HERITAGE COMMERCE CORP
Form 10-K/A
February 22, 2008

# UNITED STATES
# SECURITIES AND EXCHANGE COMMISSION
**Washington, D.C. 20549**

# FORM 10-K/A

**(Amendment No. 2)**

**(MARK ONE)**

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

**For the fiscal year ended December 31, 2006**

**OR**

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

**FOR THE TRANSITION PERIOD FROM TO**

**Commission file number 000-23877**

# Heritage Commerce Corp

(Exact name of Registrant as Specified in its Charter)

| | |
|---|---|
| **California** | **77-0469558** |
| (State or Other Jurisdiction of Incorporation or Organization) | (I.R.S. Employer Identification Number) |

**150 Almaden Boulevard**
**San Jose, California 95113**
(Address of Principal Executive Offices including Zip Code)

**(408) 947-6900**
(Registrant s Telephone Number, Including Area Code)

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

| **Title of Each Class** | **Name of Each Exchange on which Registered** |
|---|---|
| Common Stock, no par value | The NASDAQ Stock 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 o No x

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 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 if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K 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/A, or any amendment to this Form 10-K/A. x

Indicate by check mark whether the Registrant is an large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act.

Large accelerated filer o Accelerated filer x Non-accelerated filer 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 stock held by non-affiliates of the Registrant, based upon the closing price of its common stock as of June 30, 2006 ($24.69 per share), as reported on the Nasdaq Global Select Market, was approximately $258 million.

As of February 12, 2007, there were 11,658,109 shares of the Registrant s common stock (no par value) outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

| DOCUMENTS INCORPORATED | PARTS OF FORM 10-K INTO WHICH INCORPORATED |
|---|---|
| Definitive proxy statement for the Company s 2007 Annual Meeting of Shareholders to be filed within 120 days of the end of the fiscal year ended December 31, 2006. | Part III |

**HERITAGE COMMERCE CORP**
**INDEX TO ANNUAL REPORT AMENDMENT NO. 2 ON FORM 10-K/A**
**FOR YEAR ENDED DECEMBER 31, 2006**

## PART I

### EXPLANATORY NOTE

**Heritage Commerce Corp is filing this Amendment No. 2 to its Annual Report on Form 10-K for the year ended December 31, 2006, to reflect the restatement of Heritage Commerce Corp s Consolidated Balance Sheets and Consolidated Statements of Cash Flows, as discussed in Note 17 of the Notes to the Consolidated Financial Statements contained in Part II, Item 8, Financial Statements and Supplementary Data. Except for Part II, Item 8, and related changes to conform Item 6, Selected Financial Data, and Item 7, Management s Discussion and Analysis of Financial Condition and Results of Operations, of Part II and certain other information contained herein related to the restated financial statements, no other information in the Form 10-K or Form 10-K/A, Amendment No. 1, for the year ended December 31, 2006 is being amended by this Amendment No. 2. This Amendment No. 2 continues to speak as of the date of the original filing of the Form 10-K and Heritage Commerce Corp has not updated the disclosure in the Amendment to speak as of any later date.**

### ITEM 1 - BUSINESS

Discussions of certain matters in this Report on this Amendment No. 2 to Form 10-K may constitute forward looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended (the Exchange Act ), and as such, may involve risks and uncertainties. Forward-looking statements, which are based on certain assumptions and describe future plans, strategies, and expectations, are generally identifiable by the use of words such as believe , expect , intend , anticipate , estimate , project , assume, plan, predict, forecast or similar expressions. These forward-looking statements relate to, among other things, expectations of the business environment in which the Company operates, projections of future performance, potential future performance, potential future credit experience, perceived opportunities in the market, and statements regarding the Company s mission and vision. The Company s actual results, performance, and achievements may differ materially from the results, performance, and achievements expressed or implied in such forward-looking statements due to a wide range of factors. The factors include, but are not limited to changes in interest rates, reducing interest margins or increasing interest rate risk, general economic conditions nationally or in the State of California, legislative and regulatory changes adversely affecting the business in which the Company operates, monetary and fiscal policies of the US Government, real estate valuations, the availability of sources of liquidity at a reasonable cost, competition in the financial services industry, the occurrence of events such as the terrorist acts of September 11, 2001, and other risks. All of the Company s operations and most of its customers are located in California. In addition, acts and threats of terrorism or the impact of military conflicts have increased the uncertainty related to the national and California economic outlook and could have an effect on the future operations of the Company or its customers, including borrowers. See Item 1A Risk Factors for further discussion of factors that could cause actual results to differ from forward-looking statements. The Company does not undertake, and specifically disclaims any obligation, to update any forward-looking statements to reflect occurrences or unanticipated events or circumstances after the date of such statements.

