights to dividends or dividend equivalents are participating securities and are included in the computation of EPS pursuant to the two-class method. The two-class method is an earnings allocation formula that determines earnings per share for each class of common stock and participating security according to dividends declared (or accumulated) and participation rights in undistributed earnings. Certain of the Company s nonvested restricted stock awards qualify as participating securities.

Net income, less any preferred dividends accumulated for the period (whether or not declared), is allocated between the common stock and participating securities pursuant to the two-class method, based on their rights to receive dividends, participate in earnings or absorb losses. *Basic earnings per common share* is computed by dividing net earnings available to common shareholders by the weighted average number of common shares outstanding during the period, excluding participating nonvested restricted shares.

Diluted earnings per common share is computed in a similar manner, except that first the denominator is increased to include the number of additional common shares that would have been outstanding if potentially dilutive common shares, excluding the participating securities, were issued using the treasury stock method. For all periods presented, warrants, stock options, certain restricted stock awards and restricted stock units are the only potentially dilutive non-participating instruments issued by the Company. Next, we determine and include in diluted earnings per common share calculation the more dilutive effect of the participating securities using the treasury stock method or the two-class method. Undistributed losses are not allocated to the nonvested share-based payment awards (the participating securities) under the two-class method as the holders are not contractually obligated to share in the losses of the Company.

All earnings per common share amounts for 2008 have been retrospectively adjusted to conform to the revised provisions of FASB ASC 260. The impact of the revised provisions had no effect for the year ended December 31, 2008.

Advertising expenses Advertising costs are generally expensed as incurred.

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Umpqua Holdings Corporation and Subsidiaries

Fair Value Measurements FASB ASC 820, *Fair Value Measurements and Disclosures,* defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. FASB ASC 820 establishes a three-level hierarchy for disclosure of assets and liabilities recorded at fair value. The classification of assets and liabilities within the hierarchy is based on whether the inputs to the valuation methodology used for measurement are observable or unobservable. Observable inputs reflect market-derived or market-based information obtained from independent sources, while unobservable inputs reflect our estimates about market data. In general, fair values determined by Level 1 inputs utilize quoted prices for identical assets or liabilities traded in active markets that the Company has the ability to access. Fair values determined by Level 2 inputs utilize inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly or indirectly. Level 2 inputs include quoted prices for similar assets and liabilities in active markets, and inputs other than quoted prices that are observable for the asset or liability, such as interest rates and yield curves that are observable at commonly quoted intervals. Level 3 inputs are unobservable inputs for the asset or liability, and include situations where there is little, if any, market activity for the asset or liability. In certain cases, the inputs used to measure fair value may fall into different levels of the fair value hierarchy. In such cases, the level in the fair value hierarchy within which the fair value measurement in its entirety falls has been determined based on the lowest level input that is significant to the fair value measurement in its entirety. The Company s assessment of the significance of a particular input to the fair value measurement in its entirety requires judgment, and considers factors specific to the asset or liability.

Recently Issued Accounting Pronouncements In December 2009, FASB issued ASU No. 2009-17, *Transfers and Servicing (Topic 860) Accounting for Transfers of Financial Assets.* This update codifed SFAS No. 166, *Accounting for Transfers of Financial Assets an Amendment of FASB Statement No. 140*, which was previously issued by FASB in June 2009 but was not included in the original codification. ASU 2009-17 eliminates the concept of a qualifying special-purpose entity, creates more stringent conditions for reporting a transfer of a portion of a financial asset as a sale, clarifies other sale-accounting criteria, and changes the initial measurement of a transferor s interest in transferred financial assets. This statement is effective for annual reporting periods beginning after November 15, 2009, and for interim periods therein. This standard will primarily impact the Company s accounting and reporting of transfers representing a portion of a financial asset for which the Company has a continuing involvement, generally known as loan participations. In order to recognize the transfer of a portion of a financial asset as a sale, the transferred portion and any portion that continues to be held by the transferor must represent a participating interest, and the transfer of the participating interest must meet the conditions for surrender of control. To qualify as a participating interest (i) the portions of a financial asset must represent a proportionate ownership interest in an entire financial asset, (ii) from the date of transfer, all cash flows received from the entire financial asset must be divided proportionately among the participating interest holders in an amount equal to their share of ownership, (iii) involve no recourse (other than standard representation and warranties) to, or subordination by, any participating interest holder, and (iv) no party has the right to pledge or exchange the entire financial asset. If the participating interest or surrender of control criteria are not met the transfer is not accounted for as a sale and derecognition of the asset is not appropriate. Rather the transaction is accounted for as a secured borrowing arrangement. The impact of certain participations being reported as secured borrowings rather than derecognizing a portion of a financial asset would increase total assets (loans), liabilities (term debt) and their respective interest income and expense. An increase in total assets also increases regulatory risk-weighted assets and could negatively impact our capital ratios. The Company reviews our participation agreements to ensure new originations meet the criteria to allow for sale accounting in order to limit the impact upon our financial statements. The terms contained in certain participation and loan sale agreements, however, are outside the control of the Company. These arrangements largely relate to Small Business Administration (SBA) loan sales. These sales agreements contain recourse provisions (generally 90 days) that will initially preclude sale accounting. However, once the recourse provision expires, transfers of portions of financial assets may be reevaluated to determine if they meet the participating interest definition. As a result, we expect to report SBA and potentially certain other transfers of financial assets as secured borrowings which will defer the gain of sale on these transactions, at least until the recourse provision expires, assuming all other sales criteria for each transaction are met. The Company does not believe it has or will have a significant amount of participations subject to recourse provisions or other features that would preclude derecognition of the assets transferred. The adoption of ASU No. 2009-17 did not materially impact the Company s consolidated financial statements.

In December 2009, FASB issued ASU No. 2009-18, *Consolidations (Topic 810) Improvements to Financial Reporting by Enterprises Involved with Variable Interest Entities.* This update codifed SFAS No. 167, *Amendments to FASB Interpretation No. 46(R)*, which was previously issued by FASB in June 2009 but was not included in the original codification. ASU 2009-18 eliminates FASB Interpretations 46(R) (FIN 46(R)) exceptions to consolidating qualifying special-purpose entities, contains new criteria for determining the primary beneficiary, and increases the frequency of required reassessments to determine whether a company is the primary beneficiary of a variable interest entity (VIE). Under the revised guidance, the primary beneficiary of a VIE (party who must consolidate the VIE) is the enterprise that has (i) the power to direct the activities of the VIE that most significantly impact the VIE s economic performance, and (ii) the obligation to absorb losses of the VIE that could potentially be significant to the VIE, or the right to receive benefits of the VIE that could potentially be significant to the VIE. ASU 2009-18 also contains a new requirement that any term, transaction, or arrangement that does not have a substantive effect on an entity s status as a variable interest entity, a company s power over a variable interest entity, or a company s obligation to absorb losses or its right to receive benefits of an entity must be disregarded in applying FIN 46(R) provisions. The elimination of the qualifying special-purpose entity concept and its consolidation exceptions means more entities will be subject to consolidation assessments and reassessments. This statement requires additional disclosures regarding an entity s involvement in a variable interest entity. This statement is effective for annual reporting periods beginning after November 15, 2009, and for interim periods therein. The Company has evaluated the impact of this guidance in regards to our involvement with variable interest entities. This guidance potentially impacts the accounting for our limited partnership equity investments in affordable housing development funds and real estate investment funds. In regards to affordable housing investments, the primary activities that most significantly impacts the VIE s economic performance include leasing rental units at appropriate rent rates in compliance with low income housing restrictions and requirements, operating the rental property thereby generating income/loss from the partnership operations, and protecting the low income housing tax credits from recapture. As a limited partner, the Company generally does not participate in the control of the partnerships business, our involvement is limited to providing a stated amount of financial support (commitment or subscription) as stated within contractual agreements, and the primary purpose of the investment is to receive the tax attributes (tax credits) of the partnership. The general partner, which generally are a developer or non-profit organization, exercise the day-to-day control and management of the partnerships that most significantly impacts the VIE s economic performance. In regards to the real estate investment funds, the primary activities that most significantly impacts the VIE s economic performance include the development, financing, and leasing of real estate related properties, and ultimately finding a profitable exit from such investments. The Company s involvement in these funds are a limited partners minority interest. According to the terms of the partnerships, the general partners have exclusive control to manage the enterprise and power to direct activities that impact the VIE s economic performance. The impact of adoption did not result in the Company consolidating or deconsolidating any variable interest entities as accounted for under previous guidance and, therefore, did not have a material impact on the Company s consolidated financial statements.

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

In February 2010, the FASB issued ASU No. 2010-09, *Subsequent Events (Topic 855) Amendments to Certain Recognition and disclosure Requirements.* This ASU eliminated the requirement for to disclose the date through which a Company has evaluated subsequent events and refines the scope of the disclosure requirements for reissued financial statements. This ASU was effective for the first quarter of 2010. This ASU did not have a material impact on the Company s consolidated financial statements.

In March 2010, the FASB issued ASU No. 2010-11, *Derivatives and Hedging (Topic 815) Scope Exception Related to Embedded Credit Derivatives*. The ASU eliminated the scope exception for bifurcation of embedded credit derivatives in interests in securitized financial assets, unless they are created solely by subordination of one financial instrument to another. The ASU was effective the first quarter beginning after June 15, 2010. The adoption of this ASU did not have a material impact on the Company s consolidated financial statements.

