HANMI FINANCIAL CORP
Form 10-Q
August 09, 2012
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the Quarterly Period Ended June 30, 2012

or

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

For the Transition Period From To

Commission File Number: 000-30421

HANMI FINANCIAL CORPORATION

(Exact Name of Registrant as Specified in its Charter)

Delaware	**95-4788120**
(State or Other Jurisdiction of Incorporation or Organization)	**(I.R.S. Employer Identification No.)**
3660 Wilshire Boulevard, Penthouse Suite A Los Angeles, California	**90010**
(Address of Principal Executive Offices)	**(Zip Code)**

(213) 382-2200

(Registrant s Telephone Number, Including Area Code)

Not Applicable

(Former Name, Former Address and Former Fiscal Year, If Changed Since Last Report)

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 x No ¨

Indicate by check mark whether the Registrant has submitted electronically and posted on its corporate Website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the Registrant was required to submit and post such files). Yes x No ¨

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	¨	Accelerated Filer	x
Non-Accelerated Filer	¨ (Do Not Check if a Smaller Reporting Company)	Smaller Reporting Company	¨

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

As of July 31, 2012, there were 31,489,201 outstanding shares of the Registrant s Common Stock.

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HANMI FINANCIAL CORPORATION AND SUBSIDIARIES

QUARTERLY REPORT ON FORM 10-Q

THREE AND SIX MONTHS ENDED JUNE 30, 2012

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PART I FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

HANMI FINANCIAL CORPORATION AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS *(UNAUDITED)*

(In Thousands, Except Share Data)

	June 30, 2012	December 31, 2011
ASSETS		
Cash and Due From Banks	$ 73,645	$ 80,582
Interest-Bearing Deposits in Other Banks	197,760	101,101
Federal Funds Sold	33,000	20,000
Cash and Cash Equivalents	304,405	201,683
Restricted Cash	3,819	1,818
Term Federal Funds Sold	110,000	115,000
Securities Available for Sale, at Fair Value (Amortized Cost of $315,712 as of June 30, 2012 and $377,747 as of December 31, 2011)	319,154	381,862
Securities Held to Maturity, at Amortized Cost (Fair Value of $54,573 as of June 30, 2012 and $59,363 as of December 31, 2011)	53,130	59,742
Loans Held for Sale, at the Lower of Cost or Fair Value	5,138	22,587
Loans Receivable, Net of Allowance for Loan Losses of $71,893 as of June 30, 2012 and $89,936 as of December 31, 2011	1,878,367	1,849,020
Accrued Interest Receivable	7,168	7,829
Premises and Equipment, Net	15,912	16,603
Other Real Estate Owned, Net	1,071	180
Customers Liability on Acceptances	1,443	1,715
Servicing Assets	5,003	3,720
Other Intangible Assets, Net	1,417	1,533
Investment in Federal Home Loan Bank Stock, at Cost	20,687	22,854
Investment in Federal Reserve Bank Stock, at Cost	10,261	8,558
Deferred Taxes Assets	47,483	
Current Tax Assets	13,952	9,073
Bank-Owned Life Insurance	28,581	28,289
Prepaid Expenses	2,726	1,598
Other Assets	16,935	11,160
TOTAL ASSETS	$ 2,846,652	$ 2,744,824
LIABILITIES AND STOCKHOLDERS EQUITY		
LIABILITIES:		
Deposits:		
Non-interest-Bearing	$ 679,085	$ 634,466
Interest-Bearing	1,706,022	1,710,444
	2,385,107	2,344,910
Accrued Interest Payable	14,882	16,032
Bank s Liability on Acceptances	1,443	1,715
Federal Home Loan Bank Advances	3,122	3,303

Junior Subordinated Debentures	82,406	82,406
Accrued Expenses and Other Liabilities	11,236	10,850
TOTAL LIABILITIES	2,498,196	2,459,216
COMMITMENTS AND CONTINGENCIES		
STOCKHOLDERS EQUITY:		
Common Stock, $0.008 Par Value; Authorized 62,500,000 Shares; Issued 32,066,987 Shares (31,489,201 Shares Outstanding) as of June 30, 2012 and December 31, 2011	257	257
Additional Paid-In Capital	549,796	549,744
Unearned Compensation	(116)	(166)
Accumulated Other Comprehensive Income Unrealized Gain on Securities Available for Sale and Loss on Interest-Only Strips, Net of Income Taxes of $302 as of June 30, 2012 and $602 as of December 31, 2011	3,154	3,524
Accumulated Deficit	(134,777)	(197,893)
Less Treasury Stock, at Cost; 577,786 Shares as of June 30, 2012 and as of December 31, 2011	(69,858)	(69,858)
TOTAL STOCKHOLDERS EQUITY	348,456	285,608
TOTAL LIABILITIES AND STOCKHOLDERS EQUITY	$ 2,846,652	$ 2,744,824

See Accompanying Notes to Consolidated Financial Statements. (Unaudited)

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HANMI FINANCIAL CORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF OPERATIONS *(UNAUDITED)*

(In Thousands, Except Per Share Data)

