HOPE BANCORP INC
Form 10-K
March 01, 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 Number 000-50245

HOPE BANCORP, INC.
(Exact name of registrant as specified in its charter)

Delaware	95-4849715
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
3200 Wilshire Boulevard, Suite 1400, Los Angeles, California	90010
(Address of principal executive offices)	(Zip Code)

(213) 639-1700
(Registrant’s telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act:

Title of class	Name of exchange on which registered
Common Stock, par value $0.001 per share	NASDAQ Global Select Market

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 x No o

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 o No x

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

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 and post such files). x Yes o 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 x

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, smaller reporting company, or an emerging growth company. See definition of “large accelerated filer,” “accelerated filer,” “smaller reporting company,” and “emerging growth company” in Rule 12b-2 of the Exchange Act.

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

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. o

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

The aggregate market value of the common stock held by non-affiliates of the registrant based upon the closing sale price of the common stock as of the last business day of the registrant's most recently completed second fiscal quarter, June 30, 2018, as reported on the NASDAQ Global Select Market, was approximately $2,228,005,491.

Number of shares outstanding of the registrant's common stock as of February 25, 2019: 126,642,148

Documents Incorporated by Reference: The information required in Part III, Items 10 through 14 is incorporated herein by reference to the registrant's definitive proxy statement for the 2019 annual meeting of stockholders which will be filed with the Securities and Exchange Commission within 120 days of the registrant's fiscal year end.

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Forward-Looking Information

Certain statements in this Annual Report on Form 10-K constitute forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended (the "Securities Act") and Section 21E of the Securities Exchange Act of 1934, as amended (the "Exchange Act"). These forward-looking statements relate to, among other things, expectations regarding the business environment in which we operate, projections of future performance, and our business strategies, objectives and vision. Forward-looking statements include, but are not limited to, statements preceded by, followed by or that include the words "will," "believes," "expects," "anticipates," "intends," "plans," "estimates," or similar expressions. With respect to any such forward-looking statements Hope Bancorp, Inc. claims the protection provided for in the Private Securities Litigation Reform Act of 1995. These statements involve risks and uncertainties. Our actual results, performance or achievements may differ significantly from the results, performance or achievements expressed or implied in any forward-looking statements. The risks and uncertainties include: deterioration in economic conditions in our areas of operation; interest rate risk associated with volatile interest rates and related asset-liability matching risk; liquidity risks; risk of significant non-earning assets, and net credit losses that could occur, particularly in times of weak economic conditions or times of rising interest rates; and regulatory risks associated with current and future regulations. For a more detailed discussion of factors that might cause such a difference, see Item 1A, "Risk Factors" herein. Hope Bancorp, Inc. does not undertake, and specifically disclaims any obligation, to update any forward looking statements to reflect the occurrence of events or circumstances after the date of such statements except as required by law.

PART I

Item 1. BUSINESS

General

Hope Bancorp, Inc. ("Hope Bancorp" on a parent-only basis, and the "Company," "we" or "our" on a consolidated basis with the Bank of Hope) is a bank holding company headquartered in Los Angeles, California. The Company was incorporated in Delaware in the year 2000. Previously known as BBCN Bancorp Inc., the Company changed its name to Hope Bancorp at the time of the merger with Wilshire Bancorp Inc. ("Wilshire") on July 29, 2016. We offer commercial and retail banking loan and deposit products through our wholly-owned subsidiary, Bank of Hope (formerly BBCN Bank), a California state-chartered bank (the "Bank" or "Bank of Hope"). The Bank primarily focuses its business in ethnic communities in California, New Jersey and New York City, Chicago, Houston, Dallas, Seattle and Washington, D.C. metropolitan areas. Our headquarters are located at 3200 Wilshire Boulevard, Suite 1400, Los Angeles, California 90010, and our telephone number at that address is (213) 639-1700.

Hope Bancorp exists primarily for the purpose of holding the stock of the Bank and other subsidiaries it may acquire or establish. Bank of Hope's deposits are insured by the Federal Deposit Insurance Corporation (the "FDIC"), up to applicable limits.

We file reports with the Securities and Exchange Commission (the "SEC"), which include annual reports on Form 10-K, quarterly reports on Form 10-Q and current reports on Form 8-K, as well as proxy and information statements in connection with our stockholders' meetings. The SEC maintains a website that contains the reports, proxy and information statements and other information regarding issuers that file electronically with the SEC. The address of the website is www.sec.gov. Our website address is www.bankofhope.com. Electronic copies of our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and other information and reports we file with the SEC and amendments to those reports, are available free of charge by visiting the Investor Relations section of our website. These reports are generally posted as soon as reasonably practicable after they are electronically filed with the SEC. None of the information on or hyperlinked from the Company's website is incorporated into this Annual Report on Form 10-K.

Mergers and Acquisitions

On July 29, 2016, we completed the acquisition of Wilshire, previously headquartered in Los Angeles, California. With the completion of the acquisition, 35 branches in California, New York, New Jersey, Texas, Alabama, and Georgia were added to our existing branch network in addition to six loan production offices. Some of these branch

locations and loan production offices were subsequently closed as part of our consolidation plan. Our current consolidated network consists of 63 branches and 11 loan production offices.

The Wilshire acquisition was accounted for in accordance with Accounting Standard Codification ("ASC") 805 "Business Combinations," and the assets and liabilities of Wilshire were recorded at fair value at the date of acquisition. The fair value of assets acquired from Wilshire totaled approximately $4.63 billion and goodwill recorded from acquisitions consummated in 2016 totaled $359.0 million.

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Business Overview

Our principal business activities are conducted through the Bank and primarily consist of earning interest on loans and investment securities that are primarily funded by customer deposits and other borrowings. Operating revenues consist of the difference between interest received and interest paid, gains and losses on the sale of financial assets, and fees earned for financial services provided to our customers. Interest rates are highly sensitive to many factors that are beyond our control, such as general economic conditions, new legislation and the policies of various governmental and regulatory authorities. Although our business may vary with local and national economic conditions, such variations are not generally seasonal in nature.

Through our current network of 63 branches and 11 loan production offices, we offer core business banking products for small and medium-sized businesses and individuals. We accept deposits and originate a variety of loans, including commercial business loans, commercial real estate loans, trade finance loans, Small Business Administration ("SBA") loans, auto loans, single-family mortgages, warehouse lines of credit, personal loans, and credit cards. We offer cash management services to our business customers, which include remote deposit capture, lock box, and ACH origination services. We offer comprehensive investment and wealth management services to high-net-worth clients. We also offer a mobile banking application for smart devices that extends access to banking services, such as mobile deposits and bill payment, for our customers at all times. In an effort to better meet our customers' needs, our mini-market branches generally offer hours from 9 a.m. to 6 p.m. Most of our branches offer 24-hour automated teller machines ("ATMs"). We also offer debit card services to all customers. In addition, most of our branches offer foreign exchanges services, safe deposit boxes, and other customary bank services. Our website at www.bankofhope.com offers internet banking services and applications in both English and Korean.

Lending Activities

Commercial Business Loans

We provide commercial loans to businesses for various purposes such as for working capital, purchasing inventory, debt refinancing, business acquisitions, and other business related financing needs. Commercial loans are typically classified as (1) short-term loans (or lines of credit) or (2) long-term loans (or term loans to businesses). Short-term loans are often used to finance current assets such as inventory and accounts receivable and typically have terms of one year with interest paid monthly on the outstanding balance with the principal balance due at maturity. Long-term loans typically have terms of five to seven years with principal and interest paid monthly. The credit worthiness of our borrowers is determined before a loan is originated and is periodically reviewed to ascertain whether credit quality changes have occurred. Commercial business loans are typically collateralized by the borrower's business assets and/or real estate. We seek to establish deposit relationships with all of our commercial business loan customers.

Our commercial business loan portfolio includes trade finance loans from our Corporate Banking Center, which generally serves businesses involved in international trade activities. These loans are typically collateralized by business assets and are used to meet the short-term working capital needs (accounts receivable and inventory financing) of our borrowers. Our International Operations Department issues and advises on letters of credit for export and import businesses. The underwriting procedure for this type of credit is the same as for commercial business loans. We offer the following types of letters of credit to customers:

- Commercial: An undertaking by the issuing bank to pay for a commercial transaction.
- Standby: An undertaking by the issuing bank to pay for the non-performance of the applicant customer.
- Revocable: Letter of credit that can be modified or cancelled by the issuing bank at any time with notice to the beneficiary (does not provide the beneficiary with a firm promise of payment).
- Irrevocable: Letter of credit that cannot be altered or cancelled without mutual consent of all parties.
- Sight: Letter of credit requiring payment upon presentation of conforming shipping documents.
- Usance: Letter of credit that allows the buyer to delay payment up to a designated number of days after presentation of shipping documents.
- Import: Letter of credit issued to assist customers in purchasing goods from overseas.
- Export: Letter of credit issued to assist customers in selling goods overseas.

- Transferable: Letter of credit that allows the beneficiary to transfer its drawing (payment) rights, in part or full, to another.
- Non-transferable: Letter of credit that does not allow the beneficiary to transfer their right, in part or full, to another.

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Our trade finance services include the issuance and negotiation of letters of credit, as well as the handling of documentary collections. On the export side, we provide advice and negotiation of commercial letters of credit and we transfer and issue back-to-back letters of credit. We also provide importers with trade finance lines of credit, which allow for the issuance of commercial letters of credit and the financing of documents received under such letters of credit, as well as documents received under documentary collections. Exporters are assisted through export lines of credit as well as through immediate financing of clean documents presented under export letters of credit.

We provide commercial equipment lease financing through a relationship with a third-party leasing company. Equipment leasing loans are generally capital leases with maturities up to five years.

We also provide warehouse lines of credit to mortgage loan originators. The lines of credit are used by these originators to fund mortgages which are then pledged to the Bank as collateral until the mortgage loans are sold and the lines of credit are paid down. The typical duration of these lines of credit from the time of funding to pay-down ranges from 10-30 days. Although collateralized by mortgage loans, the structure of warehouse lending agreements results in the commercial and industrial loan treatment for these types of loans.

Commercial Real Estate Loans

Real estate loans are extended for the purchase and refinance of commercial real estate and are generally secured by first deeds of trust. The maturities on the majority of such loans are generally five to seven years with a 25-year principal amortization schedule and a balloon payment due at maturity. We offer both fixed and floating rate commercial real estate loans. It is our general policy to restrict commercial real estate loan amounts to 75% of the appraised value of the property at the date of origination.

We originate loans to finance construction projects including one-to-four family residences, multifamily residences, senior housing, and commercial projects. Residential construction loans are due upon the sale of the completed project and are generally collateralized by first liens on the real estate and have floating interest rates. Construction loans are considered to have higher risks than other loans due to the ultimate repayment being sensitive to interest rate changes, governmental regulation of real property, and the availability of long-term financing. Economic conditions may also impact our ability to recover our investment in construction loans. Adverse economic conditions may negatively impact the real estate market, which could affect the borrowers' ability to complete and sell the project. Additionally, the fair value of the underlying collateral may fluctuate as market conditions change. As construction loans make up only a small percentage of the total loan portfolio, these loans are not further broken down into classes.

Small Business Administration Loans

We extend loans partially guaranteed by the SBA. We primarily extend SBA loans known as SBA 7(a) loans and SBA 504 loans. SBA 7(a) loans are typically extended for working capital needs, purchase of inventory, purchase of machinery and equipment, debt refinance, business acquisitions, start-up financing, or to purchase or construct owner-occupied commercial property. SBA 7(a) loans are typically term loans with maturities up to 10 years for loans not secured by real estate and up to 25 years for real estate secured loans. SBA loans are fully amortizing with monthly payments of principal and interest. SBA 7(a) loans are typically floating rate loans that are secured by business assets and/or real estate. Depending on the loan amount, each loan is typically guaranteed 75% to 85% by the SBA, with a maximum gross loan amount to any one small business borrower of $5.0 million and a maximum SBA guaranteed amount of $3.75 million.

We are generally able to sell the guaranteed portion of the SBA 7(a) loans in the secondary market at a premium, while earning servicing fee income on the sold portion over the remaining life of the loan. In addition to the interest yield earned on the unguaranteed portion of the SBA 7(a) loans that are not sold, we can recognize income from gains on sales and from loan servicing on the SBA 7(a) loans that are sold. Although we have historically sold the guaranteed portion of SBA 7(a) loans that we originated, we recently made the decision to retain these loans due to the decline in premiums offered in the secondary market. Therefore, for the time being, we will be retaining these loans and earn interest income on the guaranteed portion of SBA loans as well the unguaranteed portions.

SBA 504 loans are typically extended for the purpose of purchasing owner-occupied commercial real estate or long-term capital equipment. SBA 504 loans are typically extended for up to 20 years or the life of the asset being financed. SBA 504 loans are financed as a participation loan between the Bank and the SBA through a Certified Development Company ("CDC"). Generally, the loans are structured to give the Bank a 50% first deed of trust ("TD"), the

CDC a 40% second TD, and the remaining 10% is funded by the borrower. Interest rates for first TD Bank loans are subject to normal bank commercial rates and terms, and the second TD CDC loans are fixed for the life of the loans based on certain indices.

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All of our SBA loans are originated through our SBA Loan Departments. The SBA Loan Departments are staffed by loan officers who provide assistance to qualified businesses. The Bank has been designated as an SBA Preferred Lender, which is the highest designation awarded by the SBA. This designation generally facilitates a more efficient marketing and approval process for SBA loans. We have attained SBA Preferred Lender status nationwide.

Consumer Loans

Our consumer loans consist of single-family mortgages, home equity, auto loans, and personal loans, with a majority of our consumer loan portfolio currently consisting of single-family mortgages secured by a first deed of trust on single family residences under a variety of loan products including fixed-rate and adjustable-rate mortgages with either 30-year or 15-year terms. Adjustable rate mortgage loans are also offered with flexible initial and periodic adjustments ranging from five to seven years.

Investing Activities

The main objective of our investment strategy is to provide a source of on-balance sheet liquidity while providing a means to manage our interest rate risk, and to generate an adequate level of interest income without taking undue risks. Subject to various restrictions, our investment policy permits investment in various types of securities, certificates of deposit ("CDs"), and federal funds sold. Our investment portfolio has consisted of government sponsored agency bonds, mortgage-backed securities, collateralized mortgage obligations ("CMOs"), corporate securities, municipal securities, and mutual funds. For a detailed breakdown of our investment portfolio, see Item 7 "Management's Discussion and Analysis of Financial Condition and Results of Operations – Financial Condition – Investment Security Portfolio."

Our securities are classified for accounting purposes as available for sale. We do not maintain held to maturity or trading investment portfolios. Securities purchased to meet investment-related objectives, such as liquidity management or interest rate risk and which may be sold as necessary to implement management strategies, are designated as available for sale at the time of purchase.

Deposit Activities

We attract both short-term and long-term deposits from the general public by offering a wide range of deposit products and services. Through our branch network, we provide our banking customers with personal and business checking accounts, money market accounts, savings accounts, time deposit accounts, individual retirement accounts, 24-hour ATMs, internet banking and bill-pay, remote deposit capture, lock boxes, and ACH origination services. In addition to our retail and business deposits, we obtain both secured and unsecured wholesale deposits including public deposits such as State of California Treasurer's time deposits, brokered money market and time deposits, and deposits gathered from outside of the Bank's normal market area through deposit listing services.

FDIC-insured deposits are our primary source of funds. As part of our asset-liability management, we analyze our retail and wholesale deposit maturities and interest rates to monitor and manage our cost of funds, to the extent feasible in the context of changing market conditions, as well as to promote stability in our supply of funds. For additional information on deposits, see Item 7 "Management's Discussion and Analysis of Financial Condition and Results of Operations – Financial Condition – Deposits."

Borrowing Activities

When we have more funds than required for our reserve requirements or short-term liquidity needs, we may sell federal funds to other financial institutions. Conversely, when we have less funds than required, we may borrow funds from the Federal Home Loan Bank of San Francisco (the "FHLB"), the Federal Reserve Bank of San Francisco ("the Federal Reserve Bank"), or our correspondent banking relationships. In addition, we may borrow from the FHLB on a longer term basis to provide funding for certain loan or investment securities strategies, as well as asset-liability management strategies.

The FHLB functions in a reserve credit capacity for qualifying financial institutions. As a member, we are required to own capital stock in the FHLB and may apply for advances from the FHLB on an unsecured basis or by utilizing qualifying loans and certain securities as collateral. The FHLB offers a full range of borrowing programs on its advances, with terms ranging from one day to thirty years, at competitive market rates. A prepayment penalty is usually imposed for early repayment of these advances. Information concerning FHLB advances and other borrowings is included in Note 9 of "Notes to Consolidated Financial Statements."

We may also borrow from the Federal Reserve Bank. The maximum amount that we may borrow from the Federal Reserve Bank’s discount window is up to 95% of the outstanding principal balance of the qualifying loans and the fair value of the securities that we pledge.