In April 2010, the FASB issued ASU No. 2010-18, *Receivables (Topic 310) Effect of a Loan Modification When the Loan Is Part of a Pool That is Accounted for as a Single Asset*. This ASU clarified that modifications of loans that are accounted for within a pool under Topic 310-30 do not result in the removal of those loans from the pool even if the modification of those loans would otherwise be considered a troubled debt restructuring. An entity will continue to be required to consider whether the pool of assets in which the loan is included is impaired if expected cash flows for the pool change. No additional disclosures are required with this ASU. The amendments in this ASU are effective for modifications of loans accounted for within pools under Topic 310-30 occurring in the first interim or annual period ending on or after July 15, 2010. The amendments are to be applied prospectively and early application is permitted. Upon initial adoption of the guidance in this ASU, an entity may make a onetime election to terminate accounting for loans as a pool under Topic 310-30. This election may be applied on a pool-by-pool basis and does not preclude an entity from applying pool accounting to subsequent acquisitions of loans with credit deterioration. The adoption of this ASU did not have a material impact on the Company s consolidated financial statements.

In July 2010, the FASB issued ASU No. 2010-20, *Receivables (Topic 310): Disclosures about the Credit Quality of Financing Receivables and the Allowance for Credit Losses.* The ASU expands existing disclosures to require an entity to provide additional information in their disclosures about the credit quality of their financing receivables and the credit reserves held against them. Specifically, entities will be required to present a roll forward of activity in the allowance for credit losses, the nonaccrual status of financing receivables by class of financing receivables, and impaired financing receivables by class of financing receivables, all on a disaggregated basis. The ASU also requires an entity to provide additional disclosures on credit quality indicators of financing receivables at the end of the reporting period by class of financing receivables, the aging of past due financing receivables at the end of the reporting period by class of financing receivables, the nature and extent of troubled debt restructurings that occurred during the period by class of financing receivables and their effect on the allowance for credit losses and significant purchases and sales of financing receivables during the reporting period disaggregated by portfolio segment. For public entities, the disclosures of period-end balances are effective for interim and annual reporting periods ending after December 15, 2010. For public entities, the disclosures of activity are effective for interim and annual reporting periods beginning on or after December 15, 2010. The adoption of this ASU did not have a material impact on the Company s consolidated financial statements.

In December 2010, the FASB issued ASU No. 2010-29, *Business Combinations (Topic 805): Disclosure of Supplementary Pro Forma Information for Business Combinations*. ASU No. 2010-29. This ASU requires that if a public entity discloses comparative financial statements, then those disclosures of revenue and earnings of the combined entity should be as though the business combination(s) that occurred during the current year had occurred as of the beginning of the comparable prior annual reporting period only. The ASU also expands the supplemental pro forma disclosures under Topic 805 to include a description of the nature and amount of material, nonrecurring pro forma adjustments directly attributable to the business combination. The ASU will be applied prospectively for business combinations that are consummated on or after the beginning of the first annual reporting period beginning on or after December 15, 2010. The adoption of this ASU will not have an impact on the Company s consolidated financial statements.

In December 2010, the FASB issued ASU No. 2010-28, *Intangibles Goodwill and Other (Topic 350): When to Perform Step 2 of the Goodwill Impairment Test for Reporting Units with Zero or Negative Carrying Amounts*. This ASU modifies Step 1 of the goodwill impairment test for reporting units with zero or negative carrying amounts. For those reporting units, an entity will be required to perform Step 2 of the goodwill impairment test if there are adverse qualitative factors that indicate that it is more likely than not that a goodwill impairment exists. The ASU is effective for fiscal years, and interim periods within those years, beginning after December 15, 2010, for public reporting entities. The adoption of this ASU will not have an impact on the Company s consolidated financial statements.

In January 2010, the FASB issued ASU No. No. 2011-01, *Deferral of the Effective Date of Disclosures about Troubled Debt Restructurings in Update No. 2010-20*. This ASU temporarily delays the effective date of the disclosures about troubled debt restructurings in Update 2010-20 for public entities. The delay is intended to allow the Board time to complete its deliberations on what constitutes a troubled debt restructuring. The effective date of the new disclosures about troubled debt restructurings for public entities and the guidance for determining what constitutes a troubled debt restructuring will then be coordinated. Currently, that guidance is anticipated to be effective for interim and annual periods ending after June 15, 2011. Accordingly, the Company has not included the disclosures deferred by this ASU.

Reclassifications Certain amounts reported in prior years financial statements have been reclassified to conform to the current presentation. The results of the reclassifications are not considered material and have no effect on previously reported net earnings (losses) available to common shareholders and earnings (losses) per common share.

NOTE 2. BUSINESS COMBINATIONS

On January 22, 2010, the Washington Department of Financial Institutions closed EvergreenBank (Evergreen), Seattle, Washington and appointed the Federal Deposit Insurance Corporation (FDIC) as receiver. That same date, Umpqua Bank assumed the banking operations of Evergreen from the FDIC under a whole bank purchase and assumption agreement with loss-sharing. Under the terms of the loss-sharing agreement, the FDIC will cover a substantial portion of any future losses on loans, related unfunded loan commitments, other real estate owned (OREO) and accrued interest on loans for up to 90 days. The FDIC will absorb 80% of losses and share in 80% of loss recoveries on the first $90.0 million on covered assets for Evergreen and absorb 95% of losses and share in 95% of loss recoveries exceeding $90.0 million, except the Bank will incur losses up to $30.2 million before the loss-sharing will commence. The loss-sharing arrangements for non-single family residential and single family residential loans are in effect for 5 years and 10 years, respectively, and the loss recovery provisions are in effect for 8 years and 10 years, respectively, from the acquisition date. With this agreement, Umpqua Bank assumed six additional store locations in the greater Seattle, Washington market. This acquisition is consistent with our community banking expansion strategy and provides further opportunity to fill in our market presence in the greater Seattle, Washington market.

On February 26, 2010, the Washington Department of Financial Institutions closed Rainier Pacific Bank (Rainier), Tacoma, Washington and appointed the FDIC as receiver. That same date, Umpqua Bank assumed the banking operations of Rainier from the FDIC under a whole bank purchase and assumption agreement with loss-sharing. Under the terms of the loss-sharing agreement, the FDIC will cover a substantial portion of any future losses on loans, related unfunded loan commitments, OREO and accrued interest on loans for up to 90 days. The FDIC will absorb 80% of losses and share in 80% of loss recoveries on the first $95.0 million of losses on covered assets and absorb 95% of losses and share in 95% of loss recoveries exceeding $95.0 million. The loss-sharing arrangements for non-single family residential and single family residential loans are in effect for 5 years and 10 years, respectively, and the loss recovery provisions are in effect for 8 years and 10 years, respectively, from the acquisition dates. With this agreement, Umpqua Bank assumed 14 additional store locations in Pierce County and surrounding areas. This acquisition expands our presence in the south Puget Sound region of Washington State.

The operations of Evergreen and Rainier are included in our operating results from January 23, 2010 and February 27, 2010, respectively, and added combined revenue of $54.0 million, non-interest expense of $23.6 million, and earnings of $11.0 million, net of tax, for the year ended December 31, 2010. These operating results include a bargain purchase gain of $6.4 million, which is not indicative of future operating results. Evergreen s and Rainiers s results of operations prior to the acquisition are not included in our operating results. Merger-related expenses of $4.4 million for the year ended December 31, 2010 have been incurred in connection with these acquisitions and recognized in a separate line item on the *Condensed Consolidated Statements of Operations*.

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On June 18, 2010, the Nevada State Financial Institutions Division closed Nevada Security Bank (Nevada Security), Reno, Nevada and appointed the FDIC as receiver. That same date, Umpqua Bank assumed the banking operations of Nevada Security from the FDIC under a whole bank purchase and assumption agreement with loss-sharing. Under the terms of the loss-sharing agreement, the FDIC will cover a substantial portion of any future losses on loans, related unfunded loan commitments, OREO, and accrued interest on loans for up to 90 days. The FDIC will absorb 80% of losses and share in 80% of loss recoveries on all covered assets. The loss-sharing arrangements for non-single family residential and single family residential loans are in effect for 5 years and 10 years, respectively, and the loss recovery provisions are in effect for 8 years and 10 years, respectively, from the acquisition dates. With this agreement, Umpqua Bank assumed five additional store locations, including three in Reno, Nevada, one in Incline Village, Nevada, and one in Roseville, California. This acquisition expands our presence into the State of Nevada.

The operations of Nevada Security are included in our operating results from June 19, 2010, and added revenue of $15.1 million, non-interest expense of $7.3 million, and earnings of $1.3 million, net of tax, for the year ended December 31, 2010. Nevada Security s results of operations prior to the acquisition are not included in our operating results. Merger-related expenses of $1.7 million for the year ended December 31, 2010 have been incurred in connection with the acquisition of Nevada Security and recognized as a separate line item on the *Condensed Consolidated Statements of Operations*.

We refer to the acquired loan portfolios and other real estate owned as covered loans and covered other real estate owned , respectively, and these are presented as separate line items in our consolidated balance sheet. Collectively these balances are referred to as covered assets .