	Three Months Ended June 30, 2012	Three Months Ended June 30, 2011	Six Months Ended June 30, 2012	Six Months Ended June 30, 2011
INTEREST AND DIVIDEND INCOME:				
Interest and Fees on Loans	$ 27,241	$ 29,249	$ 54,783	$ 60,154
Taxable Interest on Investment Securities	2,190	3,094	4,288	5,767
Tax-Exempt Interest on Investment Securities	99	37	201	77
Interest on Term Federal Funds Sold	168	18	493	45
Dividends on Federal Reserve Bank Stock	148	112	276	224
Interest on Federal Funds Sold and Securities Purchased Under Resale Agreements	31	9	33	17
Interest on Interest-Bearing Deposits in Other Banks	59	79	127	168
Dividends on Federal Home Loan Bank Stock	29	20	58	41
Total Interest and Dividend Income	29,965	32,618	60,259	66,493
INTEREST EXPENSE:				
Interest on Deposits	3,953	6,192	8,872	12,927
Interest on Federal Home Loan Bank Advances	43	239	86	572
Interest on Junior Subordinated Debentures	797	711	1,596	1,409
Interest on Other Borrowing		1		1
Total Interest Expense	4,793	7,143	10,554	14,909
NET INTEREST INCOME BEFORE PROVISION FOR CREDIT LOSSES	25,172	25,475	49,705	51,584
Provision for Credit Losses	4,000		6,000	
NET INTEREST INCOME AFTER PROVISION FOR CREDIT LOSSES	21,172	25,475	43,705	51,584
NON-INTEREST INCOME:				
Service Charges on Deposit Accounts	2,936	3,278	6,104	6,419
Insurance Commissions	1,294	1,203	2,530	2,463
Remittance Fees	487	499	941	961
Trade Finance Fees	292	328	584	625
Other Service Charges and Fees	380	368	744	701
Bank-Owned Life Insurance Income	238	233	637	463
Net Gain on Sales of SBA Loans	5,473		5,473	
Net (Loss) on Sales of Other Loans	(5,326)	(77)	(7,719)	(415)
Net Gain (Loss) on Sales of Investment Securities	1,381	(70)	1,382	(70)
Impairment Loss on Investment Securities:				
Total Other-than-temporary Impairment Loss on Investment Securities	(116)		(116)	
Less: Portion of Loss Recognized in Other Comprehensive Income				
Net Impairment Loss Recognized in Earnings	(116)		(116)	

Other Operating Income	150	255	262	378
Total Non-Interest Income	7,189	6,017	10,822	11,525
NON-INTEREST EXPENSE:				
Salaries and Employee Benefits	9,449	8,762	18,559	17,886
Occupancy and Equipment	2,621	2,650	5,216	5,215
Deposit Insurance Premiums and Regulatory Assessments	1,498	1,377	2,899	3,447
Data Processing	1,298	1,487	2,551	2,886
Other Real Estate Owned Expense	69	806	25	1,635
Professional Fees	1,089	1,138	1,838	1,927
Directors and Officers Liability Insurance	295	733	592	1,467
Supplies and Communications	576	496	1,134	1,074
Advertising and Promotion	1,009	908	1,610	1,474
Loan-Related Expense	88	184	288	409
Amortization of Other Intangible Assets	45	190	116	408
Expense related to Unconsumated Capital Offerings		2,220		2,220
Other Operating Expenses	1,726	1,935	3,681	3,899
Total Non-Interest Expense	19,763	22,886	38,509	43,947
INCOME BEFORE (BENEFIT) PROVISION FOR INCOME TAXES	8,598	8,606	16,018	19,162
(Benefit) Provision for Income Taxes	(47,177)	605	(47,098)	724
NET INCOME	**$ 55,775**	**$ 8,001**	**$ 63,116**	**$ 18,438**
EARNINGS PER SHARE:				
Basic	$ 1.77	$ 0.42	$ 2.01	$ 0.98
Diluted	$ 1.77	$ 0.42	$ 2.00	$ 0.98
WEIGHTED-AVERAGE SHARES OUTSTANDING:				
Basic	31,475,610	18,888,080	31,473,065	18,885,368
Diluted	31,499,803	18,907,299	31,489,943	18,907,169

See Accompanying Notes to Consolidated Financial Statements. (Unaudited)

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HANMI FINANCIAL CORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME *(UNAUDITED)*

(In Thousands)

	Three Months Ended June 30, 2012	Three Months Ended June 30, 2011	Six Months Ended June 30, 2012	Six Months Ended June 30, 2011
NET INCOME	$ 55,775	$ 8,001	$ 63,116	$ 18,438
OTHER COMPREHENSIVE INCOME, NET OF TAX				
Unrealized gains on securities				
Unrealized holding gains arising during period	214	6,172	888	6,216
Less: Reclassification adjustment for (gains) losses included in net income	(1,266)	70	(1,266)	70
Unrealized gains on interest rate swap	8	1	9	2
Unrealized (losses) gains on interest-only strip of servicing assets	(3)	1	(1)	1
Other Comprehensive (Loss) Income	(1,047)	6,244	(370)	6,289
COMPREHENSIVE INCOME	**$ 54,728**	**$ 14,245**	**$ 62,746**	**$ 24,727**

See Accompanying Notes to Consolidated Financial Statements. (Unaudited)

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HANMI FINANCIAL CORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS EQUITY *(UNAUDITED)*

(In Thousands)