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Long-Term Debt

At December 31, 2018, nine wholly-owned subsidiary grantor trusts ("Trusts") had issued $126.0 million of pooled trust preferred securities ("Trust Preferred Securities"). The Trust Preferred Securities accrue and pay distributions periodically at specified annual rates as provided in the related indentures for the securities. The Trusts used the net proceeds from the offering of the Trust Preferred Securities to purchase a like amount of subordinated debentures (the "Debentures") issued by us. The Debentures are the sole assets of the trusts. Our obligations under the Debentures and related documents, taken together, constitute a full and unconditional guarantee by us of the obligations of the trusts. The Trust Preferred Securities are mandatorily redeemable upon the maturity of the Debentures (which have maturity dates ranging from 2033 to 2037), or upon earlier redemption as provided in the indentures. We have the right to redeem the Debentures in whole (but not in part) on a quarterly basis at a specified redemption price. We also have the right to defer interest on the Debentures for up to five years.

In 2018, we issued $217.5 million aggregate principal amount of 2.00% convertible senior notes maturing on May 15, 2038 in a private offering to investors. Holders of the convertible notes can convert to shares of our common stock at a specified conversion rate at any time on or after February 15, 2023. Prior to February 15, 2023, the convertible notes cannot be converted unless under certain specified scenarios. The convertible notes can be settled in entirely cash, stock, or a combination of stock and cash at our option. We have the right to call the convertible notes on or after May 20, 2023 and holder of the notes can put the note on certain dates on or after May 15, 2023. The convertible notes were issued as part of our plan to repurchase shares of our common stock. Subsequent to the issuance of the convertible notes, we repurchased $150.0 million in common stock during 2018.

Market Area and Competition

We currently have 63 banking offices in areas having high concentrations of Korean-Americans, of which 35 are located in the Los Angeles, Orange County, Oakland and Silicon Valley (Santa Clara County) areas of California, 10 are located in the New York City metropolitan area and New Jersey, six are in the Chicago metropolitan area, four are in the Seattle metropolitan area, four are in Texas, two are in Virginia, one is in Alabama, and one is in Georgia. We also have 11 loan production offices located in Dallas, Seattle, Atlanta, Denver, Portland, Fremont, and Southern California and a representative office in Seoul, South Korea. The banking and financial services industry generally, and in our market areas specifically, is highly competitive. The increasingly competitive environment is a result primarily of strong competition among the banks servicing the Korean-American community, changes in regulations, changes in technology and product delivery systems, and consolidation among financial services companies. In addition, federal legislation may have the effect of further increasing the pace of consolidation within the financial services industry. See "Supervision and Regulation."

We compete for loans, deposits, and customers with other commercial banks, savings and loan associations, securities and brokerage companies, mortgage companies, insurance companies, marketplace finance platforms, money market funds, credit unions, and other non-bank financial service providers. Many of these competitors are much larger in total assets and capitalization, have greater access to capital markets, are more widely recognized, have broader geographic scope, and offer a broader range of financial services than we do.

Economic Conditions, Government Policies and Legislation

Our profitability, like that of most financial institutions, depends, among other things, on interest rate differentials. In general, the difference between the interest expense on interest bearing liabilities, such as deposits, borrowings, and debt, and the interest income on our interest earning assets, such as loans we extend to our customers and securities held in our investment portfolio, as well as the level of noninterest bearing deposits, have a significant impact on our profitability. Interest rates are highly sensitive to many factors that are beyond our control, such as the economy, inflation, unemployment, consumer spending, and political changes and events. The impact that future changes in domestic and foreign economic and political conditions might have on our performance cannot be predicted.

Our business is also influenced by the monetary and fiscal policies of the federal government and the policies of regulatory agencies, particularly the Board of Governors of the Federal Reserve System (the "FRB"). The FRB implements national monetary policies (with objectives such as curbing inflation or preventing recession) through its open-market operations in U.S. government securities, by adjusting the required level of reserves for depository institutions subject to its reserve requirements, and by varying the targeted federal funds and discount rates applicable

to borrowings by depository institutions. The actions of the FRB in these areas influence the growth of bank loans, investments, and deposits and also affect interest rates earned on interest earning assets and paid on interest bearing liabilities. The nature and impact on Hope Bancorp, and the Bank, of future changes in monetary and fiscal policies cannot be predicted.

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From time to time, legislation and regulations are enacted or adopted which have the effect of increasing the cost of doing business, limiting, or expanding permissible activities, or affecting the competitive balance between banks and other financial services providers. Proposals to change the laws and regulations governing the operations and taxation of banks, bank holding companies, financial holding companies, and other financial institutions and financial services providers are frequently made in the U.S. Congress, in state legislatures, and by various regulatory agencies. These proposals may result in changes in banking statutes and regulations and our operating environment in substantial and unpredictable ways. If enacted, such legislation could increase the cost of doing business, limit permissible activities, or affect the competitive balance among banks, savings associations, credit unions, and other financial institutions. We cannot predict whether any of this potential legislation will be enacted, and if enacted, the effect that it, or any implementing regulations, would have on our financial condition or results of operations. See "Supervision and Regulation."

Supervision and Regulation

General

Hope Bancorp and the Bank are subject to extensive regulation and supervision under state and federal banking laws. This regulatory framework covers substantially all of the business activities of Hope Bancorp and the Bank. In the exercise of their supervisory and examination authority, the bank regulatory agencies have recently emphasized capital planning and stress testing, liquidity management, enterprise risk management, corporate governance, anti-money laundering compliance, information technology adequacy, cybersecurity preparedness, vendor management, and fair lending and other consumer compliance obligations. The federal and state regulatory systems are intended primarily for the protection of depositors, customers, the FDIC deposit insurance fund (the "DIF") and the banking system as a whole, rather than for the protection of shareholders or other investors.

The following summarizes certain laws and regulations that apply to Hope Bancorp and the Bank. These descriptions of statutes and regulations and their possible effects do not purport to be complete descriptions of all of the provisions of those statutes and regulations and their possible effects on us, nor do they purport to identify every statute and regulation that may apply to us.

Bank Holding Company Regulation

Hope Bancorp is a registered bank holding company. As a bank holding company, is subject to regulation, supervision and regular examination by the FRB under the Bank Holding Company Act. Hope Bancorp is also required to file periodic reports of its operations with the FRB and other such reports as the FRB may require.

Bank holding companies are required to maintain certain levels of capital (See "Capital Adequacy Requirements") and must serve as a source of financial and managerial strength to subsidiary banks and commit resources as necessary to support each subsidiary bank. FRB regulations and polices limit the dividends a bank holding company may pay to its shareholders and the amount of its shares that it may repurchase. (See "Dividends and Stock Repurchases".) FRB rules and policies also regulate provisions of certain bank holding company debt and the FRB may impose interest ceilings and reserve requirements on such debt and require prior approval to purchase or redeem debt securities in certain situations.

The FRB may require a bank holding company to terminate an activity or terminate control of or liquidate or divest certain subsidiaries, affiliates or investments if the FRB believes the activity or the control of the subsidiary or affiliate constitutes a significant risk to the financial safety, soundness or stability of any bank subsidiary. Under certain circumstances, the FRB could, for example, prohibit Hope Bancorp from paying dividends or repurchasing is common stock on the basis that doing would be an unsafe or unsound banking practice.

The activities in which a bank holding company may engage are limited to those activities determined by the FRB to be so closely related to banking or managing or controlling banks as to be a proper incident thereto. Bank holding companies that elect and retain "financial holding company" status pursuant to the Gramm-Leach-Bliley Act of 1999 (the "GLBA") may also engage in broader securities, insurance, merchant banking and other activities that are determined to be "financial in nature" or are incidental or complementary to activities that are financial in nature. To elect and retain financial holding company status, a bank holding company and all depository institution subsidiaries of a bank holding company must be considered well capitalized and meet certain other requirements. Hope Bancorp has not elected financial holding company status and neither Hope Bancorp nor the Bank has engaged in any activities

determined by the FRB to be financial in nature or incidental or complementary to activities that are financial in nature.

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A bank holding company must seek approval from the FRB prior to acquiring all or substantially all of the assets of any bank or bank holding company or the ownership or control of voting shares of any bank or bank holding company if, after giving effect to such acquisition, it would own or control, directly or indirectly, more than 5 percent of a bank. Under the Bank Merger Act, the prior approval of the FDIC is required for the Bank to merge with another bank or purchase all or substantially all of the assets or assume any of the deposits of another FDIC-insured depository institution. Federal banking regulators review competitive, management, financial, compliance and other factors when considering applications for these approvals. Similar California or other state banking agency approvals may also be required.

The Company is also a bank holding company within the meaning of Section 3700 of the California Financial Code. Therefore, the Bank and any of its subsidiaries are subject to examination by, and may be required to file reports with, the DBO. DBO approvals are also required for certain mergers and acquisitions

Bank Regulation

The Bank is a California state-chartered bank whose deposit accounts are insured by the FDIC, up to applicable limits. As such, the Bank is subject to regulation, supervision and regular examination by the California Department of Business Oversight (the “DBO”) and the FDIC. In addition, while the Bank is not a member of the FRB, the Bank is subject to certain regulations of the FRB.

Federal and state laws and regulations applicable to banks regulate, among other things, the scope of their business, their investments, their reserves against deposits, lending activities, servicing and foreclosing on loans, borrowings, capital requirements, certain check-clearing activities, dividends, branching, and mergers and acquisitions. California banks are also subject to statutes and regulations including FRB Regulation O and Federal Reserve Act Sections 23A and 23B and Regulation W, which restrict or limit loans or extensions of credit to “insiders”, including officers, directors, and principal shareholders, and loans or extension of credit by banks to affiliates or purchases of assets from affiliates, including parent bank holding companies, except pursuant to certain exceptions and only on terms and conditions at least as favorable to those prevailing for comparable transactions with unaffiliated parties. The Dodd-Frank Act expanded definitions and restrictions on transactions with affiliates and insiders under Sections 23A and 23B and also lending limits for derivative transactions, repurchase agreements and securities lending and borrowing transactions.

Under the Federal Deposit Insurance Act (“FDI Act”) and the California Financial Code, California state chartered commercial banks may generally engage in any activity permissible for national banks. Therefore, the Bank may form subsidiaries to engage in the many so-called “closely related to banking” or “nonbanking” activities commonly conducted by national banks in operating subsidiaries or by subsidiaries of bank holding companies. Further, California state chartered banks may conduct certain financial activities permitted under GLBA in a “financial subsidiary” to the same extent as a national bank, provided the bank is and remains well-capitalized, well-managed and in satisfactory compliance with the Community Reinvestment Act (the “CRA”). The Bank currently conducts no non-banking or financial activities through subsidiaries.

Capital Adequacy Requirements

Hope Bancorp and the Bank are subject to similar regulatory capital requirements administered by their primary federal supervisory banking agencies. Pursuant to the Dodd-Frank Wall Street Reform and Consumer Protection Act (the “Dodd-Frank Act”), the federal banking agencies have adopted capital rules (the “New Capital Rules”) based on the Basel III Accord. The New Capital Rules became effective on January 1, 2015, subject to certain phase-in provisions. The New Capital Rules are risk-based, meaning that the levels of capital required vary based on the perceived degree of risk associated with a banking organization’s balance sheet assets, such as loans and investment securities, and those recorded as off-balance sheet items, such as commitments, letters of credit, and recourse arrangements. Bank holding companies and banks engaged in significant trading activity may also be subject to the market risk capital guidelines and be required to incorporate additional market and interest rate risk components into their risk-based capital standards. The classifications and, therefore, the required capital amounts are also subject to qualitative judgments by regulators about components, risk-weighting, and other factors.

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The New Capital Rules (i) introduce a new capital measure called "common equity Tier 1 and a related regulatory capital ratio of common equity Tier 1 to risk weighted assets, (ii) specify that Tier 1 capital consists of common equity Tier 1 and "additional Tier 1 capital" instruments meeting certain requirements, (iii) mandate that most deductions and adjustments to regulatory capital measures be made to common equity Tier 1 and not to the other components of capital, and (iv) expand the scope of the deductions from and adjustments to capital compared to prior capital rules. The New Capital Rules also changed the risk-weights of certain assets used to calculate the risk-based capital ratios, such as those for high volatility commercial real estate acquisition, development and construction loans, certain past due non-residential mortgage loans and certain mortgage-backed and other securities exposure. The New Capital Rules also change the permitted composition of Tier 1 capital to exclude trust preferred securities (subject to certain grandfathering exceptions for organizations like Hope Bancorp, which had less than $15 billion in assets as of December 31, 2009), mortgage servicing rights and certain deferred tax assets and to include unrealized gains and losses on available for sale debt and equity securities (unless the organization opts out of including such unrealized gains and losses).

Under the New Capital Rules, the minimum capital ratios applicable to Hope Bancorp and the Bank are as follows:

- 4.5% common equity Tier 1 to risk weighted assets;
- 6.0% Tier 1 capital (that is, common equity Tier 1 plus additional Tier 1 capital) to risk weighted assets;
- 8.0% total capital (that is, Tier 1 capital plus Tier 2 capital) to risk weighted assets; and
- 4.0% Tier 1 capital to average consolidated assets as reported on regulatory financial statements (known as the "leverage ratio"). (To be considered well-capitalized under the Prompt Corrective Action framework, the Bank must maintain a minimum Tier 1 leverage ratio of at least 5%.)

At December 31, 2018, the respective capital ratios of Hope Bancorp and the Bank exceeded the minimum percentage requirements to generally be deemed "well-capitalized" for bank regulatory purposes. See "Management's Discussion and Analysis of Financial Condition and Results of Operations."

The New Capital Rule create an additional "capital conservation buffer" of 2.5% of risk-weighted assets above the regulatory minimum capital ratios. If Hope Bancorp and the Bank do not maintain capital sufficient to satisfy the capital conservation buffer, they would face restrictions in their ability to pay dividends, repurchase shares and pay discretionary bonuses. The capital conservation buffer was phased in in increments of 0.625% beginning in 2015 through January 1, 2019.

Including the capital conservation buffer of 2.5%, which was fully phased in as of January 1, 2019, the minimum ratios for a banking organization to be considered "well capitalized" for bank regulatory purposes are as follows: (i) a common equity Tier 1 capital ratio of 7.0%, (ii) a Tier 1 capital ratio of 8.5% and (iii) a total capital ratio of 10.5%. Management believes that, as of December 31, 2018, Hope Bancorp and the Bank met all requirements under the New Capital Rules applicable to them on a fully phased-in basis as if such requirements were then in effect, including the capital conservation buffer.

While the New Capital Rules set higher regulatory capital standards for Hope Bancorp and the Bank, bank regulators may also continue their past policies of expecting banks to maintain additional capital beyond the new minimum requirements. The implementation of the New Capital Rules or more stringent requirements to maintain higher levels of capital or to maintain higher levels of liquid assets could adversely impact the Company's net income and return on equity, restrict the ability to pay dividends or executive bonuses and require the raising of additional capital.

The Bank is also subject to capital adequacy requirements under the California Financial Code.

See "Management's Discussion and Analysis of Financial Condition and Results of Operations."

Increased Supervision and Regulation for Bank Holding Companies with Consolidated Assets of More than $10 Billion

As a banking organization with consolidated assets exceeding $10 billion, the Company is subject to heightened supervision and regulation imposed by the Dodd-Frank Act, such as the following:

- We are subject to periodic examination by the Consumer Finance Protection Bureau ("CFPB") with respect to compliance with federal consumer laws. Although we were previously subject to regulations issued by the CFPB, the Bank's primary federal regulatory, the FDIC, previously had responsibility for our consumer compliance exams. See "Consumer Finance Protection Bureau."

- We are subject to the maximum permissible interchange fee for swipe transactions, equal to no more than 21 cents plus 5 basis points of the transaction value for many types of debit interchange transactions.
- We calculate our FDIC deposit assessment base using a performance score and a loss-severity score system described below in “Deposit Insurance.”

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- We are subject to the "Volcker Rule," which generally restricts us from engaging in activities that are considered proprietary trading and from sponsoring or investing in certain entities, including hedge or private equity funds that are considered covered funds. While Hope Bancorp and the Bank had no investment positions or relationships at December 31, 2018 that were subject to the Volcker Rule, we may be subject to the compliance and recording keeping provisions of this rule.

The Dodd-Frank Act requires banking organizations with consolidated assets exceeding $10 billion to establish board-level risk committees and to perform annual stress tests. The Economic Growth, Regulatory Relief, and Consumer Protection Act enacted in 2018 raises the asset thresholds for these requirements to $50 billion and $100 billion, respectively.

Many aspects of the Dodd-Frank Act continue to be subject to rule-making and have yet to take full effect, making it difficult to anticipate the overall financial impact on the Company, its customers or the financial industry generally. Provisions in the legislation that affect deposit insurance assessments, payment of interest on demand deposits and interchange fees could increase the costs associated with deposits as well as place limitations on certain revenues those deposits may generate.

Prompt Corrective Action

The FDI Act requires the federal bank regulatory agencies to take "prompt corrective action" with respect to a depository institution that does not meet certain capital adequacy standards, including requiring the prompt submission of an acceptable capital restoration plan. Depending on the bank's capital ratios, the agencies' regulations define five categories in which an insured depository institution will be placed: well-capitalized, adequately capitalized, undercapitalized, significantly undercapitalized, and critically undercapitalized. At each successive lower capital category, an insured bank is subject to more restrictions, including restrictions on the bank's activities, operational practices or the ability to pay dividends or executive bonuses.

