

PACWEST BANCORP
Form 10-K
February 27, 2019

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
Form 10-K
ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934
For the fiscal year ended December 31, 2018
Commission File No. 001-36408

PACWEST BANCORP
(Exact name of registrant as specified in its charter)
Delaware 33-0885320
(State of Incorporation) (I.R.S. Employer Identification No.)
9701 Wilshire Blvd., Suite 700
Beverly Hills, CA 90212
(Address of Principal Executive Offices, Including Zip Code)
(310) 887-8500

(Registrant's Telephone Number, Including Area Code)
Common Stock, par value \$0.01 per share The Nasdaq Stock Market, LLC
(Title of Each Class) (Name of Exchange on Which Registered)

Securities Registered Pursuant to Section 12(g) of the Act: None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes No

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). Yes No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§ 229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer Accelerated filer
 Non-accelerated filer Smaller reporting company
 Emerging growth company
 If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new

or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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

As of June 30, 2018, the aggregate market value of the voting common stock held by non-affiliates of the registrant, computed by reference to the average high and low sales prices on The Nasdaq Global Select Market as of the close of business on June 29, 2018, was approximately \$6.1 billion. Registrant does not have any nonvoting common equities. As of February 21, 2019, there were 120,800,873 shares of registrant's common stock outstanding, excluding 1,431,616 shares of unvested restricted stock.

DOCUMENTS INCORPORATED BY REFERENCE

The information required by Items 10, 11, 12, 13 and 14 of Part III of this Annual Report on Form 10-K will be found in the Company's definitive proxy statement for its 2019 Annual Meeting of Stockholders, to be filed pursuant to Regulation 14A under the Securities Exchange Act of 1934, as amended, and such information is incorporated herein by this reference.

PACWEST BANCORP
2018 ANNUAL REPORT ON FORM 10-K
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PART I

Forward-Looking Information

This Form 10-K contains certain “forward-looking statements” about the Company and its subsidiaries within the meaning of the Private Securities Litigation Reform Act of 1995, including certain plans, strategies, goals, and projections and including statements about our expectations regarding our operating expenses, profitability, allowance for loan and lease losses, net interest margin, net interest income, deposit growth, loan and lease portfolio growth and production, acquisitions, maintaining capital adequacy, liquidity, goodwill, and interest rate risk management. All statements contained in this Form 10-K that are not clearly historical in nature are forward-looking, and the words “anticipate,” “assume,” “intend,” “believe,” “forecast,” “expect,” “estimate,” “plan,” “continue,” “will,” “should,” “look forward,” and similar expressions are generally intended to identify forward-looking statements. You should not place undue reliance on these statements as they involve risks, uncertainties and contingencies, many of which are beyond our control, which may cause actual results, performance, or achievements to differ materially from those expressed in them. Actual results could differ materially from those anticipated in such forward-looking statements as a result of risks and uncertainties more fully described under “Item 1A. Risk Factors.” Factors that might cause such differences include, but are not limited to:

- our ability to compete effectively against other financial service providers in our markets;
- the effect of the current interest rate environment or impact of changes in interest rates or levels of market activity, especially on the fair value of our loan and investment portfolios;
- economic deterioration or a recession that may affect the ability of borrowers to make contractual payments on loans and may affect the value of real property or other property held as collateral for such loans;
- changes in credit quality and the effect of credit quality on our provision for credit losses and allowance for loan and lease losses;
- our ability to attract and retain deposits and other sources of funding or liquidity;
- the need to retain capital for strategic or regulatory reasons;
- compression of the net interest margin due to changes in the interest rate environment, forward yield curves, loan products offered, spreads on newly originated loans and leases, and/or changes in our asset or liability mix;
- reduced demand for our services due to strategic or regulatory reasons;
- our ability to successfully execute on initiatives relating to enhancements of our technology infrastructure, including client-facing systems and applications;
- our ability to complete future acquisitions and to successfully integrate such acquired entities or achieve expected benefits, synergies and/or operating efficiencies within expected time frames or at all;
- legislative or regulatory requirements or changes, including an increase to capital requirements, and increased political and regulatory uncertainty;
- the impact of the Dodd-Frank Act on our business, business strategies and cost of operations;
- the impact on our reputation and business from our interactions with business partners, counterparties, service providers and other third parties;
- higher than anticipated increases in operating expenses;
- lower than expected dividends paid from the Bank to the holding company;
- a deterioration in the overall macroeconomic conditions or the state of the banking industry that could warrant further analysis of the carrying value of goodwill and could result in an adjustment to its carrying value resulting in a non-cash charge;
- the effectiveness of our risk management framework and quantitative models;
- the costs and effects of failure, interruption or breach of security of our systems or the systems of our contracted vendors;
- the costs and effects of legal, compliance, and regulatory actions, changes and developments, including the impact of adverse judgments or settlements in litigation, the initiation and resolution of regulatory or other governmental inquiries or investigations, and/or the results of regulatory examinations or reviews;
- the impact of the Tax Cuts and Jobs Act on our business and business strategies, or if other changes are made to tax laws or regulations affecting our business, including the disallowance of tax benefits by tax authorities and/or changes