The assets acquired and liabilities assumed from the Evergreen, Rainier, and Nevada Security acquisitions have been accounted for under the acquisition method of accounting. The assets and liabilities, both tangible and intangible, were recorded at their estimated fair values as of the acquisition dates. The fair values of the assets acquired and liabilities assumed were determined based on the requirements of the Fair Value Measurements and Disclosures topic of the Financial Accounting Standards Board Accounting Standards Codification (the FASB ASC). The fair values of assets and liabilities acquired, including the calculation of the undiscounted contractual cash flows and beginning accretable yield relating to the acquired loan portfolios, and the indemnification asset are still pending finalization and are subject to change for up to one year after the closing date of each acquisition, as additional information relating to closing data becomes available. The amounts are also subject to adjustments based upon final settlement with the FDIC. In addition, the tax treatment of FDIC-assisted acquisitions is complex and subject to interpretations that may result in future adjustments of deferred taxes as of the acquisition date. The terms of the agreements provide for the FDIC to indemnify the Bank against claims with respect to liabilities of Evergreen, Rainier, and Nevada Security not assumed by the Bank and certain other types of claims identified in the agreement. The application of the acquisition method of accounting resulted in the recognition of a bargain purchase gain of $6.4 million in the Evergreen acquisition, $35.6 million of goodwill in the Rainier acquisition and $10.4 million of goodwill in the Nevada Security acquisition.

A summary of the net assets (liabilities) received from the FDIC and the estimated fair value adjustments are presented below:

(in thousands)

	Evergreen January 22, 2010	Rainier February 26, 2010	Nevada Security June 18, 2010
Cost basis net assets (liabilities)	$ 58,811	$ (50,295)	$ 53,629
Cash payment received from (paid to) the FDIC		59,351	(29,950)
Fair value adjustments:			
Loans	(117,449)	(103,137)	(112,975)
Other real estate owned	(2,422)	(6,581)	(17,939)
Other intangible assets	440	6,253	322
FDIC indemnification asset	71,755	76,847	99,160
Deposits	(1,023)	(1,828)	(1,950)
Term debt	(2,496)	(13,035)	
Other	(1,179)	(3,135)	(690)
Bargain purchase gain (goodwill)	$ 6,437	$ (35,560)	$ (10,393)

In FDIC-assisted transactions, only certain assets and liabilities are transferred to the acquirer and, depending on the nature and amount of the acquirer s bid, the FDIC may be required to make a cash payment to the acquirer or the acquirer may be required to make payment to the FDIC.

In the Evergreen acquisition, cost basis net assets of $58.8 million were transferred to the Company. The bargain purchase gain represents the excess of the estimated fair value of the assets acquired over the estimated fair value of the liabilities assumed. Core deposit intangible assets of $250,000 recognized are deductible for income tax purposes.

In the Rainier acquisition, cost basis net liabilities of $50.3 million and a cash payment received from the FDIC of $59.4 million were transferred to the Company. The goodwill represents the excess of the estimated fair value of the liabilities assumed over the estimated fair value of the assets acquired. Goodwill of $27.5 million and core deposit intangible assets of $1.1 million recognized are deductible for income tax purposes.

In the Nevada Security acquisition, cost basis net assets of $53.6 million were transferred to the Company and a cash payment of $30.0 million was made to the FDIC. The goodwill represents the excess of the estimated fair value of the liabilities assumed over the estimated fair value of the assets acquired. Goodwill of $10.4 million and core deposit intangible assets of $322,000 recognized are deductible for income tax purposes.

The Bank did not immediately acquire all the real estate, banking facilities, furniture or equipment of Evergreen, Rainier, or Nevada Security as part of the purchase and assumption agreements. Rather, the Bank was granted the option to purchase or lease the real estate and furniture and equipment from the FDIC. The term of this option expired 90 days from the acquisition dates, unless extended by the FDIC. Acquisition costs of the real estate and furniture and equipment are based on current mutually agreed upon appraisals. Prior to the expiration of option term, Umpqua exercised the right to purchase approximately $344,000 of furniture and equipment for Evergreen, $26.3 million of real estate and furniture and equipment for Rainier, and $153,000 of furniture and equipment for Nevada Security. The Bank has the option to purchase one store location as part of the Nevada Security acquisition and expects resolution in the first quarter of 2011.

The statement of assets acquired and liabilities assumed at their estimated fair values of Evergreen, Rainier, and Nevada Security are presented below:

(in thousands)

	Evergreen January 22, 2010	Rainier February 26, 2010	Nevada Security June 18, 2010
Assets Acquired:			
Cash and equivalents	$ 18,919	$ 94,067	$ 66,060
Investment securities	3,850	26,478	22,626
Covered loans	252,493	458,340	215,507
Premises and equipment		17	50
Restricted equity securities	3,073	13,712	2,951
Goodwill		35,560	10,393
Other intangible assets	440	6,253	322
Mortgage servicing rights		62	
Covered other real estate owned	2,421	6,580	17,938
FDIC indemnification asset	71,755	76,847	99,160
Other assets	328	3,258	2,588
Total assets acquired	$ 353,279	$ 721,174	$ 437,595
Liabilities Assumed:			
Deposits	$ 285,775	$ 425,771	$ 437,299
Term debt	60,813	293,191	
Other liabilities	254	2,212	296
Total liabilities assumed	346,842	721,174	437,595
Net assets acquired/bargain purchase gain	$ 6,437	$	$

Rainier s assets and liabilities were significant at a level to require disclosure of one year of historical financial statements and related pro forma financial disclosure. However, given the pervasive nature of the loss-sharing agreement entered into with the FDIC, the historical information of Rainier is much less relevant for purposes of assessing the future operations of the combined entity. In addition, prior to closure Rainier had not completed an audit of their financial statements, and we determined that audited financial statements were not and would not be reasonably available for the year ended December 31, 2009. Given these considerations, the Company requested, and received, relief from the Securities and Exchange Commission from submitting certain financial information of Rainier. The assets and liabilities of Evergreen and Nevada Security were not at a level that requires disclosure of historical or pro forma financial information.

On January 16, 2009, the Washington Department of Financial Institutions closed the Bank of Clark County, Vancouver, Washington, and appointed the FDIC as its receiver. The FDIC entered into a purchase and assumption agreement with Umpqua Bank to assume the insured non-brokered deposit balances, which totaled $183.9 million, at no premium. The Company recorded the deposit related liabilities at book value. In connection with the assumption, Umpqua Bank acquired certain assets totaling $23.0 million, primarily cash and marketable securities, with the difference of $160.9 million representing funds received directly from the FDIC. Through this agreement, Umpqua Bank now operates two additional store locations in Vancouver, Washington. In addition, the FDIC reimbursed Umpqua Bank for all overhead costs related to the acquired Bank of Clark County operations for 90 days following closing, while Umpqua Bank paid the FDIC a servicing fee on assumed deposit accounts for that same period.

The results of the Bank of Clark County s operations have been included in the consolidated financial statements beginning January 17, 2009 and contributed net earnings of approximately $2.0 million and $1.6 million for the years ended December 31, 2010 and 2009, net of tax, respectively, which primarily represents interest income earned from the proceeds of the assumption which were invested in investment securities available for sale and service income on deposits. This was partially offset by interest expense on deposits, salaries and employee benefits expense, and the accrued servicing fee paid to the FDIC. Umpqua did not incur the FDIC servicing fee expense during the second or third quarter of 2009, but began incurring overhead expenses such as salaries and employee benefits expense and rent expense.

The Company incurs significant expenses related to mergers that cannot be capitalized. Generally, these expenses begin to be recognized while due diligence is being conducted and continue until such time as all systems have been converted and operational functions become fully integrated. Merger-related expenses are presented as a line item on the *Consolidated Statements of Operations*.

The following table presents the key components of merger-related expense for years ended December 31, 2010 and 2009. The Company incurred no merger-related expenses in 2008. Substantially all of the merger-related expenses incurred during 2010 were in connection with the FDIC-assisted purchase and assumption of Evergreen, Rainier, and Nevada Security. Substantially all of the merger-related expenses incurred during 2009 were in connection with the FDIC-assisted purchase and assumption of certain assets and liabilities of the Bank of Clark County.

Merger-Related Expense

(in thousands)

	2010	2009
Professional fees	$ 2,984	$ 143
Compensation and relocation	962	39
Communications	330	61
Premises and equipment	630	2
Travel	710	
Other	1,059	28
Total	$ 6,675	$ 273

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No additional merger-related expenses are expected in connection with the FDIC-assisted purchase and assumption of certain assets and liabilities of the Bank of Clark County or any other prior acquisitions, however additional merger-related expense may be recorded related to the Evergreen, Rainier, and Nevada Securities assumptions.

NOTE 3. CASH AND DUE FROM BANKS

The Bank is required to maintain an average reserve balance with the Federal Reserve Bank or maintain such reserve balance in the form of cash. The amount of required reserve balance at December 31, 2010 and 2009 was approximately $31.8 million and $58.6 million, respectively, and was met by holding cash and maintaining an average balance with the Federal Reserve Bank.