The prompt corrective action standards were revised to conform with the New Capital Rules. Under current standards, in order to be generally considered well-capitalized for bank regulatory purposes, the Bank is required maintain the following minimum capital ratios: a common equity Tier 1 ratio of 6.5%, a Tier 1 ratio of 8%, a total capital ratio of 10% and a leverage ratio of 5%. A bank meeting the minimum capital ratios required to be considered well-capitalized, adequately capitalized, or undercapitalized may, however, may be treated as though it were in the next lower capital category if the appropriate federal banking agency, after notice and opportunity for hearing, determines that an unsafe or unsound condition or practice warrants such treatment.

The federal banking agencies also may require banks and bank holding companies subject to enforcement actions to maintain capital ratios in excess of the minimum ratios otherwise generally required to be deemed well capitalized for bank regulatory purposes, in which case institutions may no longer be deemed to be well capitalized and may therefore be subject to certain restrictions such as on taking brokered deposits.

Consumer Compliance Laws

The Bank must comply with numerous federal and state consumer protection statutes and implementing regulations, including, but not limited to, the Fair Debt Collection Practices Act, the Fair Credit Reporting Act, the Equal Credit Opportunity Act, the Truth in Lending Act, the Fair Housing Act, the Home Mortgage Disclosure Act, the Real Estate Settlement Procedures Act, the National Flood Insurance Act, the California Homeowner Bill of Rights and various federal and state privacy protection laws, including the Telephone Consumer Protection Act, and CAN-SPAM Act. The Bank and Hope Bancorp are also subject to federal and state laws prohibiting unfair or fraudulent business practices, untrue or misleading advertising and unfair competition.

These laws and regulations mandate certain disclosure and reporting requirements and regulate the manner in which financial institutions must deal with customers when taking deposits, making loans, servicing, collecting and foreclosure of loans, and providing other services. Failure to comply with these laws and regulations can subject the Bank to various penalties, including but not limited to enforcement actions, injunctions, fines or criminal penalties, punitive damages to consumers, and the loss of certain contractual rights.

Community Reinvestment Act

The Bank is subject to the Community Reinvestment Act ("CRA"), which requires federal banking regulators to evaluate the record of a financial institution in meeting the credit needs of its local communities, including low and

moderate income neighborhoods. The federal banking agencies consider a financial institution's compliance with the CRA into account when considering regulatory applications for mergers and other expansionary activities. The Bank received a "Satisfactory" rating in the most recent public disclosure of CRA performance evaluation released by the FDIC in 2018, which states that the Bank's CRA performance under the Lending, Investment, and Service Tests supports the overall rating.

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USA PATRIOT Act and Anti-Money Laundering Laws

Under the USA PATRIOT Act of 2001, financial institutions are subject to prohibitions against specified financial transactions and account relationships, as well as enhanced due diligence standards that are intended to prevent and detect the use of the United States financial system for money laundering and terrorist financing activities. The act requires financial institutions, including banks, to establish anti-money laundering programs, including employee training and independent audit requirements, meet minimum standards specified by the act, follow minimum standards for customer identification and maintenance of customer identification records, and regularly compare customer lists against lists of suspected terrorists, terrorist organizations and money launderers.

The Bank Secrecy Act (the "BSA") establishes requirements for recordkeeping and reporting by banks and other financial institutions that are intended to help identify the source, volume and movement of currency and other monetary instruments into and out of the United States in order to help detect and prevent money laundering connected with drug trafficking, terrorism and other criminal activities. Under the BSA and related regulations, banking institutions must file suspicious activity reports and maintain programs designed to assure and monitor compliance with certain recordkeeping and reporting requirements regarding currency transactions. The programs must include systems and internal controls to assure ongoing compliance, provide for independent testing of such systems and compliance and provide appropriate personnel training.

Loans to One Borrower

Under California law, the Bank's ability to make aggregate secured and unsecured loans to borrower is limited to 25% and 15%, respectively, of the Bank's unimpaired capital and surplus. The Bank has established internal loan limits that are lower than the legal lending limits for a California bank.

Deposit Insurance

The FDIC is an independent federal agency that insures deposits, up to prescribed statutory limits, of federally insured banks and savings institutions, and safeguards the safety and soundness of the depository institutions. The FDIC insures our customer deposits through the DIF up to prescribed limits. The FDIC may terminate a depository institution's deposit insurance upon a finding that the institution's financial condition is unsafe or unsound, or that the institution has engaged in unsafe or unsound practices that pose a risk to the DIF or that may prejudice the interest of the bank's depositors. The termination of the Bank's deposit insurance would result in the revocation of the Bank's charter by the DBO.

We are generally unable to control the amount of assessments that we pay for FDIC insurance, which can be affected by the cost of bank failures to the FDIC, among other factors. The Dodd-Frank Act revised the FDIC's DIF management authority by setting requirements for the Designated Reserve Ratio (the DIF balance divided by estimated insured deposits) and redefining the assessment base which is used to calculate banks' quarterly assessments. The amount of FDIC assessments paid by each DIF member institution is based on its asset size and its relative risk of default as measured by regulatory capital ratios and other supervisory factors.

In 2016, the FDIC adopted a rule increasing the DIF's minimum reserve ratio to 1.35% as required by the Dodd Frank Act. As required by the Dodd-Frank Act, the costs of increasing the DIF's reserve ratio from 1.15% to 1.35% was borne by depository institutions with total consolidated assets of $10 billion or more, which had an impact on the Bank's deposit insurance assessments because the Bank exceeded $10 billion in assets. In 2018, the FDIC reached the minimum reserve ratio of 1.35% and as a result the FDIC does not currently assesses a surcharge on banks with total assets in excess of $10 billion. Any future changes in FDIC insurance assessments may have a material and adverse effect on our earnings and could have a material adverse effect on the value of, or market for, our common stock.

Safety and Soundness Standards; Regulatory Enforcement Authority

The federal and California bank regulatory agencies have extensive discretion in connection with their supervisory and enforcement activities and examination policies, including policies with respect to the classification of assets and the establishment of appropriate loan loss reserves for regulatory purposes. The federal bank regulatory agencies have adopted guidelines to assist in identifying and addressing potential safety and soundness concerns before an institution's capital becomes impaired. The guidelines establish operational and managerial standards generally relating to: (1) internal controls, information systems, and internal audit systems; (2) loan documentation; (3) credit underwriting; (4) interest-rate exposure; (5) asset growth and asset quality; and (6) compensation, fees, and benefits.

Further, the regulatory agencies have adopted safety and soundness guidelines for asset quality and for evaluating and monitoring earnings to ensure that earnings are sufficient for the maintenance of adequate capital and reserves.

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If, as a result of an examination, the FRB, the FDIC or the DBO should determine that the financial condition, capital resources, asset quality, earnings prospects, management, liquidity, or other aspects of the Company's or the Bank's operations are unsatisfactory or that the Company or the Bank or management is violating or has violated any law or regulation, these agencies have the authority to:

- Require affirmative action to correct any conditions resulting from any violation or practice;
- Direct an increase in capital and the maintenance of higher specific minimum capital ratios, which could preclude the Hope Bancorp or the Bank from being deemed well capitalized which, in the case of the Bank, would restrict its ability to accept certain brokered deposits, for example;
- Restrict Hope Bancorp's or the Bank's growth geographically, by products and services, or by mergers and acquisitions;
- Enter into or issue informal or formal enforcement actions, including required board resolutions, memoranda of understanding, written agreements and consent or cease and desist orders or prompt corrective action orders to take corrective action and cease unsafe and unsound practices;
- Assess civil money penalties;
- Require prior approval of senior executive officer or director changes; remove officers and directors and assess civil monetary penalties; and
- Terminate FDIC insurance, revoke the charter and/or take possession of and close and liquidate the Bank or appoint the FDIC as receiver.

Dividends and Stock Repurchases

Hope Bancorp's ability to pay dividends or repurchase shares of its common stock is subject to restrictions set forth in the Delaware General Corporation Law. The Delaware General Corporation Law provides that a Delaware corporation may pay dividends or repurchase its shares either (i) out of the corporation's surplus (as defined by Delaware law), or (ii) if there is no surplus, out of the corporation's net profits for the fiscal year in which the dividend is declared and/or the preceding fiscal year. It is the FRB's policy, however, that bank holding companies should generally pay dividends on common stock only out of income available over the past year, and only if prospective earnings retention is consistent with the organization's expected future needs and financial condition. FRB policy requires that a banking holding company must notify the FRB its repurchase or redemption of shares would cause a net reduction of in the amount of such capital instrument outstanding at the beginning of the quarter in which the redemption or repurchase occurs. It is also the FRB's policy that bank holding companies should not maintain dividend levels or repurchase shares in amounts that would that undermine their ability to be a source of strength to its banking subsidiaries. The FRB also discourages dividend payment ratios that are at maximum allowable levels unless both asset quality and capital are very strong. In addition, if Hope Bancorp does not maintain an adequate capital conservation buffer under the New Capital Rules, its ability to pay dividends to or repurchase shares from shareholders may be restricted.

The Bank is a legal entity that is separate and distinct from Hope Bancorp. Hope Bancorp depends the Bank's payment of dividends as primary source of cash for use in Hope Bancorp's operations, Hope Bancorp's payment of dividends to shareholders and Hope Bancorp's stock repurchases. The Bank's ability to pay dividends to Hope Bancorp is subject to provisions of the California Financial Code that limit the amount available for cash dividends to the lesser of a bank's retained earnings or net income for its last three fiscal years (less any distributions to shareholders made during such period). Where the above test is not met, cash dividends may still be paid, with the prior approval of the DBO, in an amount not exceeding the greatest of (1) retained earnings of the bank; (2) the net income of the bank for its last fiscal year; or (3) the net income of the bank for its current fiscal year. The Bank's ability to pay cash dividends to Hope Bancorp will also depend upon management's assessment of future capital requirements, contractual restrictions, and other factors. If the Bank does not maintain an adequate capital conservation buffer under the New Capital Rules, the Bank may face restrictions on its ability to pay dividends to Hope Bancorp.

Consumer Financial Protection Bureau

The Dodd-Frank Act created the CFPB as an independent entity within the FRB with broad rulemaking, supervisory and enforcement authority over consumer financial products and services, including deposit products, residential mortgages, home-equity loans and credit cards. The bureau's functions include investigating consumer complaints,

conducting market research, rulemaking, supervising and examining bank consumer transactions, and enforcing rules related to consumer financial products and services. CFPB regulations and guidance apply to all financial institutions and banks with $10 billion or more in assets are subject to examination by the CFPB. Banks with less than $10 billion in assets continue to be examined for compliance by their primary federal banking agency. The Bank is subject to examination by the CFPB. The CFPB has the authority to bring formal and informal enforcement actions against the Bank similar to those that may be brought by the federal banking regulators discussed above.

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In 2014, the CFPB adopted revisions to Regulation Z, which implement the Truth in Lending Act, pursuant to the Dodd-Frank Act, and apply to consumer mortgages. The revisions mandate specific underwriting criteria for home loans in order for creditors to make a reasonable, good faith determination of a consumer’s ability to repay and establish certain protections from liability under the requirements for “qualified mortgages” that meet certain specific standards. As required by the Dodd-Frank Act, the CFPB also promulgated TILA-RESPA Integrated Disclosure (”TRID”) rules which became effective in 2015 and require new mortgage disclosures. The Bank believes it has fully implemented the TRID requirements.

Employees

As of December 31, 2018, we had 1,494 full-time equivalent employees compared to 1,470 full-time equivalent employees at December 31, 2017. None of our employees are represented by a union or covered by a collective bargaining agreement. Management believes that its relations with its employees are good.

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Item 1A. RISK FACTORS

In the course of conducting its business operations, we are exposed to a variety of risks, some of which are inherent in the financial services industry and others of which are more specific to its own business. The following discussion addresses the most significant risks that could affect our business, financial condition, liquidity, results of operations, and capital position. The risks and uncertainties described below are not the only ones we face. Additional risks and uncertainties not presently known to us or that we currently deem immaterial may also affect our business. If any of these known or unknown risks or uncertainties actually occurs, our business, financial condition and results of operations may be materially and adversely effected. In that event, the market price for our common stock will likely decline.

Economic conditions in the markets in which we operate may adversely affect our loan portfolio and reduce the demand for our services. We focus our business primarily in Korean-American communities in California, the greater New York City, Chicago, Houston and Dallas, and Seattle metropolitan areas, New Jersey, Virginia, Alabama, and Georgia. Adverse economic conditions in our market areas could potentially have a material adverse impact on the quality of our business. A renewed economic slowdown in the markets in which we operate currently and in the future may have any or all of the following consequences, any of which may reduce our net income and adversely affect our financial condition:

- loan delinquencies may increase;
- problem assets and foreclosures may increase;
- the level and duration of deposits may decline;
- demand for our products and services may decline; and
- collateral for loans may decline in value below the principal amount owed by the borrower.

We have a high level of loans secured by real estate collateral. A downturn in the real estate market may seriously impair our loan portfolio. As of December 31, 2018, approximately 80% of our loan portfolio consisted of loans secured by various types of real estate (including 1-4 family residential loans in our consumer loan portfolio). Following the financial crisis of 2008, there was a general slowdown in the economy and declines in the value of real estate. Although the economy has rebounded and real estate prices have gradually recovered from their earlier low levels, it is possible that there will be renewed deterioration in the real estate market generally and in commercial real estate values in particular. Such developments may result in additional loan charge-offs and provisions for loan losses, which may have a material and adverse effect on our net income and capital levels.

Our commercial loan and commercial real estate loan portfolios expose us to risks that may be greater than the risks related to our other loans. Our loan portfolio includes commercial loans and commercial real estate loans, which are secured by hotels and motels, shopping/retail centers, service station and car wash, industrial and warehouse properties, and other types of commercial properties. Commercial and commercial real estate loans carry more risk as compared to other types of lending, because they typically involve larger loan balances often concentrated with a single borrower or groups of related borrowers.

Accordingly, charge-offs on commercial and commercial real estate loans may be larger on a per loan basis than those incurred with our residential or consumer loan portfolios. In addition, these loans expose a lender to greater credit risk than loans secured by residential real estate. The payment experience on commercial real estate loans that are secured by income producing properties are typically dependent on the successful operation of the related real estate project and thus, may subject us to adverse conditions in the real estate market or to the general economy. The collateral securing these loans typically cannot be liquidated as easily as residential real estate. If we foreclose on these loans, our holding period for the collateral typically is longer than residential properties because there are fewer potential purchasers of the collateral.

Unexpected deterioration in the credit quality of our commercial or commercial real estate loan portfolios would require us to increase our provision for loan losses, which would reduce our profitability and could materially adversely affect our business, financial condition, results of operations and prospects.

In addition, with respect to commercial real estate loans, federal and state banking regulators are examining commercial real estate lending activity with heightened scrutiny and may require banks with higher levels of commercial real estate loans to implement more stringent underwriting, internal controls, risk management policies

and portfolio stress testing, as well as possibly higher levels of allowances for losses and capital levels as a result of commercial real estate lending growth and exposures. Because a significant portion of our loan portfolio is comprised of commercial real estate loans, the banking regulators may require us to maintain higher levels of capital than we would otherwise be expected to maintain, which could limit our ability to leverage our capital and have a material adverse effect on our business, financial condition, results of operations and prospects.

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Our allowance for loan losses may not cover our actual loan losses. If our actual loan losses exceed the amount we have allocated for estimated probable incurred losses, our business will be adversely affected. We attempt to limit the risk that borrowers will fail to repay loans by carefully underwriting our loans, but losses nevertheless occur in the ordinary course of business operations. We create allowances for estimated loan losses through provisions that are recorded as reductions in income in our accounting records. We base these allowances on estimates of the following:

- historical experience with our loans;
- evaluation of current economic conditions and other factors;
- reviews of the quality, mix and size of the overall loan portfolio;
- reviews of delinquencies; and
- the quality of the collateral underlying our loans.

If our allowance estimates are inadequate, we may incur losses, our financial condition may be materially and adversely affected and we may be required to try and raise additional capital to enhance our capital position. In addition, various regulatory agencies, as an integral part of their examination process, periodically review the adequacy of our allowance. These agencies may require us to establish additional allowances based on their judgment of the information available at the time of their examinations. No assurance can be given that we will not sustain loan losses in excess of present or future levels of the allowance for loan losses or that regulatory agencies will not require us to increase our allowance thereby impacting our profitability.

Changes in interest rates affect our profitability. The interest rate risk inherent in our lending, investing, and deposit taking activities is a significant market risk to us and our business. We derive our income mainly from the difference or “spread” between the interest earned on loans, securities and other interest earning assets, and interest paid on deposits, borrowings and other interest bearing liabilities. In general, the wider the spread, the more net interest income we earn. When market rates of interest change, the interest we receive on our assets and the interest we pay on our liabilities will fluctuate. This can cause decreases in our spread and can greatly affect our income. In addition, interest rate fluctuations can affect how much money we may be able to lend. There can be no assurance that we will be successful in minimizing the potentially adverse effects of changes in interest rates.