in tax filing jurisdictions or entity classifications; and
our success at managing risks involved in the foregoing items and all other risk factors described in our audited
consolidated financial statements, and other risk factors described in this Form 10-K and other documents filed or
furnished by PacWest with the SEC.

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

Available Information

We maintain a corporate website at <http://www.pacwestbancorp.com> and a website for the Bank at <http://www.pacificwesternbank.com>. At <http://www.pacwestbancorp.com> and via the "Investor Relations" link at the Bank's website, our Annual Report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and amendments to such reports filed or furnished pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended, are available, free of charge, as soon as reasonably practicable after such forms are electronically filed with, or furnished to, the SEC. The SEC maintains an Internet website at <http://www.sec.gov> that contains reports, proxy and information statements, and other information regarding issuers that file electronically with the SEC. You may obtain copies of the Company's filings on the SEC website. These documents may also be obtained in print upon request by our stockholders to our Investor Relations Department.

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

Our Investor Relations Department can be contacted at PacWest Bancorp, 9701 Wilshire Blvd., Suite 700, Beverly Hills, CA 90212, Attention: Investor Relations, telephone (310) 887-8521, or via e-mail to investor_relations@pacwestbancorp.com.

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

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Glossary of Acronyms, Abbreviations, and Terms

The acronyms, abbreviations, and terms listed below are used in various sections of this Form 10-K, including "Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations" and "Item 8. Financial Statements and Supplementary Data."

AFX	American Financial Exchange	FRB	Board of Governors of the Federal Reserve System
ALLL	Allowance for Loan and Lease Losses	FRBSF	Federal Reserve Bank of San Francisco
ALM	Asset Liability Management	FSOC	Financial Stability Oversight Council
ASC	Accounting Standards Codification	GLBA	Gramm-Leach-Bliley Act of 1999
ASU	Accounting Standards Update	IPO	Initial Public Offering
ATM	Automated Teller Machine	IRR	Interest Rate Risk
Basel III	A comprehensive capital framework and rules for U.S. banking organizations approved by the FRB and the FDIC in 2013.	LIHTC	Low Income Housing Tax Credit
BHCA	Bank Holding Company Act of 1956, as amended	MBS	Mortgage-Backed Securities
BOLI	Bank Owned Life Insurance	MVE	Market Value of Equity
Brexit	Britain Exit (from the European Union)	NII	Net Interest Income
California Privacy Act	California Consumer Privacy Act of 2018	NIM	Net Interest Margin
CDI	Core Deposit Intangible Assets	Non-PCI	Non-Purchased Credit Impaired Office of the Comptroller of the Currency
CECL	Current Expected Credit Loss	OCC	U.S Treasury Department of Office of Foreign Assets Control
CET1	Common Equity Tier 1	OFAC	Other Real Estate Owned
CFPB	Consumer Financial Protection Bureau	OREO	Probability of Default/Loss Given Default
CMOs	Collateralized Mortgage Obligations	PD/LGD	Pacific Western Equipment Finance
CRA	Community Reinvestment Act	PWEF	Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act of 2001
CRI	Customer Relationship Intangible Assets	PATRIOT Act	
CUB	CU Bancorp (a company acquired on October 20, 2017)	PCI	Purchased Credit Impaired
CU Bank	California United Bank (a wholly-owned subsidiary of CUB)	PRSU _s	Performance-Based Restricted Stock Units
DBO	California Department of Business Oversight	S1AM	Square 1 Asset Management, Inc.
DGCL	Delaware General Corporation Law	SBA	Small Business Administration
Dodd-Frank Act	Dodd-Frank Wall Street Reform and Consumer Protection Act	SEC	Securities and Exchange Commission
DTAs	Deferred Tax Assets	SNC _s	Shared National Credits
EGRRCPA	Economic Growth, Regulatory Relief, and Consumer Protection Act	Square 1	Square 1 Financial, Inc. (a company acquired on October 6, 2015)

