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MALAGA
FINANCIAL CORPORATION

A N N U A L R E P O R T



Experience the Malaga Bank difference.

- Financial Strength
- Personalized Service
- Community Partner

What is the Malaga Bank difference?

Financial Strength

- BauerFinancial Inc. Five-Star rating for 9 consecutive quarters.

Personalized Service

- What our customers are saying:

"No other bank in the South Bay comes close to providing the level of service I consistently receive at Malaga Bank." *Chuck Chambers*

"Your quick efficient responses are a welcome reprieve from the mega banks!" *Anonymous*

"I never miss a chance to tell others about Malaga." *Tom Penland*

Community Partner

- We work and live in the communities we serve.

We support numerous non-profit organizations such as the Peninsula Education Foundation, Boys & Girls Clubs of the Los Angeles Harbor, Grand Vision Foundation and the Palos Verdes Art Center. Our staff is very active in supporting the business communities through our local Chambers of Commerce.

DEAR SHAREHOLDERS AND FRIENDS,

As we celebrate our 25th year, we take pride in continuing to provide a strong and safe place to bank for our customers, shareholders and communities. We are pleased to report that in this challenging environment, Malaga Financial Corporation and its banking subsidiary Malaga Bank had a 34% increase in net income in 2009, to \$9,494,000, another record year.

We were also able to continue to grow our assets, which increased 6% to \$811 million at December 31, 2009 compared to \$764 million at December 31, 2008. The loan portfolio at December 31, 2009 was \$761 million, an increase of \$30 million or 4% from December 31, 2008. We had no delinquent loans or other non-performing assets at December 31, 2009.

Our deposit strategy in 2009 continued to focus on attracting new customers and expanding existing relationships at our branches. Total deposits increased by \$125 million to \$494 million, a 34% increase, at December 31, 2009. As a result of this, we were able to substantially reduce our cost of funds by reducing our higher cost borrowings from the Federal Home Loan Bank of San Francisco.

In order to continue to better serve the South Bay community, our Torrance branch moved to its new location on the corner of Crenshaw Boulevard and Rolling Hills Road effective July 20, 2009.

In December 2009 and January 2010, Malaga Financial Corporation completed a private offering \$10 million principal amount of 9.25% Senior Subordinated Notes. We contributed all of the proceeds of this offering to the capital of Malaga Bank, further increasing the bank's already strong capital position. This increased regulatory capital will enable us to pursue growth opportunities and will provide a further cushion against any losses or reserves on its loan portfolio in this recessionary economy.

At December 31, 2009, Malaga Bank was in compliance with all applicable regulatory capital requirements and was deemed "well-capitalized" under applicable regulations. Core capital and risk-based capital ratios were 10.10% and 17.04%, respectively, and exceeded the minimum "well-capitalized" requirements of 5.00% and 10.00% respectively at December 31, 2009.

In these difficult economic times our strategy continues to be moderate growth combined with prudent loan underwriting and diligent cost control. Malaga Bank continues to receive a five-star rating, the highest rating available from BauerFinancial Inc.

We are proud of our strength, our exceptional team of bankers and our leadership in the communities we serve. On behalf of Malaga Financial Corporation and Malaga Bank, we thank our board of directors, management and staff for their dedication to our continued success and we thank you, our shareholders, for your support, your business and your investment.



Randy C. Bowers

President and
Chief Executive Officer



Robert E. Kershaw

Chairman of the Board

MANAGEMENT'S DISCUSSION AND ANALYSIS

The following discussion and financial information is presented to aid in understanding results of operations and financial condition of Malaga Financial Corporation ("MFC") and its consolidated subsidiary, Malaga Bank FSB ("Malaga Bank"). In this discussion, references to the "Company" or "we" or "us" refer to MFC and Malaga Bank.

OVERVIEW

MFC is the holding company for Malaga Bank, and the stock of Malaga Bank is MFC's primary asset. Malaga Bank is a full service community bank with headquarters located on the Palos Verdes Peninsula in Southern California. It is the largest independent bank headquartered in the South Bay area of Los Angeles.

We originate primarily adjustable rate multifamily (apartment) mortgage loans in Los Angeles and Orange counties and to a lesser extent single-family residential loans, consumer loans, construction loans, commercial mortgage loans and commercial loans. At December 31, 2009, multifamily mortgage loans represented 73% of our loan portfolio and loans represented 94% of our total assets.

In 2009, our market area for deposits continued to be concentrated in the areas immediately surrounding our four branch offices in Palos Verdes Estates, Rolling Hills Estates, Torrance and San Pedro, California.

RESULTS OF OPERATIONS

Our net income was \$9.5 million in 2009 compared to net income of \$7.1 million in the previous year, an increase of \$2.4 million or 34%. Earnings per share for 2009 were \$1.65 (basic) and \$1.64 (fully diluted), compared to \$1.24 (basic and fully diluted) in 2008.

Our return on average assets (ROA) was 1.20% in 2009 compared to 0.97% in 2008. Our return on average equity (ROE) was 16.17% in 2009 compared to 13.94% in 2008.

The following selected financial data for the past five years:

	2009	2008	2007	2006	2005
Total assets (000's)	\$ 810,850	\$ 763,946	\$ 703,972	\$ 672,976	\$ 581,493
Stockholders' equity (000's)	\$ 62,998	\$ 54,533	\$ 48,633	\$ 46,222	\$ 42,449
Net income (000's)	\$ 9,494	\$ 7,076	\$ 5,967	\$ 5,213	\$ 4,758
Basic earnings per share	\$ 1.65	\$ 1.24	\$ 1.02	\$ 0.90	\$ 0.84
Diluted earnings per share	\$ 1.64	\$ 1.24	\$ 1.01	\$ 0.88	\$ 0.81
ROA	1.20%	0.97%	0.86%	0.82%	0.89%
ROE	16.17%	13.94%	12.24%	11.67%	11.80%

NET INTEREST INCOME

Net interest income is the primary component of our income. The chief determinants of net interest income are the dollar amounts of interest-earning assets and interest-bearing liabilities and the interest rates earned or paid on these assets and liabilities. The greater the excess of average interest-earning assets over average interest-bearing liabilities, the more beneficial the impact on net interest income.

Our net interest income increased by \$5.3 million in 2009 as a result of continued growth in interest-earning assets and an improvement in the interest rate spread. Average interest-earning assets (principally loans) increased \$56 million (8%) from 2008. The interest rate spread (the difference between the weighted-average yield on average interest-earning assets and the weighted-average rate paid on average interest-bearing liabilities) increased from 2.69% in 2008 to 3.24% in 2009. This increase in spread was due in part to continued low market interest rates, which enabled us to reduce our cost of funds at a faster pace than the readjustments on our variable rate interest-earning assets. It was also due to replacing higher cost FHLB borrowings with lower cost deposits.

The following table sets forth the weighted-average balances, yields earned and rates paid with respect to the major components of our interest-earning assets and interest-bearing liabilities, and net interest income, for the periods indicated:

WEIGHTED-AVERAGE BALANCES

	YEARS ENDED DECEMBER 31	
	2009	2008
Loans	\$ 749,285,215	\$ 690,206,376
Federal funds sold	713,250	2,517,188
Interest-bearing deposits in banks	6,050,710	8,184,360
FHLB Stock	15,681,286	14,639,688
Total interest-earning assets	771,730,461	715,547,612
Deposits	411,572,197	353,338,683
FHLB borrowings	297,517,905	303,799,714
Senior subordinated notes	175,342	-
Junior subordinated debentures	13,404,000	13,404,000
Total interest-bearing liabilities	722,669,444	670,542,397
Excess of interest-earning assets over interest-bearing liabilities	\$ 49,061,017	\$ 45,005,215

WEIGHTED-AVERAGE YIELDS EARNED AND RATES PAID

Loans	5.69%	6.25%
Federal funds sold	0.27	3.07
Interest-bearing deposits in banks	2.69	4.07
FHLB stock	0.21	3.94
Total interest-earning assets	5.55	6.17
Deposits	1.02	2.40
FHLB borrowings	4.00	4.63
Senior subordinated notes	9.25	-
Junior subordinated debentures	4.48	5.72
Total interest-bearing liabilities	2.31	3.48
Interest rate spread	3.24	2.69
Net yield on interest-earning assets	3.38	2.91

PROVISIONS FOR LOAN LOSSES

We recorded provisions for loan losses of \$120,000 in 2009 versus \$329,000 in 2008. The decrease in provision was attributable to lower net loan growth (loan originations less amortizations and payoffs) of \$35 million in 2009 versus \$59 million in 2008. One consumer loan totaling \$9,000 was charged off in 2009 and we had no delinquent loans as of December 31, 2009. There were no charge offs and two delinquent consumer loans totaling \$15,000 as of December 31, 2008.