NOTE 4. INVESTMENT SECURITIES

The following table presents the amortized costs, unrealized gains, unrealized losses and approximate fair values of investment securities at December 31, 2010 and 2009:

December 31, 2010

(in thousands)

	Amortized Cost	Unrealized Gains	Unrealized Losses	Fair Value
AVAILABLE FOR SALE:				
U.S. Treasury and agencies	$ 117,551	$ 1,239	$ (1)	$ 118,789
Obligations of states and political subdivisions	213,129	4,985	(1,388)	216,726
Residential mortgage-backed securities and collateralized mortgage obligations	2,543,974	57,506	(19,976)	2,581,504
Other debt securities	152			152
Investments in mutual funds and other equity securities	1,959	50		2,009
	$ 2,876,765	$ 63,780	$ (21,365)	$ 2,919,180
HELD TO MATURITY:				
Obligations of states and political subdivisions	$ 2,370	$ 5	$	$ 2,375
Residential mortgage-backed securities and collateralized mortgage obligations	2,392	216	(209)	2,399
	$ 4,762	$ 221	$ (209)	$ 4,774

December 31, 2009

(in thousands)

	Amortized Cost	Unrealized Gains	Unrealized Losses	Fair Value
AVAILABLE FOR SALE:				
U.S. Treasury and agencies	$ 11,588	$ 208	$ (2)	$ 11,794
Obligations of states and political subdivisions	205,549	6,480	(204)	211,825
Residential mortgage-backed securities and collateralized mortgage obligations	1,533,149	40,272	(3,572)	1,569,849
Other debt securities	145	14		159
Investments in mutual funds and other equity securities	1,959	30		1,989
	$ 1,752,390	$ 47,004	$ (3,778)	$ 1,795,616
HELD TO MATURITY:				
Obligations of states and political subdivisions	$ 3,216	$ 11	$	$ 3,227
Residential mortgage-backed securities and collateralized mortgage obligations	2,845	251	(187)	2,909

	$	6,061	$	262	$	(187)	$	6,136

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Umpqua Holdings Corporation and Subsidiaries

Investment securities that were in an unrealized loss position as of December 31, 2010 and 2009 are presented in the following tables, based on the length of time individual securities have been in an unrealized loss position. In the opinion of management, these securities are considered only temporarily impaired due to changes in market interest rates or the widening of market spreads subsequent to the initial purchase of the securities, and not due to concerns regarding the underlying credit of the issuers or the underlying collateral:

December 31, 2010

(in thousands)

	Less than 12 Months		12 Months or Longer		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
AVAILABLE FOR SALE:						
U.S. Treasury and agencies	$	$	$ 110	$ 1	$ 110	$ 1
Obligations of states and political subdivisions	60,110	1,366	1,003	22	61,113	1,388
Residential mortgage-backed securities and collateralized mortgage obligations	1,238,483	19,968	1,539	8	1,240,022	19,976
Total temporarily impaired securities	$ 1,298,593	$ 21,334	$ 2,652	$ 31	$ 1,301,245	$ 21,365
HELD TO MATURITY:						
Residential mortgage-backed securities and collateralized mortgage obligations	$	$	$ 658	$ 209	$ 658	$ 209
Total temporarily impaired securities	$	$	$ 658	$ 209	$ 658	$ 209

December 31, 2009

(in thousands)

	Less than 12 Months		12 Months or Longer		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
AVAILABLE FOR SALE:						
U.S. Treasury and agencies	$	$	$ 133	$ 2	$ 133	$ 2
Obligations of states and political subdivisions	13,209	123	1,937	81	15,146	204
Residential mortgage-backed securities and collateralized mortgage obligations	293,035	3,529	958	43	293,993	3,572
Total temporarily impaired securities	$ 306,244	$ 3,652	$ 3,028	$ 126	$ 309,272	$ 3,778
HELD TO MATURITY:						
Residential mortgage-backed securities and collateralized mortgage obligations	$	$	$ 620	$ 187	$ 620	$ 187
Total temporarily impaired securities	$	$	$ 620	$ 187	$ 620	$ 187

The unrealized losses on investments in U.S. Treasury and agencies securities were caused by interest rate increases subsequent to the purchase of these securities. The contractual terms of these investments do not permit the issuer to settle the securities at a price less than par. Because the Bank does not intend to sell the securities in this class and it is not likely that the Bank will be required to sell these securities before recovery of their amortized cost bases, which may include holding each security until contractual maturity, the unrealized losses on these investments are not considered other-than-temporarily impaired.

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The unrealized losses on obligations of political subdivisions were caused by changes in market interest rates or the widening of market spreads subsequent to the initial purchase of these securities. Management monitors published credit ratings of these securities and no adverse ratings changes have occurred since the date of purchase of obligations of political subdivisions which are in an unrealized loss position as of December 31, 2010. Because the decline in fair value is attributable to changes in interest rates or widening market spreads and not credit quality, and because the Bank does not intend to sell the securities in this class and it is not likely that Bank will be required to sell these securities before recovery of their amortized cost bases, which may include holding each security until maturity, the unrealized losses on these investments are not considered other-than-temporarily impaired.

All of the available for sale residential mortgage-backed securities and collateralized mortgage obligations portfolio in an unrealized loss position at December 31, 2010 are issued or guaranteed by governmental agencies. The unrealized losses on residential mortgage-backed securities and collateralized mortgage obligations were caused by changes in market interest rates or the widening of market spreads subsequent to the initial purchase of these securities, and not concerns regarding the underlying credit of the issuers or the underlying collateral. It is expected that these securities will not be settled at a price less than the amortized cost of each investment. Because the decline in fair value is attributable to changes in interest rates or widening market spreads and not credit quality, and because the Bank does not intend to sell the securities in this class and it is not likely that the Bank will be required to sell these securities before recovery of their amortized cost bases, which may include holding each security until contractual maturity, the unrealized losses on these investments are not considered other-than-temporarily impaired.

We review investment securities on an ongoing basis for the presence of other-than-temporary impairment (OTTI) or permanent impairment, taking into consideration current market conditions, fair value in relationship to cost, extent and nature of the decline in fair value, issuer rating changes and trends, whether we intend to sell a security or if it is likely that we will be required to sell the security before recovery of our amortized cost basis of the investment, which may be maturity, and other factors. For debt securities, if we intend to sell the security or it is likely that we will be required to sell the security before recovering its cost basis, the entire impairment loss would be recognized in earnings as an OTTI. If we do not intend to sell the security and it is not likely that we will be required to sell the security but we do not expect to recover the entire amortized cost basis of the security, only the portion of the impairment loss representing credit losses would be recognized in earnings. The credit loss on a security is measured as the difference between the amortized cost basis and the present value of the cash flows expected to be collected. Projected cash flows are discounted by the original or current effective interest rate depending on the nature of the security being measured for potential OTTI. The remaining impairment related to all other factors, the difference between the present value of the cash flows expected to be collected and fair value, is recognized as a charge to other comprehensive income (OCI). Impairment losses related to all other factors are presented as separate categories within OCI. For investment securities held to maturity, this amount is accreted over the remaining life of the debt security prospectively based on the amount and timing of future estimated cash flows. The accretion of the OTTI amount recorded in OCI will increase the carrying value of the investment, and would not affect earnings. If there is an indication of additional credit losses, the security is re-evaluated accordingly to the procedures described above.

The following tables present the OTTI losses for the years ended December 31, 2010, 2009 and 2008.

(in thousands)

	2010		2009		2008	
	Held To Maturity	Available For Sale	Held To Maturity	Available For Sale	Held To Maturity	Available For Sale
Total other-than-temporary impairment losses	$ 93	$	$ 12,317	$ 239	$ 4,041	$ 139
Portion of other-than-temporary impairment losses transferred from (recognized in) other comprehensive income(1)	321		(1,983)			
Net impairment losses recognized in earnings(2)	$ 414	$	$ 10,334	$ 239	$ 4,041	$ 139

(1) Represents other-than-temporary impairment losses related to all other factors.
(2) Represents other-than-temporary impairment losses related to credit losses.

New guidance related to the recognition and presentation of OTTI of debt securities became effective beginning in the second quarter of 2009. Rather than asserting whether a Company has the ability and intent to hold an investment until a market price recovery, a Company must consider whether they intend to sell a security or if it is likely that they would be required to sell the security before recovery of the amortized cost basis of the investment, which may be maturity. The $8.2 million in OTTI recognized on investment securities held to maturity subsequent to March 31, 2009 primarily relates to 29 non-agency residential collateralized mortgage obligations. Each of these securities holds various levels of credit subordination. The underlying mortgage loans of these securities were originated from 2003 through 2007. At origination, the weighted average loan-to-value of the underlying mortgages was 69%; the underlying borrowers had weighted average FICO scores of 731, and 59% were limited documentation loans. These securities are valued by third-party pricing services using matrix or model pricing methodologies and were corroborated by broker indicative bids. We estimate cash flows of the underlying collateral for each security considering credit, interest and prepayment risk models that incorporate management s estimate of projected key assumptions including prepayment rates, collateral default rates and loss severity. Assumptions utilized vary from security to security, and are influenced by factors such as loan interest rates, geographic location, borrower characteristics and vintage, and historical experience. We then used a third party to obtain information about the structure of each security, including subordination and other credit enhancements, in order to determine how the underlying collateral cash flows will be distributed to each security issued in the structure. These cash flows are then discounted at the interest rate used to recognize interest income on each security. We review the actual collateral performance of these securities on a quarterly basis and update the inputs as appropriate to determine the projected cash flows. The following table presents a summary of the significant inputs utilized to measure management s estimate of the credit loss component on these non-agency residential collateralized mortgage obligations as of December 31, 2010 and 2009:

	2010			2009		
	Range		Weighted	Range		Weighted
	Minimum	Maximum	Average	Minimum	Maximum	Average
Constant prepayment rate	5.0%	20.0%	14.9%	4.0%	25.0%	14.8%
Collateral default rate	5.0%	15.0%	10.6%	8.0%	45.0%	16.7%
Loss severity	25.0%	55.0%	37.9%	20.0%	40.0%	31.4%

In the second quarter of 2009 the Company recorded an OTTI charge of $239,000 related to an available for sale collateralized debt obligation that holds trust preferred securities. Management noted certain deferrals and defaults in the pool and believes the impairment represents credit loss in its entirety. Through December 31, 2010, no further OTTI charges have been recorded on available for sale securities.