	Common Stock Number of Shares			Stockholders Equity						
	Gross Shares Issued and Outstanding	**Treasury Shares**	**Net Shares Issued and Outstanding**	**Common Stock**	**Additional Paid-in Capital**	**Unearned Compensation**	**Accumulated Other Comprehensive Income (Loss)**	**Retained Earnings (Deficit)**	**Treasury Stock, at Cost**	**Total Stockholders Equity**
BALANCE AT JANUARY 1, 2011	**19,478,862**	**(579,063)**	**18,899,799**	**$ 156**	**$ 472,335**	**$ (219)**	**$ (2,964)**	**$ (226,040)**	**$ (70,012)**	**$ 173,256**
Share-Based Compensation Expense					304	78				382
Restricted Stock Awards	7,500		7,500		78	(78)				
Comprehensive Loss:										
Net Income								18,438		18,438
Change in Unrealized Gain on Securities Available for Sale and Interest-Only Strips, Net of Income Taxes							6,289			6,289
Total Comprehensive Income										24,727
BALANCE AT JUNE 30, 2011	**19,486,362**	**(579,063)**	**18,907,299**	**$ 156**	**$ 472,717**	**$ (219)**	**$ 3,325**	**$ (207,602)**	**$ (70,012)**	**$ 198,365**
BALANCE AT JANUARY 1, 2012	**32,066,987**	**(577,786)**	**31,489,201**	**$ 257**	**$ 549,744**	**$ (166)**	**$ 3,524**	**$ (197,893)**	**$ (69,858)**	**$ 285,608**
Share-Based Compensation Expense					77	25				102
Restricted Stock Awards					(25)	25				
Comprehensive Income:										
Net Income								63,116		63,116
Change in Unrealized Gain on Securities Available for Sale and Interest-Only Strips, Net of Income Taxes							(370)			(370)
Total Comprehensive Income										62,746
BALANCE AT JUNE 30, 2012	**32,066,987**	**(577,786)**	**31,489,201**	**$ 257**	**$ 549,796**	**$ (116)**	**$ 3,154**	**$ (134,777)**	**$ (69,858)**	**$ 348,456**

See Accompanying Notes to Consolidated Financial Statements. (Unaudited)

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HANMI FINANCIAL CORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS *(UNAUDITED)*

(In Thousands)

	Six Months Ended June 30, 2012	Six Months Ended June 30, 2011
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net Income	$ 63,116	$ 18,438
Adjustments to Reconcile Net Income to Net Cash (Used In) Provided By Operating Activities:		
Depreciation and Amortization of Premises and Equipment	1,087	1,083
Amortization of Premiums and Accretion of Discounts on Investment Securities, Net	2,005	1,227
Amortization of Other Intangible Assets	116	408
Amortization of Servicing Assets	419	345
Share-Based Compensation Expense	102	382
Provision for Credit Losses	6,000	
Net Gain on Sales of Investment Securities	(1,382)	70
Other-Than-Temporary Loss on Investment Securities	116	
FRB and FHLB Stock Dividends	334	265
Deferred Tax Benefit	(47,184)	
Net Loss (Gain) on Sales of Loans	465	(2,489)
Loss on Sales of Other Real Estate Owned		681
Valuation Impairment on Other Real Estate Owned	57	470
Lower of Cost or Fair Value Adjustment for Loans Held for Sale	1,781	2,903
Gain on Bank-Owned Life Insurance	(163)	
Increase in Cash Surrender Value of Bank-Owned Life Insurance	(473)	(463)
Origination of Loans Held for Sale	(60,589)	(16,056)
Net Proceeds from Sales of Loans Held for Sale	72,223	
Changes in Fair Value of Stock Warrants	137	
Loss on Investment in Affordable Housing Partnership	440	440
Decrease in Accrued Interest Receivable	661	536
Increase in Restricted Cash	(2,001)	
Increase in Prepaid Expenses	(1,128)	
Increase in Other Assets	(7,909)	(1,054)
Increase in Current Tax Assets	(4,879)	
Decrease in Accrued Interest Payable	(1,150)	(1,636)
Increase in Other Liabilities	882	(521)
Net Cash Provided By Operating Activities	23,083	5,029
CASH FLOWS FROM INVESTING ACTIVITIES:		
Proceeds from Redemption of Federal Home Loan Bank and Federal Reserve Bank Stock	2,109	2,206
Proceeds from Matured or Called Securities Available for Sale	71,339	70,841
Proceeds from Sales of Securities Available for sale	88,538	157,777
Proceeds from Matured or Called Securities Held to Maturity	6,338	12
Proceeds from Sales of Other Real Estate Owned		3,736
Proceeds from Sales of Loans Held for Sale	65,470	45,963
Proceeds from Matured Term Federal Funds	160,000	
Proceeds from Insurance Settlement on Bank-Owned Life Insurance	344	
Net (Increase) Decrease in Loans Receivable	(16,160)	83,809
Purchase of Federal Reserve Bank Stock	(1,979)	(40)
Purchase of Loans Receivable	(82,669)	
Purchases of Term Federal Fund	(155,000)	

Purchases of Securities Available for Sale	(98,311)	(200,724)
Purchases of Premises and Equipment	(396)	(353)
Net Cash Provided By Investing Activities	39,623	163,227
CASH FLOWS FROM FINANCING ACTIVITIES:		
Increase (Decrease) in Deposits	40,197	(68,346)
Repayment of Long-Term Federal Home Loan Bank Advances	(181)	(171)
Net Change in Short-Term Federal Home Loan Bank Advances and Other Borrowings		(150,536)
Net Cash Provided By (Used In) Financing Activities	40,016	(219,053)
NET DECREASE IN CASH AND CASH EQUIVALENTS	102,722	(50,797)
Cash and Cash Equivalents at Beginning of Year	201,683	249,720
CASH AND CASH EQUIVALENTS AT END OF PERIOD	**$ 304,405**	**$ 198,923**
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:		
Cash Paid During the Period for:		
Interest Paid	11,704	16,649
Income Taxes Paid	4,912	3
Non-Cash Activities:		
Transfer of Loans to Other Real Estate Owned	948	2,752
Transfer of Loans to Loans Held for Sale	64,471	37,806
Transfer of Loans Held for Sale to Loans	1,779	
Loans Provided in the Sale of Loans Held for Sale		5,750
Loans Provided in the Sale of Other Real Estate Owned		510

See Accompanying Notes to Consolidated Financial Statements. (Unaudited)

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HANMI FINANCIAL CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(UNAUDITED)*

THREE AND SIX MONTHS ENDED JUNE 30, 2012 AND 2011 *(Continued)*

NOTE 1 BASIS OF PRESENTATION

Hanmi Financial Corporation (Hanmi Financial, we or us) is a Delaware corporation and is subject to the Bank Holding Company Act of 1956, as amended. Our primary subsidiary is Hanmi Bank (the Bank), a California state chartered bank. Our other subsidiaries are Chun-Ha Insurance Services, Inc., a California corporation (Chun-Ha), and All World Insurance Services, Inc., a California corporation (All World).