OTHER OPERATING INCOME

Other operating income increased \$82,000 due primarily to higher fees from increased levels of transaction accounts.

OTHER OPERATING EXPENSES

The main components of other operating expenses or "overhead" are compensation, office rent and utilities, regulatory assessments and general and administrative expenses. Operating expenses increased \$1,535,000 or 17% from \$8,924,000 in 2008 to \$10,459,000 in 2009. This increase was due primarily to a \$1,044,000 increase in FDIC insurance premiums. In addition, salaries and related benefits increased \$504,000 due primarily to lower deferred loan origination costs as a result of lower loan origination volume.

We employed 70 full-time equivalent employees at December 31, 2009 with an average of 4.6 years of service. The tenure and experience of our employees continue to be a major part of our successful and efficient operations.

Banks measure their ability to manage overhead through an efficiency ratio, i.e., total overhead expenses as a percentage of net interest income and other operating income. Malaga Bank's efficiency ratios of 38.03% in 2009 and 40.50% in 2008 continued to be very favorable compared to the efficiency ratios of our peers, which averaged 75.07% in 2009 and 74.59% in 2008. Another measure of overhead efficiency is the percentage of overhead expense to average assets. Malaga Bank's ratio was 1.32% in 2009 versus 1.22% in 2008, which compared with a peer group average of 2.61% and 2.48% in 2009 and 2008, respectively. Malaga Bank had \$11.3 million in average assets per employee at December 31, 2009 as compared to \$10.7 million in average assets per employee at December 31 2008.

FINANCIAL CONDITION

We continued to grow in 2009, as our total assets increased from \$764 million at December 31, 2008 to \$811 million at December 31, 2009.

LOAN PORTFOLIO

Total gross loans at December 31, 2009 were \$761 million, up \$30 million or 4% from the prior year-end. Our primary lending emphasis continued to be multifamily real estate loans, which comprised 73% of our portfolio at December 31, 2009. The weighted-average yield of the loan portfolio was 5.69% at December 31, 2009 and 6.25% at December 31, 2008.

LOAN LOSS RESERVES AND NON-PERFORMING ASSETS

Our allowance for loan losses, including reserves for losses on commitments for lines of credit and construction loans, totaled \$2.9 million at December 31, 2009 as compared to \$2.8 million at December 31, 2008. We had no non-performing loans at year-end 2009 and one consumer loan in the amount of \$9,000 that was classified as a non-performing asset at year-end 2008. Our allowance for loan losses to total loans outstanding was 0.37% at December 31, 2009 and 0.38% at December 31, 2008.

Management's determination of the adequacy of the allowance for loan losses requires the use of judgment and estimates that may change in the future. Some factors considered by management in determining the adequacy of the allowance include: detailed reviews of individual loans; gross and net charge-offs in the current year; historical loss levels; past due and non-accruing loans; collateral values of properties securing loans; types of loans and risk profiles; and management's analysis of current economic conditions and the resulting impact on the loan portfolio. Changes in the factors used by management to determine the adequacy of the allowance, or the availability of new information, could cause the allowance for loan losses to be increased or decreased. In addition, bank regulatory agencies, as a part of their examination process, may require that additions be made to the allowance for loan losses based on their judgment and estimates.

DEPOSITS

Our deposit strategy in 2009 continued to focus on attracting customer relationships at our branches. Total deposits increased by \$125 million to \$493.8 million at December 31, 2009. During the year non-interest bearing demand deposits increased \$9.4 million to \$36.0 million, lower cost money market and other accounts increased \$19.5 million to \$153.7 million and certificates of deposit increased \$96.2 million to \$304.1 million. The increase in non-interest bearing deposits is primarily due to expansion of our branch system and increased focus on lower cost deposits. At December 31, 2009, we had outstanding certificates of deposit



from the State of California totaling \$48 million bearing interest at a weighted-average rate of .09%. Our weighted-average cost of deposits was .81% at December 31, 2009 compared to 1.62% at December 31, 2008.

FHLB BORROWINGS

Another major source of funding for us is advances from the Federal Home Loan Bank of San Francisco (“FHLB”). As of December 31, 2009, we had FHLB advances totaling \$228 million, all of which were fixed rate, as compared to \$322 million at December 31, 2008. Our FHLB borrowings at December 31, 2009 had an average remaining maturity of 34 months and bore interest at a weighted-average rate of 4.71%. At that date, we had approximately \$151 million of unused FHLB borrowing capacity.

SENIOR SUBORDINATED NOTES

In December 2009, in order to obtain funds to increase the regulatory capital of Malaga Bank, MFC commenced a private offering up to \$10 million principal amount of 9.25% Senior Subordinated Notes at par. As of December 31, 2009, MFC had issued \$7,250,000 of the Notes and had contributed the proceeds to Malaga Bank as capital. In January 2010, MFC issued an additional \$2,750,000 of the Notes, completing the offering. The Notes bear interest at a rate of 9.25% per annum, payable quarterly, and are due and payable on the earlier to occur of December 31, 2016 or upon a change of control. All Notes were issued to related parties of MFC. The Notes are subordinated to all borrowings (other than the outstanding junior subordinated debentures) and may not be prepaid prior to maturity. The increased regulatory capital at Malaga Bank will enable it to pursue growth opportunities and will provide a further cushion against any losses or reserves on its loan portfolio in this recessionary economy.

JUNIOR SUBORDINATED DEBENTURES

From time to time MFC has issued junior subordinated debentures related to issuance of trust-preferred securities by business trusts MFC has formed in order to generate regulatory capital. This capital has a relatively low cost as interest payments on the debentures are deductible for income tax purposes. At December 31, 2009, MFC had \$13.4 million junior subordinated debentures outstanding bearing interest at a weighted-average rate of 4.08% per annum. These debentures mature commencing 2033.

STOCKHOLDERS’ EQUITY AND REGULATORY CAPITAL

Our stockholders’ equity grew by \$8.5 million or 16% to \$63 million at December 31, 2009, from \$54.5 million at December 31, 2008. The increase was due principally to retained earnings of \$9.5 million and proceeds from the exercise of stock options of \$729,000, net of \$1.8 million of dividends paid.

Malaga Bank continues to be “well capitalized” under applicable regulations with its regulatory capital ratios increasing over the previous year. The following table compares Malaga Bank’s actual capital ratios at December 31, 2009 to those required by regulatory agencies for capital adequacy and well capitalized classification purposes:

	Malaga Bank	Minimum Capital Requirements	Well Capitalized Requirements
Tier 1 Leverage Capital Ratio	10.10%	4.00%	5.00%
Tier 1 Risk-Based Capital to Risk-Weighted Assets	16.48	N/A	6.00
Total Risk-Based Capital to Risk-Weighted Assets	17.04	8.00	10.00

SHAREHOLDERS AND STOCK INFORMATION

At December 31, 2009, MFC had 133 shareholders of record. Many of our shareholders purchased stock in connection with the organization of Malaga Bank. Our Board of Directors owns approximately 66% of the total outstanding shares. MFC’s common stock is traded over-the-counter under the symbol MLGF.OB.



MALAGA FINANCIAL CORPORATION AND SUBSIDIARY

CONSOLIDATED BALANCE SHEETS

DECEMBER 31

	2009	2008
ASSETS		
Cash and due from banks	\$ 8,018,848	\$ 7,253,273
Federal funds sold	10,393,888	3,063,828
Cash and cash equivalents	18,412,736	10,317,101
Interest-bearing deposits in banks	5,158,000	5,792,000
Loans receivable, net of allowance for loan loss of \$2,813,644 (2009) and \$2,741,485 (2008)	758,854,119	723,766,069
Accrued interest receivable	3,019,088	3,079,889
Building, office properties and equipment—net	6,288,086	4,411,336
Investment in FHLB stock—at cost	15,696,600	15,428,200
Other assets	3,421,083	1,151,080
TOTAL	\$ 810,849,712	\$ 763,945,675

LIABILITIES AND STOCKHOLDERS' EQUITY

LIABILITIES:

Deposits:

Noninterest-bearing	\$ 36,003,390	\$ 26,581,225
Interest-bearing	457,765,593	342,085,388
Total deposits	493,768,983	368,666,613
FHLB borrowings	228,000,000	322,206,210
Senior subordinated notes	7,250,000	-
Junior subordinated debentures	13,404,000	13,404,000
Accrued interest payable	99,041	211,335
Other liabilities	3,033,232	2,661,599
Deferred tax liability	2,296,177	2,262,928
Total liabilities	747,851,433	709,412,685

COMMITMENTS AND CONTINGENCIES (Note 4)

STOCKHOLDERS' EQUITY:

Common stock, \$.001 par value—authorized, 20,000,000 shares; outstanding 5,799,212 shares (2009) and 5,733,712 shares (2008)	5,799	5,734
Additional paid-in capital	13,692,353	12,876,333
Retained earnings	49,300,127	41,650,923
Total stockholders' equity	62,998,279	54,532,990
TOTAL	\$ 810,849,712	\$ 763,945,675

See notes to consolidated financial statements.