### GENERAL

Heritage Commerce Corp (the Company ) is registered with the Board of Governors of the Federal Reserve System ( FRB ) as a Bank Holding Company under the Bank Holding Company Act ( BHCA ). The Company was

organized in 1997 to be the holding company for Heritage Bank of Commerce ( HBC ). Subsequent to 1997, the Company became the holding company for Heritage Bank East Bay ( HBEB ), Heritage Bank South Valley ( HBSV ), and Bank of Los Altos ( BLA ). On January 1, 2003, HBEB, HBSV, and BLA were merged into Heritage Bank of Commerce. The former HBEB, HBSV, and BLA now operate as branch offices of HBC and continue to serve their local markets.

The Company s only other direct subsidiaries are Heritage Capital Trust I (formed 2000), Heritage Statutory Trust I (formed 2000), Heritage Statutory Trust II (formed 2001) and Heritage Statutory Trust III (formed 2002) (collectively, Subsidiary Trusts ), which were formed solely to facilitate the issuance of capital trust pass-through securities to enhance regulatory capital and liquidity. Pursuant to FASB Interpretation No. 46, *Consolidation of Variable Interest Entities* (FIN 46), the Subsidiary Trusts are not reflected on a consolidated basis in the financial statements of the Company.

The Company s principal source of income is dividends from HBC. The expenditures of the Company, including (but not limited to) the payment of dividends to shareholders, if and when declared by the Board of Directors, the cost of servicing debt, legal fees, audit fees, and shareholder costs will generally be paid from dividends paid to the Company by HBC.

At December 31, 2006, the Company had consolidated assets of $1.04 billion, deposits of $847 million and shareholders equity of $123 million. The Company s liabilities include $24 million in debt obligations due to the Subsidiary Trusts related to capital trust pass-through securities issued by those entities.

The Internet address of the Company s website is http://www.heritagecommercecorp.com. The Company makes available free of charge through the Company s website, the Company s annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and amendments to these reports. The Company makes these reports available on its website on the same day they appear on the SEC s website.

***Heritage Bank of Commerce***

Heritage Bank of Commerce ( HBC ) is a California state-chartered bank headquartered in San Jose, California. It was incorporated in November 1993 and opened for business in January 1994. HBC is a multi-community independent bank that offers a full range of banking services to small to medium sized businesses and their owners, managers and employees residing in Santa Clara, Alameda and Contra Costa counties in California. We operate nine full service branch offices throughout this geographic footprint. The locations of HBC s current offices are:

| | |
|---|---|
| San Jose: | Administrative Office<br>Main Branch<br>150 Almaden Boulevard |
| Los Gatos: | Branch Office<br>15575 Los Gatos Boulevard |
| Fremont: | Branch Office<br>3077 Stevenson Boulevard |
| Danville: | Branch Office<br>310 Hartz Avenue |
| Morgan Hill: | Branch Office<br>18625 Sutter Boulevard |
| Gilroy: | Branch Office<br>7598 Monterey Street |
| Los Altos: | Branch Office<br>369 S. San Antonio Road |
| Los Altos: | Branch Office<br>4546 El Camino Real |
| Mountain View: | Branch Office<br>175 E. El Camino Real |

HBC s gross loan balances at the end of 2006 totaled $709 million, excluding loans held for sale. HBC s lending activities are diversified and include commercial, real estate, construction loans, and consumer loans. HBC s commercial loans are made for working capital, financing the purchase of equipment or for other business purposes. Such loans include loans with maturities ranging from thirty days to one year and term loans, with maturities normally ranging from one to five years. Short-term business loans are generally intended to finance current transactions and typically provide for periodic principal payments, with interest payable monthly. Term loans normally provide for floating interest rates, with monthly payments of both principal and interest. HBC s commercial loans are centered in locally-oriented commercial activities in markets where HBC has a physical presence through its branch offices and loan production offices.