If we lose key employees, our business may suffer. There is intense competition for experienced and highly qualified personnel in the Korean-American banking industry and the banking industry more broadly. Our future success depends on the continued employment of existing senior management personnel. If we lose key employees temporarily or permanently, it may hurt our business. We may be particularly hurt if our key employees, including any of our executive officers, became employed by our competitors in the Korean-American banking industry.

Environmental laws may force us to pay for environmental problems. The cost of cleaning up or paying damages and penalties associated with environmental problems may increase our operating expenses. When a borrower defaults on a loan secured by real property, we often purchase the property in foreclosure or accept a deed to the property surrendered by the borrower. We may also take over the management of commercial properties whose owners have defaulted on loans. We also lease premises where our branches and other facilities are located, all where environmental problems may exist. Although we have lending, foreclosure and facilities guidelines that are intended to exclude properties with an unreasonable risk of contamination, hazardous substances may exist on some of the properties that we own, lease, manage or occupy. We may face the risk that environmental laws may force us to clean up the properties at our expense. The cost of cleaning up a property may exceed the value of the property. We may also be liable for pollution generated by a borrower’s operations if we take a role in managing those operations after a default. We may find it difficult or impossible to sell contaminated properties.

We are exposed to the risks of natural disasters. A significant portion of our operations is concentrated in Southern California, which is an earthquake and fire prone region. A major earthquake or fire may result in material loss to us. A significant percentage of our loans are and will be secured by real estate. Many of our borrowers may suffer uninsured property damage, experience interruption of their businesses or lose their jobs after an earthquake or fire. Those borrowers might not be able to repay their loans, and the collateral for such loans may decline significantly in value. Unlike a bank with operations that are more geographically diversified, we are vulnerable to greater losses if an earthquake, fire, flood, mudslide or other natural catastrophe occurs in Southern California.

An increase in nonperforming assets would reduce our income and increase our expenses. If the level of nonperforming assets increases in the future, it may adversely affect our operating results and financial condition. Nonperforming assets are mainly loans on which the borrowers are not making their required payments. Nonperforming assets also include loans that have been restructured to permit the borrower to make payments and real estate that has been acquired through foreclosure or deed in lieu of foreclosure of unpaid loans. To the extent that assets are nonperforming, we have less earning assets generating interest income and an increase in credit related expenses, including provisions for loan losses.

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We may experience adverse effects from acquisitions. We have acquired other banking companies and bank offices in the past, and will consider additional acquisitions as opportunities arise. If we do not adequately address the financial and operational risks associated with acquisitions of other companies, we may incur material unexpected costs and disruption of our business. Future acquisitions may increase the degree of such risks.
Risks involved in acquisitions of other companies include:

- the risk of failure to adequately evaluate the asset quality of the acquired company;
- difficulty in assimilating the operations, technology and personnel of the acquired company;
- diversion of management's attention from other important business activities;
- difficulty in maintaining good relations with the loan and deposit customers of the acquired company;
- inability to maintain uniform and effective operating standards, controls, procedures and policies;
- potentially dilutive issuances of equity securities or the incurrence of debt and contingent liabilities; and
- amortization of expenses related to acquired intangible assets that have finite lives.

Liquidity risks may impair our ability to fund operations and jeopardize our financial condition. Liquidity is essential to our business. An inability to raise funds through deposits, borrowings, the sale of loans, and other sources may have a material adverse effect on our liquidity. Our access to funding sources in amounts adequate to finance our activities may be impaired by factors that affect us specifically or the financial services industry in general. Factors that may detrimentally impact our access to liquidity sources include a decrease in the level of our business activity due to a market downturn or adverse regulatory action against us. Our ability to acquire deposits or borrow may also be impaired by factors that are not specific to us, such as a disruption of the financial markets or negative views and expectations about the prospects for the banking industry or the general financial services industry as a whole.
Increases in the level of our problem assets, occurrence of operating losses or a failure to comply with requirements of the agencies which regulate us may result in regulatory actions against us which may materially and adversely affect our business and the market price of our common stock. The DBO, the FDIC, and the FRB each have authority to take actions to require that we comply with applicable regulatory capital requirements, cease engaging in what they perceive to be unsafe or unsound practices or make other changes in our business. Among others, the corrective measures that such regulatory authorities may take include requiring us to enter into informal or formal agreements regarding our operations, the issuance of cease and desist orders to refrain from engaging in unsafe and unsound practices, removal of officers and directors and the assessment of civil monetary penalties. See "Item 1. Business – Supervision and Regulation" for a further description of such regulatory powers.
Changes in accounting standards may affect how we record and report our financial condition and results of operations. Our accounting policies and methods are fundamental to how we record and report our financial condition and results of operations. From time to time, the Financial Accounting Standards Board and SEC change the financial accounting and reporting standards that govern the preparation of our financial statements. These changes and their impacts on us can be hard to predict and may result in unexpected and materially adverse impacts on our reported financial condition and results of operations.
For example, in June 2016, the Financial Accounting Standards Board issued ASU 2016-13, Financial Instruments - Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments. ASU 2016-13 requires banking organizations to determine the adequacy of their allowance for loan losses with an expected loss model, which is referred to as the current expected credit loss ("CECL") model. Under the CECL model, banking organizations will be required to present certain financial assets carried at amortized cost, such as loans held for investment and held-to-maturity debt securities, at the net amount expected to be collected. The measurement of expected credit losses is to be based on information about past events, including historical experience, current conditions, and reasonable and supportable forecasts that affect the collectability of the reported amount. This measurement will take place at the time the financial asset is first added to the balance sheet and periodically thereafter. This differs significantly from the "incurred loss" model required under current GAAP, which delays recognition until it is probable a loss has been incurred. Adoption of the CECL model will significantly change the manner in which the Company determines the adequacy of its allocation for loan losses. ASU 2016-13 is expected to be effective for public business entities for fiscal years after December 15, 2019. The Company is evaluating the impact the CECL model will have on its accounting, but the Company may recognize a one-time cumulative-effect adjustment to the allowance for loan

losses as of the beginning of the first reporting period in which the new standard is effective. The Company cannot yet determine the magnitude of any such one-time cumulative adjustment or of the overall impact of the new standard on its financial condition or results of operations. The federal banking regulators have adopted a rule that gives a banking organization the option to phase in over a three-year period the day-one adverse effects of CECL on its regulatory capital.

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We face a risk of noncompliance and enforcement action with the Bank Secrecy Act and other anti-money laundering statutes and regulations. The Bank Secrecy Act, the USA PATRIOT Act of 2001, and other laws and regulations require financial institutions, among other duties, to institute and maintain an effective anti-money laundering program and file suspicious activity and currency transaction reports as appropriate. The federal Financial Crimes Enforcement Network is authorized to impose significant civil money penalties for violations of those requirements and has recently engaged in coordinated enforcement efforts with the individual federal banking regulators, as well as the U.S. Department of Justice, Drug Enforcement Administration, and Internal Revenue Service. We are also subject to increased scrutiny of compliance with the rules enforced by the Office of Foreign Assets Control and compliance with the Foreign Corrupt Practices Act. If our policies, procedures and systems are deemed deficient, we would be subject to liability, including fines and regulatory actions, which may include restrictions on our ability to pay dividends and the necessity to obtain regulatory approvals to proceed with certain aspects of our business plan. Failure to maintain and implement adequate programs to combat money laundering and terrorist financing could also have serious reputational consequences for us. Any of these results could materially and adversely affect our business, financial condition and results of operations.

The occurrence of fraudulent activity, breaches or failures of our information security controls or cybersecurity-related incidents could have a material adverse effect on our business. As a financial institution, we are susceptible to fraudulent activity, information security breaches and cybersecurity-related incidents that may be committed against us or our clients, which may result in financial losses or increased costs to us or our clients, disclosure or misuse of our information or our client information, misappropriation of assets, privacy breaches against our clients, litigation, or damage to our reputation. Such fraudulent activity may take many forms, including check fraud, electronic fraud, wire fraud, phishing, social engineering, and other dishonest acts. Information security breaches and cybersecurity-related incidents may include fraudulent or unauthorized access to systems used by us or our clients, denial or degradation of service attacks, and malware, or other cyber-attacks. In recent periods, there continues to be a rise in electronic fraudulent activity, security breaches, and cyber-attacks within the financial services industry, especially in the commercial banking sector due to cyber criminals targeting commercial bank accounts. Consistent with industry trends, we have also experienced an increase in attempted electronic fraudulent activity, security breaches and cybersecurity-related incidents in recent periods. Moreover, in recent periods, several large corporations, including financial institutions and retail companies, have suffered major data breaches, in some cases exposing not only confidential and proprietary corporate information, but also sensitive financial and other personal information of their customers and employees and subjecting them to potential fraudulent activity. Some of our clients may have been affected by these breaches, which increase their risks of identity theft, credit card fraud and other fraudulent activity that could involve their accounts with us.

Information pertaining to us and our clients is maintained, and transactions are executed, on the networks and systems of us, our clients and certain of our third party partners, such as our online banking or reporting systems. The secure maintenance and transmission of confidential information, as well as execution of transactions over these systems, are essential to protect us and our clients against fraud and security breaches and to maintain our clients’ confidence. Breaches of information security also may occur, and in infrequent cases have occurred, through intentional or unintentional acts by those having access to our systems or our clients’ or counterparties’ confidential information, including employees. In addition, increases in criminal activity, levels and sophistication, advances in computer capabilities, new discoveries, vulnerabilities in third-party technologies (including browsers and operating systems) or other developments could result in a compromise or breach of the technology, processes and controls that we use to prevent fraudulent transactions and to protect data about us, our clients and underlying transactions, as well as the technology used by our clients to access our systems. Although we have developed, and continue to invest in, systems and processes that are designed to detect and prevent security breaches and cyber-attacks and periodically test our security, our inability to anticipate, or failure to adequately mitigate, breaches of security could result in: losses to us or our clients; our loss of business and/or clients; damage to our reputation; the incurrence of additional expenses; disruption to our business; our inability to grow our online services or other businesses; additional regulatory scrutiny or penalties; or our exposure to civil litigation and possible financial liability - any of which could have a material adverse effect on our business, financial condition and results of operations.

More generally, publicized information concerning security and cyber-related problems could inhibit the use or growth of electronic or web-based applications or solutions as a means of conducting commercial transactions. Such publicity may also cause damage to our reputation as a financial institution. As a result, our business, financial condition and results of operations could be adversely affected.

We are subject to operational risks relating to our technology and information systems. The continued efficacy of our technology and information systems, related operational infrastructure and relationships with third party vendors in our ongoing operations is integral to our performance. Failure of any of these resources, including but not limited to operational or systems failures, interruptions of client service operations and ineffectiveness of or interruption in third party data processing or other vendor support, may cause material disruptions in our business, impairment of customer relations and exposure to liability for our customers, as well as action by bank regulatory authorities.

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Our business reputation is important and any damage to it may have a material adverse effect on our business. Our reputation is very important for our business, as we rely on our relationships with our current, former, and potential clients and stockholders in the communities we serve. Any damage to our reputation, whether arising from regulatory, supervisory or enforcement actions, matters affecting our financial reporting or compliance with SEC and exchange listing requirements, negative publicity, our conduct of our business or otherwise may have a material adverse effect on our business.

As we expand outside our California markets, we may encounter additional risks that may adversely affect us. Currently, the majority of our offices are located in California, but we also have offices in the New York City, Chicago, Houston, Dallas, and Seattle metropolitan areas, New Jersey, Virginia, Alabama, and Georgia. Over time, we may seek to establish offices to serve Korean-American communities in other parts of the United States as well. In the course of these expansion activities, we may encounter significant risks, including unfamiliarity with the characteristics and business dynamics of new markets, increased marketing and administrative expenses and operational difficulties arising from our efforts to attract business in new markets, manage operations in noncontiguous geographic markets, comply with local laws and regulations and effectively and consistently manage our non-California personnel and business. If we are unable to manage these risks, our operations may be materially and adversely affected.

Adverse conditions in South Korea or globally may adversely affect our business. A substantial number of our customers have economic and cultural ties to South Korea and, as a result, we are likely to feel the effects of adverse economic and political conditions there. If economic or political conditions in South Korea deteriorate, we may, among other things, be exposed to economic and transfer risk, and may experience an outflow of deposits by our customers with connections to South Korea. Transfer risk may result when an entity is unable to obtain the foreign exchange needed to meet its obligations or to provide liquidity. This may materially and adversely impact the recoverability of investments in or loans made to such entities. Adverse economic conditions in South Korea may also negatively impact asset values and the profitability and liquidity of our customers who operate in this region. In addition, a general overall decline in global economic conditions may materially and adversely affect our profitability and overall results of operations.

Our use of appraisals in deciding whether to make loans secured by real property does not ensure that the value of the real property collateral will be sufficient to repay our loans. In considering whether to make a loan secured by real property, we require an appraisal of the property. However, an appraisal is only an estimate of the value of the property at the time the appraisal is made and requires the exercise of a considerable degree of judgment. If the appraisal does not accurately reflect the amount that may be obtained upon sale or foreclosure of the property, whether due to a decline in property value after the date of the original appraisal or defective preparation of the appraisal, we may not realize an amount equal to the indebtedness secured by the property and as a result, we may suffer losses.

Governmental regulation and regulatory actions against us may further impair our operations or restrict our growth. We are subject to significant governmental supervision and regulation. These regulations affect our lending practices, capital structure, investment practices, dividend policy and growth, among other things. Congress and federal regulatory agencies continually review banking laws, regulations and policies for possible changes. Statutes and regulations affecting our business may be changed at any time and the interpretation of these statutes and regulations by examining authorities may also change. In addition, regulations may be adopted which increase our deposit insurance premiums and enact special assessments which could increase expenses associated with running our business and adversely affect our earnings.

There can be no assurance that such statutes and regulations, any changes thereto or to their interpretation will not adversely affect our business. In particular, these statutes and regulations, and any changes thereto, could subject us to additional costs (including legal and compliance costs), limit the types of financial services and products we may offer and/or increase the ability of non-banks to offer competing financial services and products, among other things. In addition to governmental supervision and regulation, we are subject to changes in other federal and state laws, including changes in tax laws, which could materially affect us and the banking industry generally. We are subject to the rules, regulations of, and examination by the FRB, the FDIC and the DBO, and the CFPB. In addition, we are subject to the rules and regulation of the Nasdaq Stock Market and the SEC and are subject to enforcement actions

and other punitive actions by these agencies. If we fail to comply with federal and state regulations, the regulators may limit our activities or growth, impose fines on us or in the case of our bank regulators, ultimately require our bank to cease its operations. Bank regulations can hinder our ability to compete with financial services companies that are not regulated in the same manner or are less regulated. Federal and state bank regulatory agencies regulate many aspects of our operations. These areas include:

- the capital that must be maintained;
- the kinds of activities that can be engaged in;
- the kinds and amounts of investments that can be made;
- the locations of offices;
- insurance of deposits and the premiums that we must pay for this insurance;
- procedures and policies we must adopt;

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- conditions and restrictions on our executive compensation; and
- how much cash we must set aside as reserves for deposits.

In addition, bank regulatory authorities have the authority to bring enforcement actions against banks and bank holding companies, including the Bank and Hope Bancorp, for unsafe or unsound practices in the conduct of their businesses or for violations of any law, rule or regulation, any condition imposed in writing by the appropriate bank regulatory agency or any written agreement with the authority. Enforcement actions against us could include a federal conservatorship or receivership for the bank, the issuance of additional orders that could be judicially enforced, the imposition of civil monetary penalties, the issuance of directives to enter into a strategic transaction, whether by merger or otherwise, with a third party, the termination of insurance of deposits, the issuance of removal and prohibition orders against institution-affiliated parties, and the enforcement of such actions through injunctions or restraining orders. In addition, as we have grown beyond $10 billion in assets, we are subject to enhanced CFPB examination as well as required to perform more comprehensive stress-testing on our business and operations.

SBA lending is an important part of our business. Our SBA lending program is dependent upon the federal government, and we face specific risks associated with originating SBA loans. Our SBA lending program is dependent upon the federal government. As an SBA Preferred Lender, we enable our clients to obtain SBA loans without being subject to the potentially lengthy SBA approval process necessary for lenders that are not SBA Preferred Lenders. The SBA periodically reviews the lending operations of participating lenders to assess, among other things, whether the lender exhibits prudent risk management. When weaknesses are identified, the SBA may request corrective actions or impose enforcement actions, including revocation of the lender’s Preferred Lender status. If we lose our status as a Preferred Lender, we may lose some or all of our customers to lenders who are SBA Preferred Lenders, and as a result we could experience a material adverse effect to our financial results. Any changes to the SBA program, including changes to the level of guarantee provided by the federal government on SBA loans, may also have a material adverse effect on our business.