MALAGA FINANCIAL CORPORATION AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF OPERATIONS

YEARS ENDED DECEMBER 31

	2009	2008
INTEREST INCOME:		
Interest on loans	\$ 42,660,130	\$ 43,130,921
Interest on other investments	197,732	986,939
Total interest income	42,857,862	44,117,860
INTEREST EXPENSE:		
Deposits	4,204,247	8,464,348
Borrowings	11,909,832	14,057,521
Senior subordinated notes	16,219	-
Junior subordinated debentures	600,932	766,279
Total interest expense	16,731,230	23,288,148
NET INTEREST INCOME	26,126,632	20,829,712
PROVISION FOR LOAN LOSSES	120,400	329,270
NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES	26,006,232	20,500,442
OTHER OPERATING INCOME	508,469	426,182
OTHER OPERATING EXPENSE:		
Compensation	5,245,727	4,741,704
Office rent and utilities	960,125	934,455
Professional services	144,733	235,440
Data processing	675,686	534,291
Deposit insurance premiums	1,166,867	122,541
Depreciation and amortization	383,642	243,987
General and administrative	1,882,387	2,111,503
Total other operating expense	10,459,167	8,923,921
INCOME BEFORE INCOME TAXES	16,055,534	12,002,703
INCOME TAX EXPENSE	6,561,855	4,926,354
NET INCOME	\$ 9,493,679	\$ 7,076,349
BASIC EARNINGS PER SHARE	\$ 1.65	\$ 1.24
DILUTED EARNINGS PER SHARE	\$ 1.64	\$ 1.24

See notes to consolidated financial statements.

MALAGA FINANCIAL CORPORATION AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY

FOR THE YEARS ENDED DECEMBER 31, 2009 AND 2008

	Common Stock		Additional Paid-in Capital	Retained Earnings	Comprehensive Income	Total Stockholders' Equity
	Number of Shares	Amount				
BALANCE—January 1, 2008	5,661,768	\$ 5,662	\$ 12,224,482	\$ 36,402,929		\$ 48,633,073
Net income				7,076,349	\$ 7,076,349	7,076,349
Cash dividends				(1,828,355)		(1,828,355)
Common stock repurchased	(24,847)	(25)	(236,021)			(236,046)
Stock options exercised	96,791	97	817,604			817,701
Stock options compensation expense			46,668			46,668
Tax benefit from exercise of stock options			23,600			23,600
Total comprehensive income					\$ 7,076,349	
BALANCE—December 31, 2008	5,733,712	5,734	12,876,333	41,650,923		54,532,990
Net income				9,493,679	\$ 9,493,679	9,493,679
Cash dividends				(1,844,475)		(1,844,475)
Stock options exercised	65,500	65	728,652			728,717
Stock options compensation expense			61,668			61,668
Tax benefit from exercise of stock options			25,700			25,700
Total comprehensive income					\$ 9,493,679	
BALANCE—December 31, 2009	5,799,212	\$ 5,799	\$ 13,692,353	\$ 49,300,127		\$ 62,998,279

See notes to consolidated financial statements.

MALAGA FINANCIAL CORPORATION AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF CASH FLOWS

FOR YEARS ENDED DECEMBER 31

	2009	2008
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	\$ 9,493,679	\$ 7,076,349
Adjustments to reconcile net income to net cash provided by operating activities:		
Amortization of deferred loan fees—net of costs	187,805	441,401
FHLB stock dividends	-	(748,000)
Provision for loan losses	120,400	329,270
Loss on sale of equipment	-	37
Tax (benefit) related to exercise of stock options	(25,700)	(23,600)
Depreciation and amortization	383,643	243,987
Deferred income taxes	33,249	(53,528)
Stock option compensation expense	61,668	46,668
Net (increase) decrease in accrued interest receivable and other assets	(2,209,202)	269,235
Net increase (decrease) in accrued interest payable and other liabilities	276,975	(122,337)
Net cash provided by operating activities	8,322,517	7,459,482
CASH FLOWS FROM INVESTING ACTIVITIES:		
Net decrease in interest-bearing deposits in banks	634,000	354,142
Net increase in loans receivable	(35,396,255)	(59,421,250)
Purchase of FHLB stock	(268,400)	(1,240,400)
Purchase of premises and equipment	(2,260,393)	(2,286,513)
Net cash used in investing activities	(37,291,048)	(62,594,021)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Net increase in deposits	125,102,370	17,826,855
Net (decrease) increase in FHLB borrowings	(94,206,210)	36,436,228
Proceeds from issuance of long-term debt	7,250,000	-
Stock repurchased	-	(236,046)
Dividends paid	(1,836,411)	(1,818,248)
Proceeds from exercise of stock options	728,717	817,701
Tax effect related to exercise of stock options	25,700	23,600
Net cash provided by financing activities	37,064,166	53,050,090
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	8,095,635	(2,084,449)
CASH AND CASH EQUIVALENTS—Beginning of year	10,317,101	12,401,550
CASH AND CASH EQUIVALENTS—End of year	\$ 18,412,736	\$ 10,317,101
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION		
Cash paid during the year for:		
Interest	\$ 16,843,524	\$ 23,421,181
Income taxes	\$ 6,639,000	\$ 5,275,000
SUPPLEMENTAL SCHEDULE OF NONCASH FINANCING ACTIVITIES		
Dividend payable	\$ 481,754	\$ 473,690

See notes to consolidated financial statements.

MALAGA FINANCIAL CORPORATION AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS AS OF AND FOR THE YEARS ENDED DECEMBER 31, 2009 AND 2008

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Principles of Consolidation and Presentation—

The consolidated financial statements include the accounts of Malaga Financial Corporation (“MFC”) and its wholly owned subsidiary, Malaga Bank FSB (the “Bank”) (collectively, the “Company”). All intercompany balances and transactions have been eliminated in consolidation.

MFC was formed in 2002, to operate as a holding company for the Bank. In 2003, MFC and the Bank completed a holding company reorganization in which MFC acquired all of the outstanding capital stock of the Bank and the shareholders of the Bank became shareholders of MFC.

*Nature of Operations—*The Company’s primary operations are related to traditional banking activities, including the acceptance of deposits and the lending and investing of money. The Company’s customers consist of individuals and small-to-midsize businesses located primarily in the Palos Verdes Peninsula and adjoining areas of Los Angeles and Orange Counties. The Company operates through five locations, four branches and one loan center, including its headquarters located in the city of Palos Verdes Estates.

*Use of Estimates in the Preparation of Consolidated Financial Statements—*The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States of America (“GAAP”) requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, 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. Significant estimates include estimates of the allowance for loan losses.

*Cash and Cash Equivalents—*Cash and cash equivalents include cash and due from banks and overnight federal funds sold, all of which have original maturities of less than 90 days at the time of purchase. The Company is required to maintain reserve balances with the Federal Reserve Bank under the Federal Reserve Act. The reserve balance was approximately \$2,234,000

and \$1,685,000 at December 31, 2009 and 2008, respectively.

*Interest-Bearing Deposits in Banks—*Interest-bearing deposits in banks mature within one year and are carried at cost.

*Investment Securities—*Debt securities that management has the positive intent and ability to hold to maturity are classified as “held to maturity” and recorded at amortized cost. Securities not classified as held to maturity or trading, including equity securities with readily determinable fair values, are classified as “available for sale” and recorded at fair value, with unrealized gains and losses excluded from earnings and reported in other comprehensive income, unless there is other-than-temporary impairment on the securities. Credit related declines in the fair value of held-to-maturity and available-for-sale securities below their cost that are deemed to be other-than-temporary are reflected in earnings as realized losses, and there were no such other-than-temporary impairment in 2009 or 2008.