HBC s real estate term loans consist primarily of loans made based on the borrower s cash flow and are secured by deeds of trust on commercial and residential property to provide a secondary source of repayment. HBC generally restricts real estate term loans to no more than 80% of the property s appraised value or the purchase price of the property, depending on the type of property and its utilization. HBC offers both fixed and floating rate loans. Maturities on such loans are generally restricted to between five and ten years (with amortization ranging from fifteen to twenty-five years and a balloon payment due at maturity); however, Small Business Administration (SBA) loans and certain other real estate loans that may be sold in the secondary market may be granted for longer maturities.

HBC s real estate land and construction loans are primarily short term interim loans to finance the construction of commercial and single family residential properties. HBC utilizes underwriting guidelines to assess the likelihood of repayment from sources such as sale of the property or permanent mortgage financing prior to making the construction loan.

HBC makes consumer loans for the purpose of financing automobiles, various types of consumer goods, and other personal purposes. Additionally, HBC makes home equity lines of credit available to its clientele. Consumer loans generally provide for the monthly payment of principal and interest. Most of HBC s consumer loans are secured by the personal property being purchased or, in the instances of home equity loans or lines, real property.

We also actively engage in SBA lending. We have been designated as an SBA preferred Lender since 1999 and HBC is a participant in the SBA s innovative Community Express program. HBC regularly makes SBA-guaranteed loans; the guaranteed portion of these loans may be sold in the secondary market depending on market conditions. As of December 31, 2006, the percentage of our total loans guaranteed by the SBA was 5%.

As of December 31, 2006, the percentage of our total loans for each of the principal areas in which we directed our lending activities were as follows: (i) commercial 40%, (ii) real estate secured loans 34%, (iii) construction loans 20%, and (iv) consumer (including home equity) 6%. While no specific industry concentration is considered significant, our lending operations are located in market areas dependent on technology and real estate industries and their supporting companies.

In addition to loans, we offer a wide range of deposit products for retail and business banking markets including checking accounts, interest-bearing transaction accounts, savings accounts, time deposits and retirement accounts. We attract deposits from throughout our market area with a customer-oriented product mix, competitive pricing, and convenient locations. At December 31, 2006 we had 13,000 deposit accounts totaling approximately $847 million, compared to 14,000 deposit accounts totaling approximately $940 million as of December 31, 2005.

We offer a multitude of other products and services to complement our lending and deposit services. These include cashier s checks, traveler s checks, bank-by-mail, ATM, night depository, safe deposit boxes, direct deposit, automated payroll services, electronic funds transfers, on-line banking, and other customary banking services. We currently operate ATM s at four different locations. In addition, we have established a convenient customer service group accessible by toll-free telephone to answer questions and promote a high level of customer service. HBC does not have a trust department.

***Recent Developments***

**Merger Agreement with Diablo Valley Bank.**

On February 8, 2007, the Company, HBC and Diablo Valley Bank ( Diablo ) entered into an Agreement and Plan of Merger (the Merger Agreement ), pursuant to which, among other things, Diablo will merge with and into HBC, with HBC surviving the merger (the Merger ) in a cash and stock transaction valued at approximately $70 million. The Merger Agreement has been unanimously approved by the Boards of Directors of the Company, HBC and Diablo. The Merger is subject to approval by the Diablo shareholders.

Under the terms of the Merger Agreement, the Company will pay a fixed number of 1,732,298 shares of the Company s common stock and an aggregate of $15 million in cash for all of the issued and outstanding shares of Diablo common stock. Each Diablo common shareholder will be entitled to receive at the shareholder s election (subject to certain prorating procedures) cash or the Company s common stock. The per share consideration for each share of Diablo common stock will be calculated by reference to the Company s average closing price over a 20 trading day period ending 5 days before the effective date of the Merger ( Average Closing Price ). Based on the closing price of the Company s common stock of $27.25 on February 8, 2007, the per share consideration would be $24.87. The per share consideration will float within a band of $23.00 to $25.00 if the Average Closing Price is between $24.55 and $27.44. If the Average Closing Price is above $27.44, the per share consideration will be increased to reflect one-third of the increase in the Average Closing Price above $27.44. If the Average Closing Price is below $24.55, the aggregate amount of cash paid in the Merger will be increased to an amount necessary to maintain a minimum per share consideration of $23.00. If the Average Closing Price falls below $23.50, the