We historically sold the guaranteed portion of our SBA 7(a) loans in the secondary market, but during the end of 2018, we made the decision to retain most of the SBA 7(a) loans that we originate due to the low premiums being offered in the secondary market. These sales of SBA 7(a) loans have historically resulted in both premium income for us at the time of sale, and created a stream of future servicing income. We may not be able to continue originating these loans or return to selling them in the secondary market. Furthermore, even if we are able to continue originating and return to selling SBA 7(a) loans in the secondary market, we might not continue to realize premiums upon the sale of the guaranteed portion of these loans. When we sell the guaranteed portion of our SBA 7(a) loans, we incur credit risk on the non-guaranteed portion of the loans, and if a customer defaults on the non-guaranteed portion of a loan, we share any loss and recovery related to the loan pro-rata with the SBA. If the SBA establishes that a loss on an SBA guaranteed loan is attributable to significant technical deficiencies in the manner in which the loan was originated, funded or serviced by us, the SBA may seek recovery of the principal loss related to the deficiency from us, which could materially adversely affect our business, financial condition, results of operations and prospects.

The laws, regulations and standard operating procedures that are applicable to SBA loan products may change in the future. We cannot predict the effects of these changes on our business and profitability. Because government regulation greatly affects the business and financial results of all commercial banks and bank holding companies and especially our organization, changes in the laws, regulations and procedures applicable to SBA loans could adversely affect our ability to operate profitably.

Our stock price may be volatile, which may result in substantial losses for our stockholders. The market price of our common stock may be subject to fluctuations in response to a number of factors, including:

- issuing new equity securities;
- the amount of our common stock outstanding and the trading volume of our stock;
- actual or anticipated changes in our future financial performance;
- changes in financial performance estimates by us or by securities analysts;
- competitive developments, including announcements by us or our competitors of new products or services or acquisitions, strategic partnerships, joint ventures or capital commitments;
- the operating and stock performance of our competitors;

- changes in interest rates;
- changes in key personnel;
- changes in economic conditions that affect the Bank’s performance; and
- changes in legislation or regulations that affect the Bank.

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We may raise additional capital, which could have a dilutive effect on the existing holders of our common stock and adversely affect the market price of our common stock. We periodically evaluate opportunities to access capital markets, taking into account our financial condition, regulatory capital ratios, business strategies, anticipated asset growth and other relevant considerations. It is possible that future acquisitions, organic growth or changes in regulatory capital requirements could require us to increase the amount or change the composition of our current capital, including our common equity. For all of these reasons and others, and always subject to market conditions, we may issue additional shares of common stock or other capital securities in public or private transactions.
The issuance of additional common stock, debt, or securities convertible into or exchangeable for our common stock or that represent the right to receive common stock, or the exercise of such securities, could be substantially dilutive to holders of our common stock. Holders of our common stock have no preemptive or other rights that would entitle them to purchase their pro rata share of any offering of shares of any class or series and, therefore, such sales or offerings could result in dilution of the ownership interests of our stockholders.
We may reduce or discontinue the payment of dividends on common stock. Our stockholders are only entitled to receive such dividends as our Board may declare out of funds legally available for such payments. Although we have historically declared cash dividends on our common stock, we are not required to do so and may reduce or eliminate our common stock dividend in the future. Our ability to pay dividends to our stockholders is subject to the restrictions set forth in Delaware law, by the FRB, and by certain covenants contained in our subordinated debentures. Notification to the FRB is also required prior to our declaring and paying a cash dividend to our stockholders during any period in which our quarterly and/or cumulative twelve-month net earnings are insufficient to fund the dividend amount, among other requirements. We may not pay a dividend if the FRB objects or until such time as we receive approval from the FRB or we no longer need to provide notice under applicable regulations. In addition, we may be restricted by applicable law or regulation or actions taken by our regulators, now or in the future, from paying dividends to our stockholders. We cannot provide assurance that we will continue paying dividends on our common stock at current levels or at all. A reduction or discontinuance of dividends on our common stock could have a material adverse effect on our business, including the market price of our common stock.
The conditional conversion features of the convertible notes issued by the Company, if met, may adversely affect our financial condition and operating results. In the event the conditional conversion features of the convertible notes issued by the Company are met, holders of convertible notes will be entitled to convert the notes at any time during specified periods at their option. If one or more holders elect to convert their notes, unless we elect to satisfy our conversion obligation by delivering solely shares of our common stock (other than paying cash in lieu of delivering any fractional share), we would be required to settle a portion or all of our conversion obligation through the payment of cash, which could adversely affect our liquidity.
We may not have the ability to raise the funds necessary to settle conversions of the convertible notes in cash or to repurchase the convertible notes if holders of the convertible note exercise their repurchase rights or upon a fundamental change, and our future debt may contain limitations on our ability to pay cash upon conversion or repurchase of the convertible notes. Holders of the convertible notes will have the right to require us to repurchase all or a portion of their convertible notes on certain specified dates or upon the occurrence of a fundamental change at a repurchase price equal to 100% of the principal amount of the convertible notes to be repurchased, plus accrued and unpaid special interest, if any. We may not have enough available cash or be able to obtain financing at the time we are required to repurchase convertible notes surrendered or pay cash with respect to the convertible notes being converted if we elect not to issue shares, which could harm our reputation and affect the trading price of our common stock.
The value of our securities in our investment portfolio may decline in the future. The fair value of our investment securities may be adversely affected by market conditions, including changes in interest rates, implied credit spreads, and the occurrence of any events adversely affecting the issuer of particular securities in our investments portfolio or any given market segment or industry in which we are invested. We analyze our securities on a quarterly basis to determine if an other-than-temporary impairment has occurred. The process for determining whether impairment is other-than-temporary usually requires complex, subjective judgments about the future financial performance of the issuer in order to assess the probability of receiving all contractual principal and interest payments on the security.

Because of changing economic and market conditions affecting issuers, we may be required to recognize other-than-temporary impairment in future periods, which could have a material adverse effect on our business, financial condition, or results of operations.

If we fail to maintain an effective system of internal controls and disclosure controls and procedures, we may not be able to accurately report our financial results or prevent fraud. Effective internal control over financial reporting and disclosure controls and procedures are necessary for us to provide reliable financial reports, effectively prevent fraud and to operate successfully as a public company. If we cannot provide reliable financial reports or prevent fraud, our reputation and business would be harmed. In addition, failure in our internal control over financial reporting and disclosure controls and procedures could cause us to fail to meet the continued listing requirements of the Nasdaq Global Select Market and, as a result, adversely impact the liquidity and trading price of our securities.

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Anti-takeover provisions in our charter documents and applicable federal and state law may limit the ability of another party to acquire us, which could cause our stock price to decline. Various provisions of our charter documents could delay or prevent a third-party from acquiring us, even if doing so might be beneficial to our shareholders. These include, among other things, advance notice requirements to submit stockholder proposals at stockholder meetings and the authorization to issue “blank check” preferred stock by action of the Board of Directors acting alone, thus without obtaining stockholder approval. In addition, applicable provisions of federal and state law require regulatory approval in connection with certain acquisitions of our common stock and supermajority voting provisions in connection with certain transactions. In particular, both federal and state law limit the acquisition of ownership of, generally, 10% or more of our common stock without providing prior notice to the regulatory agencies and obtaining prior regulatory approval or non-objection or being able to rely on an exemption from such requirement. Collectively, these provisions of our charter documents and applicable federal and state law may prevent a merger or acquisition that would be attractive to stockholders and could limit the price investors would be willing to pay in the future for our common stock.

Our common stock is equity and therefore is subordinate to our subsidiaries’ indebtedness and preferred stock. Our common stock constitutes equity interests and does not constitute indebtedness. As such, common stock will rank junior to all current and future indebtedness and other non-equity claims on us with respect to assets available to satisfy claims against us, including in the event of our liquidation. We may, and the bank and our other subsidiaries may also, incur additional indebtedness from time to time and may increase our aggregate level of outstanding indebtedness. Additionally, holders of common stock are subject to the prior dividend and liquidation rights of any holders of our preferred stock that may be outstanding from time to time. The Board of Directors is authorized to cause us to issue additional classes or series of preferred stock without any action on the part of our stockholders. If we issue preferred shares in the future that have a preference over our common stock with respect to the payment of dividends or upon liquidation, or if we issue preferred shares with voting rights that dilute the voting power of the common stock, then the rights of holders of our common stock or the market price of our common stock could be materially adversely affected.

Our common stock is not insured and you could lose the value of your entire investment. An investment in our common stock is not a deposit and is not insured against loss by any government agency.

Implementation of the various provisions of the Dodd-Frank Act-in particular provisions that are applicable to banks and bank holding companies with $10 billion or more in assets-may delay the receipt of regulatory approvals and increase our operating costs or otherwise have a material effect on our financial condition, results of operations and stock price. The Dodd-Frank Wall Street Reform and Consumer Protection Act (the “Dodd-Frank Act”) enacted in 2010 significantly changes the bank regulatory structure and affects the lending, deposit, investment, trading and operating activities of financial institutions and their holding companies. The Dodd-Frank Act requires various federal agencies to adopt a broad range of new implementing rules and regulations and to prepare numerous studies and reports for Congress. The federal agencies are given significant discretion in drafting the implementing rules and regulations, and the rule-making process is still underway.

Several requirements in the Dodd-Frank Act for new banking regulations are applicable to certain banks and bank holding companies with $10 billion or more in assets. As a result of the merger, we surpassed this threshold, and these provisions, subject to a phase in period, will significantly increase compliance and operating costs and otherwise may have a significant impact on our business, financial condition, results of operations and stock price. Such provisions include the following:

- The Dodd-Frank Act created the CFPB, which has broad powers to supervise and enforce consumer protection laws. The CFPB has broad rule-making authority for a wide range of consumer protection laws that apply to all banks, including the authority to prohibit “unfair, deceptive or abusive” acts and practices. The CFPB has examination and enforcement authority over all banks with more than $10 billion in assets, and accordingly has assumed examination and enforcement authority over us post-merger.
- The Dodd-Frank Act increased the authority of the FRB to examine us and our non-bank subsidiaries and gave the FRB the authority to establish rules regarding interchange fees charged for an electronic debit transaction by a payment card issuer that, together with its affiliates, has assets of $10 billion or more, and to enforce a new statutory

requirement that such fees be reasonable and proportional to the actual cost of a transaction to the issuer (the "Durbin Amendment"). By regulation, the FRB has limited the fees for such a transaction to the sum of 21 cents plus five basis points times the value of the transaction, plus up to one cent for fraud prevention costs. The effect of the Durbin Amendment has significantly lowered our interchange or "swipe" revenue, but such lower fees are not expected to have a material adverse effect on our results of operations.

- The Dodd-Frank Act established 1.35% as the minimum Designated Reserve Ratio ("DRR"). The FDIC has determined that the DRR should be 2.0% and has adopted a plan under which it will meet the statutory minimum DRR of 1.35% by the statutory deadline of September 30, 2020. The Dodd-Frank Act requires the FDIC to offset the effect of the increase in the statutory minimum DRR to 1.35% from the former statutory minimum of 1.15% on institutions with assets less than $10 billion. As a result of the merger, we are no longer entitled to benefit from the offset.

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It is difficult to predict the overall compliance cost of these provisions, which became effective (with phase-in periods) when the merger was consummated. Compliance with these provisions will require additional staffing, engagement of external consultants and other operating costs that could have a material adverse effect on our future financial condition, results of operations and stock price.

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Item 1B. UNRESOLVED STAFF COMMENTS

None.

Item 2. PROPERTIES

Our principal executive offices are located at 3200 Wilshire Blvd., Suite 1400, Los Angeles, California 90010. As of December 31, 2018, we operated full-service branches at 56 leased and seven owned facilities, and we operated loan production offices at 11 leased facilities. Expiration dates of our leases range from 2019 to 2030. We believe our present facilities are suitable and adequate for our current operating needs.

Item 3. LEGAL PROCEEDINGS

In the normal course of business, we are involved in various legal claims. We have reviewed all legal claims against us with counsel and have taken into consideration the views of such counsel as to the potential outcome of the claims. Accrued loss contingencies for all legal claims totaled approximately $755 thousand at December 31, 2018. It is reasonably possible we may incur losses in addition to the amounts we have accrued. However, at this time, we are unable to estimate the range of additional losses that are reasonably possible because of a number of factors, including the fact that certain of these litigation matters are still in their early stages and involve claims for which, at this point, we believe have little to no merit. Management has considered these and other possible loss contingencies and does not expect the amounts to be material to any of the consolidated financial statements.

Item 4. MINE SAFETY DISCLOSURES

Not applicable.

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Part II

Item 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

Our common stock is traded on the NASDAQ Global Select Market under the symbol "HOPE."
The closing price for our common stock on the NASDAQ Global Select Market on February 25, 2019 was $14.68 per share. As of February 25, 2019, there were 1,200 stockholders of record of our common stock.

Stock Performance Graph
The following graph compares the yearly percentage change in the cumulative total shareholder return (stock price appreciation plus reinvested dividends) on our common stock with (i) the cumulative total return of the NASDAQ Composite Index, (ii) the cumulative total return of the S&P Small Cap 600 Index, (iii) a published index comprised of banks and thrifts selected by SNL Financial LLC, and (iv) the cumulative total return of the S&P 500 Index. The graph assumes an initial investment of $100 and reinvestment of dividends. Points on the graph represent the performance as of the last business day of each of the years indicated. The graph is not indicative of future price performance. The graph does not constitute soliciting material and shall not be deemed filed or incorporated by reference into any filing by Hope Bancorp under the Securities Act of 1933, as amended, or the Securities Exchange Act of 1934, as amended, except to the extent that we may specifically incorporate this graph by reference.

ASSUMES $100 INVESTED ON DECEMBER 31, 2013
ASSUMES DIVIDENDS REINVESTED
FISCAL YEAR ENDING DECEMBER 31, 2018

	Period Ending					
Stock/Index	12/31/2013	12/31/2014	12/31/2015	12/31/2016	12/31/2017	12/31/2018
Hope Bancorp, Inc.	$100.00	$88.77	$109.30	$143.04	$122.44	$82.21
NASDAQ Composite	$100.00	$114.75	$122.74	$133.62	$173.22	$168.30
S&P 600 Index	$100.00	$105.76	$103.67	$131.20	$148.56	$135.96
SNL Bank and Thrift	$100.00	$111.63	$113.89	$143.78	$169.07	$140.45
S&P 500 Index	$100.00	$113.69	$115.26	$129.05	$157.22	$150.33

Share Repurchase Program
On April 26, 2018, our Board of Directors approved a share repurchase program that authorized the repurchase of up to $100.0 million in common stock. We completed the repurchase of $100.0 million in common stock in July 2018. Subsequently on September 20, 2018, the Board of Directors approved another share repurchase program that authorized the repurchase of up to $50.0 million in common stock. We completed the repurchase of $50.0 million in common stock in November 2018. Altogether, we repurchased approximately 9.0 million shares totaling $150.0 million in 2018 at an average weighted price of $16.65.
The following table summarizes share repurchase activities during the fourth quarter of 2018:

Period	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Program	Approximate Dollar Value of Shares that May Yet Be Purchased Under the Program (Dollars in thousands)
October 1, 2018 to October 31, 2018	1,296,969	$ 14.00	1,296,969	$ 31,798
November 1, 2018 to November 30, 2018	2,139,788	14.83	2,139,788	—

December 1, 2018 to December 31, 2018	—	—	—	—
Total	3,436,757	$ 14.52	3,436,757	

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Item 6. SELECTED FINANCIAL DATA

The following table presents selected financial and other data for each of the years in the five-year period ended December 31, 2018. The information below should be read in conjunction with, the more detailed information included elsewhere herein, including our Audited Consolidated Financial Statements and Notes thereto.