The following table presents a roll forward of the credit loss component of held to maturity debt securities that have been written down for OTTI with the credit loss component recognized in earnings and the remaining impairment loss related to all other factors recognized in OCI for the years ended December 31, 2010 and 2009, respectively, since the adoption of the revised guidance related to the recognition and presentation of OTTI of debt securities:

(in thousands)

	2010	2009
Balance, beginning of period	$ 12,364	$
Cumulative OTTI credit losses upon adoption of new OTTI guidance		5,952
Additions:		
Initial OTTI credit losses		7,211
Subsequent OTTI credit losses	414	986
Reductions:		
Securities sold, matured or paid-off		(1,785)
Balance, end of period	$ 12,778	$ 12,364

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Prior to the Company s adoption of the new guidance related to the recognition and presentation of OTTI of debt securities which became effective in the second quarter of 2009, the Company would assess an OTTI or permanent impairment based on the nature of the decline and whether the Company had the ability and intent to hold the investments until a market price recovery. In the three months ended March 31, 2009, the Company recorded a $2.1 million OTTI charge. This charge related to three non-agency residential collateralized mortgage obligations carried as held to maturity for which the default rates and loss severities of the underlying collateral and credit coverage ratios of the security indicated that it was probable that credit losses were expected to occur. In 2008, the Company recorded $4.2 million in OTTI. Charges of $3.8 million related to seven non-agency residential collateralized mortgage obligations carried as held to maturity for which the default rates and loss severities of the underlying collateral and credit coverage ratios of the security indicated that it was probable that credit losses were expected to occur. These securities were valued by third party pricing services using matrix or model pricing methodologies, and were corroborated by broker indicative bids. The remaining non-agency securities within residential mortgage-backed securities and collateralized mortgage obligations carried as held to maturity were specifically evaluated for OTTI, and the default rates and loss severities of the underlying collateral indicated that credit losses are not expected to occur. Upon adoption of the new OTTI guidance in the second quarter of 2009, the Company analyzed these securities as well as other securities where OTTI had been previously recognized, and determined that as of the adoption date such losses were credit related. As such, there was no cumulative effect adjustment to the opening balance of retained earnings or a corresponding adjustment to accumulated OCI.

In addition, during 2008 the Company recorded an OTTI charge of $139,000 related to a collateralized debt obligation that holds trust preferred securities in investments available for sale where default and deferrals on the underlying debt indicate credit losses are expected to occur within the security. An additional $225,000 charge was recognized during 2008 for preferred stock carried as an investment held to maturity.

The following table presents the maturities of investment securities at December 31, 2010:

(in thousands)

	Available For Sale		Held To Maturity	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
AMOUNTS MATURING IN:				
Three months or less	$ 5,939	$ 5,959	$ 340	$ 341
Over three months through twelve months	326,696	337,305	1,485	1,488
After one year through five years	2,168,213	2,203,498	581	586
After five years through ten years	305,940	303,540	92	95
After ten years	68,018	66,869	2,264	2,264
Other investment securities	1,959	2,009		
	$ 2,876,765	$ 2,919,180	$ 4,762	$ 4,774

The amortized cost and fair value of collateralized mortgage obligations and mortgage-backed securities are presented by expected average life, rather than contractual maturity, in the preceding table. Expected maturities may differ from contractual maturities because borrowers have the right to prepay underlying loans without prepayment penalties.

Umpqua Holdings Corporation and Subsidiaries

The following table presents the gross realized gains and gross realized losses on the sale of securities available for sale for the years ended December 31, 2010, 2009 and 2008:

(in thousands)

	2010		2009		2008	
	Gains	Losses	Gains	Losses	Gains	Losses
U.S. Treasury and agencies	$	$ 1	$	$	$ 522	$
Obligations of states and political subdivisions	3	7		1	6	
Residential mortgage-backed securities and collateralized mortgage obligations	2,331		9,409	591	6,681	145
Investments in mutual funds and other equity securities						1,535
	$ 2,334	$ 8	$ 9,409	$ 592	$ 7,209	$ 1,680

The following table presents, as of December 31, 2010, investment securities which were pledged to secure borrowings and public deposits as permitted or required by law:

(in thousands)

	Amortized Cost	Fair Value
To Federal Home Loan Bank to secure borrowings	$ 290,983	$ 307,348
To state and local governments to secure public deposits	861,472	888,565
To U.S. Treasury and Federal Reserve to secure customer tax payments	4,879	5,148
Other securities pledged, principally to secure deposits	261,807	269,448
Total pledged securities	$ 1,419,141	$ 1,470,509

The carrying value of investment securities pledged as of December 31, 2009 was $1.5 billion.

NOTE 5. NON-COVERED LOANS AND LEASES

The following table presents the major types of non-covered loans recorded in the balance sheets as of December 31, 2010 and 2009:

(in thousands)

	2010	2009
Commercial real estate		
Term & multifamily	$ 3,483,475	$ 3,523,104
Construction & development	247,814	366,680
Residential development	147,813	225,809
Commercial		
Term	509,453	585,856
LOC & other	747,419	804,635
Residential		
Mortgage	222,416	182,757
Home equity loans & lines	278,585	285,729
Consumer & other	33,043	36,098

Total	5,670,018	6,010,668
Deferred loan fees, net	(11,031)	(11,401)
Total	$ 5,658,987	$ 5,999,267

As of December 31, 2010, loans totaling $3.0 billion were pledged to secure borrowings and available lines of credit.

NOTE 6. ALLOWANCE FOR NON-COVERED LOAN LOSS AND CREDIT QUALITY

The Bank has a management Allowance for Loan and Lease Losses (ALLL) Committee, which is responsible for, among other things, regularly reviewing the ALLL methodology, including loss factors, and ensuring that it is designed and applied in accordance with generally accepted accounting principles. The ALLL Committee reviews and approves loans and leases recommended for impaired status. The ALLL Committee also approves removing loans and leases from impaired status. The Bank s Audit and Compliance Committee provides board oversight of the ALLL process and reviews and approves the ALLL methodology on a quarterly basis.

Our methodology for assessing the appropriateness of the ALLL consists of three key elements, which include 1) the Formula Allowance; 2) the Specific Allowance; and 3) the Unallocated Allowance. By incorporating these factors into a single allowance requirement analysis, all risk-based activities within the loan portfolio are simultaneously considered.

Formula Allowance

The Bank performs regular credit reviews of the loan and lease portfolio to determine the credit quality and adherence to underwriting standards. When loans and leases are originated, they are assigned a risk rating that is reassessed periodically during the term of the loan through the credit review process. The Company s risk rating methodology assigns risk ratings ranging from 1 to 10, where a higher rating represents higher risk. The 10 risk rating categories are a primary factor in determining an appropriate amount for the Formula allowance for loan and lease losses.

The Formula Allowance is calculated by applying risk factors to various segments of pools of outstanding loans. Risk factors are assigned to each portfolio segment based on management s evaluation of the losses inherent within each segment. Segments or regions with greater risk of loss will therefore be assigned a higher risk factor.

Base risk The portfolio is segmented into loan categories, and these categories are assigned a Base Risk factor based on an evaluation of the loss inherent within each segment.

Extra risk Additional risk factors provide for an additional allocation of ALLL based on the loan risk rating system and loan delinquency, and reflect the increased level of inherent losses associated with more adversely classified loans.

Changes to risk factors Risk factors may be changed periodically based on management s evaluation of the following factors: loss experience; changes in the level of non-performing loans; regulatory exam results; changes in the level of adversely classified loans (positive or negative); improvement or deterioration in local economic conditions; and any other factors deemed relevant.

Specific Allowance

Regular credit reviews of the portfolio also identify loans that are considered potentially impaired. Potentially impaired loans are referred to the ALLL Committee which reviews and approves designated loans as impaired. A loan is considered impaired when based on current information and events, we determine that we will probably not be able to collect all amounts due according to the loan contract, including scheduled interest payments. When we identify a loan as impaired, we measure the impairment using discounted cash flows, except when the sole remaining source of the repayment for the loan is the liquidation of the collateral. In these cases, we use the current fair value of the collateral, less selling costs, instead of discounted cash flows. If we determine that the value of the impaired loan is less than the recorded investment in the loan, we either recognize an impairment reserve as a Specific Allowance to be provided for in the allowance for loan and lease losses or charge-off the impaired balance on collateral dependent loans if it is determined that such amount represents a confirmed loss. Loans determined to be impaired with a specific allowance are excluded from the formula allowance so as not to double-count the loss exposure. Prior to the second quarter of 2008, we would recognize the charge-off of the impairment reserve of a collateral depending non-accrual loan when the loan was resolved, sold, or foreclosed/transferred to OREO. Starting in the second quarter of 2008, we accelerated the charge-off of the impairment reserve to the period in which it arises. Therefore the non-accrual impaired loans as of period end have already been partially charge off to their estimated net realizable value, and are expected to be resolved over the coming quarters with no additional loss, absent further decline in market prices.

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The combination of the Formula allowance component and the Specific allowance component lead to an allocated allowance for loan and lease losses.