Company has the right to terminate the Merger Agreement. All Diablo stock options will be terminated at the effective time of the Merger and option holders will receive cash in the amount of the per share consideration minus the exercise price of the option (in the aggregate approximately $8 million). Diablo s issued and outstanding Series A Preferred Stock will be redeemed in full at $32 per share by Diablo prior to the effective time of the Merger (approximately $6.5 million).

The Merger Agreement contains customary representations and warranties of the Company, HBC and Diablo. Consummation of the Merger is subject to certain conditions, including, among others, (i) approval by the Diablo common shareholders, (ii) receipt of certain regulatory approvals, (iii) the filing of a registration statement on Form S-4 to register the Company s common stock to be issued in the Merger with the Securities and Exchange Commission (SEC) and receipt of the SEC s order that such registration statement is effective, (iv) listing of the Company s common stock to be issued in the Merger with NASDAQ, (v) satisfaction of tangible net worth and customer deposit tests, (vi) redemption of Diablo s Series A Preferred Stock, and (vii) the accuracy of representations and warranties of Diablo, the Company and HBC.

Certain shareholders of Diablo have entered into Shareholder Agreements with the Company pursuant to which they have agreed to vote their Diablo shares in favor of the Merger. The Diablo Board of Directors has agreed to recommend to its shareholders the approval of the Merger. The Merger Agreement provides for the payment of a Termination Fee in the amount of $3,380,000, payable to the Company, if the Merger Agreement is terminated by the Company or Diablo under specified circumstances.

On the effective date of the Merger, two members of the Diablo Board of Directors, John J. Hounslow and Mark E. Lefanowicz will be added to the Company and HBC s Board of Directors.

In connection with the Merger Agreement, the Company and/or HBC entered into the following agreements which will become effective upon June 20, 2007, the effective date of the Merger: (i) a three year employment agreement with James Mayer (the President of Diablo) for annual salaries of $220,000, $240,000 and $250,000 and the grant (subject to approval of the Company s Compensation Committee and Board of Directors) of stock options for 20,000 shares of the Company s common stock pursuant to its 2004 Stock Option Plan, (ii) a consulting agreement with John J. Hounslow (the Chairman of the Board of Diablo) pursuant to which Mr. Hounslow will receive $400,000, and (iii) non-compete agreements with Mr. Mayer and Mr. Hounslow (for which Mr. Hounslow will receive $200,000). Mr. Mayer and Mr. Hounslow have agreed to forego certain severance payments due to them as a result of the Merger in exchange for the Agreements with the Company and HBC.

The transaction is expected to close during the second or third quarter of 2007.

**Personnel Changes**

On May 5, 2006, Kenneth A. Corsello resigned as the Company s Executive Vice President and Chief Credit Officer.

On May 12, 2006, Richard E. Hagarty was promoted to Executive Vice President and Chief Credit Officer of Heritage Bank of Commerce.

On July 27, 2006, the Company s Board of Directors elected Jack W. Conner as Chairman of the Board, succeeding William Del Biaggio, Jr., who will remain on the Board of Directors as a director and Founding Chairman and will continue serving the Bank as an Executive Vice President.

***Correspondent Banks***

Correspondent bank deposit accounts are maintained to enable the Company to transact types of activity that it would otherwise be unable to perform or would not be cost effective due to the size of the Company or volume of activity. The Company has utilized several correspondent banks to process a variety of transactions.