	As of or For The Year Ended December 31,				
	2018	2017	2016	2015	2014
	(Dollars in thousands, except share and per share data)				
Income Statement Data:					
Interest income	$650,172	$572,104	$421,934	$313,660	$302,657
Interest expense	162,245	90,724	58,579	40,618	36,060
Net interest income	487,927	481,380	363,355	273,042	266,597
Provision for loan losses	14,900	17,360	9,000	8,000	12,638
Net interest income after provision for loan losses	473,027	464,020	354,355	265,042	253,959
Noninterest income	60,180	66,415	51,819	43,691	44,187
Noninterest expense	277,726	266,601	214,975	153,384	151,624
Income before income tax provision	255,481	263,834	191,199	155,349	146,522
Income tax provision	65,892	124,389	77,452	63,091	57,907
Net income	$189,589	$139,445	$113,747	$92,258	$88,615
Per Common Share Data:					
Earnings - basic	$1.44	$1.03	$1.10	$1.16	$1.11
Earnings - diluted	$1.44	$1.03	$1.10	$1.16	$1.11
Book value (period end)	$15.03	$14.23	$13.72	$11.79	$11.10
Cash dividends declared per common share	$0.54	$0.50	$0.45	$0.42	$0.35
Number of common shares outstanding (period end)	126,639,912	135,511,891	135,240,079	79,566,356	79,503,552
Balance Sheet Data—At Period End:					
Assets	$15,305,952	$14,206,717	$13,441,422	$7,912,648	$7,140,330
Securities available for sale	$1,846,265	$1,720,257	$1,556,740	$1,010,556	$792,523
Loans receivable, net of unearned loan fees and discounts (excludes loans held for sale)	$12,098,115	$11,102,575	$10,543,332	$6,248,341	$5,565,192
Deposits	$12,155,656	$10,846,609	$10,642,035	$6,340,976	$5,693,452
FHLB advances and federal funds purchased	$821,280	$1,227,593	$754,290	$530,591	$480,975
Subordinated debentures	$101,929	$100,853	$99,808	$42,327	$42,158
Convertible notes, net	$194,543	$—	$—	$—	$—
Stockholders’ equity	$1,903,211	$1,928,255	$1,855,473	$938,095	$882,773
Average Balance Sheet Data:					
Assets	$14,749,166	$13,648,963	$10,342,063	$7,389,530	$6,830,244
Securities available for sale	$1,772,080	$1,679,468	$1,276,068	$871,010	$713,775
Gross loans, including loans held for sale	$11,547,022	$10,642,349	$8,121,897	$5,846,658	$5,355,243
Deposits	$11,628,177	$10,751,886	$8,232,984	$5,879,704	$5,439,920
Stockholders’ equity	$1,910,224	$1,907,746	$1,342,954	$912,609	$848,443

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	As of or For The Year Ended December 31,				
	2018	2017	2016	2015	2014
	(Dollars in thousands)				
Selected Performance Ratios:					
Return on average assets[1]	1.29 %	1.02 %	1.10 %	1.25 %	1.30 %
Return on average stockholders' equity[2]	9.92 %	7.31 %	8.47 %	10.11 %	10.44 %
Average stockholders' equity to average assets	12.95 %	13.98 %	12.99 %	12.35 %	12.42 %
Dividend payout ratio (dividends per share/earnings per share)	37.58 %	48.54 %	40.86 %	36.21 %	31.53 %
Net interest spread[3]	3.04 %	3.46 %	3.49 %	3.62 %	3.88 %
Net interest margin[4]	3.53 %	3.80 %	3.75 %	3.88 %	4.13 %
Yield on interest earning assets[5]	4.71 %	4.51 %	4.36 %	4.46 %	4.68 %
Cost of interest bearing liabilities[6]	1.67 %	1.05 %	0.87 %	0.84 %	0.80 %
Efficiency ratio[7]	50.67 %	48.67 %	51.78 %	48.43 %	48.79 %
Regulatory Capital Ratios:					
Hope Bancorp:					
Common Equity Tier 1	11.44 %	12.30 %	12.10 %	12.08 %	12.96 %
Tier 1 Leverage	10.55 %	11.54 %	11.49 %	11.53 %	11.62 %
Tier 1 risk-based	12.21 %	13.11 %	12.92 %	12.67 %	13.64 %
Total risk-based	12.94 %	13.82 %	13.64 %	13.80 %	14.80 %
Bank of Hope:					
Common Equity Tier 1	13.63 %	12.95 %	12.75 %	12.56 %	13.44 %
Tier 1 Leverage	11.76 %	11.40 %	11.33 %	11.43 %	11.45 %
Tier I risk-based	13.63 %	12.95 %	12.75 %	12.56 %	13.44 %
Total risk-based	14.36 %	13.66 %	13.46 %	13.69 %	14.61 %
Asset Quality Data:					
Nonaccrual loans	$53,286	$46,775	$40,074	$40,801	$46,353
Loans 90 days or more past due and still accruing [8]	1,529	407	305	375	361
Restructured loans (accruing)	50,410	67,250	48,874	47,984	57,128
Total nonperforming loans	105,225	114,432	89,253	89,160	103,842
Other real estate owned	7,754	10,787	21,990	21,035	21,938
Total nonperforming assets	$112,979	$125,219	$111,243	$110,195	$125,780
Asset Quality Ratios:					
Nonaccrual loans to loans receivable	0.44 %	0.42 %	0.38 %	0.65 %	0.83 %
Nonperforming loans to loans receivable	0.87 %	1.03 %	0.85 %	1.43 %	1.87 %
Nonperforming assets to total assets	0.74 %	0.88 %	0.83 %	1.39 %	1.76 %
Nonperforming assets to loans receivable and other real estate owned	0.93 %	1.13 %	1.05 %	1.76 %	2.25 %
Allowance for loan losses to loans receivable	0.77 %	0.76 %	0.75 %	1.22 %	1.22 %
Allowance for loan losses to nonaccrual loans	173.70 %	180.74 %	197.99 %	187.27 %	146.18 %
Allowance for loan losses to nonperforming loans	87.96 %	73.88 %	88.90 %	85.70 %	65.25 %
Allowance for loan losses to nonperforming assets	81.92 %	67.51 %	71.32 %	69.34 %	53.87 %
Net charge-offs (recoveries) to average loans receivable	0.06 %	0.11 %	0.07 %	(0.01)%	0.23 %

(1) Net income divided by average assets.

(2) Net income divided by average stockholders’ equity.
(3) Difference between the average yield earned on interest earning assets and the average rate paid on interest bearing liabilities.
(4) Net interest income expressed as a percentage of average interest earning assets.
(5) Interest income divided by average interest earning assets.
(6) Interest expense divided by average interest bearing liabilities.
(7) Noninterest expense divided by the sum of net interest income plus noninterest income.
(8) Excludes acquired credit impaired loans totaling $14.1 million, $18.1 million, $19.6 million, $12.2 million, and $30.4 million as of December 31, 2018, 2017, 2016, 2015, and 2014, respectively.

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Item 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

You should read the following discussion and analysis of our financial condition and results of operations together with our Consolidated Financial Statements and accompanying notes presented elsewhere in this Report. This discussion and analysis contains forward-looking statements that involve risks, uncertainties and assumptions. Our actual results may differ materially from those anticipated in these forward-looking statements as a result of many factors, including those set forth under Item 1A "Risk Factors" and elsewhere in this Report. Please see the "Forward Looking Information" immediately preceding Part I of this Report.

Overview

We offer a full range of commercial and retail banking loan and deposit products through Bank of Hope. We have 63 banking offices in California, New York/New Jersey, Illinois, Washington, Texas, Virginia, Alabama, and Georgia. We have 11 loan production offices located in Atlanta, Dallas, Denver, Portland, Seattle, Fremont, and in Southern California We offer our banking services through our network of banking offices and loan production offices to our customers who typically are small to medium-sized businesses in our market areas. We accept deposits and originate a variety of loans including commercial business loans, commercial real estate loans, trade finance loans, SBA loans, and consumer loans.

Our results are affected by economic conditions in our markets and to a lesser degree in South Korea. A decline in economic and business conditions in our market areas or in South Korea may have a material adverse impact on the quality of our loan portfolio or the demand for our products and services, which in turn may have a material adverse effect on our financial condition and results of operations.

Our principal business involves earning interest on loans and investment securities that are funded primarily by customer deposits and other borrowings. Our operating income and net income are derived primarily from the difference between interest income received from interest earning assets and interest expense paid on interest bearing liabilities and, to a lesser extent, from fees received in connection with servicing loan and deposit accounts and income from the sale of loans. Historically, we sold most the guaranteed portion of SBA loans we originated on the secondary market, but due to the reduced premiums received on secondary market for SBA guaranteed sales, we made the decision to retain the loans on our balance sheet. Our major expenses are the interest we pay on deposits and borrowings, provisions for loan losses and general operating expenses, which primarily consist of salaries and employee benefits, occupancy costs, and other operating expenses. Interest rates are highly sensitive to many factors that are beyond our control, such as changes in the national economy and in the related monetary policies of the FRB, inflation, unemployment, consumer spending and political changes and events. We cannot predict the impact that these factors and future changes in domestic and foreign economic and political conditions might have on our performance.

Mergers and Acquisitions

On January 23, 2017, we announced the signing of a definitive agreement and plan of merger (the "U & I Merger Agreement") with U & I Financial Corporation ("U & I") pursuant to which U & I would have merged with and into Hope Bancorp with Hope Bancorp as the surviving corporation. As part of the merger, UniBank, a wholly-owned subsidiary of U & I, would have merged with and into the Bank. Subsequently on September 15, 2017, we announced the termination of the proposed merger with U & I as regulatory approval had not been obtained. The Mutual Termination Agreement provides, among other things, that each party will bear its own costs and expenses in connection with the terminated transaction, without penalties or termination fees. In connection with the termination, the parties have provided mutual releases to one another relating to the merger transaction.

On July 29, 2016, we completed the merger with Wilshire Bancorp, Inc ("Wilshire"). Through the merger, we acquired Wilshire's thirty-five full-service branch offices, twenty-two of which were located in California, eight in New York and New Jersey, three in Texas, and one of each in Georgia and Alabama. Under the terms of the Merger Agreement, Wilshire shareholders had the right to receive 0.7034 of a share of our common stock in exchange for each share of Wilshire common stock they own in a 100% stock-for-stock transaction.

Each acquisition was accounted for as an acquisition in accordance with the acquisition method of accounting as detailed in Accounting Standards Codification ("ASC") 805, Business Combinations. The acquisition method of

accounting requires an acquirer to recognize the assets acquired, the liabilities assumed, and any non-controlling interest in the acquiree based on their fair values as of the date of acquisition. This process is heavily reliant on measuring and estimating the fair values of all the assets and liabilities of the acquired entities. To the extent we did not have the requisite expertise to determine the fair values of the assets acquired and liabilities assumed, we engaged third party valuation specialists to assist us in determining such values.

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Critical Accounting Policies

Our financial statements are prepared in accordance with generally accepted accounting principles in the United States of America ("GAAP") and generally accepted practices within the banking industry. The financial information contained within these statements is, to a significant extent, financial information that is based on approximate measures of the financial effects of transactions and events that have already occurred. All of our significant accounting policies are described in Note 1 of our Consolidated Financial Statements presented elsewhere in this Report and are essential to understanding Management's Discussion and Analysis of Financial Condition and Results of Operations. GAAP requires management to make estimates and judgments that affect the reported amounts of assets and liabilities, revenues and expenses, and related disclosures of contingent assets and liabilities at the date of our financial statements. Actual results may materially and adversely differ from these estimates under different assumptions or conditions.

The following is a summary of the more subjective and complex accounting estimates and principles affecting the financial condition and results reported in our financial statements. In each area, we have identified the variables we believe to be the most important in the estimation process. We use the best information available to us to make the estimations necessary to value the related assets and liabilities in each of these areas.

Business Combinations

Mergers and acquisitions are accounted for in accordance with ASC 805 "Business Combinations" using the acquisition method of accounting. Assets and liabilities acquired and assumed are generally recorded at their fair values as of the date of the transaction. The excess of purchase price over the fair value of assets acquired and liabilities assumed is recorded as goodwill. Significant estimates and judgments are involved in the fair valuation and purchase price allocation process. Critical accounting policies related to acquired loans is discussed in more detail below under "Acquired Loans and Purchase Credit Impaired Loans".

Investment Securities

The fair values of investment securities are generally determined by quoted market prices obtained from independent external broker or external pricing services providers who have experience in valuing these securities. We perform a monthly analysis on the broker quotes received from third parties to assess whether the prices represent a reasonable estimate of the fair value. The procedures include, but are not limited to, initial and on-going review of third party pricing methodologies as well as independent auditors' reports from the third party regarding its controls over valuation of financial instruments, review of pricing trends and monitoring of trading volumes. We also compare the market prices obtained from one source to another reputable independent external broker or independent external pricing service provider for the reasonableness of the initial market prices obtained on a quarterly basis. We did not adjust any of the prices provided to us by the independent pricing services at December 31, 2018 or 2017.

We evaluate securities for other-than-temporary impairment on at least a quarterly basis, and more frequently when economic or market concerns warrant such evaluation. Consideration is given to the financial condition and near-term prospects of the issuer; the length of time and the extent to which the fair value has been less than cost, and our intention to sell, or whether it is more likely than not that we will be required to sell, a security in an unrealized loss position before recovery of its amortized cost basis. In analyzing an issuer's financial condition, we consider whether the securities are issued by the federal government or its agencies, whether downgrades by bond rating agencies have occurred, and the results of reviews of the issuer's financial condition. We do not believe that we had any investment securities available for sale with unrealized losses that would be deemed to be other-than-temporarily impaired as of December 31, 2018. Investment securities are discussed in more detail under "Financial Condition—Investment Securities Portfolios" below.

Allowance for Loan Losses

Accounting for the allowance for loan losses involves significant judgments and assumptions by management, which has a material impact on the carrying value of net loans. The judgments and assumptions used by management are based on historical data and management's analysis of other qualitative factors, including the current economic environment as described under "Financial Condition—Allowance for Loan Losses" below.

Purchased Credit Impaired ("PCI") Loans

In accordance with ASC 310-30, PCI loans were aggregated into pools based on individually evaluated common risk characteristics and expected cash flows were estimated on a pool basis. Each pool is accounted for as a single asset with a single interest rate, cumulative loss rate and cash flow expectation. A loan will be removed from a pool of loans at its carrying value only if the loan is sold or foreclosed, assets are received in satisfaction of the loan or the loan is written off.

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The cash flows expected to be received over the life of the pools were estimated by management with the assistance of a third party valuation specialist. These cash flows were utilized in calculating the carrying values of the pools and underlying loans, book yields, effective interest income and impairment, if any, based on actual and projected events. Default rates, loss severity and prepayment speeds assumptions are periodically reassessed and updated within the accounting model to update the expectation of future cash flows. The excess of the cash expected to be collected over the pool's carrying value is considered to be the accretable yield and is recognized as interest income over the estimated life of the loan pool using the effective interest yield method. The accretable yield will change due to changes in the timing and amounts of expected cash flows. Changes in the accretable yield are disclosed quarterly. The excess of the contractual balances due over the cash flows expected to be collected is considered to be nonaccretable difference. The nonaccretable difference represents our estimate of the credit losses expected to occur and was considered in determining the fair value of the loans as of their acquisition date. Subsequent to their acquisition date, any increases in expected cash flows over those expected at the acquisition date in excess of fair value are adjusted through the accretable difference on a prospective basis. Any subsequent decreases in expected cash flows over those expected at their acquisition date are recognized by recording a provision for loan losses.
PCI loans that met the criteria for nonaccrual of interest prior to the acquisition are considered performing upon acquisition, regardless of whether the customer is contractually delinquent, if we can reasonably estimate the timing and amount of the expected cash flows on such loans and if we expect to collect the new carrying value of the loans in full. As such, we no longer consider the loan to be nonaccrual or nonperforming and accrue interest on these loans, including the impact of any accretable discount. We have determined that we can reasonably estimate future cash flows on any such acquired loans that are past due 90 days or more and on which we are accruing interest and we expect to fully collect the carrying value of the loans.

Goodwill

We assess goodwill for impairment annually. Before applying the two-step goodwill impairment test, in accordance with ASC 350 "Intangibles - Goodwill and Other", we make a qualitative assessment of whether it is more likely than not that a reporting unit's fair value is less than its carrying amount. If we conclude that it is not more likely than not that the fair value of a reporting unit is less than its carrying amount, we do not perform the two-step impairment test. We assessed certain qualitative factors to determine whether impairment was likely including: our market capitalization, capital adequacy, continued performance compared to peers, and continued improvement in asset quality trends, among others. Based on our qualitative assessment, we were not required to perform the two-step impairment test as of December 31, 2018.
Goodwill may also be tested for impairment on an interim basis if circumstances change or an event occurs between annual tests that would more likely than not reduce the fair value of the reporting unit below its carrying amount. Significant judgment is applied when goodwill is assessed for impairment. This judgment includes developing cash flow projections, selecting appropriate discount rates, identifying relevant market comparables, incorporating general economic and market conditions and selecting an appropriate control premium. The selection and weighting of the various fair value techniques may result in a higher or lower fair value. Judgment is applied in determining the weighting that is most representative of fair value.

Income Taxes

The provision for income taxes is based on income reported for financial statement purposes, and differs from the amount of taxes currently payable, since certain income and expense items are reported for financial statement purposes in different periods than those for tax reporting purposes. Taxes are discussed in more detail in Note 11 to our Consolidated Financial Statements presented elsewhere in this Report. Accrued taxes represent the net estimated amount due or to be received from taxing authorities. In estimating accrued taxes, we assess the relative merits and risks of the appropriate tax treatment of transactions taking into account statutory, judicial, and regulatory guidance in the context of our tax position. We account for income taxes using the asset and liability approach, the objective of which is to establish deferred tax assets and liabilities for the temporary differences between the financial reporting basis and the tax basis of our assets and liabilities at enacted tax rates expected to be in effect when such amounts are realized or settled. Deferred tax assets are reduced by a valuation allowance when, in the opinion of management, it is more likely than not that some portion, or all, of the deferred tax asset will not be realized. In assessing the realization

of deferred tax assets, management evaluates both positive and negative evidence, including the existence of any cumulative losses in the current year and the prior two years, the amount of taxes paid in available carry-back years, the forecasts of future income and taxable income, applicable tax planning strategies, and assessments of current and future economic and business conditions. This analysis is updated quarterly and adjusted as necessary.