The Company did not own any investment securities as of December 31, 2009 or 2008.

Investment in the stock of the Federal Home Loan Bank (“FHLB”) is not subject to classification in the aforementioned categories as it is not a readily marketable security and it is carried at cost.

*Loans Receivable—*Loans receivable is stated at unpaid principal balances, plus premiums on purchased loans, less the allowance for loan losses and unamortized deferred loan origination fees and costs. Loan origination fees, net of certain direct origination costs, are deferred and recognized as an adjustment of the loan yield using the interest method. Premiums on loans are amortized to interest income using the interest method over the remaining period to contractual maturity. The accrual of interest on loans is discontinued at the time the loan is 90 days delinquent, unless the credit is well secured and in the process of collection. Loans are placed on nonaccrual or charged off at an earlier date, if collection of principal or interest is considered doubtful. All interest accrued but not collected for loans that are placed on nonaccrual or charged off are reversed against interest income. The interest on these loans is accounted for on the cash-basis or cost-recovery method, until qualifying for return

to accrual. Loans are returned to accrual status when all the principal and interest amounts contractually due are brought current and future payments are reasonably assured.

Loan fees and certain direct loan origination costs are deferred, and the net fee or cost is recognized as an adjustment to interest income using the interest method over the contractual life of the loans. Other loan fees and charges, representing service costs for prepayment of loans, for delinquent payments or for miscellaneous loan services, are recorded as income when collected.

The Company's lending is concentrated in surrounding areas of Los Angeles and Orange Counties, and substantially, all of the Company's loans have adjustable interest rates.

Allowance for Loan Losses—Management's periodic evaluation of the adequacy of the allowance is based on the Company's past loan loss experience, known and inherent risks in the portfolio, adverse situations that may affect borrowers' ability to repay, estimated value of underlying collateral, and current economic conditions. Although management believes that the level of the allowance as of December 31, 2009, is adequate to absorb known and inherent risks in the loan portfolio, no assurances can be given that adverse future economic conditions will not lead to higher amounts of problem loans, provisions for credit losses, or charge-offs.

A loan is considered impaired when it is probable that the Company will be unable to collect all amounts due according to the contractual terms of the loan. Impaired loans are measured based on the present value of expected future cash flows discounted at the loans' effective interest rates or the fair value of the collateral, if the loans are collateral dependent. If the fair value of an impaired loan is less than the carrying value, a specific reserve is included in the allowance for loan losses. Impairment is measured on a loan-by-loan basis for construction and commercial loans. Large groups of smaller balance homogenous loans are collectively evaluated for impairment.

Building, Office Properties and Equipment—Building, leasehold improvements, office properties and equipment are carried at cost, less accumulated depreciation and amortization. The cost of the building is depreciated using the straight-line method over 39 years. Office properties and equipment are depreciated using the straight-line method over the estimated useful lives of the assets (three to seven years). The cost of leasehold improvements is being amortized using the straight-line method over the terms of the related leases or the estimated

lives of the improvements, whichever is shorter.

Real Estate Owned—Real estate acquired through foreclosure is stated at the lower of cost or fair value, less estimated selling costs. Any subsequent holding costs and gains or losses on disposition of real estate owned are recorded in current operations. Substantial capital improvements are recorded as additions to cost of the real estate. Reductions in fair value identified subsequent to foreclosure are recognized in an allowance for losses on real estate owned. The Company did not have any real estate owned as of December 31, 2009 or 2008.

Impairment of Long-Lived Assets—Long-lived assets are reviewed at least annually for impairment. When impairment is indicated, the amount of impairment is the excess of the asset's net book value over its fair value. Furthermore, long-lived assets to be disposed of are reported at the lower of historical cost or fair value, less cost to sell.

Income Taxes—The Company utilizes the liability method in accounting for income taxes. Deferred tax assets or liabilities shown on the balance sheets reflect the tax effects of differences between the tax bases of assets and liabilities and their reported amounts in the financial statements.

Earnings Per Share ("EPS")—Basic earnings per share are determined by dividing net income by the average number of shares of common stock outstanding, while diluted earnings per share are determined by dividing net income by the average number of shares of common stock outstanding, adjusted for the dilutive effect of common stock equivalents.

Dividends—The Company paid dividends of \$0.32 per share of common stock in each of 2009 and 2008.

Stock-Based Compensation—The Company issued stock-based compensation to certain employees, officers, and directors. On January 1, 2006, the Company adopted Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC" or "Codification") 718-10 (formerly FASB Statement No. 123R), *Share-Based Payment*, for stock-based compensation. ASC 718-10 allows for two alternative transition methods. The Company follows the modified prospective method, which requires application of the new statement to new awards and to awards modified, repurchased, or cancelled after the required effective date. Accordingly, prior-period amounts have not been restated. Additionally, compensation cost for the portion of awards for which the requisite service has not been rendered that are outstanding as of January 1, 2006, are recognized as the

requisite services are rendered on or after January 1, 2006. The compensation cost of that portion of awards is based on the grant-date fair value of those awards as calculated for pro forma disclosures under the original ASC 718-10.

Recent Accounting Pronouncements—In June 2009, the FASB issued FASB Statement No. 168, The FASB ASC and the Hierarchy of Generally Accepted Accounting Principles, a replacement of FASB Statement No. 162, which is now codified in FASB ASC Topic 105, *The Hierarchy of Generally Accepted Accounting Principles*. The FASB Codification will become the source of authoritative U.S. GAAP recognized by the FASB to be applied by nongovernmental entities. Rules and interpretive releases of the Securities and Exchange Commission (“SEC”) under authority of federal securities laws are also sources of authoritative GAAP for SEC registrants. On the effective date of this statement, the Codification will supersede all then-existing non-SEC accounting and reporting standards. All other nongrandfathered non-SEC accounting literature not included in the Codification will become nonauthoritative. ASC Topic 105 is effective for interim and annual financial statements issued after September 15, 2009. The adoption of ASC Topic 105 did not have a material impact on the consolidated financial statements.

FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes — an interpretation of FASB Statement No. 109* (incorporated into, codified, and referred to herein as “amendments to FASB ASC Topic 740”) prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. This Interpretation also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure and transition. This new guidance is effective for fiscal years beginning after December 15, 2008. The Company adopted these amendments to FASB ASC 740 effective January 1, 2009. The adoption of this new accounting guidance did not have a material impact on the Company’s consolidated financial statements.

In April 2009, the FASB issued ASC 820-10-65-4 (formerly FSP FASB Statement No. 157-4), *Determining Fair Value When the Volume and Level of Activity for the Asset or Liability Have Significantly Decreased and Identifying Transactions That Are Not Orderly*, to provide additional guidance for estimating fair value in accordance with ASC Topic 820, *Fair Value Measurements and Disclosures*, when the volume and level of activity for the asset or

liability have significantly decreased. As some constituents indicated that ASC Topic 820 (FASB Statement No. 157) and ASC 820-10-35 (FSP FASB Statement No. 157-3), *Determining the Fair Value of a Financial Asset When the Market for That Asset Is Not Active*, did not provide sufficient guidance on how to determine whether a market for a financial asset that historically was active, is no longer active, and whether a transaction is not orderly. Therefore, this ASC 820-10-65-4 includes guidance on identifying circumstances that indicate a transaction is not orderly. We adopted ASC 820-10-65-4 in the second quarter of 2009 and the adoption did not have a material impact on the consolidated financial statements.

In April 2009, the FASB issued ASC 320-10-65 (formerly FSP FASB Statement No. 115-2 and FASB Statement No. 124-2, *Recognition and Presentation of Other-Than-Temporary Impairments*), which amends the other-than-temporary impairment (“OTTI”) guidance for debt securities to make the guidance more operational and to improve the presentation and disclosure of OTTI on debt and equity securities in the financial statements. This ASC 320-10-65 does not amend existing recognition and measurement guidance related to OTTI of equity securities. This issuance also requires increased and more timely disclosures sought by investors regarding expected cash flows, credit losses, and an aging of securities with unrealized losses. ASC 320-10-65 is effective for interim and annual reporting periods ending after June 15, 2009. The adoption of ASC 320-10-65 did not have a material impact on the consolidated financial statements.