In the opinion of management, the accompanying unaudited consolidated financial statements of Hanmi Financial Corporation and Subsidiaries reflect all adjustments of a normal and recurring nature that are necessary for a fair presentation of the results for the interim period ended June 30, 2012, but are not necessarily indicative of the results that will be reported for the entire year. Certain information and footnote disclosures normally included in annual financial statements prepared in accordance with U.S. generally accepted accounting principles (GAAP) have been condensed or omitted. In the opinion of management, the aforementioned unaudited consolidated financial statements are in conformity with GAAP. Such interim consolidated financial statements have been prepared in accordance with the instructions to Form 10-Q pursuant to the rules and regulations of the Securities and Exchange Commission. The interim information should be read in conjunction with our Annual Report on Form 10-K for the fiscal year ended December 31, 2011 (the 2011 Annual Report on Form 10-K).

The preparation of interim consolidated financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Descriptions of our significant accounting policies are included in *Note 2 Summary of Significant Accounting Policies* in our 2011 Annual Report on Form 10-K.

Certain reclassifications were made to the prior period s presentation to conform to the current period s presentation.

The number of shares of Hanmi Financial s common stock and the computation of basic and diluted earnings per share were adjusted retroactively for all periods presented to reflect the 1-for-8 reverse stock split of Hanmi Financial s common stock, which became effective on December 19, 2011.

NOTE 2 REGULATORY MATTERS

On November 2, 2009, the members of the Board of Directors of the Bank consented to the issuance of the Final Order (Final Order) with the California Department of Financial Institutions (the DFI). The Final Order contained a list of requirements ranging from a capital directive to developing a contingency funding plan. Following a target joint examination of the Bank by the DFI and Federal Reserve Bank of San Francisco (the FRB) which commenced in February 2012, and based on the improved condition of the Bank noted at the examination, on May 1, 2012, the Bank entered into a Memorandum of Understanding (MOU) with the DFI. Concurrently with the entry into the MOU, the DFI issued an order terminating the Final Order.

On November 2, 2009, Hanmi Financial and the Bank entered into a Written Agreement (the Written Agreement) with the FRB. The Written Agreement contains a list of strict requirements ranging from a capital directive to developing a contingency funding plan.

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HANMI FINANCIAL CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(UNAUDITED)*

THREE AND SIX MONTHS ENDED JUNE 30, 2012 AND 2011 *(Continued)*

NOTE 2 REGULATORY MATTERS *(Continued)*

While Hanmi Financial has taken such actions as necessary to enable Hanmi Financial and the Bank to comply with the requirements of the Written Agreement and the MOU, there can be no assurance that compliance with the Written Agreement and the MOU will not have material and adverse effects on the operations and financial condition of Hanmi Financial and the Bank. Any material failure to comply with the provisions of the Written Agreement and the MOU could result in further enforcement actions by both the DFI and the FRB, or the placing of the Bank into conservatorship or receivership.

Written Agreement and MOU

Pursuant to the Written Agreement, the Board of Directors of the Bank prepared and submitted written plans to the FRB that addressed the following items: (i) strengthening board oversight of the management and operation of the Bank; (ii) strengthening credit risk management practices; (iii) improving credit administration policies and procedures; (iv) improving the Bank s position with respect to problem assets; (v) maintaining adequate reserves for loan and lease losses; (vi) improving the capital position of the Bank and of Hanmi Financial; (vii) improving the Bank s earnings through a strategic plan and a budget; and (viii) improving the Bank s liquidity position, funds management practices, and contingency funding plan. In addition, the Written Agreement places restrictions on the Bank s lending to borrowers who have adversely classified loans with the Bank. The Written Agreement also requires the Bank to charge off or collect certain problem loans and review and revise its methodology for calculating allowance for loan and lease losses consistent with relevant supervisory guidance. Hanmi Financial and the Bank are also prohibited from paying dividends without prior approval from the FRB.

Hanmi Financial and the Bank are required to notify the FRB if their respective capital ratios fall below those set forth in the capital plan approved by the FRB.

The MOU imposes substantially less requirements on the Bank than the Final Order. Pursuant to the MOU, the Bank is required to continue to (i) maintain strong board oversight, management and operations of the Bank, (ii) review and implement policies and procedures to address credit administration and credit risk management, (iii) maintain an acceptable methodology for calculating loan and lease losses, (iv) obtain approval from the DFI prior to declaring and paying dividends, and (v) maintain a ratio of tangible stockholders equity to total tangible assets of not less than 9.5 percent.

On November 18, 2011, we completed an underwritten public offering of our common stock by which we raised $77.1 million in net proceeds. As a result, we satisfied the requirement that the ratio of tangible stockholders equity to total tangible assets be not less than 9.5 percent as of December 31, 2011. As of June 30, 2012, Hanmi Financial and the Bank had a ratio of tangible stockholders equity to total tangible assets of 12.20 percent and 14.34 percent, respectively.

Based on submissions to and consultations with the DFI and the FRB, we believe that the Bank has taken the required corrective action and has complied with substantially all of the requirements of the Written Agreement and the MOU.