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Section 382 of the Internal Revenue Code imposes a limitation ("382 Limitation") on a corporation's ability to use any net unrealized built in losses and other tax attributes, such as net operating loss and tax credit carry-forwards, when it undergoes a 50% ownership change over a designated testing period not to exceed three years ("382 Ownership Change"). As a result of the acquisition on July 29, 2016, Wilshire Bancorp underwent a 382 Ownership Change resulting in a 382 Limitation to its net operating loss and tax credit carry-forwards. Wilshire Bancorp did not have a net unrealized built in loss as of the 382 Ownership Change date. Given the applicable 382 Limitation, we expect to fully utilize Wilshire Bancorp's net operating loss and tax credit carry-forwards before expiration. However, future transactions, such as issuances of common stock or sales of shares of our stock by certain holders of our shares, including persons who have held, currently hold or may accumulate in the future 5% or more of our outstanding common stock for their own account, could trigger a future Section 382 Ownership Change, which could limit our use of these tax attributes.

On December 22, 2017, the U.S. government enacted comprehensive tax legislation commonly referred to as the Tax Cuts and Jobs Act ("Tax Act"). Among other changes, the Tax Act reduces the U.S. federal corporate tax rate from 35% to 21%. We reasonably estimated the effects of the Tax Act and recorded a provisional amount increasing income tax expense by $25.4 million for the year ended December 31, 2017 in accordance with SEC Staff Accounting Bulletin No. 118 ("SAB 118"). This amount is comprised of the re-measurement of federal net deferred tax assets and impairment of the low-income housing investment, resulting from the permanent reduction in the U.S. statutory corporate tax rate to 21% from 35%. As required by SAB 118, we continued to reassess and refine the effects of the Tax Act on its deferred tax amounts during 2018. As a result, we recorded an income tax expense of $442 thousand during the year ended December 31, 2018. As of December 31, 2018, we have completed the accounting for the income tax effects of the Tax Act. See Note 11 to the consolidated financial statements for further details.

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Results of Operations

Operations Summary

Our most significant source of income is net interest income, which is the difference between our interest income and our interest expense. Generally, interest income is generated from the loans we extend to our customers and from investments, and interest expense is generated from interest bearing deposits our customers have with us and from borrowings that we may have, such as FHLB advances, federal funds purchased, convertible notes, and subordinated debentures. Our ability to generate profitable levels of net interest income is largely dependent on our ability to manage the levels of interest earning assets and interest bearing liabilities, and the rates received or paid on them, as well as our ability to maintain sound asset quality and appropriate levels of capital and liquidity. As mentioned above, interest income and interest expense may fluctuate based on factors beyond our control, such as economic or political conditions.

We attempt to minimize the effect of interest rate fluctuations on net interest margin by monitoring our interest sensitive assets and our interest sensitive liabilities. Net interest income can be affected by a change in the composition of assets and liabilities, such as replacing higher yielding loans with a like amount of lower yielding investment securities. Changes in the level of nonaccrual loans and changes in volume and interest rates can also affect net interest income. Volume changes are caused by differences in the level of interest earning assets and interest bearing liabilities. Interest rate changes result from differences in yields earned on assets and rates paid on liabilities.

The other source of our income is noninterest income, including service charges and fees on deposit accounts, loan servicing fees, fees from trade finance activities, net gains on sale of loans that were held for sale and investment securities available for sale, and other income and fees. Our noninterest income can be reduced by charges for other than temporary impairment on investment securities.

In addition to interest expense, our income is impacted by provisions for loan losses and noninterest expense, primarily salaries and benefits and occupancy expense. The following table presents our condensed consolidated statements of income and the increases year over year.

	Year Ended December 31, 2018	Increase (Decrease) Amount	Increase (Decrease) %	Year Ended December 31, 2017	Increase Amount	Increase %	Year Ended December 31, 2016
	(Dollars in thousands)						
Interest income	$650,172	$78,068	14 %	$572,104	$150,170	36%	$421,934
Interest expense	162,245	71,521	79 %	90,724	32,145	55%	58,579
Net interest income	487,927	6,547	1 %	481,380	118,025	32%	363,355
Provision for loan losses	14,900	(2,460)	(14)%	17,360	8,360	93%	9,000
Noninterest income	60,180	(6,235)	(9)%	66,415	14,596	28%	51,819
Noninterest expense	277,726	11,125	4 %	266,601	51,626	24%	214,975
Income before income tax provision	255,481	(8,353)	(3)%	263,834	72,635	38%	191,199
Income tax provision	65,892	(58,497)	(47)%	124,389	46,937	61%	77,452
Net income	$189,589	$50,144	36 %	$139,445	$25,698	23%	$113,747

Net Income

Our net income was $189.6 million for 2018 compared to $139.4 million for 2017 and $113.7 million for 2016. Our earnings per common share based on fully diluted shares were $1.44, $1.03, and $1.10 for 2018, 2017, and 2016, respectively. The return on average assets was 1.29%, 1.02%, and 1.10% and the return on average stockholders' equity was 9.92%, 7.31%, and 8.47% for 2018, 2017, and 2016, respectively. The increase in net income for 2018 compared to 2017 was due to the reduction in tax provision expense as a result of the Tax Cuts and Jobs Act which reduced the corporate federal income tax rate from 35% to 21% starting on January 1, 2018.

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Impact of Acquisitions

The comparability of our operating results is affected by our acquisition of Wilshire Bancorp in July 2016. We acquired $4.63 billion in total assets from Wilshire at the time of the acquisition. The acquisition was accounted for using the acquisition method of accounting and, accordingly, Wilshire's operating results have been included in the consolidated financial statements from the acquisition date. Financial information for the years 2018 and 2017 reflect full years of combined operations subsequent to the merger with Wilshire, while 2016 reflects seven months of stand-alone operations and five months of combined operations.

Income before income tax provision for the year ended December 31, 2018, 2017, and 2016 were impacted by the accretion of discounts and the amortization of premiums relating to past acquisitions. The following table summarizes the accretion and amortization adjustments that are included in net income for the periods indicated below:

	Year Ended December 31,		
	2018	2017	2016
	(Dollars in thousands)		
Accretion on purchased non-impaired loans	$11,715	$18,372	$9,330
Accretion on purchased credit-impaired loans	21,837	21,542	15,817
Amortizations of premium on low income housing tax credits	(338)	(338)	(127)
Amortization of premiums on acquired FHLB borrowings	1,413	1,597	973
Accretion of discounts on acquired subordinated debt	(1,076)	(1,045)	(539)
Amortization of premiums on acquired time deposits and savings	1	4,903	5,857
Amortization of core deposit intangibles	(2,461)	(2,703)	(1,732)
Total acquisition accounting adjustments	$31,091	$42,328	$29,579
Merger-related expenses	7	(1,781)	(16,914)
Total	$31,098	$40,547	$12,665

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Net Interest Margin and Net Interest Rate Spread

We analyze our earnings performance using, among other measures, net interest spread and net interest margin. The net interest spread represents the difference between the weighted average yield earned on interest earning assets and average rate paid on interest bearing liabilities. Net interest income, when expressed as a percentage of average total interest earning assets, is referred to as the net interest margin. Our net interest margin is affected by changes in the yields earned on assets and rates paid on liabilities, as well as the ratio of the amounts of interest earning assets to interest bearing liabilities.

Interest rates charged on our loans are affected principally by the demand for such loans, the supply of money available for lending purposes, the interest rate environment, and other competitive factors. These factors are in turn affected by general economic conditions and other factors beyond our control, such as federal economic policies, the general supply of money in the economy, legislative tax policies, governmental budgetary matters, and the actions of the FRB.

The following table presents our net interest margin, net interest rate spread, and our condensed consolidated average balance sheet information, together with interest rates earned and paid on the various sources and uses of funds, for the periods indicated:

	Year Ended December 31,								
	2018			2017			2016		
	Average Balance	Interest Income/ Expense	Average Yield/ Rate	Average Balance	Interest Income/ Expense	Average Yield/ Rate	Average Balance	Interest Income/ Expense	Average Yield/ Rate
	(Dollars in thousands)								
INTEREST EARNING ASSETS:									
Loans[1][2][3]	$11,547,022	$594,103	5.15 %	$10,642,349	$529,760	4.98 %	$8,121,897	$392,127	4.83 %
Securities[3]	1,772,080	45,342	2.56 %	1,679,468	36,917	2.20 %	1,276,068	25,442	1.99 %
FRB and FHLB stock and other investments	487,922	10,727	2.20 %	360,086	5,427	1.51 %	281,824	4,365	1.55 %
Total interest earning assets	13,807,024	650,172	4.71 %	12,681,903	572,104	4.51 %	9,679,789	421,934	4.36 %
Total noninterest earning assets	942,142			967,060			662,274		
Total assets	$14,749,166			$13,648,963			$10,342,063		
INTEREST BEARING LIABILITIES:									
Deposits:									
Demand, interest bearing	$3,276,815	43,252	1.32 %	$3,490,440	31,856	0.91 %	2,587,548	21,136	0.82 %
Savings	229,608	1,889	0.82 %	268,292	1,354	0.50 %	234,332	1,282	0.55 %
Time deposits	5,107,698	89,817	1.76 %	4,037,259	41,692	1.03 %	3,219,484	25,673	0.80 %
Total interest bearing deposits	8,614,121	134,958	1.57 %	7,795,991	74,902	0.96 %	6,041,364	48,091	0.80 %
FHLB advances and federal funds purchased	870,124	15,127	1.74 %	787,119	10,706	1.36 %	619,557	7,560	1.22 %
Convertible notes, net	123,040	5,797	4.65 %	—	—	— %	—	—	— %

Other borrowings	97,455	6,363	6.44 %	96,363	5,116	5.24 %	64,165	2,928	4.49 %
Total interest bearing liabilities	9,704,740	162,245	1.67 %	8,679,473	90,724	1.05 %	6,725,086	58,579	0.87 %
Noninterest bearing liabilities and equity:									
Noninterest bearing demand deposits	3,014,056			2,955,895			2,191,620		
Other liabilities	120,146			105,849			82,403		
Stockholders' equity	1,910,224			1,907,746			1,342,954		
Total liabilities and stockholders' equity	$14,749,166			$13,648,963			$10,342,063		
Net interest income		$487,927			$481,380			$363,355	
Net interest margin			3.53 %			3.80 %			3.75 %
Net interest spread[4]			3.04 %			3.46 %			3.49 %
Cost of funds[5]			1.28 %			0.78 %			0.66 %
Cost of deposits			1.16 %			0.70 %			0.58 %

(1) Interest income on loans includes accretion of net deferred loan origination fees and costs, prepayment fees received on loan pay-offs and accretion of discounts on acquired loans. See the table below for detail.
(2) Average balances of loans are net of deferred loan origination fees and costs and include nonaccrual loans and loans held for sale.
(3) Interest income and yields are not presented on a tax-equivalent basis.
(4) Yield on interest earning assets minus cost of interest bearing liabilities.
(5) Yield on interest bearing liabilities and noninterest bearing deposits.

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The following table presents net loan origination fees, loan prepayments fee income, interest reversed for nonaccrual loans, and discount accretion income included as part of loan interest income for the years indicated:

Year ended December 31,	Net Loan Origination Fees	Loan Prepayment Fee Income	Interest Reversed for Nonaccrual Loans, Net of Income Recognized	Accretion of Discounts on Acquired Loans
	(Dollars in thousands)			
2018	$1,492	$ 2,603	$ (590)	$ 33,552
2017	$1,485	$ 3,963	$ (419)	$ 39,914
2016	$1,798	$ 3,491	$ (483)	$ 25,147

Net Interest Income

Net interest income was $487.9 million for 2018, compared to $481.4 million for 2017 and $363.4 million for 2016. Changes in net interest income are a function of changes in interest rates and volume of interest earning assets and interest bearing liabilities. The table below sets forth information regarding the changes in interest income and interest expense for the periods indicated. The total change for each category of interest earning assets and interest bearing liabilities is segmented into the change attributable to variations in volume (changes in volume multiplied by the old rate) and the change attributable to variations in interest rates (changes in rates multiplied by the old volume). Nonaccrual loans are included in average loans used to compute this table.

	For the year ended December 31,					
	2018 Compared to 2017			2017 Compared to 2016		
	Net	Change due to		Net	Change due to	
	Increase	Rate	Volume	Increase	Rate	Volume
	(Dollars in thousands)					
INTEREST INCOME:						
Interest and fees on loans	$64,343	$18,225	$46,118	$137,633	$12,512	$125,121
Interest on securities	8,425	6,305	2,120	11,475	2,810	8,665
Interest on other investments	5,300	2,988	2,312	1,062	(120)	1,182
TOTAL INTEREST INCOME	$78,068	$27,518	$50,550	$150,170	$15,202	$134,968
INTEREST EXPENSE:						
Interest on demand deposits	$11,396	$13,451	$(2,055)	$10,720	$2,697	$8,023
Interest on savings	535	753	(218)	72	(104)	176
Interest on time deposits	48,125	34,943	13,182	16,019	8,608	7,411
Interest on FHLB advances and federal funds purchased	4,421	3,206	1,215	3,146	937	2,209
Convertible notes, net	5,797	—	5,797	—	—	—
Interest on other borrowings	1,247	1,188	59	2,188	545	1,643
TOTAL INTEREST EXPENSE	$71,521	$53,541	$17,980	$32,145	$12,683	$19,462
NET INTEREST INCOME	$6,547	$(26,023)	$32,570	$118,025	$2,519	$115,506

Net interest income before provision for loan losses increased by $6.5 million, or 1%, during 2018. The increase was primarily due to an increase in average interest earning assets by 9% during the year which resulted in an increase of $50.6 million in interest income due to volume. Interest bearing liabilities increased by 12% for 2018 compared to the previous year which resulted in an increase of $18.0 million in interest expense due to volume. Interest expense change in 2018 compared to 2017 due to change in rate amounted to $53.5 million mostly due to the increase in interest rates in 2018 and repricing of deposits. Although yields on interest earnings assets increased for 2018 compared to 2017, the increase was offset by the increase in cost of deposits for the same period.

Net interest income before provision for loan losses increased by $118.0 million, or 32%, during 2017. The increase was primarily due to an increase in average interest earning assets by 31% during the year which resulted in an

increase of $135.0 million in interest income due to volume. Interest bearing liabilities increased by 29% for 2017 compared to the previous year, which resulted in an increase of $19.5 million in interest expense due to volume. Although yields on interest earnings assets increased for 2017 compared to 2016, the increase was largely offset by the increase in cost of deposits for the same period.

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Average interest earnings assets and liabilities for 2018 and 2017 included the full year impact from assets acquired and liabilities assumed from Wilshire, while average interest earnings assets and liabilities for 2016 included only five months of asset and liability balances acquired from Wilshire.

Interest Income

Interest income was $650.2 million for 2018, compared to $572.1 million for 2017 and $421.9 million for 2016. The yield on average interest earning assets was 4.71% for 2018, compared to 4.51% for 2017 and 4.36% for 2016.

Comparison of 2018 with 2017

The increase in interest income of $78.1 million, or 14%, for 2018 compared to 2017 was primarily a result of the growth in total loans and investments. The increase in interest income was primarily attributable to the increase in loans as a result of higher rates on new originations as well as an increase in loan rates for variable rate loans. Average total loans increased by $904.7 million in 2018 compared to 2017 and total investments and FHLB stock and other investments together increased $220.4 million in the same period. Discount accretion income on acquired loans decreased in 2018 totaling $33.6 million compared to $39.9 million for 2017.

Comparison of 2017 with 2016

The increase in interest income of $150.2 million, or 36%, for 2017 compared to 2016 was primarily a result of the growth in total loans and investments. The increase in 2017 was a result of both organic growth and the full year impact of the assets acquired from Wilshire compared to only a five month impact of assets acquired from Wilshire for 2016. Average total loans increased $2.52 billion in 2017 compared to 2016, and total investments increased $403.4 million in the same period. Discount accretion income on acquired loans increased in 2017 totaling $39.9 million compared to $25.1 million for 2016. Accretion income on loans acquired from Wilshire was recognized throughout the entire year in 2017, whereas in 2016, accretion income was recorded in only the last five months of the year subsequent to the acquisition in July 2016.

Interest Expense

Deposits

Interest expense on deposits was $135.0 million for 2018 compared to $74.9 million for 2017 and $48.1 million for 2016. The average cost of deposits was 1.16% for 2018, compared to 0.70% for 2017 and 0.58% for 2016. The average cost of interest bearing deposits was 1.57% for 2018, compared to 0.96% for 2017 and 0.80% for 2016.