Unallocated Allowance

The Bank may also maintain an unallocated allowance amount to provide for other credit losses inherent in a loan and lease portfolio that may not have been contemplated in the credit loss factors. This unallocated amount generally comprises less than 10% of the allowance, but may be maintained at higher levels during times of deteriorating economic conditions characterized by falling real estate values. The unallocated amount is reviewed quarterly with consideration of factors including, but not limited to:

Changes in lending policies and procedures, including changes in underwriting standards and collection, charge-off, and recovery practices not considered elsewhere in estimating credit losses;

Changes in international, national, regional, and local economic and business conditions and developments that affect the collectability of the portfolio, including the condition of various market segments;

Changes in the nature and volume of the portfolio and in the terms of loans;

Changes in the experience and ability of lending management and other relevant staff;

Changes in the volume and severity of past due loans, the volume of nonaccrual loans, and the volume and severity of adversely classified or graded loans;

Changes in the quality of the institution s loan review system;

Changes in the value of underlying collateral for collateral-depending loans;

The existence and effect of any concentrations of credit, and changes in the level of such concentrations;

The effect of other external factors such as competition and legal and regulatory requirements on the level of estimated credit losses in the institutions existing portfolio.

These factors are evaluated through a management survey of the Chief Credit Officer, Chief Lending Officers, Special Asset Manager, and Credit Review Manager. The survey requests responses to evaluate current changes in the nine qualitative factors. This information is then incorporated into our understanding of the reasonableness of the formula factors and our evaluation of the unallocated portion of the ALLL.

The reserve for unfunded commitments (RUC) is established to absorb inherent losses associated with our commitment to lend funds, such as with a letter or line of credit. The adequacy of the ALLL and RUC are monitored on a regular basis and are based on management s evaluation of numerous factors. For each portfolio segment, these factors include:

The quality of the current loan portfolio;

The trend in the loan portfolio s risk ratings;

Current economic conditions;

Loan concentrations;

Loan growth rates;

Past-due and non-performing trends;

Evaluation of specific loss estimates for all significant problem loans;

Historical short (one year), medium (three year), and long-term charge-off rates,

Recovery experience;

Peer comparison loss rates.

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There have been no significant changes to the Bank s methodology or policies in the periods presented.

Management believes that the ALLL was adequate as of December 31, 2010. There is, however, no assurance that future loan losses will not exceed the levels provided for in the ALLL and could possibly result in additional charges to the provision for loan and lease losses. In addition, bank regulatory authorities, as part of their periodic examination of the Bank, may require additional charges to the provision for loan and lease losses in future periods if warranted as a result of their review. Approximately 82% of our loan portfolio is secured by real estate, and a significant decline in real estate market values may require an increase in the allowance for loan and lease losses. The U.S. recession, the housing market downturn, and declining real estate values in our markets have negatively impacted aspects of our residential development, commercial real estate, commercial construction and commercial loan portfolios. A continued deterioration in our markets may adversely affect our loan portfolio and may lead to additional charges to the provision for loan and lease losses.

Activity in the Non-Covered Allowance for Loan and Lease Losses

The following table summarizes activity related to the allowance for non-covered loan and lease losses by non-covered loan portfolio segment for the years ended December 31, 2010 and 2009:

(in thousands)

						December 31, 2010
	Commercial Real Estate	Commercial	Residential	Consumer & Other	Unallocated	Total
Allowance:						
Balance at beginning of year:	$ 67,281	$ 24,583	$ 5,811	$ 455	$ 9,527	$ 107,657
Charge-offs	(71,030)	(50,242)	(5,168)	(2,061)		(128,501)
Recoveries	6,980	1,318	334	465		9,097
Provision	61,174	46,487	4,949	1,944	(886)	113,668
Ending balance	$ 64,405	$ 22,146	$ 5,926	$ 803	$ 8,641	$ 101,921
Ending balance: individually evaluated for impairment	$ 2,520	$ 2,711	$ 8	$		$ 5,239
Non-covered Loans and leases:						
Ending balance(1)	$ 3,879,102	$ 1,256,872	$ 501,001	$ 33,043		$ 5,670,018
Ending balance: individually evaluated for impairment	$ 186,933	$ 35,507	$ 179	$		$ 222,619

(1) The gross non-covered loan and lease balance excludes deferred loans fees of $11.0 million for the year ended December 31, 2010.

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	December 31, 2009					
	Commercial Real Estate	Commercial	Residential	Consumer & Other	Unallocated	Total
Allowance:						
Balance at beginning of year:	$ 57,907	$ 23,104	$ 5,778	$ 484	$ 8,592	$ 95,865
Charge-offs	(136,382)	(57,932)	(4,331)	(2,222)		(200,867)
Recoveries	1,334	1,549	126	526		3,535
Provision	144,422	57,862	4,238	1,667	935	209,124
Ending balance	$ 67,281	$ 24,583	$ 5,811	$ 455	$ 9,527	$ 107,657
Ending balance: individually evaluated for impairment	$ 3,319	$ 15	$ 153	$		$ 3,487
Non-covered Loans and leases:						
Ending balance(1)	$ 4,115,593	$ 1,390,491	$ 468,486	$ 36,098		$ 6,010,668
Ending balance: individually evaluated for impairment	$ 254,657	$ 68,215	$ 5,167	$		$ 328,039

(1) The gross non-covered loan and lease balance excludes deferred loans fees of $11.4 million for the year ended December 31, 2009.
Additional allowance for covered loan loss of $375,000 was recorded at December 31, 2010. See Note 7 for discussion on covered assets.

Summary of Reserve for Unfunded Commitments Activity

The following table presents a summary of activity in the reserve for unfunded commitments (RUC) and unfunded commitments at December 31, 2010 and 2009:

(in thousands)

	December 31, 2010				
	Commercial Real Estate	Commercial	Residential	Consumer & Other	Total
Balance, beginning of year	$ 57	$ 484	$ 144	$ 46	$ 731
Net change to other expense	(24)	91	14	6	87
Balance, end of year	$ 33	$ 575	$ 158	$ 52	$ 818
Unfunded commitments	$ 33,326	$ 548,920	$ 210,574	$ 45,556	$ 838,376

	December 31, 2009				
	Commercial Real Estate	Commercial	Residential	Consumer & Other	Total
Balance, beginning of year	$ 151	$ 625	$ 161	$ 46	$ 983
Net change to other expense	(94)	(141)	(17)		(252)

Balance, end of year	$ 57	$ 484	$ 144	$ 46	$ 731
Unfunded commitments	$ 58,206	$ 479,153	$ 220,697	$ 39,354	$ 797,410

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Non-covered loans sold

In the course of managing the loan portfolio, at certain times, management may decide to sell loans prior to resolution. The following table summarizes loans sold by loan portfolio during the years ended December 31:

(in thousands)

	2010	2009
Commercial Real Estate		
Term & multifamily	$ 8,848	$ 3,540
Construction & development	4,686	2,625
Residential development	15,255	1,450
Commercial		
Term	9,915	4,904
LOC & other	40	
Total	$ 38,744	$ 12,519

Asset Quality and Non-Performing Loans

We manage asset quality and control credit risk through diversification of the non-covered loan portfolio and the application of policies designed to promote sound underwriting and loan monitoring practices. The Bank s Credit Quality Group is charged with monitoring asset quality, establishing credit policies and procedures and enforcing the consistent application of these policies and procedures across the Bank. Reviews of non-performing, past due non-covered loans and larger credits, designed to identify potential charges to the allowance for loan and lease losses, and to determine the adequacy of the allowance, are conducted on an ongoing basis. These reviews consider such factors as the financial strength of borrowers, the value of the applicable collateral, loan loss experience, estimated loan losses, growth in the loan portfolio, prevailing economic conditions and other factors.

A loan is considered impaired when based on current information and events, we determine it is probable that we will not be able to collect all amounts due according to the loan contract, including scheduled interest payments. Generally, when loans are identified as impaired they are moved to our Special Assets Division. When we identify a loan as impaired, we measure the loan for potential impairment using discount cash flows, except when the sole remaining source of the repayment for the loan is the liquidation of the collateral. In these cases, we use the current fair value of collateral, less selling costs. The starting point for determining the fair value of collateral is through obtaining external appraisals. Generally, external appraisals are updated every six to nine months. We obtain appraisals from a pre-approved list of independent, third party, local appraisal firms. Approval and addition to the list is based on experience, reputation, character, consistency and knowledge of the respective real estate market. At a minimum, it is ascertained that the appraiser is: (a) currently licensed in the state in which the property is located, (b) is experienced in the appraisal of properties similar to the property being appraised, (c) is actively engaged in the appraisal work, (d) has knowledge of current real estate market conditions and financing trends, (e) is reputable, and (f) is not on Freddie Mac s nor the Bank s Exclusionary List of appraisers and brokers. In certain cases appraisals will be reviewed by our Real Estate Valuation Services group to ensure the quality of the appraisal and the expertise and independence of the appraiser. Upon receipt and review, an external appraisal is utilized to measure a loan for potential impairment. Our impairment analysis documents the date of the appraisal used in the analysis, whether the officer preparing the report deems it current, and, if not, allows for internal valuation adjustments with justification. Typical justified adjustments might include discounts for continued market deterioration subsequent to appraisal date, adjustments for the release of collateral contemplated in the appraisal, or the value of other collateral or consideration not contemplated in the appraisal. An appraisal over one year old in most cases will be considered stale dated and an updated or new appraisal will be required. Any adjustments from appraised value to net realizable value are detailed and justified in the impairment analysis, which is reviewed and approved by senior credit quality officers and the Company s Allowance for Loan and Lease Losses (ALLL) Committee. Although an external appraisal is the primary source to value collateral dependent loans, we may also utilize values obtained through purchase and sale agreements, negotiated short sales, broker price opinions, or the sales price of the note. These alternative sources of value are used only if deemed to be more representative of value based on updated information regarding collateral resolution. Impairment analyses are updated, reviewed and approved on a quarterly basis at or near the end of each reporting period. Based on these processes, we do not believe there are significant time lapses for the recognition of additional loan loss provisions or charge-offs from the date they become known.