**COMPETITION**

The banking and financial services business in California generally, and in the Company s market areas specifically, is highly competitive. The increasingly competitive environment is a result primarily of changes in regulation, changes in technology and product delivery systems, and the consolidation among financial service providers. The Company competes for loans, deposits and customers for financial services with other commercial banks, savings and loan associations, securities and brokerage companies, mortgage companies, insurance companies, finance companies, 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 and offer a broader array of financial services than the Company. In order to compete with the other financial service providers, the Company principally relies upon local promotional activities, personal relationships established by officers, directors, and employees with its customers, and specialized services tailored to meet its customers needs. In those instances where the Company is unable to accommodate a customer s needs, the Company seeks to arrange for such loans on a participation basis with other financial institutions or to have those services provided in whole or in part by its correspondent banks. See Item 1 - *BUSINESS - Supervision and Regulation.*

**SUPERVISION AND REGULATION**

***Introduction***

Banking is a complex, highly regulated industry. The primary goals of the regulatory scheme are to maintain a safe and sound banking system, protect depositors and the Federal Deposit Insurance Corporation s insurance fund, and facilitate the conduct of sound monetary policy. In furtherance of these goals, Congress and the states have created several largely autonomous regulatory agencies and enacted numerous laws that govern banks, bank holding companies and the financial services industry. Consequently, the growth and earnings performance of the Company and HBC can be affected not only by management decisions and general economic conditions, but also by the requirements of applicable state and federal statues, regulations and the policies of various governmental regulatory authorities, including the Board of Governors of the Federal Reserve System, ( FRB ), and the California Department of Financial Institutions, ( DFI ).

The system of supervision and regulation applicable to financial services businesses governs most aspects of the business of the Company and HBC, including: (i) the scope of permissible business; (ii) investments; (iii) reserves that must be maintained against deposits; (iv) capital levels that must be maintained; (v) the nature and amount of collateral that may be taken to secure loans; (vi) the establishment of new branches; (vii) mergers and consolidations with other financial institutions; and (viii) the payment of dividends.

From time to time laws or regulations are enacted which have the effect of increasing the cost of doing business, limiting or expanding the scope of permissible activities, or changing the competitive balance between banks and other financial and non-financial institutions. Proposals to change the laws and regulations governing the operations of banks and bank holding companies are frequently made in Congress, in the California legislature and by various bank and other regulatory agencies. Future changes in the laws, regulations or polices that impact the Company and HBC cannot necessarily be predicted, but they may have a material effect on the business and earnings of the Company and HBC.

***The Company***

*General*. As a bank holding company, the Company is registered under the Bank Holding Company Act of 1956, as amended, or the BHCA, and is subject to regulation by the FRB. According to FRB policy, the Company is expected to act as a source of financial strength for HBC, to commit resources to support it in circumstances where the Company might not otherwise do so. Under the BHCA, the Company is subject to periodic examination by the FRB. The Company is also required to file periodic reports of its operations and any additional information regarding its activities and those of its subsidiaries, as may be required by the FRB.

The Company is also a bank holding company within the meaning of Section 3700 of the California Financial Code. Consequently, the Company and HBC are subject to examination by, and may be required to file reports with, the DFI. Regulations have not yet been proposed or adopted or steps otherwise taken to implement the DFI s powers under this statute.

*Bank Holding Company Liquidity.* The Company is a legal entity, separate and distinct from HBC. The Company has the ability to raise capital on its own behalf or borrow from external sources. The Company may also obtain additional funds from dividends paid by, and fees charged for services provided to, HBC. However, regulatory constraints on HBC may restrict or totally preclude the payment of dividends by HBC to the Company.

The Company is entitled to receive dividends, when and as declared by HBC s Board of Directors. Those dividends may come from funds legally available for those dividends, as specified and limited by the California Financial Code. Under the California Financial Code, funds available for cash dividends by a California-chartered bank are restricted to the lesser of: (i) the bank s retained earnings; or (ii) the bank s net income for its last three fiscal years (less any distributions to shareholders made during such period). With the prior approval of the DFI, cash dividends may also be paid out of the greater of: (a) the bank s retained earnings; (b) net income for the bank s last preceding fiscal year; or (c) net income of the bank s current fiscal year.

If the DFI determines that the shareholders equity of the bank paying the dividend is not adequate or that the payment of the dividend would be unsafe or unsound for the bank, the DFI may order the bank not to pay the dividend. Since HBC is an FDIC insured institution, it is also possible, depending upon its financial condition and other factors, that the FDIC could assert that the payment of dividends or other payments might, under some circumstances, constitute an unsafe or unsound practice and thereby prohibit such payments.

