DR REDDYS LABORATORIES LTD
Form SC 13G/A
February 14, 2005

SCHEDULE 13G

Amendment No. 1
Dr. Reddys Laboratories Limited
Common Stock
Cusip # Y21089159

Cusip # Y21089159
Item 1: Reporting Person - FMR Corp.
Item 4: Delaware
Item 5: 30,100
Item 6: 0
Item 7: 2,663,200
Item 8: 0
Item 9: 2,663,200
Item 11: 3.480%
Item 12: HC

Cusip # Y21089159
Item 1: Reporting Person - Edward C. Johnson 3d
Item 4: United States of America
Item 5: 0
Item 6: 0
Item 7: 2,663,200
Item 8: 0
Item 9: 2,663,200
Item 11: 3.480%
Item 12: IN

Cusip # Y21089159
Item 1: Reporting Person - Abigail P. Johnson
Item 4: United States of America
Item 5: 0
Item 6: 0
Item 7: 2,663,200
Item 8: 0
Item 9: 2,663,200
Item 11: 3.480%
Item 12: IN

SCHEDULE 13G - TO BE INCLUDED IN
STATEMENTS
FILED PURSUANT TO RULE 13d-1(b) or 13d-2(b)

Item 1(a). Name of Issuer:

Dr. Reddys Laboratories Limited

Item 1(b). Name of Issuer's Principal Executive Offices:

7-1-27 Ameerpet
Hyderabad, India 500-016

Item 2(a). Name of Person Filing:

FMR Corp.

Item 2(b). Address or Principal Business Office or, if None, Residence:

82 Devonshire Street, Boston, Massachusetts 02109

Item 2(c). Citizenship:

Not applicable

Item 2(d). Title of Class of Securities:

Common Stock

Item 2(e). CUSIP Number:

Y21089159

Item 3. This statement is filed pursuant to Rule 13d-1(b) or 13d-2(b) and the person filing, FMR Corp., is a parent holding company in accordance with Section 240.13d-1(b)(ii)(G). (Note: See Item 7).

Item 4. Ownership

(a) Amount Beneficially Owned: 2,663,200

(b) Percent of Class: 3.480%

(c) Number of shares as to which such person has:

(i) sole power to vote or to direct the vote: 30,100

(ii) shared power to vote or to direct the vote: 0

(iii) sole power to dispose or to direct the disposition of: 2,663,200

(iv) shared power to dispose or to direct the disposition of: 0

Item 5. Ownership of Five Percent or Less of a Class.

If this statement is being filed to report the fact that as of the date hereof, the reporting person has ceased to be the beneficial owner of more than five percent of the class of securities, check the following (X).

Item 6. Ownership of More than Five Percent on Behalf of Another

Person.

Not applicable

Item 7. Identification and Classification of the Subsidiary Which Acquired the Security Being Reported on By the Parent Holding Company.

See attached Exhibit(s) A, B, and C.

Item 8. Identification and Classification of Members of the Group.

Not Applicable. See attached Exhibit A.

Item 9. Notice of Dissolution of Group.

Not applicable.

Item 10. Certification.

Inasmuch as the reporting persons are no longer the beneficial owners of more than five percent of the number of shares outstanding, the reporting persons have no further reporting obligation under Section 13(d) of the Securities and Exchange Commission thereunder, and the reporting persons have no obligation to amend this Statement if any material change occurs in the facts set forth herein.

Signature

After reasonable inquiry and to the best of my knowledge and belief, I certify that the information set forth in this Schedule 13G in connection with FMR Corp.'s beneficial ownership of the Common Stock of Dr. Reddys Laboratories Limited at December 31, 2004 is true, complete and correct.

February 14, 2005
Date

/s/Eric D. Roiter
Signature

Eric D. Roiter
Duly authorized under Power of Attorney
dated December 30, 1997 by and on behalf
of FMR Corp. and its direct and indirect
subsidiaries

SCHEDULE 13G - TO BE INCLUDED IN STATEMENTS
FILED PURSUANT TO RULE 13d-1(b) or 13d-2(b)

Pursuant to the instructions in Item 7 of Schedule 13G, Fidelity Management & Research Company ("Fidelity"), 82 Devonshire Street, Boston, Massachusetts 02109, a wholly-owned subsidiary of FMR Corp. and an investment adviser registered under Section 203 of the Investment Advisers Act of 1940, is the beneficial owner of

2,577,000 shares or 3.368% of the Common Stock outstanding of Dr. Reddys Laboratories Limited ("the Company") as a result of acting as investment adviser to various investment companies registered under Section 8 of the Investment Company Act of 1940.

Edward C. Johnson 3d, FMR Corp., through its control of Fidelity, and the funds each has sole power to dispose of the 2,577,000 shares owned by the Funds.

