PUBLIC DISCLOSURE

August 26, 2002

COMMUNITY REINVESTMENT ACT PERFORMANCE EVALUATION

Bank of Los Altos

RSSD – 455561

4546 El Camino Real

Los Altos, California 94022

Federal Reserve Bank of San Francisco
101 Market Street
San Francisco, California 94105

NOTE: This document is an evaluation of this institution's record of meeting the credit needs of its entire community, including low- and moderate-income neighborhoods, consistent with safe and sound operation of the institution. This evaluation is not, nor should it be construed as, an assessment of the financial condition of this institution. The rating assigned to this institution does not represent an analysis, conclusion or opinion of the federal financial supervisory agency concerning the safety and soundness of this financial institution.

TABLE OF CONTENTS

INSTITUTION

Institution's CRA Rating: This institution is rated satisfactory**.**

Bank of Los Altos demonstrates an overall satisfactory level of performance under the Community Reinvestment Act. The loan-to-deposit ratio is consistent with banks within the same market, and a reasonable percentage of originations are within the assessment area. Overall, the dispersion of lending is reasonable throughout the assessment area, and there are no conspicuous gaps in the lending patterns.

PERFORMANCE CONTEXT

Description of Institution

Bank of Los Altos (BOLA) is a $271 million community bank headquartered in Los Altos, California. BOLA currently operates three full-service branch offices, two in Los Altos and one in Mountain View.[1] It was originally founded in 1975 as Foothill Bank. The name was changed in 1995 from Foothill Bank to Bank of Los Altos when the bank became a subsidiary of Western Holdings Bancorp. In October 2000, Western Holdings Bancorp merged into Heritage Commerce Corp (HCC) . Since that time, BOLA has operated as one of four wholly-owned bank subsidiaries of HCC. As of June 30, 2002, HCC maintained total consolidated assets of $926 million, 29 percent of which represented BOLA.

BOLA's provides complete banking services to professionals, individuals and businesses in northern Santa Clara County. Its business focus has shifted over time from construction and land loans to residential mortgage (primarily home equity loans for both consumer and business purposes) and commercial purpose loans. Accordingly, the loan portfolio is primarily composed of commercial purpose loans and loans secured by residential real estate. Construction lending remains a focus and, therefore, continues to represent a sizeable portion of the loan portfolio. Most of the construction loans are on residential properties located in Los Altos, though the portfolio also contains owner-occupied residential and commercial projects throughout Santa Clara County. The lending portfolio, as of June 30, 2002, is detailed in the following table.

Loan Type	Dollar Amount ('000's)	% of Loan Portfolio
Commercial / Industrial & Non Farm / Non Residential Real Estate	$74,127	42%
Secured by 1 - 4 Family Residential Real Estate	$51,104	29%
Construction	$47,449	27%
Consumer	$4,940	3%
Multifamily Housing	$187	0%
All Other	$4	0%
Farmland and Agriculture	$0	0%
Total Loans[2]	**$177,616**	**100%**

[1] In January 2001, BOLA consolidated its two San Antonio Road offices in an effort to eliminate duplicative operations.

[2] Total Loans represents: Total Gross Loans Less Unearned Income of $195M.

The Federal Deposit Insurance Corporation last conducted a CRA examination of the bank on July 6, 1998 and assigned a satisfactory rating. In the time period between examinations there were no legal or financial constraints that would impede the bank's ability to meet the credit needs of the communities in which it operates consistent with its business strategy, size, financial capacity and local economic conditions.

Description of Assessment Area

BOLA continues to define its assessment area as the northwest quadrant of Santa Clara County plus the adjacent southeastern tip of San Mateo County. The assessment area contains 97 census tracts and includes the cities of Cupertino, East Palo Alto, Los Altos, Los Altos Hills, Mountain View, Palo Alto (with the exception of the undeveloped southern Black Mountain area northwest of Big Basin Way), Santa Clara and Sunnyvale. All of the cities are within Santa Clara County with the exception of East Palo Alto, which is in San Mateo County. According to the 1990 census data, the single low-income census tract is a sparsely populated, rural subdivision within the city of Sunnyvale. All of these cities comprise a contiguous group of whole census tracts and are within the San Francisco Consolidated Metropolitan Statistical Area (CMSA). The following table illustrates the assessment area by tract and income levels based on 1990 Census data.