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Efficiency Ratio	Noninterest expense (less intangible asset amortization, net foreclosed assets income/expense, and acquisition, integration and reorganization costs) divided by net revenues (the sum of tax equivalent net interest income plus noninterest income, less gain/loss on sale of securities and gain/loss on sales of assets other than loans and leases)	Tax Equivalent Net Interest Income	Net interest income adjusted for tax equivalent adjustments related to tax-exempt interest on certain loans and municipal securities
FASB	Financial Accounting Standards Board	Tax Equivalent NIM	NIM adjusted for tax equivalent adjustments related to tax-exempt interest on certain loans and municipal securities
FDIA	Federal Deposit Insurance Act	TCJA	Tax Cuts and Jobs Act
FDIC	Federal Deposit Insurance Corporation	TDRs	Troubled Debt Restructurings
FDICIA	Federal Deposit Insurance Corporation Improvement Act	TRSAs	Time-Based Restricted Stock Awards
FHLB	Federal Home Loan Bank of San Francisco	TruPS	Trust Preferred Securities
FinCEN	Financial Crimes Enforcement Network	U.S. GAAP	U.S. Generally Accepted Accounting Principles
		VIE	Variable Interest Entity

ITEM 1. BUSINESS

General

PacWest Bancorp, a Delaware corporation, is a bank holding company registered under the BHCA with our corporate headquarters located in Beverly Hills, California. Our principal business is to serve as the holding company for our wholly-owned subsidiary, Pacific Western Bank. References to "Pacific Western" or the "Bank" refer to Pacific Western Bank together with its wholly-owned subsidiaries. References to "we," "us," or the "Company" refer to PacWest Bancorp together with its subsidiaries on a consolidated basis. When we refer to "PacWest" or to the "holding company," we are referring to PacWest Bancorp, the parent company, on a stand-alone basis.

The Bank is focused on relationship-based business banking to small, middle-market, and venture-backed businesses nationwide. The Bank offers a broad range of loan and lease and deposit products and services through 74 full-service branches located throughout the state of California, one branch located in Durham, North Carolina, and numerous loan production offices across the country through our Community Banking, National Lending and Venture Banking groups. Community Banking provides real estate loans, commercial loans, and comprehensive deposit and treasury management services to small and medium-sized businesses conducted primarily through our California-based branch offices. National Lending provides asset-based, equipment, real estate, and security cash flow loans and treasury management services to established middle-market businesses on a national basis. Venture Banking offers loans and a comprehensive suite of financial services focused on entrepreneurial businesses and their venture capital and private equity investors, with offices located in key innovation hubs across the United States. In addition, we provide investment advisory and asset management services to select clients through Square 1 Asset Management, Inc., a wholly-owned subsidiary of the Bank and a SEC-registered investment adviser.

PacWest Bancorp was established in October 1999 and has achieved strong market positions by developing and maintaining extensive local relationships in the communities we serve. By leveraging our business model, service-driven focus, and presence in attractive markets, as well as maintaining a highly efficient operating model and robust approach to risk management, we have achieved significant and profitable growth, both organically and through disciplined acquisitions. We have successfully completed 29 acquisitions since 2000 which have contributed to our growth and expanded our market presence throughout the United States.

As of December 31, 2018, we had total assets of \$25.7 billion, total loans and leases, net of deferred fees, of \$18.0 billion, total deposits of \$18.9 billion, and stockholders' equity of \$4.8 billion.

Our Business Strategy

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

Our loan and lease portfolio consists primarily of real estate mortgage loans, real estate construction and land loans, and commercial loans and leases. We pursue attractive growth opportunities to expand and enter new markets aligned with our business model and strategic plans. Additionally, we focus on cultivating strong relationships with private equity and venture capital firms nationwide, many of which are also our clients and/or may invest in our clients.