Loans are classified as non-accrual when collection of principal or interest is doubtful generally if they are past due as to maturity or payment of principal or interest by 90 days or more unless such loans are well-secured and in the process of collection. Additionally, all loans that are impaired are considered for non-accrual status. Loans placed on non-accrual will typically remain on non-accrual status until all principal and interest payments are brought current and the prospects for future payments in accordance with the loan agreement appear relatively certain.

Loans are reported as restructured when the Bank grants a concession(s) to a borrower experiencing financial difficulties that it would not otherwise consider. Examples of such concessions include a reduction in the loan rate, forgiveness of principal or accrued interest, extending the maturity date(s) or providing a lower interest rate than would be normally available for a transaction of similar risk. As a result of these concessions, restructured loans are impaired as the Bank will not collect all amounts due, both principal and interest, in accordance with the terms of the original loan agreement. Impairment reserves on non-collateral dependent restructured loans are measured by comparing the present value of expected future cash flows on the restructured loans discounted at the interest rate of the original loan agreement to the loan s carrying value. These impairment reserves are recognized as a specific component to be provided for in the allowance for loan and lease losses.

The Company has written down impaired, non-accrual loans as of December 31, 2010 to their estimated net realizable value, generally based on disposition value, and expects resolution with no additional material loss, absent further decline in market prices.

Non-Covered Non-Accrual Loans and Loans Past Due

The following table summarizes our non-accrual loans and loans past due by loan class as of December 31, 2010 and December 31, 2009:

(in thousands)

							December 31, 2010
	30-59 Days Past Due	60-89 Days Past Due	Greater Than 90 Days and Accruing	Total Past Due	Nonaccrual	Current	Total Non-covered Loans and Leases
Commercial real estate							
Term & multifamily	$ 14,596	$ 8,328	$ 3,008	$ 25,932	$ 49,162	$ 3,408,381	$ 3,483,475
Construction & development	2,172	6,726		8,898	20,124	218,792	247,814
Residential development	640			640	34,586	112,587	147,813
Commercial							
Term	2,010	932		2,942	6,271	500,240	509,453
LOC & other	5,939	1,418	18	7,375	28,034	712,010	747,419
Residential							
Mortgage	1,314	1,101	3,372	5,787		216,629	222,416
Home equity loans & lines	1,096	1,351	232	2,679		275,906	278,585
Consumer & other	361	233	441	1,035		32,008	33,043
Total	$ 28,128	$ 20,089	$ 7,071	$ 55,288	$ 138,177	$ 5,476,553	$ 5,670,018
Deferred loan fees, net							(11,031)
Total							$ 5,658,987

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	December 31, 2009						
	30-59 Days Past Due	60-89 Days Past Due	Greater Than 90 Days and Accruing	Total Past Due	Nonaccrual	Current	Total Non-covered Loans and Leases
Commercial real estate							
Term & multifamily	$ 8,839	$ 9,809	$ 247	$ 18,895	$ 62,379	$ 3,441,830	$ 3,523,104
Construction & development	442	793		1,235	36,658	328,787	366,680
Residential development	7,500	1,449		8,949	45,484	171,376	225,809
Commercial							
Term	4,806	836	29	5,671	8,821	571,364	585,856
LOC & other	2,044	1,083	1,250	4,377	39,776	760,482	804,635
Residential							
Mortgage	1,861	79	4,113	6,053		176,704	182,757
Home equity loans & lines	1,011	269	232	1,512		284,217	285,729
Consumer & other	218	420	38	676		35,422	36,098
Total	$ 26,721	$ 14,738	$ 5,909	$ 47,368	$ 193,118	$ 5,770,182	$ 6,010,668
Deferred loan fees, net							(11,401)
Total							$ 5,999,267

Had non-accrual loans performed according to their original terms, additional interest income of approximately $9.7 million, $9.6 million, and $7.2 million would have been recognized in 2010, 2009 and 2008, respectively.

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Non-covered Impaired Loans

The following table summarizes our impaired loans by loan class as of December 31, 2010 and December 31, 2009:

(in thousands)

	Unpaid Principal Balance	Recorded Investment	Related Allowance	Average Recorded Investment	2010 Interest Income Recognized
With no related allowance recorded					
Commercial real estate					
Term & multifamily	$ 62,605	$ 49,790	$	$ 56,003	$
Construction & development	33,091	25,558		27,588	
Residential development	63,859	39,011		37,603	
Commercial					
Term	8,024	6,969		9,420	
LOC & other	56,046	19,814		38,215	
Residential					
Mortgage					
Home equity loans & lines					
Consumer & other					
With an allowance recorded					
Commercial real estate					
Term & multifamily	$ 29,926	$ 28,070	$ 1,614	$ 28,518	$ 823
Construction & development				1,706	38
Residential development	46,059	44,504	906	54,607	1,474
Commercial					
Term	205	205	9	402	48
LOC & other	9,878	8,519	2,702	1,884	14
Residential					
Mortgage	179	179	8	3,750	6
Home equity loans & lines				21	
Consumer & other					
Total					
Commercial Real Estate	235,540	186,933	2,520	206,025	2,335
Commercial	74,153	35,507	2,711	49,921	62
Residential	179	179	8	3,771	6
Consumer & Other					
Total	$ 309,872	$ 222,619	$ 5,239	$ 259,717	$ 2,403

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	Unpaid Principal Balance	Recorded Investment	Related Allowance	Average Recorded Investment	2009 Interest Income Recognized
With no related allowance recorded					
Commercial real estate					
Term & multifamily	$ 94,616	$ 65,020	$	$ 36,038	$
Construction & development	60,673	36,659		19,654	
Residential development	88,341	54,925		77,819	
Commercial					
Term	11,384	10,484		4,923	
LOC & other	87,001	56,695		21,150	
Residential					
Mortgage					
Home equity loans & lines					
Consumer & other					
With an allowance recorded					
Commercial real estate					
Term & multifamily	$ 39,105	$ 39,105	$ 731	$ 20,720	$ 763
Construction & development				1,574	
Residential development	60,373	58,948	2,588	36,556	1,288
Commercial					
Term	436	436	12	7,287	26
LOC & other	600	600	3	7,681	156
Residential					
Mortgage	5,082	5,167	153	2,022	194
Home equity loans & lines	66			18	2
Consumer & other	18				
Total					
Commercial Real Estate	343,108	254,657	3,319	192,361	2,051
Commercial	99,421	68,215	15	41,041	182
Residential	5,148	5,167	153	2,040	196
Consumer & Other	18				
Total	$ 447,695	$ 328,039	$ 3,487	$ 235,442	$ 2,429

Loans with no related allowance reported generally represent non-accrual loans. The Company recognizes the charge-off of impairment reserves on impaired loans in the period it arises for collateral dependent loans. Therefore, the non-accrual loans as of December 31, 2010 have already been written-down to their estimated net realizable value, based on disposition value, and are expected to be resolved with no additional material loss, absent further decline in market prices. The valuation allowance on impaired loans primarily represents the impairment reserves on performing restructured loans, and is measured by comparing the present value of expected future cash flows on the restructured loans discounted at the interest rate of the original loan agreement to the loan s carrying value.

At December 31, 2010 and 2009, impaired loans of $84.4 million and $134.9 million were classified as accruing restructured loans, respectively. The restructurings were granted in response to borrower financial difficulty, and generally provide for a temporary modification of loan repayment terms. The restructured loans on accrual status represent the only impaired loans accruing interest at each respective date. In order for a restructured loan to be considered for accrual status, the loan s collateral coverage generally will be greater than or equal to 100% of the loan balance, the loan is current on payments, and the borrower must either prefund an interest reserve or demonstrate the ability to make payments from a verified source of cash flow. The Company had no obligations to lend additional funds on the restructured loans as of December 31, 2010.

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For the years ended December 31, 2010, 2009 and 2008, interest income of approximately $2.4 million, $2.4 million and $732,000, respectively, was recognized in connection with impaired loans. The impaired loans for which these interest income amounts were recognized primarily relate to accruing restructured loans.

Non-covered Credit Quality Indicators

As previously noted, the Company s risk rating methodology assigns risk ratings ranging from 1 to 10, where a higher rating represents higher risk. The Bank differentiates its lending portfolios into homogeneous loans (generally consumer loans) and non-homogeneous loans (generally all non-consumer loans). The 10 risk rating categories can be generally described by the following groupings for non-homogeneous loans:

Pass/Watch These loans range from minimal credit risk to lower than average, but still acceptable, credit risk.

Special Mention A Special Mention loan has potential weaknesses that deserve management s close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the asset or the institutions credit position at some future date. They contain unfavorable characteristics and are generally undesirable. Loans in this category are currently protected but are potentially weak and constitute an undue and unwarranted credit risk, but not to the point of a Substandard classification. A Special Mention loan has potential weaknesses, which if not checked or corrected, weaken the asset or inadequately protect the Bank s position at some future date. Such weaknesses include:

Performance is poor or significantly less than expected. There may be a temporary debt-servicing deficiency or inadequate working capital as evidenced by a cash cushion deficiency, but not to the extent that repayment is compromised. Material violation of financial covenants is common.