Comparison of 2018 with 2017

The increase in interest expense on total deposits of $60.1 million, or 80%, for 2018 compared to 2017 was due to an increase in interest bearing deposit accounts, particularly an increase in time deposits accounts, in addition to an overall increase in rates offered in 2018. Federal funds rates were increased by 25 basis points by the Federal Open Market Committee (“FOMC”) in March 2018, June 2018, September 2018, and December 2018. As a result of the interest rate hikes in 2018, many of our deposits were priced higher and time deposits were renewed and opened at higher interest rates increasing our total cost of deposits for 2018. The average balance of noninterest bearing deposits accounted for 26% of total average deposits at December 31, 2018 compared to 27% at December 31, 2017. During 2018, we issued $217.5 million in convertible notes (carried at a discount) which also contributed to the increase in interest expense for 2018 compared to 2017. The convertible notes have a coupon rate of 2.00%, but the accretion of discount and capitalization of issuance costs contributes to the increase in cost of convertible notes.

Comparison of 2017 with 2016

The increase in interest expense on total deposits of $26.8 million, or 56%, for 2017, compared to 2016 was due to an increase in interest bearing liabilities in addition to an overall increase in rates offered in 2017. Federal funds rates was increased by the Federal Open Market Committee (“FOMC”) in June of 2017 and again in December of 2017. As of result of the 25 basis point increase in interest rates in June 2017, many of our deposits were priced higher and time deposits were renewed and opened at higher interest rates increasing our total cost of deposits for 2017. In addition, average deposits for 2017 included a full year of balances assumed from Wilshire while 2016 only reflected five months of assumed deposits in the average deposit balance. The average balance of noninterest bearing deposits accounted for 27% of total average deposits at December 31, 2017 compared to 27% at December 31, 2016.

FHLB Advances and Federal Funds Purchased

FHLB advances and federal funds purchased include borrowings from the FHLB and federal funds purchased. As part of our asset-liability management, we utilize FHLB advances to supplement our deposit source of funds. Therefore, there may be fluctuations in these balances depending on the short-term liquidity and longer-term financing needs of the Bank.

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Average FHLB advances and federal funds purchased were $870.1 million in 2018, compared to $787.1 million in 2017 and $619.6 million in 2016. Interest expense on FHLB advances was $15.1 million for 2018 compared to $10.7 million for 2017 and $7.6 million for 2016. The average cost of FHLB advances was 1.74% for 2018, compared to 1.36% for 2017 and 1.22% for 2016. The average cost of FHLB advances includes the amortization of premiums recorded on advances acquired from prior acquisitions. Total amortization FHLB premiums for 2018 was $1.4 million, compared to $1.6 million in 2017 and $973 thousand in 2016. During 2018, we repaid $465.0 million in FHLB advances with an average rate of 1.61% and borrowed $130.0 million in advances with an average rate of 2.39%.

We did not have federal funds purchased at December 31, 2018 and December 31, 2016. At December 31, 2017, we had $69.9 million in federal funds purchased included in average FHLB advances and federal funds purchased, which were all fully repaid during the first quarter of 2018.

Convertible Debt

During the second quarter of 2018, we issued $217.5 million in senior convertible notes. The carrying balance of our convertible notes are net of discount to be amortized and issuance costs to be capitalized. The cost of our convertible notes for 2018 was 4.65%. We had no convertible notes outstanding in 2017 or 2016. The cost of our convertible notes consists of the 2.00% coupon rate, the non-cash conversion option rate, and the issuance cost capitalization rate. After the fifth year, the cost of the convertible notes will decline as the non-cash conversion discount will be fully amortized and the issuance costs will be fully capitalized leaving the coupon rate as the only remaining cost.

Other Borrowings

Other borrowings include subordinated debentures which bear interest at 3-month LIBOR plus a designated spread. With the acquisition of Wilshire, we assumed four subordinated debentures at a fair value of $56.9 million. There were no other changes in our balance of subordinated debentures during 2017 or 2018, aside for the increases related to the discount accretion on subordinated debentures acquired from previous acquisitions. The average rate on other borrowing increased to 6.44% for 2018 compared to 5.24% for 2017 and 4.49% for 2016. The increase in cost of other borrowings in 2017 and 2018 was due to the increase in the 3-month LIBOR rate.

Provision for Loan Losses

The provision for loan losses reflects our judgment of the current period cost associated with credit risk inherent in our loan portfolio. The loan loss provision for each period is dependent upon many factors, including loan growth, net charge-offs, changes in the composition of the loan portfolio, delinquencies, assessments by management, third parties' and regulators' examination of the loan portfolio, the value of the underlying collateral on problem loans and the general economic conditions in our market areas. Specifically, the provision for loan losses represents the amount charged against current period earnings to achieve an allowance for loan losses that, in our judgment, is adequate to absorb probable incurred losses inherent in our loan portfolio. Periodic fluctuations in the provision for loan losses result from management's assessment of the adequacy of the allowance for loan losses; however, actual loan losses may vary in material respects from current estimates. If the allowance for loan losses is inadequate, we may be required to record additional loan loss provision, which may have a material adverse effect on our business and our financial condition.

Comparison of 2018 with 2017

The provision for loan losses was $14.9 million for 2018, a decrease of $2.5 million, or 14%, from $17.4 million for 2017. The decrease in provision for loan losses for 2018 compared to 2017 was largely due the reduction in net charge-offs for 2018 compared to 2017. The allowance for loan losses requirement increased only slightly in 2018 to 0.77% of total loans compared to 0.76% of total loans for 2017. The reduction in net charge-offs for 2018 resulted in a reduction in reduction in provision for loans losses required to replenish the allowance for loan losses for the year. Net charge offs totaled $6.9 million for 2018 compared to $12.2 million for 2017.

Comparison of 2017 with 2016

The provision for loan losses was $17.4 million for 2017, an increase of $8.4 million, or 93%, from $9.0 million for 2016. The provision was calculated based on net charge offs of $12.2 million during the year and an increase in the required allowance for loan losses primarily due to an increase in loan volume which also contributed to the increase in provision.

See “Financial Condition—Allowance for Loan Losses” for a description of our methodology for determining the allowance for loan losses.

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Noninterest Income

Noninterest income is primarily comprised of service charges on deposit accounts, net gains on sales of SBA and residential mortgage loans, and other fees and income. Noninterest income was $60.2 million for 2018 compared to $66.4 million for 2017 and $51.8 million for 2016.

Comparison of 2018 with 2017

The decrease in noninterest income for 2018 over 2017 primarily reflected decreases in service charges on deposit accounts, loan servicing fees, and net gain on sales of SBA and other loans.

Service charges on deposits decreased $2.1 million, or 10%, to $18.6 million due mostly to a decrease of $1.2 million in non-sufficient funds collected from business and personal accounts and a decrease of $758 thousand in analysis fees charged on demand deposits accounts.

Loan servicing fees decreased by $737 thousand, or 13.6%, to $4.7 million in 2018 compared to $5.4 million in 2017. The decrease in loan servicing fees in 2018 was primarily a result of an increase in payoffs of loans we service. When loans that we service are paid off, the remaining unamortized servicing asset originally recorded is charged against servicing fees reducing our overall fee income.

Net gains on sales of SBA loans decreased by $3.1 million, or 24%, to $9.7 million in 2018 from $12.8 million in 2017. The volume of sales of SBA loans and the net gains recorded from the sales largely depends on the production of SBA loans which decreased during in 2018. During the fourth quarter of 2018, we made the decision discontinue the practice of regularly selling the guaranteed portion of SBA loans on the secondary market and to retain these loans on our balance sheet due to the decline in premiums offered in the secondary market for the guaranteed portions SBA loans. SBA loans sold totaled $159.8 million in 2018 compared to $177.4 million in 2017.

Other income and fees increased by $625 thousand, or 4.2%, to $15.4 million in 2018 from $14.8 million in 2017. Other income and fees are comprised of loan recoveries on pre-merger charged-off loans, fair value changes of equity investments, swap fee income, gain/losses on sale of fixed assets, income from bank owned life insurance, and miscellaneous income. The increase in 2018 was largely due to an increase in the fair value of equity investments and recoveries on pre-merger charged off loans, offset by a decline in swap fee income, gain on sale of fixed assets, and miscellaneous income.

Comparison of 2017 with 2016

The increase in noninterest income for 2017 over 2016 primarily reflected increases in service charges on deposit accounts, loan servicing fees, net gain on sales of SBA loans, and other income and fees. These increases were largely due to the increase in operations from the acquisition of Wilshire.

Service charges on deposits increased $4.7 million, or 29%, to $20.6 million due mostly to an increase of $2.8 million in analysis fees charged on demand deposits accounts and an increase of $1.3 million in non-sufficient funds collected from business and personal accounts. The increase in deposits service charges in 2017 was largely due to the full year impact of the increase in deposits from the acquisition of Wilshire.

Loan servicing fees increased by $1.9 million, or 54%, to $5.4 million in 2017 compared to $3.5 million in 2016. The increase in loan servicing fees in 2017 was primarily a result of an increase in sales of residential loans and SBA loans in 2016 and 2017. We earn servicing fees on loans we continue to service subsequent to the sales of the loans. As more loans continue to be sold, our servicing fees continue to increase until the loans are paid off.

Net gains on sales of SBA loans increased by $4.0 million, or 46%, to $12.8 million in 2017 from $8.8 million in 2016. The volume of sales of SBA loans and the net gains recorded from the sales are primarily driven by the production of SBA loans which increased during in 2017. SBA loans sold totaled $177.4 million in 2017 compared to $116.1 million in 2016. The increase in SBA loans sold in 2017 was due to the full year operations of the combined bank after the acquisition of Wilshire, while 2016 represented only five months of combined operations.

Other income and fees increased by $3.1 million, or 27% in 2017 compared to 2016. Loan recoveries on pre-merger charged-off loans and miscellaneous income increased $1.2 million in 2017 and gains on sale of fixed assets increased by $1.0 million in 2017 compared to the previous year mostly due to the sale of a building and associated land at the end of 2017.

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A breakdown of noninterest income by category is shown below:

(Dollars in thousands)	Year Ended December 31, 2018	Increase (Decrease) Amount	%	Year Ended December 31, 2017	Increase (Decrease) Amount	%	Year Ended December 31, 2016
Service fees on deposit accounts	$ 18,551	$(2,068)	(10)%	$ 20,619	$4,655	29 %	$ 15,964
International service fees	4,371	(123)	(3)%	4,494	801	22 %	3,693
Loan servicing fees, net	4,696	(737)	(14)%	5,433	1,914	54 %	3,519
Wire transfer fees	4,934	(123)	(2)%	5,057	731	17 %	4,326
Net gains on sales of SBA loans	9,708	(3,066)	(24)%	12,774	4,024	46 %	8,750
Net gains on sales of other loans	2,485	(442)	(15)%	2,927	7	— %	2,920
Net gains on sales or called securities available for sale	—	(301)	(100)%	301	(649)	(68)%	950
Other income and fees	15,435	625	4 %	14,810	3,113	27 %	11,697
Total noninterest income	$ 60,180	$(6,235)	(9)%	$ 66,415	$14,596	28 %	$ 51,819

Noninterest Expense

Noninterest expense is primarily comprised of salaries and benefit expense, occupancy expense, furniture and equipment expense, advertising expenses, data processing and communications expenses, professional fees, investment in affordable housing partnership expenses, and other expenses. Noninterest expense was $277.7 million for 2018, compared to $266.6 million for 2017 and $215.0 million for 2016. The increases in noninterest expenses were $11.1 million, or 4%, for 2018 compared to 2017, and $51.6 million, or 24%, for 2017 compared to 2016. Noninterest expense as a percentage of average assets for 2018 was 1.88% compared to 1.95% for 2017 and 2.08% for 2016.

Comparison of 2018 with 2017

The increase in noninterest expense for 2018 over 2017 was due mostly to increases in salaries and employee benefits, occupancy expenses, data processing expenses, professional fees, Federal Deposit Insurance Corporation (“FDIC”) assessment expenses, credit related expenses, and branch restructuring costs, partially offset by a decline in investment in affordable housing partnership expenses, OREO expenses, merger and integration expenses, and other expenses.

Salaries and employee benefits totaled $153.5 million for 2018, an increase of $8.9 million, or 6%, compared to $144.7 million for 2017. The increase was comprised of a $10.1 million increase in employee salary expenses and a decrease of $1.2 million in employee benefits. These increases reflect increases in the number of full-time equivalent employees to 1,494 at December 31, 2018, from 1,470 at December 31, 2017, as well as an increase in commission and other types of compensation. During the third quarter of 2018, we restructured our incentive compensation plans, which lowered our bonus accruals for the second half of 2018, offsetting a portion of the salaries and benefits increase due to the rise in employees. In order to improve our deposit mix, our incentive compensation plan was restructured so that a more significant portion of the incentive compensation is now tied to core deposit gathering.

Occupancy expense increased $1.8 million, or 6%, to $30.4 million for 2018 compared to $28.6 million for 2017. The increase in occupancy expense was due mostly to an increase in lease expenses as a result of annual rent escalations for 2018.

Data processing and communications expenses increased $2.1 million, or 17%, to $14.2 million for 2018 compared to $12.2 million for 2017. The increase in deposit and loan accounts in 2018 compared to 2017, led to an increase in the total number of deposit and loan transactions which resulted in higher data processing expenses paid for 2018 compared to 2017. During the fourth quarter of 2018, we renegotiated our contract with our core banking platform provider, whose fees make up a significant portion of our data processing and communications expenses. As a result of the newly negotiated contract, our fees related to the use of the third party core banking system will be reduced in future periods.

Professional fees increased $1.3 million, or 9%, to $16.3 million for 2018 compared to $15.0 million for 2017. Compliance requirements as a result of exceeding $10 billion in total assets has resulted in additional spending to

improve upon our infrastructure in fields related to IT, accounting, compliance, and risk management. For 2018, management chose to deploy a portion of the savings in tax provision that resulted from the reduction in the corporate tax rate to improve certain key areas with the assistance of third party consultants. Professional fees for 2018 also included fees paid to third parties for assistance with the upcoming implementation of the new accounting standard for current expected credit loss and implementation of the new lease accounting standard.

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Investments in affordable housing partnership expenses decreased $1.8 million, or 13%, to $12.1 million for 2018 compared to $13.9 million for 2017. In 2017, we recorded an impairment of $3.3 million on our investments in affordable housing partnerships after an analysis of the individual investment carrying values compared to their expected future tax benefits. We did not record an impairment on our investments in affordable housing partnerships in 2018 which resulted in a decline in investments in affordable housing partnership expenses. We make investments in affordable housing partnerships and receive Community Reinvestment Act credit and tax credits which reduces our overall tax provision expense. Investments in affordable housing partnership expenses that are not impairment related are based on the performance of the underlying investment. We receive updated financial information for our affordable housing partnerships investments and record losses based on the performance of the investment. These losses will eventually be offset by tax credits which reduce our tax provision expense. Investments in affordable housing partnerships increased from $81.0 million at December 31, 2017 to $92.0 million at December 31, 2018.

FDIC assessment expenses increased $1.4 million, or 27%, to $6.6 million for 2018 compared to $5.2 million for 2017. The FDIC assessment premium utilizes an initial base assessment rate which is calculated as a percentage of our average consolidated total assets less average tangible equity. In addition to the initial assessment base, adjustments are added based on our regulatory rating and certain financial measures. The increase in consolidated assets resulted in additional FDIC assessment premiums paid in 2018 compared to 2017. During the fourth quarter, the FDIC reached the minimum reserve ratio of 1.35% and announced it would no longer assess the large institution surcharge (surcharge on institution in excess of $10 billion in consolidated assets). As a result, we experienced a small decline in our FDIC assessment expense for the fourth quarter of 2018.

Credit related expenses increased $2.3 million, or 392%, to $2.9 million for 2018 compared to $582 thousand for 2017. Credit related expenses increased in 2018 compared to 2017 largely due to a decrease in provision reversals for off balance sheet unfunded commitments. For 2018, credit for off balance sheet unfunded commitments totaled $100 thousand compared to a credit off balance sheet unfunded commitments of $2.4 million for 2017. Reserves for off balance sheet unfunded commitments at December 31, 2018 totaled $736 thousand compared to $836 thousand at December 31, 2017.

OREO expenses decreased $2.9 million, or 94%, to $187 thousand in 2018 compared to $3.1 million in 2017. The decrease in OREO expense in 2018 was due to a reduction in OREO valuation expenses and a reduction in expenses related to the maintenance of OREO during the year. With the reduction in OREO balance, the related expenses have declined. The total balance of OREO at December 31, 2018 was $7.8 million compared to $10.8 million at December 31, 2017.

In December 2018, we incurred a restructuring charge of $1.7 million, related to our branch rationalization plan which was announced in December 2018. The branch rationalization plan is still subject to regulatory non-objection and is expected to be implemented by the second quarter of 2019. The branch rationalization plan will impact six of our branch offices across the country. With the consolidation of these branches, we project approximately $1.9 million in pretax cost savings on an annual basis. The $1.7 million in restructuring costs consisted of $229 thousand in salaries and benefit expenses, $957 thousand in occupancy expense, and $488 thousand in other various expenditures. There were no branch restructuring costs for 2017.

In 2018 we recorded a $7 thousand reversal to merger and integration expenses resulting in a decrease $1.8 million to total merger and integration expenses for 2018 compared to 2017. Merger and integration expenses for 2017 consisted of remaining expenses related to the merger with Wilshire and expenses for the terminated merger with U & I Financial Corp.

Other expenses decreased