Our reputation, expertise, and relationship-based business banking model enable us to deepen our relationships with our customers. We leverage our relationships with existing customers by cross-selling our products and services, including attracting deposits from and offering cash management solutions to our loan and lease customers. We price our deposit products with a view to maximizing our share of each customer's financial services business and prudently managing our cost of funds.

Focusing on operational efficiency is critical to our profitability and future growth. We carefully manage our cost structure and continuously refine and implement internal processes and systems to create further efficiencies and enhance our earnings.

Our management team has extensive expertise and a successful track record in evaluating, executing and integrating attractive, franchise-enhancing acquisitions. We have successfully completed 29 acquisitions since 2000, including the CUB acquisition on October 20, 2017. We will continue to consider acquisitions that are consistent with our business strategy and financial model as opportunities arise.

Depository Products and Services

Deposits are our primary source of funds to support our interest-earning assets and provide a source of stable low-cost funds and deposit-related fee income. We offer traditional deposit products to businesses and other customers with a variety of rates and terms, including demand, money market, and time deposits. We also provide international banking services, multi-state deposit services, and asset management services. The Bank's deposits are insured by the FDIC up to statutory limits.

Our branch network allows us to gather deposits, expand our brand presence and service our customers' banking and cash management needs. In addition, as the banking industry continues to experience broader customer acceptance of on-line and mobile banking tools for conducting basic banking functions we are able to serve our customers through a wide range of non-branch channels, including on-line, mobile, remote deposit, and telephone banking platforms, all of which allows us to expand our service area to attract new depositors without a commensurate increase in branch locations or branch traffic.

At December 31, 2018, we had ATMs at 59 of our branches located in California. We are part of the MoneyPass network that enables our customers to withdraw cash surcharge-free and service charge-free at over 25,000 ATM locations across the country. We provide access to customer accounts via a 24 hour seven-day-a-week, toll-free, automated telephone customer service and secure on-line banking services.

At December 31, 2018, our total deposits consisted of \$16.3 billion in core deposits, \$2.0 billion in time deposits and \$0.5 billion in non-core non-maturity deposits. Core deposits represented 87% of total deposits at December 31, 2018, and were comprised of \$7.9 billion in noninterest-bearing deposits, \$2.8 billion in interest-bearing checking accounts, \$5.0 billion in money market accounts and \$0.6 billion in savings accounts. Our deposit base is also diversified by client type. As of December 31, 2018, no individual depositor represented more than 1.0% of our total deposits, and our top ten depositors represented 7.5% of our total deposits.

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

Client Investment Funds

In addition to deposit products, we also offer select clients non-depository cash investment options through S1AM, our registered investment adviser subsidiary, and third-party money market sweep products. S1AM provides customized investment advisory and asset management solutions. At December 31, 2018, total off-balance sheet client investment funds were \$1.9 billion, of which \$1.5 billion was managed by S1AM.

Lending Activities

Our lending activities include real estate mortgage loans, real estate construction and land loans, commercial loans and leases, and a small amount of consumer loans. Our commercial real estate loans and real estate construction loans are secured by a variety of property types. Our commercial loans and leases are diverse and generally include various asset-secured loans, equipment-secured loans and leases, venture capital loans to support venture capital firms' operations and the operations of entrepreneurial companies during the various phases of their life cycles, secured business loans originated through our Community Banking group, and loans to security alarm monitoring companies. Until December 2017, we actively originated cash flow loans used to finance business acquisitions and recapitalizations to various types of borrowers, with greater emphasis on borrowers operating in the healthcare and technology industries. In December 2017, we exited most cash flow lending business lines, and we agreed to sell \$1.5 billion of cash flow loans (of which \$481.1 million were held for sale at December 31, 2017 and were subsequently sold in the first quarter of 2018). At December 31, 2018, we held \$92.5 million of cash flow loans from the lending businesses that we exited.

We price loans to preserve our interest spread and maintain our net interest margin. Loan interest rates may be floating, fixed, or a combination thereof ("hybrid") throughout the loan term. The rates on hybrid loans typically are fixed until a "reset" date when the rates then become floating. While we do not actively solicit direct consumer loans, we hold consumer loans, consisting primarily of purchased private student loans originated and serviced by third-party lenders. We also have an additional exposure to consumer loans as many of our lender finance and timeshare loans are secured by the receivables owed to our borrowers by individual consumers.

Some of our loans are participations in larger loans, and these participations may be considered