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HANMI FINANCIAL CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(UNAUDITED)*

THREE AND SIX MONTHS ENDED JUNE 30, 2012 AND 2011 *(Continued)*

NOTE 2 REGULATORY MATTERS *(Continued)*

Risk-Based Capital

Federal bank regulatory agencies require bank holding companies such as Hanmi Financial to maintain a minimum ratio of qualifying total capital to risk-weighted assets of 8.0 percent and a minimum ratio of Tier 1 capital to risk-weighted assets of 4.0 percent. In addition to the risk-based guidelines, federal bank regulatory agencies require bank holding companies to maintain a minimum ratio of Tier 1 capital to average total assets, referred to as the leverage ratio, of 4.0 percent. In order to be considered well capitalized, federal bank regulatory agencies require depository institutions such as the Bank to maintain a minimum ratio of qualifying total capital to risk-weighted assets of 10.0 percent and a minimum ratio of Tier 1 capital to risk-weighted assets of 6.0 percent. In addition to the risk-based guidelines, the federal bank regulatory agencies require depository institutions to maintain a minimum ratio of Tier 1 capital to average total assets, referred to as the leverage ratio, of 5.0 percent. For a bank rated in the highest of the five categories used by federal bank regulatory agencies to rate banks, the minimum leverage ratio is 3.0 percent.

The capital ratios of Hanmi Financial and the Bank were as follows as of June 30, 2012 and 2011:

	Actual		Minimum Regulatory Requirement		Minimum to Be Categorized as Well Capitalized	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
			(In Thousands)			
June 30, 2012						
Total Capital (to Risk-Weighted Assets):						
Hanmi Financial	$ 422,301	20.02%	$ 168,754	8.00%	N/A	N/A
Hanmi Bank	$ 401,456	19.06%	$ 168,467	8.00%	$ 210,584	10.00%
Tier 1 Capital (to Risk-Weighted Assets):						
Hanmi Financial	$ 395,342	18.74%	$ 84,377	4.00%	N/A	N/A
Hanmi Bank	$ 374,540	17.79%	$ 84,234	4.00%	$ 126,351	6.00%
Tier 1 Capital (to Average Assets):						
Hanmi Financial	$ 395,342	14.70%	$ 107,587	4.00%	N/A	N/A
Hanmi Bank	$ 374,540	13.95%	$ 107,361	4.00%	$ 134,201	5.00%
June 30, 2011						
Total Capital (to Risk-Weighted Assets):						
Hanmi Financial	$ 301,045	13.92%	$ 173,032	8.00%	N/A	N/A
Hanmi Bank	$ 302,827	14.02%	$ 172,802	8.00%	$ 216,003	10.00%
Tier 1 Capital (to Risk-Weighted Assets):						
Hanmi Financial	$ 257,911	11.92%	$ 86,516	4.00%	N/A	N/A
Hanmi Bank	$ 274,785	12.72%	$ 86,401	4.00%	$ 129,602	6.00%
Tier 1 Capital (to Average Assets):						
Hanmi Financial	$ 257,911	9.09%	$ 113,504	4.00%	N/A	N/A
Hanmi Bank	$ 274,785	9.70%	$ 113,260	4.00%	$ 141,576	5.00%

Reserve Requirement

The Bank is required to maintain a certain percentage of its deposits as reserves at the FRB. The daily average reserve balance required to be maintained with the FRB was $1.5 million, and the Bank was in compliance with the such requirement as of June 30, 2012 and December 31, 2011, respectively.

Federal Reserve Notices of Proposed Rulemaking.

On June 7, 2012, the Board of Governors of the Federal Reserve System approved for publication in the Federal Register three related notices of proposed rulemaking (collectively, the Notices) relating to the implementation of revised capital rules to reflect the requirements of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 as well as the Basel III international capital standards. Among other things, if adopted as proposed, the Notices would establish a new capital standard consisting of common equity Tier 1 capital; increase the capital ratios required for certain existing capital categories and add a requirement for a capital conservation buffer (failure to meet these standards would result in limitations on capital distributions as well as executive bonuses); and add more conservative standards for including securities in regulatory capital, which would phase-out trust preferred securities as a component of Tier 1 capital effective January 1, 2013. In addition, the Notices contemplate the deduction of certain assets from regulatory capital and revisions to the methodologies for determining risk weighted assets, including applying a more risk-sensitive treatment to residential mortgage exposures and to past due or nonaccrual loans. The Notices provide for various phase-in periods over the next several years. Hanmi Financial and the Bank will be subject to many provisions in the Notices, but until final regulations are issued pursuant to the Notices, Hanmi Financial cannot predict the actual effect of the Notices.

HANMI FINANCIAL CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS ***(UNAUDITED)***

THREE AND SIX MONTHS ENDED JUNE 30, 2012 AND 2011 *(Continued)*

NOTE 3 FAIR VALUE MEASUREMENTS

Fair Value Option and Fair Value Measurements

FASB ASC 820, Fair Value Measurements and Disclosures, defines fair value, establishes a framework for measuring fair value and expands disclosures about fair value measurements. It also establishes a fair value hierarchy about the assumptions used to measure fair value and clarifies assumptions about risk and the effect of a restriction on the sale or use of an asset.

FASB ASC 825, Financial Instruments, provides additional guidance for estimating fair value in accordance with FASB ASC 820 when the volume and level of activity for the asset or liability have significantly decreased. It also includes guidance on identifying circumstances that indicate a transaction is not orderly. FASB ASC 825 emphasizes that even if there has been a significant decrease in the volume and level of activity for the asset or liability and regardless of the valuation technique(s) used, the objective of a fair value measurement remains the same. FASB ASC 825 also requires additional disclosures relating to fair value measurement inputs and valuation techniques, as well as disclosures of all debt and equity investment securities by major security types rather than by major security categories that should be based on the nature and risks of the securities during both interim and annual periods. FASB ASC 825 became effective for interim and annual reporting periods ending after June 15, 2009 and did not require disclosures for earlier periods presented for comparative purposes at initial adoption. In periods after initial adoption, FASB ASC 825 requires comparative disclosures only for periods ending after initial adoption. We adopted FASB ASC 825 in the second quarter of 2009. The adoption of FASB ASC 825 resulted in additional disclosures that are presented in Note 4 Investment Securities.