In August 2009, the FASB issued Accounting Standards Update (“ASU”) 2009-05, *Fair Value Measurements and Disclosures (Topic 820): Measuring Liabilities at Fair Value*, which provides guidance on measuring the fair value of liabilities under FASB ASC Topic 820. ASU 2009-05 clarifies that the unadjusted quoted price for an identical liability, when traded as an asset in an active market is a Level 1 measurement for the liability and provides guidance on the valuation techniques to estimate fair value of a liability in the absence of a Level 1 measurement. ASU 2009-05 is effective for the first interim or annual reporting period beginning after its issuance. The adoption of ASU 2009-05 did not have a material effect on the consolidated financial statements.

On May 28, 2009, the FASB issued FASB Statement No. 165, *Subsequent Events* (codified and referred to herein as “FASB ASC Topic 855”). FASB ASC Topic 855 establishes general standards

of accounting for and disclosure of events that occur after the balance sheet date but before financial statements are issued or are available to be issued. Although there is new terminology, the standard is based on the same principles as those that currently exist in the American Institute of Certified Public Accountants auditing standards. The standard, which includes a new required disclosure of the date through which an entity has evaluated subsequent events, is effective for interim and annual periods ending after June 15, 2009. ASC Topic 855 was subsequently amended through the issuance of ASU 2010-09, *Subsequent Events*, on February 24, 2010 which became effective immediately upon issuance. Among other changes, this amendment provides a definition of revised financial statements and confirms the period over which entities are required to evaluate subsequent events. The Company adopted ASU 2010-09 effective December 31, 2009. The adoption of this standard, inclusive of update ASU 2010-09, did not result in a material impact on the Company's consolidated financial statements.

2. LOANS RECEIVABLE

At December 31, 2009 and 2008, loans receivable are summarized as follows:

Description	2009	2008
Residential mortgage loans—multifamily	\$ 558,856,332	\$ 537,288,081
Residential mortgage loans—single family	139,337,847	118,979,400
Commercial loans	50,288,747	49,704,344
Construction loans	6,547,500	19,590,300
Business banking loans	5,853,606	3,858,045
Land loans	-	1,500,000
Consumer loans	582,602	452,463
	761,466,634	731,372,633
Less (plus):		
Allowance for loan losses—general	2,813,644	2,732,244
Allowance for loan losses—specific	-	9,241
Construction loans in process	2,410,540	7,269,932
Deferred loan costs—net of fees	(2,611,669)	(2,404,853)
	2,612,515	7,606,564
	\$ 758,854,119	\$ 723,766,069

As of December 31, 2009 and 2008, loans with adjustable rates of interest (including loans with an initial fixed rate for 1 to 10 years which subsequently convert to adjustable rate) totaled \$756.0 million and \$725.8 million, respectively, and loans with fixed rates of interest were \$5.5 million and \$5.6 million, respectively. Adjustable-rate loans are generally indexed to the FHLB's Eleventh District Cost of Funds Index, 12-Month Constant Maturity Index, London Interbank Offered Rate ("LIBOR") or Prime Rate and are subject to limitations on the timing and extent of adjustment. Most adjustable rate loans adjust within six months of changes in the index.

At December 31, 2009 and 2008, real estate loans aggregating \$624.8 million and \$584.3 million, respectively, were pledged as collateral against FHLB borrowings and real estate loans totaling \$74.0 million and \$72.5 million were pledged to secure deposits held by the state of California, respectively. In addition, construction loans totaling \$4.0 million and home equity lines of credit totaling \$20.2 million were pledged as collateral to the Federal Reserve Bank discount window at December 31, 2009.

Activity in the allowance for loan losses and unfunded loan commitments for the years ended December 31, 2009 and 2008 is summarized as follows:

	2009	2008
Allowance for loan losses:		
Balance—beginning of year	\$ 2,741,485	\$ 2,433,285
Provision for loan losses	120,400	308,200
Charge-offs	(9,241)	-
Transfer to unfunded loan commitments	(39,000)	-
Balance—end of year	\$ 2,813,644	\$ 2,741,485
Allowance for unfunded loan commitments:		
Balance—beginning of year	\$ 60,800	\$ 39,730
Provision for unfunded loan commitments	39,000	21,070
Balance—end of year	\$ 99,800	\$ 60,800

The allowance for unfunded loan commitments is primarily related to undisbursed funds on construction loans and lines of credit. The Company evaluates credit risk associated with the loan portfolio at the same time it evaluates credit risk associated

with the unfunded loan commitments. However, the allowances necessary for the commitments are reported separately in other liabilities in the accompanying consolidated balance sheets, and not as part of the allowance for loan losses, as presented above.

There were two loans in the amount of \$3 million considered to be impaired but accruing interest with no specific reserves at December 31, 2009. There was one non-accrual consumer loan in the amount of \$9,241 considered impaired with a specific reserve of \$9,241 at December 31, 2008. The average recorded investment in impaired loans during the years ended December 31, 2009 and 2008, was \$247,522 and \$770, respectively. Interest income of \$14,759 and \$903 was recognized on impaired loans during the years ended December 31, 2009 and 2008, respectively, all of which was received in cash.

The Bank is subject to numerous lending-related regulations and may not make real estate loans to one borrower in excess of 15% of its unimpaired capital and surplus, except for loans not to exceed \$500,000. This 15% limitation resulted in a dollar limitation of approximately \$12,693,000 at December 31, 2009.

In the ordinary course of business, the Company has granted loans to certain executive officers and directors and the companies with which they are associated. In management's opinion, such loans and commitments to lend were made under terms and prevailing interest rates that are consistent with the Company's normal lending policies. Interest income from loans to executive officers and directors was \$545,388 and \$525,932 in 2009 and 2008, respectively.

A summary of related-party loan activities for the years ended December 31, 2009 and 2008 is as follows:

	2009	2008
Beginning balance	\$ 8,227,012	\$ 8,198,723
Credit granted—including renewals	731,325	3,522,972
Less: Construction loans in progress	-	(439,417)
Repayments	(3,576,418)	(3,055,266)
Ending balance	\$ 5,381,919	\$ 8,227,012

3. BUILDING, OFFICE PROPERTIES AND EQUIPMENT

Building, office properties and equipment at December 31, 2009 and 2008, are summarized as follows:

	2009	2008
Land	\$ 1,275,364	\$ 1,275,364
Building	3,562,029	-
Leasehold improvements	1,735,802	1,693,575
Equipment	1,551,953	1,441,206
Furniture and fixtures	625,076	536,970
Construction in progress (includes branch building in 2008)	44,400	1,721,646
	8,794,624	6,668,761
Accumulated depreciation and amortization	(2,506,538)	(2,257,425)
	\$ 6,288,086	\$ 4,411,336

Construction in progress in 2008 consisted primarily of costs associated with the building of a new retail branch in Torrance, California. The new branch was completed in the third quarter of 2009.

Depreciation and amortization expense for the years ended December 31, 2009 and 2008, was \$383,643 and \$243,987, respectively.

4. COMMITMENTS AND CONTINGENCIES

Off-Balance-Sheet Financial Instruments—The Company is a party to financial instruments with off-balance-sheet risk, in the normal course of business, to meet the financing needs of its customers. These financial instruments include commitments to extend credit, standby letters of credit, and financial guarantees. The Company's maximum exposure to credit loss under standby letters of credit, financial guarantees, and commitments to extend credit is represented by the contractual amount of those instruments. The Company uses the same credit policies in making commitments and conditional obligations as it does for on-balance-sheet instruments.

The Company requires collateral to support financial instruments when it is deemed necessary. The Company evaluates each customer's creditworthiness on a case-by-case basis. The amount of collateral obtained upon extension of credit is based on management's credit evaluation of the counterparty. Collateral held varies but generally includes

real estate or deposits held in the Company.

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses, and may require payment of a fee. Some of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The Company had commitments to originate loans of \$3.2 million and \$6.6 million, undisbursed funds for construction loans of \$2.4 million and \$7.3 million, and undrawn lines of credit previously granted of approximately \$30.8 million and \$34.8 million at December 31, 2009 and 2008, respectively.

From time to time, the Company enters into certain types of contracts that contingently require the Company to indemnify parties against third-party claims and other obligations customarily indemnified in the ordinary course of the Company's business. The terms of such obligations vary, and generally, a maximum obligation is not explicitly stated. Therefore, the overall maximum amount of the obligations cannot be reasonably estimated. The most significant of these contracts relate to certain agreements with the Company's officers and directors under which the Company may be required to indemnify such persons for liabilities arising out of their performance of services for the Company. Historically, the Company has not been subject to indemnification claims and no liabilities have been recorded for these obligations on its balance sheet as of December 31, 2009 and 2008.