Neither FMR Corp. nor Edward C. Johnson 3d, Chairman of FMR Corp., has the sole power to vote or direct the voting of the shares owned directly by the Fidelity Funds, which power resides with the Funds' Boards of Trustees. Fidelity carries out the voting of the shares under written guidelines established by the Funds' Boards of Trustees.

Fidelity Management Trust Company, 82 Devonshire Street, Boston, Massachusetts 02109, a wholly-owned subsidiary of FMR Corp. and a bank as defined in Section 3(a)(6) of the Securities Exchange Act of 1934, is the beneficial owner of 77,000 shares or 0.101% of the Common Stock outstanding of the Company as a result of its serving as investment manager of the institutional account(s).

Edward C. Johnson 3d and FMR Corp., through its control of Fidelity Management Trust Company, each has sole dispositive power over 77,000 shares and sole power to vote or to direct the voting of 20,500 shares, and no power to vote or to direct the voting of 56,500 shares of Common Stock owned by the institutional account(s) as reported above.

Members of the Edward C. Johnson 3d family are the predominant owners of Class B shares of common stock of FMR Corp., representing approximately 49% of the voting power of FMR Corp. Mr. Johnson 3d owns 12.0% and Abigail Johnson owns 24.5% of the aggregate outstanding voting stock of FMR Corp. Mr. Johnson 3d is Chairman of FMR Corp. and Abigail P. Johnson is a Director of FMR Corp. The Johnson family group and all other Class B shareholders have entered into a shareholders' voting agreement under which all Class B shares will be voted in accordance with the majority vote of Class B shares. Accordingly, through their ownership of voting common stock and the execution of the shareholders' voting agreement, members of the Johnson family may be deemed, under the Investment Company Act of 1940, to form a controlling group with respect to FMR Corp.

Fidelity International Limited, Pembroke Hall, 42 Crowlane, Hamilton, Bermuda, and various foreign-based subsidiaries provide investment advisory and management services to a number of non-U.S. investment companies (the "International Funds") and certain institutional investors. Fidelity International Limited is the beneficial owner of 9,200 shares or 0.012% of the Common Stock outstanding of the Company. Additional information with respect to the beneficial ownership of Fidelity International Limited is shown on Exhibit B.

Some or all of the shares of Common Stock of Dr.

Reddys Laboratories Limited owned by the investment companies at December 31, 2004 may include shares represented by American Depository Shares.

SCHEDULE 13G - TO BE INCLUDED IN STATEMENTS
FILED PURSUANT TO RULE 13d-1(b) or 13d-2(b)

Pursuant to instructions in Item 7 of Schedule 13G, this Exhibit has been prepared to identify Fidelity International Limited, Pembroke Hall, 42 Crow Lane, Hamilton, Bermuda, a Bermudan joint stock company incorporated for an unlimited duration by private act of the Bermuda Legislature (FIL) and an investment adviser to various investment companies (the "International Funds") and certain institutional investors, as a beneficial owner of the 9,200 shares or 0.012% of the Common Stock outstanding of Dr. Reddys Laboratories Limited.

Prior to June 30, 1980, FIL was a majority-owned subsidiary of Fidelity Management & Research Company (Fidelity), a wholly-owned subsidiary of FMR Corp. On that date, the shares of FIL held by Fidelity were distributed, as a dividend, to the shareholders of FMR Corp. FIL currently operates as an entity independent of FMR Corp. and Fidelity. The International Funds and FIL's other clients, with the exception of Fidelity and an affiliated company of Fidelity, are non-U.S. entities.

A partnership controlled by Edward C. Johnson 3d and members of his family owns shares of FIL voting stock with the right to cast approximately 39.89% of the total votes which may be cast by all holders of FIL voting stock. Mr. Johnson 3d is Chairman of FMR Corp. and FIL. FMR Corp. and FIL are separate and independent corporate entities, and their Boards of Directors are generally composed of different individuals. Other than when one serves as a sub adviser to the other, their investment decisions are made independently, and their clients are generally different organizations.

FMR Corp. and FIL are of the view that they are not acting as a "group" for purposes of Section 13(d) under the Securities Exchange Act of 1934 (the "1934" Act) and that they are not otherwise required to attribute to each other the "beneficial ownership" of securities "beneficially owned" by the other corporation within the meaning of Rule 13d-3 promulgated under the 1934 Act. Therefore, they are of the view that the shares held by the other corporation need not be aggregated for purposes of Section 13(d). However, FMR Corp. is making this filing on a voluntary basis as if all of the shares are beneficially owned by FMR Corp. and FIL on a joint basis.