FASB ASU 2011-04, Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs (Topic 820), provides guidance on fair value measurement and disclosure requirements that the FASB deemed largely identical across U.S. GAAP and IFRS. The requirements do not extend the use of fair value accounting, but provide guidance on how it should be applied where its use is already required or allowed. ASU 2011-04 supersedes most of the guidance in ASC topic 820, but many of the changes are clarifications of existing guidance or wording changes to reflect IFRS 13. Amendments in FASB ASU 2011-04 change the wording used to describe U.S. GAAP requirements for fair value and disclosing information about fair value measurements. FASB ASU 2011-04 became effective for interim and annual reporting periods beginning after December 15, 2011, and early application was not permitted. Our adoption of FASB ASU 2011-04 did not have a significant impact on our financial condition or result of operations.

We used the following methods and significant assumptions to estimate fair value:

Investment Securities Available for Sale The fair values of investment securities available for sale are determined by obtaining quoted prices on nationally recognized securities exchanges or matrix pricing, which is a mathematical technique used widely in the industry to value debt securities without relying exclusively on quoted prices for the specific securities but rather by relying on the securities relationship to other benchmark quoted securities. The fair values of investment securities are determined by reference to the average of at least two quoted market prices obtained from independent external brokers or independent external pricing service providers who have experience in valuing these securities. In obtaining such valuation information from third parties, we have evaluated the methodologies used to develop the resulting fair values. We perform a monthly analysis on the broker quotes received from third parties to ensure that the prices represent a reasonable estimate of the fair value. The procedures include, but are not limited to, initial and on-going review of third party pricing methodologies, review of pricing trends, and monitoring of trading volumes.

HANMI FINANCIAL CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(UNAUDITED)*

THREE AND SIX MONTHS ENDED JUNE 30, 2012 AND 2011 *(Continued)*

NOTE 3 FAIR VALUE MEASUREMENTS *(Continued)*

Level 1 investment securities include U.S. government and agency debentures and equity securities that are traded on an active exchange or by dealers or brokers in active over-the-counter markets. The fair value of these securities is determined by quoted prices on an active exchange or over-the-counter market. Level 2 investment securities primarily include mortgage-backed securities, municipal bonds, collateralized mortgage obligations, and asset-backed securities. In determining the fair value of the securities categorized as Level 2, we obtain reports from nationally recognized broker-dealers detailing the fair value of each investment security we hold as of each reporting date. The broker-dealers use observable market information to value our fixed income securities, with the primary sources being nationally recognized pricing services. The fair value of the municipal securities is based on a proprietary model maintained by the broker-dealers. We review the market prices provided by the broker-dealers for our securities for reasonableness based on our understanding of the marketplace, and we also consider any credit issues related to the bonds. As we have not made any adjustments to the market quotes provided to us and they are based on observable market data, they have been categorized as Level 2 within the fair value hierarchy.

Securities classified as Level 3 investment securities are instruments that are not traded in the market. As such, no observable market data for the instrument is available. This necessitates the use of significant unobservable inputs into our proprietary valuation model. As of June 30, 2012 and December 31, 2011, we had no level 3 investment securities.

SBA Loans Held for Sale Small Business Administration (SBA) loans held for sale are carried at the lower of cost or fair value. As of June 30, 2012 and December 31, 2011, we had $360,000 and $5.1 million of SBA loans held for sale, respectively. Management obtains quotes, bids or pricing indication sheets on all or part of these loans directly from the purchasing financial institutions. Premiums received or to be received on the quotes, bids or pricing indication sheets are indicative of the fact that cost is lower than fair value. At June 30, 2012 and December 31, 2011, the entire balance of SBA loans held for sale was recorded at its cost. We record SBA loans held for sale on a nonrecurring basis with Level 2 inputs.

Non-performing Loans Held for Sale We reclassify certain non-performing loans when we make the decision to sell those loans. The fair value of non-performing loans held for sale is generally based upon the quotes, bids or sales contract prices which approximate their fair value. Non-performing loans held for sale are recorded at estimated fair value less anticipated liquidation cost. As of June 30, 2012 and December 31, 2011, we had $3.5 million and $15.0 million of non-performing loans held for sale, respectively. We measure non-performing loans held for sale at fair value on a nonrecurring basis with Level 3 inputs.

Impaired Loans FASB ASC 820 applies to loans measured for impairment using the practical expedients permitted by FASB ASC 310, Receivables, including impaired loans measured at an observable market price (if available), or at the fair value of the loan s collateral (if the loan is collateral dependent). Fair value of the loan s collateral, when the loan is dependent on collateral, is determined by appraisals or independent valuation. These loans are classified as Level 2. Level 3 values additionally include adjustments by the Company for historical knowledge and for changes in market conditions.

Other Real Estate Owned Other real estate owned is measured at fair value less selling costs. Fair value was determined based on third-party appraisals of fair value in an orderly sale. Selling costs were based on standard market factors. We classify other real estate owned, which is subject to non-recurring fair value adjustments, as Level 3.

Servicing Assets and Servicing Liabilities The fair values of servicing assets and servicing liabilities are based on a valuation model that calculates the present value of estimated net future cash flows related to contractually specified servicing fees. The valuation model incorporates assumptions that market participants would use in estimating future cash flows. We compare the valuation model inputs and results to widely available published industry data for reasonableness. Since fair value measurements of servicing assets and servicing liabilities use significant unobservable inputs, we classify them as Level 3.