Loans with unresolved material issues that significantly cloud the debt service outlook, even though a debt servicing deficiency does not currently exist.

Modest underperformance or deviation from plan for real estate loans where absorption of rental/sales units is necessary to properly service the debt as structured. Depth of support for interest carry provided by owner/guarantors may mitigate and provide for improved rating.

This rating may be assigned when a loan officer is unable to supervise the credit properly due to inadequate expertise, an inadequate loan agreement, an inability to control collateral, failure to obtain proper documentation, or any other deviation from prudent lending practices.

Unlike a Substandard credit, there should be a reasonable expectation that these temporary issues will be corrected within the normal course of business, rather than a liquidation of assets, and in a reasonable period of time.

Substandard A substandard asset is inadequately protected by the current sound worth and paying capacity of the obligor or of the collateral pledged, if any. Assets so classified must have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt. They are characterized by the distinct possibility that the Bank will sustain some loss if the deficiencies are not corrected. Loss potential, while existing in the aggregate amount of substandard assets, does not have to exist in individual assets classified substandard. Loans are classified as Substandard when they have unsatisfactory characteristics causing unacceptable levels of risk. A substandard loan normally has one or more well-defined weaknesses that could jeopardize repayment of the debt. The likely need to liquidate assets to correct the problem, rather than repayment from successful operations is the key distinction between Special Mention and Substandard. The following are examples of well-defined weaknesses:

Cash flow deficiencies or trends are of a magnitude to jeopardize current and future payments with no immediate relief. A loss is not presently expected, however the outlook is sufficiently uncertain to preclude ruling out the possibility.

Borrower has been unable to adjust to prolonged and unfavorable industry or economic trends.

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Material underperformance or deviation from plan for real estate loans where absorption of rental/sales units is necessary to properly service the debt and risk is not mitigated by willingness and capacity of owner/guarantor to support interest payments.

Management character or honesty has become suspect. This includes instances where the borrower has become uncooperative.

Due to unprofitable or unsuccessful business operations, some form of restructuring of the business, including liquidation of assets, has become the primary source of loan repayment. Cash flow has deteriorated, or been diverted, to the point that sale of collateral is now the Bank s primary source of repayment (unless this was the original source of repayment). If the collateral is under the Bank s control and is cash or other liquid, highly marketable securities and properly margined, then a more appropriate rating might be Special Mention or Watch.

The borrower is bankrupt, or for any other reason, future repayment is dependent on court action.

There is material, uncorrectable faulty documentation or materially suspect financial information.

Doubtful/Loss Loans classified as Doubtful have all the weaknesses inherent in one classified substandard with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently existing facts, conditions and values, highly questionable and improbable. The possibility of loss is extremely high, but because of certain important and reasonably specific pending factors, which may work towards strengthening of the asset, classification as a loss (and immediate charge off) is deferred until more exact status may be determined. Pending factors include proposed merger, acquisition, liquidation procedures, capital injection, and perfection of liens on additional collateral and refinancing plans. In certain circumstances, a Doubtful rating will be temporary, while the Bank is awaiting an updated collateral valuation. In these cases, once the collateral is valued and appropriate margin applied, the remaining un-collateralized portion will be charged off. The remaining balance, properly margined, may then be upgraded to Substandard, however must remain on non-accrual. A loss rating is assigned to loans considered un-collectible and of such little value that the continuance as an active Bank asset is not warranted. This rating does not mean that the loan has no recovery or salvage value, but rather that the loan should be charged off now, even though partial or full recovery may be possible in the future.

Impaired Loans are classified as Impaired when, based on current information and events, it is probable that the Bank will be unable to collect the scheduled payments of principal and interest when due, in accordance with the terms of the original loan agreement, without unreasonable delay. This generally includes all loans classified as non-accrual and troubled debt restructurings.

The following table summarizes our internal risk rating by loan class as of December 31, 2010 and December 31, 2009:

(in thousands)

						December 31, 2010
	Pass/Watch	Special Mention	Substandard	Doubtful/Loss	Impaired	Total
Commercial real estate						
Term & multifamily	$ 2,978,116	$ 314,094	$ 113,405	$	$ 77,860	$ 3,483,475
Construction & development	145,108	25,295	51,853		25,558	247,814
Residential development	27,428	13,764	23,106		83,515	147,813
Commercial						
Term	472,512	17,658	12,109		7,174	509,453
LOC & other	646,163	30,761	42,162		28,333	747,419
Residential						
Mortgage	216,899	2,414	786	2,138	179	222,416
Home equity loans & lines	275,906	2,447	125	107		278,585
Consumer & other	32,008	595	29	411		33,043
Total	$ 4,794,140	$ 407,028	$ 243,575	$ 2,656	$ 222,619	$ 5,670,018
Deferred loan fees, net						(11,031)
Total						$ 5,658,987

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						December 31, 2009
	Pass/Watch	Special Mention	Substandard	Doubtful/Loss	Impaired	Total
Commercial real estate						
Term & multifamily	$ 3,052,419	$ 235,767	$ 130,793	$	$ 104,125	$ 3,523,104
Construction & development	231,602	45,458	52,961		36,659	366,680
Residential development	41,227	27,655	43,054		113,873	225,809
Commercial						
Term	516,503	25,081	33,352		10,920	585,856
LOC & other	654,071	48,809	44,460		57,295	804,635
Residential						
Mortgage	172,100	1,927	1,461	2,102	5,167	182,757
Home equity loans & lines	284,217	1,280	232			285,729
Consumer & other	35,426	633	34	5		36,098
Total	$ 4,987,565	$ 386,610	$ 306,347	$ 2,107	$ 328,039	$ 6,010,668
Deferred loan fees, net						(11,401)
Total						$ 5,999,267

NOTE 7. COVERED ASSETS AND INDEMNIFICATION ASSET

The following table reflects the estimated fair value of the acquired loans at the acquisition dates:

(in thousands)

	Evergreen January 22, 2010	Rainier February 26, 2010	Nevada Security June 18, 2010	Total
Commercial real estate				
Term & multifamily	$ 141,076	$ 331,869	$ 154,119	$ 627,064
Construction & development	18,832	562	9,481	28,875
Residential development	16,219	10,340	15,641	42,200
Commercial				
Term	27,272	14,850	18,257	60,379
LOC & other	23,965	18,169	11,408	53,542
Residential				
Mortgage	11,886	39,897	1,539	53,322
Home equity loans & lines	8,308	31,029	4,421	43,758
Consumer & other	4,935	11,624	641	17,200
Total	$ 252,493	$ 458,340	$ 215,507	$ 926,340

The following table presents the major types of covered loans as of December 31, 2010:

(in thousands)

	Evergreen	Rainier	Nevada Security	2010 Total
Commercial real estate				
Term & multifamily	$ 124,743	$ 303,585	$ 141,314	$ 569,642
Construction & development	14,162	854	7,419	22,435
Residential development	11,024	2,310	11,372	24,706
Commercial				
Term	18,828	10,811	12,961	42,600
LOC & other	11,876	14,320	9,031	35,227
Residential				
Mortgage	8,129	35,026	1,669	44,824
Home equity loans & lines	6,737	25,163	3,725	35,625
Consumer & other	2,781	8,058		10,839
Total	$ 198,280	$ 400,127	$ 187,491	$ 785,898

The outstanding contractual unpaid principal balance, excluding purchase accounting adjustments, at December 31, 2010 was $286.6 million, $481.7 million and $295.4 million, for Evergreen, Rainier, and Nevada Security, respectively.

Acquired loans are valued as of acquisition date in accordance with Financial Accounting Standards Board Accounting Standards Codification (FASB ASC) 805, *Business Combinations*. Loans purchased with evidence of credit deterioration since origination for which it is probable that all contractually required payments will not be collected are accounted for under FASB ASC 310-30, *Loans and Debt Securities Acquired with Deteriorated Credit Quality*. Because of the significant fair value discounts associated with the acquired portfolios, the concentration of real estate related loans (to finance or secured by real estate collateral) and the decline in real estate values in the regions serviced, and after considering the underwriting standards of the acquired originating bank, the Company elected to account for all acquired loans under ASC 310-30. Under FASB ASC 805 and ASC 310-30, loans are recorded at fair value at acquisition date, factoring in credit losses expected to be incurred over the life of the loan. Accordingly, an allowance for loan losses is not carried over or recorded as of the acquisition date.

The following table presents a reconciliation of the undiscounted contractual cash flows, nonaccretable difference, accretable yield, and fair value of covered loans for each respective acquired loan portfolio at the acquisition dates:.

(in thousands)

	Evergreen January 22, 2010	Rainier February 26, 2010	Nevada Security June 18, 2010	Total
Undiscounted contractual cash flows	$ 498,216	$ 821,972	$ 396,134	$ 1,716,322
Undiscounted cash flows not expected to be collected (nonaccretable difference)	(124,131)	(125,774)	(115,021)	(364,926)
Undiscounted cash flows expected to be collected	374,085	696,198	281,113	1,351,396
Accretable yield at acquisition	(121,592)	(237,858)	(65,606)	(425,056)
Estimated fair value of loans acquired at acquisition	$ 252,493	$ 458,340	$ 215,507	$ 926,340

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The following table presents the changes in the acc