FIL may continue to have the International Funds or other accounts purchase shares subject to a number of factors, including, among others, the availability of shares for sale at what FIL considers to be reasonable prices and other investment opportunities that may be available to the International Funds.

FIL intends to review continuously the equity position of the International Funds and other accounts in the Company. Depending upon its future evaluations of the business and prospects of the Company and upon other developments, including, but not limited to, general economic and business conditions and money market and stock market conditions, FIL may determine to cease making additional purchases of shares or to increase or decrease the equity interest in the Company by acquiring additional shares, or by disposing of all or a portion of the shares.

FIL does not have a present plan or proposal which relates to or would result in (i) an extraordinary corporate transaction, such as a merger, reorganization, liquidation, or sale or transfer of a material amount of assets involving the Company or any of its subsidiaries, (ii) any change in the Company's present Board of Directors or management, (iii) any material changes in the Company's present capitalization or dividend policy or any other material change in the Company's business or corporate structure, (iv) any change in the Company's charter or by-laws, or (v) the Company's common stock becoming eligible for termination of its registration pursuant to Section 12(g)(4) of the 1934 Act.

FIL has sole power to vote and the sole power to dispose of 9,200 shares.

SCHEDULE 13G - TO BE INCLUDED IN STATEMENTS
FILED PURSUANT TO RULE 13d-1(b) or 13d-2(b)
RULE 13d-1(f)(1) AGREEMENT

The undersigned persons, on February 14, 2005, agree and consent to the joint filing on their behalf of this Schedule 13G in connection with their beneficial ownership of the Common Stock of Dr. Reddys Laboratories Limited at December 31, 2004.

FMR Corp.

By /s/ Eric D. Roiter
Eric D. Roiter
Duly authorized under Power of Attorney
dated December 30, 1997, by and on behalf
of FMR Corp. and its direct and indirect
subsidiaries

Edward C. Johnson 3d

By /s/ Eric D. Roiter
Eric D. Roiter
Duly authorized under Power of Attorney
dated December 30, 1997, by and on behalf
of Edward C. Johnson 3d

Abigail P. Johnson

By /s/ Eric D. Roiter
Eric D. Roiter
Duly authorized under Power of Attorney

dated December 30, 1997, by and on behalf
of Abigail P. Johnson

Fidelity Management & Research Company

By /s/ Eric D. Roiter
Eric D. Roiter
Senior V.P. and General Counsel

xt-align:left;font-size:10pt;">Grade 3

2,012

4,808

775

—

7,595

Grades 4 and 5 – pass
58,179

144,230

114,766

31,600

348,775

Grade 6 – special mention
342

1,095

—

113

1,550

Grade 7 – substandard
1,245

4,539

21,617

—

27,401

Grade 8 – doubtful
—

—

—

—

—

Total
$
62,369

$
154,672

$
137,158

$
31,713

$
385,912

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December 31, 2013 (In thousands)	Commercial and Industrial	Commercial RE	RE Construction and Development	Agricultural	Total
Grades 1and 2	$355	$—	$—	$70	$425
Grade 3	44	5,287	816	—	6,147
Grades 4 and 5 – pass	69,070	127,189	66,048	30,862	293,169
Grade 6 – special mention	590	—	—	—	590
Grade 7 – substandard	627	11,443	20,140	—	32,210
Grade 8 – doubtful	—	—	—	—	—
Total	$70,686	$143,919	$87,004	$30,932	$332,541

The Company follows consistent underwriting standards outlined in its loan policy for consumer and other homogeneous loans but, does not specifically assign a risk rating when these loans are originated. Consumer loans are monitored for credit risk and are considered “pass” loans until some issue or event requires that the credit be downgraded to special mention or worse.
The following tables summarize the credit risk ratings for consumer related loans and other homogeneous loans for December 31, 2014 and 2013 (in thousands).

	December 31, 2014				December 31, 2013			
	Residential Mortgages	Home Improvement and Home Equity	Installment	Total	Residential Mortgages	Home Improvement and Home Equity	Installment	Total
Not graded	$38,207	$1,038	$10,287	$49,532	$29,063	$1,378	$7,862	$38,303
Pass	17,887	30	865	18,782	19,320	—	1,468	20,788
Special Mention	216	—	—	216	1,204	32	—	1,236
Substandard	2,785	42	650	3,477	2,449	—	—	2,449
Total	$59,095	$1,110	$11,802	$72,007	$52,036	$1,410	$9,330	$62,776

Allowance for Loan Losses

The Company analyzes risk characteristics inherent in each loan portfolio segment as part of the quarterly review of the adequacy of the allowance for loan losses. The following summarizes some of the key risk characteristics for the eleven segments of the loan portfolio (Consumer loans include three segments):

Commercial and business loans – Commercial loans are subject to the effects of economic cycles and tend to exhibit increased risk as economic conditions deteriorate, or if the economic downturn is prolonged. The Company considers this segment to be one of higher risk given the size of individual loans and the balances in the overall portfolio.