Census Tract Income Level	Census Tract		Population by Census Tract	
	Number	Percent	Number	Percent
Low	1	1.0%	373	0.1%
Moderate	17	17.5%	86,238	19.7%
Middle	52	53.6%	233,635	53.5%
Upper	27	27.8%	116,797	26.7%
Total	97	100.0%	437,043	100.0%

Bank of Los Altos operates in a highly competitive financial services market. As of June 30, 2002, BOLA captured roughly 1.38 percent of the deposit base within its assessment area, which places it fifteenth out of 29 institutions operating in the same area.[3] Competition includes national and state-chartered banks, savings and loan associations, credit unions and other non-bank financial service providers. The lead banks in this market consist of three large national banks and one state member bank.

Santa Clara County is the largest of the nine counties that contribute to the Bay Area's economy. Encompassing roughly 1,312 miles, the county's population of over 1.6 million[4] makes it the fifth largest county in the state.[5] The Northwestern region in the county is known as the Silicon Valley, an industrial region with a dense concentration of businesses that specializes in technology, software and electronics. Silicon Valley flourished in the late 1990's as evidenced by the historically low unemployment rate and high standard of living. The annual

[3] Source: FDIC / OTS Summary of Deposits as of June 30, 2002
[4] Source: U.S. Census Bureau, Census 2000
[5] Source: County of Santa Clara, Overview of County, http://www.co.santa-clara.ca.us

unemployment rate in 1996 was 3.6 percent.[6] When Silicon Valley was experiencing a boom economy in 2000, that rate fell to 2.0 percent lower than both the state and the national rates of 4.9 percent and 4.0 percent respectively.[7,8]

Employment and Economic Conditions

The economic outlook changed in 2001 with the erosion of the vibrant high-tech industry and the devastating events of September 11, 2001. Unemployment figures for March 2002 indicate Santa Clara County experienced an unemployment rate of 7.6 percent which is higher than both the state and the national unemployment rates of 6.7 percent and 5.7 percent respectively.[9] Similarly the unemployment rate in San Mateo County for the same period was 4.5 percent.[10] According to a community development source, high unemployment in conjunction with the recession has resulted in more loan demand from borrowers who wish to start a small business, save a small business that is ailing or consolidate business or personal debt. Lenders, including community development organizations, are finding it difficult to make loans due to the excessively high debt and the large number of recent business failures among applicants. Though the rise in unemployment is attributable to the technology downturn, job losses are widespread, extending from technology, manufacturing and services to financial services, travel and transportation sectors.[11]

Business Demographics

High unemployment and economic uncertainty have adversely affected small businesses. Dun and Bradstreet data for the year 2000 shows that small businesses dominated the market. Approximately 80 percent of the 26,834 businesses that were operating in the assessment area had gross annual revenues of $1 million or less. Additionally, 59 percent had less than five employees. According to a recent community contact, these smaller businesses experience more difficulties due to high labor cost and the high cost of office or rental space. The cost of doing business in San Jose, the largest city in Santa Clara, as of March 31, 2002 was 109 percent of the national average.[12]

Notwithstanding the already high cost of doing business, small business owners also are faced with the challenges presented by the faltering economy. Rising personal bankruptcies and other deteriorating credit conditions mean less disposable income for patrons and business owners alike. As a result, owners experience tighter profit margins. While community development organizations and lenders articulate a willingness to grant credit requests, the poor economic outlook and likelihood of its continuance makes lending more difficult.

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[6] Source: Précis Metro ©, 2002 Economy.com, Inc.
[7] Source: California Employment Development Department, Labor Information Division, http://www.calmis.ca.gov
[8] Source: U.S. Department of Labor, Bureau of Labor Statistics, http://www.bls.gov
[9] Source: California Employment Development Department, U.S. Department of Labor
[10] Ibid.
[11] Source: Précis Metro ©, 2002 Economy.com, Inc.
[12] Ibid.

Conclusions

The economic recession, which began in 2001, caused job losses and unemployment to rise significantly. Also, given the vast number of small businesses in the market, credit facilities for the majority of small business owners was (and continues to be) a major need. While demand for such loans may have been high during much of the review period, underwriting standards were more stringent and many borrowers did not have the capacity to support additional debt. Nonetheless, community leaders expressed the need for small dollar loans and new and innovative products, such as lines of credit, to help meet the needs of small businesses.

CONCLUSIONS WITH RESPECT TO PERFORMANCE CRITERIA

Scope of Examination

The CRA performance of Bank of Los Altos was evaluated using the small bank examination procedures. The evaluation was based upon the following performance criteria.

- Loan volume in comparison to deposits (Loan-to-Deposit Ratio)
- Lending inside and outside the assessment area (Lending in Assessment Area)
- Distribution of lending to businesses with different annual revenues (Lending by Business Revenue)
- Dispersion of lending throughout census tracts or geographic areas within the assessment area (Geographic Distribution of Loans)

Responsiveness to consumer complaints was not evaluated because there have been no complaints related to CRA performance.