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HANMI FINANCIAL CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(UNAUDITED)*

THREE AND SIX MONTHS ENDED JUNE 30, 2012 AND 2011 *(Continued)*

NOTE 3 FAIR VALUE MEASUREMENTS *(Continued)*

Other Intangible Assets Other intangible assets consist of a core deposit intangible and acquired intangible assets arising from acquisitions, including non-compete agreements, trade names, carrier relationships and client/insured relationships. The valuation of other intangible assets is based on information and assumptions available to us at the time of acquisition, using income and market approaches to determine fair value. We test our other intangible assets annually for impairment, or when indications of potential impairment exist. Fair value measurements of other intangible assets use significant unobservable inputs. As such, we classify other intangible assets, which are subject to non-recurring fair value adjustments, as Level 3.

Stock Warrants The fair value of stock warrants is determined by the Black-Scholes option pricing model. The expected stock volatility is based on historical volatility of our common stock over the expected term of the warrants. The expected life assumption is based on the contract term. The dividend yield of zero is based on the fact that we have no present intention to pay cash dividends. The risk free rate used for the warrant is equal to the zero coupon rate in effect at the time of the grant. As such, we classify stock warrants, which are subject to recurring fair value adjustments, as Level 3.

FASB ASC 320, Investments Debt and Equity Securities, amended current other-than-temporary-impairment (OTTI) guidance in GAAP for debt securities by requiring a write-down when fair value is below amortized cost in circumstances where: (1) an entity has the intent to sell a security; (2) it is more likely than not that an entity will be required to sell the security before recovery of its amortized cost basis; or (3) an entity does not expect to recover the entire amortized cost basis of the security. If an entity intends to sell a security or if it is more likely than not the entity will be required to sell the security before recovery, an OTTI write-down is recognized in earnings equal to the entire difference between the security s amortized cost basis and its fair value. If an entity does not intend to sell the security or it is not more likely than not that it will be required to sell the security before recovery, the OTTI write-down is separated into an amount representing credit loss, which is recognized in earnings, and the amount related to all other factors, which is recognized in other comprehensive income. FASB ASC 320 did not amend existing recognition and measurement guidance related to OTTI write-downs of equity securities. FASB ASC 320 also extended disclosure requirements about debt and equity securities to interim reporting periods. FASB ASC 320 does not require disclosures for earlier periods presented for comparative purposes at initial adoption. In periods after initial adoption, FASB ASC 320 requires comparative disclosures only for periods ending after initial adoption.

FASB ASC 820 defines fair value as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. FASB ASC 820 also establishes a three-level fair value hierarchy that requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The three levels of inputs that may be used to measure fair value are defined as follows:

Level 1	Quoted prices (unadjusted) for identical assets or liabilities in active markets that the entity has the ability to access as of the measurement date.
Level 2	Significant other observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities, quoted prices in markets that are not active, and other inputs that are observable or can be corroborated by observable market data.
Level 3	Significant unobservable inputs that reflect a company s own assumptions about the assumptions that market participants would use in pricing an asset or liability.

Fair value is used on a recurring basis for certain assets and liabilities in which fair value is the primary basis of accounting. Additionally, fair value is used on a non-recurring basis to evaluate assets or liabilities for impairment or for disclosure purposes in accordance with FASB ASC 825, Financial Instruments.

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HANMI FINANCIAL CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS ***(UNAUDITED)***

THREE AND SIX MONTHS ENDED JUNE 30, 2012 AND 2011 *(Continued)*

NOTE 3 FAIR VALUE MEASUREMENTS *(Continued)*

We record investment securities available for sale at fair value on a recurring basis. Certain other assets, such as loans held for sale, impaired loans, other real estate owned, and other intangible assets, are recorded at fair value on a non-recurring basis. Non-recurring fair value measurements typically involve assets that are periodically evaluated for impairment and for which any impairment is recorded in the period in which the re-measurement is performed.

Assets and Liabilities Measured at Fair Value on a Recurring Basis

There were no transfers of assets between Level 1 and Level 2 of the fair value hierarchy for the six months ended June 30, 2012. We recognize transfers of assets between levels at the end of each respective quarterly reporting period.

As of June 30, 2012 and December 31, 2011, assets and liabilities measured at fair value on a recurring basis are as follows:

	Level 1 Quoted Prices in Active Markets for Identical Assets	Level 2 Significant Observable Inputs With No Active Market With Identical Characteristics	Level 3 Significant Unobservable Inputs	Balance
		(In Thousands)		
As of June 30, 2012				
ASSETS:				
Debt Securities Available for Sale:				
Residential Mortgage-Backed Securities	$	$ 115,136	$	$ 115,136
U.S. Government Agency Securities	74,226			74,226
Collateralized Mortgage Obligations		96,582		96,582
Municipal Bonds-Tax Exempt		3,137		3,137
Municipal Bonds-Taxable		6,330		6,330
Corporate Bonds		19,901		19,901
Other Securities		3,357		3,357
Total Debt Securities Available for Sale	$ 74,226	$ 244,443	$	$ 318,669
Equity Securities Available for Sale:				
Financial Services Industry	$ 485	$	$	$ 485
Total Equity Securities Available for Sale	$ 485	$	$	$ 485
Total Securities Available for Sale	$ 74,711	$ 244,443	$	$ 319,154
LIABILITIES:				
Stock Warrants	$	$	$ 1,020	$ 1,020