*Transactions With Affiliates.* The Company and any subsidiaries it may purchase or organize are deemed to be affiliates of HBC within the meaning of Sections 23A and 23B of the Federal Reserve Act and the FRB s Regulation W. Under Sections 23A and 23B and Regulation W, loans by HBC to affiliates, investments by them in affiliates stock, and taking affiliates stock as collateral for loans to any borrower is limited to 10% of HBC s capital, in the case of any one affiliate, and is limited to 20% of HBC s capital, in the case of all affiliates. In addition, transactions between HBC and other affiliates must be on terms and conditions that are consistent with safe and sound banking practices; in particular, a bank and its subsidiaries generally may not purchase from an affiliate a low-quality asset, as defined in the Federal Reserve Act. These restrictions also prevent a bank holding company and its other affiliates from borrowing from a banking subsidiary of the bank holding company, unless the loans are secured by marketable collateral of designated amounts. The Company and HBC are also subject to certain restrictions with respect to engaging in the underwriting, public sale and distribution of securities.

*Limitations on Business and Investment Activities.* Under the BHCA, a bank holding company must obtain the FRB s approval before: (i) directly or indirectly acquiring more than 5% ownership or control of any voting shares of another bank or bank holding company; (ii) acquiring all or substantially all of the assets of another bank; (iii) or merging or consolidating with another bank holding company.

The FRB may allow a bank holding company to acquire banks located in any state of the United States without regard to whether the acquisition is prohibited by the law of the state in which the target bank is located. In approving interstate acquisitions, however, the FRB must give effect to applicable state laws limiting the aggregate amount of deposits that may be held by the acquiring bank holding company and its insured depository institutions in the state in which the target bank is located, provided that those limits do not discriminate against out-of-state depository institutions or their holding companies, and state laws which require that the target bank have been in existence for a minimum period of time, not to exceed five years, before being acquired by an out-of-state bank holding company.

In addition to owning or managing banks, bank holding companies may own subsidiaries engaged in certain businesses that the FRB has determined to be so closely related to banking as to be a proper incident thereto. The

Company, therefore, is permitted to engage in a variety of banking-related businesses.  Some of the activities that the FRB has determined, pursuant to its Regulation Y, to be related to banking are: (i) making or acquiring loans or other extensions of credit for its own account or for the account of others; (ii) servicing loans and other extensions of credit; (iii) performing functions or activities that may be performed by a trust company in the manner authorized by federal or state law under certain circumstances; (iv) leasing personal and real property or acting as agent, broker, or adviser in leasing such property in accordance with various restrictions imposed by FRB regulations; (v) acting as investment or financial advisor; (vi) providing management consulting advice under certain circumstances; (vii) providing support services, including courier services and printing and selling MICR-encoded items; (viii) acting as a principal, agent, or broker for insurance under certain circumstances; (ix) making equity and debt investments in corporations or projects designed primarily to promote community welfare or jobs for residents; (x) providing financial, banking, or economic data processing and data transmission services; (xi) owning, controlling, or operating a savings association under certain circumstances; (xii) selling money orders, travelers   checks and U.S. Savings Bonds; (xiii) providing securities brokerage services, related securities credit activities pursuant to Regulation T, and other incidental activities; and (xiv) underwriting dealing in obligations of the U.S., general obligations of states and their political subdivisions, and other obligations authorized for state member banks under federal law.

Additionally, under the Gramm-Leach-Bliley Act of 1999 qualifying bank holding companies making an appropriate election to the FRB may engage in a full range of financial activities, including insurance, securities and merchant banking.  The Company has not elected to qualify for these financial activities.

Federal law prohibits a bank holding company and any subsidiary banks from engaging in certain tie-in arrangements in connection with the extension of credit.  Thus, for example, HBC may not extend credit, lease or sell property, or furnish any services, or fix or vary the consideration for any of the foregoing on the condition that: (i) the customer must obtain or provide some additional credit, property or services from or to HBC other than a loan, discount, deposit or trust services; (ii) the customer must obtain or provide some additional credit, property or service from or to the Company or any subsidiaries; or (iii) the customer must not obtain some other credit, property or services from competitors, except reasonable requirements to assure soundness of credit extended.