The CRA evaluation was based on 182 small business loans during the sample period of April 1, 2000, through March 31, 2002. Only those loans extended inside the assessment area were used to evaluate the geographic distribution and the distribution to businesses with different revenues. Home purchase loans, reportable under the Home Mortgage Disclosure Act, were not used in the evaluation due to the limited number of loans extended during the sample period.

Loan-to-Deposit Ratio

BOLA maintains a loan-to-deposit ratio that meets standards for satisfactory performance. The bank maintained an eight-quarter-average loan-to-deposit ratio of 73.5 percent calculated using call report data from September 30, 2000, through June 30, 2002. The eight-quarter average loan-to-deposit ratio is comparable to banks with a similar asset size and branch network.

Lending in Assessment Area

The concentration of loans granted within the assessment area meets standards for satisfactory performance. Originations within the assessment area represent 69.2 percent of loan volume and 70.7 percent of the total dollar volume.

Lending by Business Revenue

Lending to businesses with gross annual revenues of $1 million or less is adequate in light of the economic conditions plaguing the assessment area. As previously noted, the economic climate of the assessment area has resulted in business failures, borrowers with higher debt ratios and tighter underwriting standards. As a result, BOLA has extended only 40.1 percent of its small business loans to small businesses. Although this number is below the number of small businesses in the area, a significant percentage of the loans (72.6 percent) made to businesses with gross annual revenues of $1 million or less were granted in smaller dollar amounts, meeting an articulated need within the community.

BOLA augments lending activity to small businesses by participating in the Lenders for Community Development (LCD), a small business loan pool. Specifically, BOLA has committed $50,000, has funded $29,400 to date and has $15,282 outstanding. LCD is a multi-bank community development non-profit organization providing financing and consulting to small businesses owned by low- and moderate-income individuals or operating within low- or moderate-income census tracts.

Overall, the lending activity in conjunction with participation in the Lenders for Community Development consortium illustrates responsiveness to the needs of small businesses within the assessment area.

Geographic Distribution of Loans

The geographic distribution of small business loans meets standards for satisfactory performance. Lending patterns reflects a reasonable dispersion throughout the assessment area. The following table illustrates the banks lending patterns by census tract compared to the distribution of businesses and the performance of large bank lenders in the market.

Census Tract Income Level	Percent of Total Census Tracts	Percent of Small Businesses	Bank Lending		Aggregate Lending	
			Percent Number Loans	Percent Dollar Volume	Percent Number	Percent Dollar Volume
Low	1.0%	8.7%	4.4%	8.1%	8.7%	14.1%
Moderate	17.5%	14.3%	22.0%	16.6%	13.9%	16.0%
Middle	53.6%	52.8%	31.9%	38.3%	54.5%	53.6%
Upper	27.8%	24.2%	41.8%	37.1%	22.9%	16.2%

The number of loans in the one low-income tract appears small when compared to the number of small businesses in that tract. However, small business lending is reasonably concentrated in the areas surrounding the three branch offices. The low-income tract is located on the perimeter of the assessment area, and there are five financial institutions located within the tract. The percentage of dollars compares favorably to the percentage of small businesses within the tract. Conversely, lending in the moderate-income tracts exceeds the distribution of businesses in these areas as well as the prevalence of these areas. Also, lending in moderate-income areas surpasses the percentage of loans when compared to the aggregate market.

Response to Complaints

Bank of Los Altos has not received any complaints relating to its CRA performance since the previous examination. Accordingly, this component was not used to determine the overall performance rating.

COMPLIANCE WITH FAIR LENDING LAWS AND REGULATIONS

BOLA is in compliance with the anti-discrimination provisions of the Fair Housing Act and the Equal Credit Opportunity Act. In addition, there was no evidence that the bank had engaged in any prohibited practices.

APPENDIX A

GLOSSARY OF TERMS

Aggregate lending: The number of loans originated and purchased by all lenders subject to reporting requirements as a percentage of the aggregate number of loans originated and purchased by all lenders in the MSA / assessment area.

Block numbering area ("BNA"): Statistical subdivisions of a county for grouping and numbering blocks in non-metropolitan counties where local census statistical area committees have not established census tracts. BNAs do not cross county lines.

Census tract: Small subdivisions of metropolitan and other densely populated counties. Census tract boundaries do not cross county lines; however, they may cross the boundaries of metropolitan statistical areas. They usually have between 2,500 and 8,000 persons, and their physical size varies widely depending upon population density. Census tracts are designed to be homogeneous with respect to population characteristics, economic status, and living conditions to allow for statistical comparisons.