Collateralized standby letters of credit and financial guarantees written are conditional commitments issued by the Company to guarantee the performance of a customer to a third party. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to customers. Management does not anticipate any material losses as a result of these transactions. Loan commitments collateralized by standby letters of credit and financial guarantees written were \$22,400 and \$27,500 at December 31, 2009 and 2008, respectively.

Leases—The Company leases office premises under operating leases that expire at various dates through September 24, 2022. Rental expense was \$639,178 and \$656,229 for the years ended December 31, 2009 and 2008, respectively. The projected

minimum rental payments under the terms of the leases at December 31, 2009, are as follows:

Years Ending December 31	
2010	\$ 599,376
2011	599,376
2012	599,376
2013	599,376
2014	401,866
Thereafter	1,382,031
	\$ 4,181,401

5. DEPOSITS

Deposit balances and the weighted-average interest rates for each category at December 31, 2009 and 2008, are summarized as follows:

	2009		2008	
	Interest Rate	Amount	Interest Rate	Amount
Demand deposits	0.00%	\$ 36,003,390	0.00%	\$ 26,581,225
NOW accounts	0.21	42,785,000	0.45	32,507,448
Passbooks	0.26	17,658,274	1.06	12,523,356
Money market accounts	0.81	93,219,204	1.14	89,151,457
Certificates of deposit—non jumbo	1.19	84,946,473	2.35	76,997,446
Certificates of deposit—jumbo	0.96	219,156,642	1.92	130,905,681
		\$ 493,768,983		\$ 368,666,613

Jumbo certificates of deposit are certificates of deposit with balances of \$100,000 or more.

Certificate of deposit maturities at December 31, 2009, are summarized as follows:

Years Ending December 31	
2010	\$ 287,900,965
2011	15,655,085
2012	350,604
2013	-
2014	196,461
	\$ 304,103,115

As of December 31, 2009 and 2008, the Company had certificates of deposit from the State of California Treasurer's Office of \$48,000,000.

6. FHLB BORROWINGS

A primary alternate funding source for the Company is a credit line with the FHLB of San Francisco of up to 50% of the Company's total assets. Interest is payable monthly at a weighted-average rate of 4.71% as of December 31, 2009. The FHLB borrowings are collateralized by real estate loans (see Note 2) and the capital stock of the FHLB owned by the Company.

Maturities of FHLB borrowings at December 31, 2009, are summarized as follows:

Years Ending December 31	
2010	\$ 44,000,000
2011	62,000,000
2012	32,000,000
2013	35,000,000
2014	14,000,000
Thereafter	41,000,000
	\$ 228,000,000

7. SENIOR SUBORDINATED NOTES

In December 2009, in order to obtain funds to increase the regulatory capital of the Bank, MFC commenced a private offering up to \$10 million principal amount of 9.25% Senior Subordinated Notes at par. As of December 31, 2009, MFC had issued \$7,250,000 of the Notes and had contributed the proceeds to the Bank as capital. The Notes are due on the earlier to occur of December 31, 2016, or upon a change of control, are subordinated to all borrowings of MFC (other than the outstanding junior subordinated debentures) and may not be prepaid prior to maturity. All Notes were issued to related parties of MFC.

8. JUNIOR SUBORDINATED DEBENTURES

MFC has from time to time issued junior subordinated debentures related to concurrent issuances of trust-preferred securities by business trusts formed by MFC in order to generate regulatory capital for the Bank. This capital has a relatively low cost as interest payments on the debentures are

deductible for income tax purposes.

In June 2003, MFC issued \$5,155,000 of junior subordinated debentures to PVP Statutory Trust I. This trust purchased the debentures with the proceeds of the sale of its common trust securities to MFC for \$155,000 and trust-preferred securities in a private placement for \$5,000,000. The debentures and trust-preferred securities have generally identical terms, including that they mature in June 2033, have been redeemable at par at MFC's option since June 2008, and require quarterly distributions/interest payments at a fixed rate of 5.67% per annum through June 2008 and thereafter at a variable rate that adjusts quarterly at the three-month LIBOR rate, plus 3.10%. The interest rate on the debentures was 3.35% per annum at December 31, 2009.

In January 2005, MFC issued \$2,578,000 of junior subordinated debentures to PVP Statutory Trust II. This trust purchased the debentures with the proceeds of the sale of its common trust securities to MFC for \$78,000 and trust-preferred securities in a private placement for \$2,500,000. The debentures and trust-preferred securities have generally identical terms, including that they mature in March 2035, are redeemable at par at MFC's option commencing March 2010, and require quarterly distributions/interest payments at a rate that adjusts quarterly at the three-month LIBOR rate, plus 1.77%. The interest rate on the debentures was 2.02% per annum at December 31, 2009.

In January 2005, MFC also issued \$5,671,000 of junior subordinated debentures to PVP Statutory Trust III. This trust purchased the debentures with the proceeds of the sale of its common trust securities to MFC for \$171,000 and trust-preferred securities in a private placement for \$5,500,000. The debentures and trust-preferred securities have generally identical terms, including that they mature in March 2035, are redeemable at par at MFC's option commencing March 2010, and require quarterly distributions/interest payments at a fixed rate of 5.67% through March 2010 and, thereafter, at a variable rate that adjusts quarterly at the three-month LIBOR rate, plus 1.77%. The interest rate on the debentures was 5.67% per annum at December 31, 2009.

MFC's investment in the common trust securities of the trusts is included in "other assets" on its balance sheets. MFC has unconditionally guaranteed distributions on, and payments on

liquidation and redemption of, all of these trust-preferred securities.

9. INCOME TAXES

A summary of income tax expense (benefit) for the years ended December 31, 2009 and 2008 is as follows:

	2009	2008
Current:		
State	\$ 1,680,725	\$ 1,195,069
Federal	4,847,881	3,784,813
	6,528,606	4,979,882
Deferred:		
State	(7,843)	49,574
Federal	41,092	(103,102)
	33,249	(53,528)
	\$ 6,561,855	\$ 4,926,354

The components of the net deferred tax (liability) asset at December 31, 2009 and 2008 are as follows:

	2009	2008
FEDERAL		
Deferred tax liabilities:		
Loan fees/costs	\$ (2,001,278)	\$ (1,897,702)
FHLB dividends	(1,309,810)	(1,309,810)
Depreciation	(165,227)	-
Other	(41,661)	(51,738)
Gross deferred tax liability	(3,517,976)	(3,259,250)
Deferred tax assets:		
California franchise tax	804,191	639,321
Depreciation	-	32,862
Bad debt and loan loss deduction	990,571	932,105
Other	111,579	84,419
Gross deferred tax asset	1,906,341	1,688,707
Net deferred tax liability	\$ (1,611,635)	\$ (1,570,543)

	2009	2008
STATE		
Deferred tax liabilities:		
Loan fees /costs	\$ (638,055)	\$ (605,032)
FHLB dividends	(417,597)	(417,597)
Depreciation	-	-
Other	(13,282)	(5,787)
Gross deferred tax liability	(1,068,934)	(1,028,416)
Deferred tax assets:		
California franchise tax	-	-
Depreciation	35,790	22,648
Bad debt and loan loss deduction	315,817	297,177
Other	32,785	16,206
Gross deferred tax asset	384,392	336,031
Net deferred tax liability	\$ (684,542)	\$ (692,385)

A reconciliation of total income tax expense for 2009 and 2008 to the expected tax expense computed by applying the statutory corporate income tax rate to pretax income is as follows for the year ended December 31:

	2009		2008	
	Amount	Percent	Amount	Percent
Tax expense at statutory rates	\$ 5,619,437	35%	\$ 4,200,946	35%
State franchise tax—net of federal benefit	1,087,373	7	821,465	7
Other	(144,955)	(1)	(96,057)	(1)
	\$ 6,561,855	41%	\$ 4,926,354	41%

Effective January 1, 2009, the Company adopted the authoritative guidance for uncertainty in income taxes included in FASB ASC Topic 740, *Income Taxes* (formerly, (“FASB”) Interpretation No. 48), as amended by Accounting Standards Update (“ASU”) 2009-06, *Implementation Guidance on Accounting for Uncertainty in Taxes and Disclosures Amendments for Nonpublic Entities*. This guidance requires the Company to determine whether a tax position of the Company is more likely than not to be sustained upon examination by the applicable taxing authority, including the resolution of any related appeals or litigation processes, based on the technical merits of the position. The tax benefit to be recognized is measured as the

largest amount of benefit that is greater than 50% likely of being realized upon ultimate settlement, which could result in the Company recording a tax liability. The Company reviews and evaluates tax positions in its major jurisdictions and determines whether or not there are uncertain tax positions that require financial statement recognition. Based on this review, the Company has determined the major tax jurisdictions as where the Company is organized and where the Company makes investments as U.S. federal, and state; however, no reserves for uncertain tax positions were required to have been recorded as a result of the adoption of such guidance for any of the Company's open tax years. The Company files income tax returns in the U.S. federal jurisdiction and in California. The Company is no longer subject to income tax examinations by taxing authorities for years before 2006 for its federal filings and 2005 for its California filings. The Company is additionally not aware of any tax positions for which it is reasonably possible that the total amounts of unrecognized tax benefits will change materially in the next 12 months. As a result, no income tax liability or expense has been recorded in the accompanying financial statements relating to uncertain tax positions. The Company accounts for interest related to uncertain tax positions as part of our provision for federal and state income taxes.