As of December 31, 2011				
ASSETS:				
Debt Securities Available for Sale:				
Residential Mortgage-Backed Securities	$	$ 113,005	$	$ 113,005
U.S. Government Agency Securities	72,548			72,548
Collateralized Mortgage Obligations		162,837		162,837
Municipal Bonds-Tax Exempt		3,482		3,482
Municipal Bonds-Taxable		6,138		6,138
Corporate Bonds		19,836		19,836
Other Securities		3,335		3,335
Total Debt Securities Available for Sale	$ 72,548	$ 308,633	$	$ 381,181
Equity Securities Available for Sale:				
Financial Services Industry	$ 681	$	$	$ 681
Total Equity Securities Available for Sale	$ 681	$	$	$ 681
Total Securities Available for Sale	$ 73,229	$ 308,633	$	$ 381,862
LIABILITIES:				
Stock Warrants	$	$	$ 883	$ 883

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HANMI FINANCIAL CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS ***(UNAUDITED)***

THREE AND SIX MONTHS ENDED JUNE 30, 2012 AND 2011 *(Continued)*

NOTE 3 FAIR VALUE MEASUREMENTS *(Continued)*

The table below presents a reconciliation and income statement classification of gains and losses for all assets and liabilities measured at fair value on a recurring basis using significant unobservable inputs (Level 3) for the six months ended June 30, 2012:

	Beginning Balance as of January 1, 2012	Purchases, Issuances and Settlements	Realized Gains or Losses in Earnings	Unrealized Gains or Losses in Other Comprehensive Income	Transfers In and/or Out of Level 3	Ending Balance as of June 30, 2012
			(In Thousands)			
LIABILITIES:						
Stock Warrants [1]	$ 883	$	$ 137	$	$	$ 1,020

[1] *Reflects warrants for our common stock issued in connection with services it provided to us as a placement agent in connection with our best efforts public offering and as our financial adviser in connection with our completed rights offering. The warrants were immediately exercisable when issued at an exercise price of $9.60 per share of our common stock and expire on October 14, 2015. See Note 8 Stockholders Equity for more details.*

Assets and Liabilities Measured at Fair Value on a Non-Recurring Basis

As of June 30, 2012 and 2011, assets and liabilities measured at fair value on a non-recurring basis are as follows:

	Level 1 Quoted Prices in Active Markets for Identical Assets	*Level 2* Significant Observable Inputs With No Active Market With Identical Characteristics	*Level 3* Significant Unobservable Inputs	Loss During The Three Months Ended June 30, 2012 and 2011	Loss During The Six Months Ended June 30, 2012 and 2011
		(In Thousands)			
June 30, 2012					
ASSETS:					
Non-performing Loans Held for Sale [1]	$	$	$ 3,489	$	$ 657
Impaired Loans [2]	$	$ 22,694	$ 10,911	$ 2,285	$ 4,690
Other Real Estate Owned [3]	$	$	$ 1,071	$ 57	$ 57

June 30, 2011					
ASSETS:					
Non-performing Loans Held for Sale [(4)]	$	$	$ 18,683	$ 682	$ 9,462
Impaired Loans [(5)]	$	$ 33,071	$ 145,019	$ 14,314	$ 23,940
Other Real Estate Owned [(6)]	$	$	$ 1,298	$ 203	$ 770

(1) Includes commercial term loans of $3.0 million, and SBA loans of $484,000.

(2) Includes real estate loans of $5.2 million, commercial and industrial loans of $27.4 million, and consumer loans of $1.0 million.

(3) Includes properties from the foreclosure of a commercial property loan of $346,000 and a SBA loan of $725,000.

(4) Includes commercial property loans of $418,000, commercial term loans of $12.0 million, SBA loans of $6.0 million and residential property loans of $266,000.

(5) Includes real estate loans of $73.7 million, commercial and industrial loans of $103.7 million, and consumer loans of $732,000.

(6) Includes properties from the foreclosure of commercial property loans of $308,000 and SBA loans of $990,000.

FASB ASC 825 requires disclosure of the fair value of financial assets and financial liabilities, including those financial assets and financial liabilities that are not measured and reported at fair value on a recurring basis or non-recurring basis. The methodologies for estimating the fair value of financial assets and financial liabilities that are measured at fair value on a recurring basis or non-recurring basis are discussed above.

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HANMI FINANCIAL CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS *(UNAUDITED)*

THREE AND SIX MONTHS ENDED JUNE 30, 2012 AND 2011 *(Continued)*

NOTE 3 FAIR VALUE MEASUREMENTS *(Continued)*

The estimated fair value of financial instruments has been determined by using available market information and appropriate valuation methodologies. However, considerable judgment is required to interpret market data in order to develop estimates of fair value. Accordingly, the estimates presented herein are not necessarily indicative of the amounts that we could realize in a current market exchange. The use of different market assumptions and/or estimation methodologies may have a material effect on the estimated fair value amounts.

The estimated fair values of financial instruments were as follows:

	June 30, 2012		December 31, 2011	
	Carrying or Contract Amount	Estimated Fair Value	Carrying or Contract Amount	Estimated Fair Value
	(In Thousands)			
Financial Assets:				
Cash and Cash Equivalents	$ 304,405	$ 304,405	$ 201,683	$ 201,683
Restricted Cash	3,819	3,819	1,818	1,818
Term Federal Funds	110,000	110,153	115,000	115,173
Investment Securities Available for Sale	319,154	319,154	381,862	381,862
Investment Securities Held to Maturity	53,130	54,573	59,742	59,363
Loans Receivable, Net of Allowance for Loan Losses	1,878,367	1,830,880	1,849,020	1,802,511
Loans Held for Sale	5,138	5,138	22,587	22,587
Accrued Interest Receivable	7,168	7,168	7,829	