Community development: Affordable housing for low- or moderate-income individuals; community services targeted to low- or moderate-income individuals, activities that promote economic development by financing businesses or farms that meet the size eligibility standards of the Small Business Administration's Development Company or Small Business Investment Company programs (13 CFR 121.301) or have gross annual revenues of $1 million or less; or, activities that revitalize or stabilize low- or moderate-income geographies,

Consumer loan: A loan to one or more individuals for household, family, or other personal expenditures. A consumer loan does not include a home mortgage, small business, or small farm loan. This definition includes the following categories of loans: motor vehicle, credit card, home equity, other secured loan, and other unsecured loan.

Family: Includes a householder and one or more other persons living in the same household who are related to the householder by birth, marriage, or adoption. The number of family households always equals the number of families; however, a family household may also include non-relatives living with the family. Families are classified by type as either a married couple family or other family, which is further classified into "male householder" (a family with a male household and no wife present) or "female householder" (a family with a female householder and no husband present).

Full review: Performance under the lending, investment, and service tests is analyzed considering performance context, quantitative factors (e.g., geographic distribution, borrower distribution, total number and dollar amount of investments, branch distribution) and qualitative factors (e.g., innovation, complexity).

Geography: A census tract or a block numbering area delineated by the U.S. Bureau of the Census in the most recent decennial census.

Home Mortgage Disclosure Act ("HMDA"): The statute that requires certain mortgage lenders that do business or have banking offices in a metropolitan statistical area to file annual summary reports of their mortgage lending activity. The reports include such data as the race, gender, and the income of applications, the amount of loan requested, and the disposition of the application (e.g., approved, denied, and withdrawn).

Home mortgage loans: Include home purchase and home improvement loans as defined in the HMDA regulation. This definition also includes multifamily (five or more families) dwelling loans, loans for the purchase of manufactured homes and refinancings of home improvement and home purchase loans.

Household: Includes all persons occupying a housing unit. Persons not living in households are classified as living in group quarters. In 100 percent tabulations, the count of households always equals the count of occupied housing units.

Low-income: Individual income that is less than 50 percent of the area median income, or a median family income that is less than 50 percent in the case of a geography.

Limited review: Performance under the lending, investment, and service tests is analyzed using only quantitative factors (e.g., geographic distribution, borrower distribution, total number and dollar amount of investments, branch distribution).

Market share: The number of loans originated and purchased by the institution as a percentage of the aggregate number of loans originated and purchased by all lenders in the MSA / assessment area.

Metropolitan area: Any primary metropolitan statistical area ("PMSA"), metropolitan statistical area ("MSA"), or consolidated metropolitan area ("CMSA"), as defined by the Office of Management and Budget, with a population of 250 thousand or more, and any other area designated as such by the appropriate federal financial supervisory agency.

Moderate-income: Individual income that is at least 50 percent and less than 80 percent of the area median income, or a median family income that is at least 50 percent and less than 80 percent in the case of a geography.

Middle-income: Individual income that is at least 80 percent and less than 120 percent of the area median income, or a median family income that is at least 80 percent and less than 120 percent in the case of a geography.

Multifamily: Refers to a residential structure that contains five or more units.

Optional loans: Includes any unreported category of loans for which the institution collects and maintains data for consideration during a CRA examination. Also includes consumer loans and other loan data an institution may provide concerning its lending performance.

Owner-occupied units: Includes units occupied by the owner or co-owner, even if the unit has not been fully paid for or is mortgaged.

Qualified investment: A qualified investment is defined as any lawful investment, deposit, membership share, or grant that has as its primary purpose community development.

Small loans to business: A loan included in “loans to small businesses” as defined in the Consolidated Report of Condition and Income (Call Report). These loans have original amounts of $1 million or less and are either secured by nonfarm nonresidential properties or are classified as commercial and industrial loans.

Small loans to farms: A loan included in “loans to small farms” as defined in the instructions for preparation of the Consolidated Report of Condition and Income (Call Report). These loans have original amounts of $500 thousand or less and are either secured by farmland, including farm residential and other improvements, or are classified as loans to finance agricultural production and other loans to farmers.

Owner-occupied units: Includes units occupied by the owner or co-owner, even if the unit has not been fully paid for or is mortgaged.

Qualified investment: A qualified investment is defined as any lawful investment, deposit, membership share, or grant that has as its primary purpose community development.

Upper-income: Individual income that is more than 120 percent of the area median income, or a median family income that is more than 120 percent in the case of a geography.