10. REGULATORY CAPITAL

The Bank is subject to various regulatory capital requirements administered by the federal banking agencies. Failure to meet minimum capital requirements can initiate certain mandatory, and possibly additional discretionary, actions by the regulators

that, if undertaken, could have a direct material effect on the Company's and the Bank's financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Bank must meet specific capital guidelines that involve quantitative measures of their assets, liabilities, and certain off-balance-sheet items that are calculated under regulatory accounting practices. The capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weighting, and other factors. Prompt corrective action provisions are not applicable to bank holding companies.

Quantitative measures established by regulation to ensure capital adequacy require the Bank to maintain minimum amounts and ratios (set forth in the table below) of total and Tier 1 capital (as defined in the regulations) to risk-weighted assets (as defined) and of Tier 1 capital (as defined) to average assets (as defined). As of December 31, 2009 and 2008, the Bank met all applicable regulatory capital requirements.

As of December 31, 2009 and 2008, the most recent notification from the Office of Thrift Supervision categorized the Bank as "well capitalized" under the regulatory framework for prompt corrective action. To be categorized as "well capitalized", the Bank must maintain minimum total risk-based, Tier 1 risk-based and Tier 1 leverage ratios as set forth in the table below.

There are no conditions or events since that notification which management believes have changed the Bank's category.

	Actual		For Capital Adequacy Purposes		Applicable Federal Regulatory Requirements To Be Categorized As Well Capitalized Under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
As of December 31, 2009:						
Total capital to risk-weighted assets:	\$ 84,620,814	17.04%	\$ 39,720,886	8.00%	\$ 49,651,107	10.00%
Core capital to adjusted tangible assets:	81,807,170	10.10	32,399,160	4.00	40,498,950	5.00
Tangible capital to adjusted tangible assets:	81,807,170	10.10	12,149,685	1.50	N/A	N/A
Tier 1 capital to risk-weighted assets:	81,807,170	16.48	N/A	N/A	29,790,664	6.00
As of December 31, 2008:						
Total capital to risk-weighted assets:	\$ 67,366,151	13.74%	\$ 39,212,888	8.00%	\$ 49,016,110	10.00%
Core capital to adjusted tangible assets:	64,633,907	8.49	30,462,198	4.00	38,077,748	5.00
Tangible capital to adjusted tangible assets:	64,633,907	8.49	11,423,324	1.50	N/A	N/A
Tier 1 capital to risk-weighted assets:	64,633,907	13.19	N/A	N/A	29,409,666	6.00

11. STOCK OPTION PLANS

The Company has in effect two stock option plans, the 2003 Stock Option Plan (the “2003 Plan”) and the 2007 Director Stock Option Plan (the “2007 Director Plan”). The 2003 Plan authorizes the Company to issue to officers, directors, employees, and consultants of the Company up to 348,115 shares of the common stock upon exercise of options. The exercise price of the options granted under the 2003 Plan may not be less than the fair market value of the common stock on the date of grant and the term of any option may not exceed 10 years.

Under the 2007 Director Plan, the Company may issue up to 300,000 shares of common stock pursuant to automatic grants to each director on January 1 of each year of an option to purchase 9,200 shares of common stock. The exercise price of each option granted under the 2007 Director Plan is the fair market value of the common stock on the date the option is granted. Each option granted under the 2007 Director Plan vests one year from the date the option was granted and expires five years from the date of grant, subject to earlier termination if the optionee ceases to be a director.

Pursuant to the adoption of ASC Topic 718, stock-based compensation expense was \$61,668 and \$46,668 for 2009 and 2008, respectively, which decreased the year’s income before taxes by such amount and its effect on basic and diluted earnings per share, was negligible. Cash provided by operating activities decreased by \$25,700 and \$23,600 for 2009 and 2008, respectively and cash provided by financing activities increased by identical amounts for both 2009 and 2008, related to excess tax benefits from stock-based arrangements.

The following table presents the status of all optioned shares and exercise price amounts during the year ended December 31, 2009:

	Number of Options	Weighted-Average Exercise Price	Weighted-Average Term	Aggregate Intrinsic Value
Outstanding—beginning of year	279,599	\$ 10.48		
Granted	55,200	10.10		
Exercised (1)	(65,504)	11.12		
Canceled	(11,147)	9.64		
Outstanding—end of year	258,148	\$ 10.27	2.69 years	\$ 674,324
Vested and expected to vest—year end	202,948	\$ 10.31	2.34 years	\$ 522,524
Exercisable—year end	202,948	\$ 10.31	2.34 years	\$ 522,524

(1) Includes fractional options aggregating to 4 options that were settled in cash and no shares were issued.

The following table presents the status of all optioned shares and exercise price amounts during the year ended December 31, 2008:

	Number of Options	Weighted-Average Exercise Price	Weighted-Average Term	Aggregate Intrinsic Value
Outstanding—beginning of year	347,452	\$ 10.03		
Granted	55,200	9.70		
Exercised	(96,791)	8.45		
Canceled	(26,262)	11.00		
Outstanding—end of year	279,599	\$ 10.48	2.92 years	\$ 181,957
Vested and expected to vest—year end	224,399	\$ 10.67	2.65 years	\$ 165,397
Exercisable—year end	224,399	\$ 10.67	2.65 years	\$ 165,397

Information pertaining to options outstanding at December 31, 2009, is as follows:

Range of Exercise Prices	Number Outstanding	Weighted-Average Remaining Contractual Life	Weighted-Average Exercise Price	Number Exercisable	Weighted-Average Exercise Price
\$4.00 – \$7.62	43,943	2.5	\$ 6.51	43,943	\$ 6.51
\$9.70 – \$12.96	214,205	2.7	11.04	159,005	11.36
	258,148	2.7	\$ 10.27	202,948	\$ 10.31

The following table presents certain information regarding options for the years ended December 31, 2009 and 2008:

	2009	2008
Weighted-average fair value of stock options granted during the year	\$ 1.12	\$ 0.70
Total intrinsic value of options exercised	113,011	150,224
Total fair value of shares vested	61,668	44,240

As of December 31, 2009, total unrecognized compensation costs related to options that have been granted prior to the end of 2009 decreased to \$0 from \$20,280 due to \$20,280 compensation expense cost recognized.

The fair value of each option grant is estimated on the date of grant using the Black-Scholes option-pricing model with the following assumptions:

	2009	2008
Expected term (1)	1 year	1 year
Expected volatility (2)	31.60%	18.77%
Expected dividend yield (3)	3.17	3.30
Risk-free interest rate (4)	0.49	3.31

(1) The expected term is the vesting period of the option.

(2) The expected volatility was based on historical volatility for a period equal to the stock option's expected term.

(3) The expected dividend yield is based on the Company's prevailing dividend rate at the time of grant.

(4) The risk-free rate is based on the U.S. Treasury strips in effect at the time of grant equal to the stock option's expected term.

12. EARNINGS PER SHARE

The following is a reconciliation of the numerator and denominator of the basic and diluted earnings per share computation for the years ended December 31:

	2009			2008		
	Income (Numerator)	Shares (Denominator)	Per-Share Amount	Income (Numerator)	Shares (Denominator)	Per-Share Amount
Basic EPS						
Income available to common stockholders	\$ 9,493,679	5,750,763	\$ 1.65	\$ 7,076,349	5,694,988	\$ 1.24
Effect of Dilutive Securities						
Options—common stock equivalent		50,941	0.01		17,082	
Diluted EPS						
Income available to common stockholders, plus assumed conversion	\$ 9,493,679	5,801,704	\$ 1.64	\$ 7,076,349	5,712,070	\$ 1.24

13. ESTIMATED FAIR VALUE INFORMATION

The Company adopted ASC Topic 820 (formerly FASB Statement No. 157) effective January 1, 2008. ASC Topic 820 provides a framework for measuring fair value under GAAP. This standard applies to all financial assets and liabilities that are being measured and reported at fair value on a recurring and nonrecurring basis. For the Company, this does not include any financial assets or liabilities.

As defined in ASC Topic 820, fair value is 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. In determining fair value, the Company may use various methods, including market and income approaches. Based on these approaches, the Company often utilizes certain assumptions that market participants would use in pricing the asset or liability. These inputs can be readily observable, market corroborated, or generally unobservable firm inputs. The Company utilizes valuation techniques that maximize the use of observable inputs and minimize the use of unobservable inputs. Based on the observability of the inputs used in the valuation techniques, the Company is required to provide the following information according to the fair value hierarchy. The hierarchy ranks the quality and reliability of the information used to determine fair values. The hierarchy gives the highest priority to quoted prices available in active markets and the lowest priority to data lacking transparency. Financial assets and liabilities carried at fair value will be classified and disclosed in one of the following three categories:

- 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 in active markets; quoted prices for identical or similar assets or liabilities in markets that are not active; or other inputs that are observable or can be derived from or corroborated by observable market data by correlation or other means.
- Level 3: Significant unobservable inputs that reflect the reporting entity's own assumptions about the assumptions that market participants would use in pricing an asset or liability.

At December 31, 2009, there were no financial assets or liabilities measured or reported at fair value.

Financial assets and liabilities recorded at carrying value have estimated fair value amounts determined by the Company using available market information and appropriate valuation methodologies. However, considerable judgment is required to interpret market data to develop the estimates of fair value. Accordingly, the estimates presented herein are not necessarily indicative of the amounts the Company 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 at December 31:

	2009		2008	
	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
Assets:				
Cash and cash equivalents	\$ 18,413,000	\$ 18,413,000	\$ 10,317,101	\$ 10,317,101
Interest-bearing deposits in banks	5,158,000	5,158,000	5,792,000	5,792,000
Loans receivable	758,854,000	763,873,000	723,766,069	721,152,000
Accrued interest receivable	3,019,000	3,019,000	3,079,889	3,079,889
Investment in FHLB stock	15,697,000	15,697,000	15,428,200	15,428,200
Liabilities:				
Deposits	\$ 493,769,000	\$ 494,546,000	\$ 368,666,613	\$ 369,289,000
FHLB borrowings	228,000,000	240,170,000	322,206,210	337,374,000
Senior subordinated notes	7,250,000	7,250,000	-	-
Junior subordinated debentures	13,404,000	13,404,000	13,404,000	13,404,000
Accrued interest payable	99,000	99,000	211,335	211,335

The methods and assumptions used to estimate the fair value of each class of financial instruments for which it is practicable to estimate that value are explained below.

For cash and cash equivalents, and accrued interest receivable and payable, the carrying amounts are considered to be their estimated fair value.

For interest-bearing deposits in banks, carrying amounts are considered to be estimated fair value due to the short-term nature of the deposits.

For FHLB stock, the carrying amount equals fair value, as the stock may be sold back to the FHLB at the carrying value.

The fair value of performing variable and fixed rate loans was estimated by discounting the remaining contractual cash flows using the estimated current rate at which similar loans would be made to borrowers with similar credit risk characteristics over the same remaining maturities, reduced by net deferred loan origination fees, and the allocable portion of the allowance for loan losses.

The estimated current rate for discounting purposes was not adjusted for any change in borrowers' credit risk since the origination of such loans. Rather, the allocable portion of the allowance for loan losses is considered to provide for such changes in estimated fair value. The fair value of nonaccrual loans has been estimated at their carrying amount because it is not practicable to reasonably assess the credit risk adjustment that would be applied in the marketplace for such loans. The fair value of commitments, which include standby letters of credit, is not material to the financial statements as a whole.

For senior subordinated notes, the carrying value is considered to be estimated fair value since the notes were issued in December 2009.

The fair value of junior subordinated debentures is estimated by discounting the cash flows through maturity based on prevailing rates offered on the five-year Treasury bond, plus the current market spread.

The fair value of passbook, NOW, and money market deposit accounts is considered to be equivalent to their withdrawable amount. The fair value of certificates of deposit and FHLB borrowings is estimated using the rates currently offered for deposits and borrowings of similar remaining maturities.

The fair value estimates presented are based on pertinent information available to management as of December 31, 2009 and 2008. Such amounts have not been comprehensively revalued for purposes of these financial statements since those dates, and therefore, current estimates of fair value may differ significantly from the amounts presented above

14. RELATED PARTY TRANSACTIONS

In 2008, Palos Verdes Financial Corporation, a subsidiary of Malaga Bank, engaged a company where one of the directors of the engaged company is also a director of MFC & Malaga Bank. The engaged company provided construction management services in connection with the construction of a branch office. The branch office was completed in the second quarter of 2009.

This company was paid \$565,800 in 2009 and \$435,700 in 2008 for these services.

15. SUBSEQUENT EVENTS

The Company has evaluated subsequent events through April 26, 2010, the date the consolidated financial statements were issued.

In January 2010, MFC completed its private offering of Senior Subordinated Notes (Note 7) by issuing an additional \$2,750,000 of the Notes.

INDEPENDENT AUDITORS' REPORT

To the Board of Directors and Stockholders of
Malaga Financial Corporation
Palos Verdes Estates, California

We have audited the accompanying consolidated balance sheets of Malaga Financial Corporation and subsidiary (the "Company") as of December 31, 2009 and 2008, and the related consolidated statements of operations, stockholders' equity, and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes 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. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such consolidated financial statements present fairly, in all material respects, the financial position of the Company at December 31, 2009 and 2008, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Deloitte + Touche LLP

Los Angeles, California
April 26, 2010

BOARD OF DIRECTORS AND OFFICERS

BOARD OF DIRECTORS*

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Chairman of the Board

Steven P. L. Sheng
Corporate Secretary

Raymond L. Craemer, M.D.

Jerry A. Donahue

Leo K. C. Lee

Richard A. Oas, M.D.

CORPORATE ADMINISTRATION

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President and Chief Executive Officer

Jasna Penich*
Executive Vice President and
Chief Financial Officer

Susanne M. Chandler*
Senior Vice President and
Chief Risk Officer

Mel Hashimoto
Vice President and Controller

Gayle CdeBaca
Assistant Vice President and
Facilities Manager

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Senior Vice President
Branch Banking Executive

Connie Begovich
Assistant Vice President
Deposit Compliance / BSA Officer

Carmela Carroll
Assistant Vice President
Retail Banking Manager

Jocelyn Papadakis
Assistant Vice President
Project Manager / Security Officer

Rose Mary Callahan
Retail Banking Manager

LENDING OPERATIONS

Mark Bustamante
Senior Vice President and
Income Property Loan Officer

Russ Ciezata
Vice President and
Home Loan Specialist

Kenneth A. Johnson
Vice President and
Income Property Loan Officer

Dennis Mezzo
Vice President
Residential Loan Production

John Turner
Vice President and
Business Banking Manager

Nina Brister
Assistant Vice President
Loan Service Manager

Cathy Jaramillo
Assistant Vice President and
Assistant Loan Operations Manager

*Directors or Officers of MFC and Malaga Bank.

MALAGA BANK CORPORATE OFFICE AND RETAIL LOCATIONS

CORPORATE HEADQUARTERS AND PALOS VERDES ESTATES OFFICE

2514 Via Tejon, Palos Verdes Estates, CA 90274
T 310-375-9000
F 310-373-3615

TORRANCE OFFICE

25700 Crenshaw Blvd., Torrance, CA 90505
T 310-784-2000
F 310-784-0326

ROLLING HILLS ESTATES OFFICE

27450 Hawthorne Boulevard, Rolling Hills Estates, CA 90274
T 310-541-3000
F 310-544-5944

LOAN CENTER

23670 Hawthorne Blvd., Suite 101, Torrance, CA 90505
T 310-544-7800
F 310-544-0819

SAN PEDRO OFFICE

1460 West 25th Street, San Pedro, CA 90732
T 310-732-1100
F 310-831-7610

Call any Branch Office TOLL-FREE 888-8-MALAGA
Call the Loan Center TOLL-FREE 888-3-MALAGA
malagabank.com

MALAGA FINANCIAL CORPORATION

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