Government program loans – This is a relatively a small part of the Company’s loan portfolio, but has historically had a high percentage of loans that have migrated from pass to substandard given there vulnerability to economic cycles.

Commercial real estate loans – This segment is considered to have more risk in part because of the vulnerability of commercial businesses to economic cycles as well as the exposure to fluctuations in real estate prices because most of these loans are secured by real estate. Losses in this segment have however been historically low because most of the loans are real estate secured.

Residential mortgages – This segment is considered to have low risk factors both from the Company and peer statistics. These loans are secured by first deeds of trust. The losses experienced over the past twelve quarters are isolated to approximately twelve loans and are generally the result of short sales.

Home improvement and home equity loans – Because of their junior lien position, these loans have an inherently higher risk level. Because residential real estate has been severely distressed in the recent past, the anticipated risk for this loan segment has increased.

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Real estate construction and development loans –In a normal economy, this segment of loans is considered to have a higher risk profile due to construction and market value issues in conjunction with normal credit risks. In the current distressed residential real estate markets the risk has increased.

Agricultural loans – This segment is considered to have risks associated with weather, insects, and marketing issues. In addition, concentrations in certain crops or certain agricultural areas can increase risk.

Installment loans (Includes consumer loans, overdrafts, and overdraft protection lines) – This segment is higher risk because many of the loans are unsecured.

Commercial lease financing – This segment of the portfolio is small, but is considered to be vulnerable to economic cycles given the nature of the leasing relationship where businesses are relatively small or have minimal cash flow. This lending program was terminated in 2005.

The following summarizes the activity in the allowance for credit losses by loan category for the years ended December 31, 2014 and 2013 (in thousands).

December 31, 2014	Commercial and Industrial	Real Estate Mortgage	RE Construction Development	Agricultural	Installment & Other	Commercial Lease Financing	Unallocated	Total
Beginning balance	$2,340	$1,862	$5,533	$583	$275	$—	$395	$10,988
Provision for credit losses	(1,129)	(89)	97	(106)	(40)	(46)	468	(845)
Charge-offs	(318)	(140)	(60)	0	—	—	(16)	(534)
Recoveries	325	20	708	5	58	46	—	1,162
Net recoveries(charge-offs)	7	(120)	648	5	58	46	(16)	628
Ending balance	$1,218	$1,653	$6,278	$482	$293	$—	$847	$10,771
Period-end amount allocated to:								
Loans individually evaluated for impairment	64	648	—	—	3	—	—	715
Loans collectively evaluated for impairment	1,154	1,005	6,278	482	290	—	847	10,056
Ending balance	$1,218	$1,653	$6,278	$482	$293	$—	$847	$10,771

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December 31, 2013	Commercial and Industrial	Real Estate Mortgage	RE Construction Development	Agricultural	Installment & Other	Commercial Lease Financing	Unallocated	Total
Beginning balance	$1,614	$1,292	$2,814	$352	$288	$1	$5,423	$11,784
Provision for credit losses	1,134	1,101	1,285	222	160	(1)	(4,999)	(1,098)
Charge-offs	(542)	(540)	(95)	(136)	(244)	—	(29)	(1,586)
Recoveries	134	9	1,529	145	71	—	—	1,888
Net recoveries (charge-offs)	(408)	(531)	1,434	9	(173)	—	(29)	302
Ending balance	$2,340	$1,862	$5,533	$583	$275	$—	$395	$10,988
Period-end amount allocated to:								
Loans individually evaluated for impairment	9	753	—	—	—	—	—	762
Loans collectively evaluated for impairment	2,331	1,109	5,533	583	275	—	395	10,226
Ending balance	$2,340	$1,862	$5,533	$583	$275	$—	$395	$10,988

The following summarizes information with respect to the loan balances at December 31, 2014 and 2013.

	December 31, 2014			December 31, 2013		
(In thousands)	Loans Individually Evaluated for Impairment	Loans Collectively Evaluated for Impairment	Total Loans	Loans Individually Evaluated for Impairment	Loans Collectively Evaluated for Impairment	Total Loans
Commercial and Business Loans	$1,000	$59,422	$60,422	$677	$67,783	$68,460
Government Program Loans	421	1,526	1,947	—	2,226	2,226
Total Commercial and Industrial	1,421	60,948	62,369	677	70,009	70,686
Commercial Real Estate Loans	3,145	151,527	154,672	10,189	133,730	143,919
Residential Mortgage Loans	4,326	54,769	59,095	5,384	46,652	52,036
Home Improvement and Home Equity Loans	42	1,068	1,110	—	1,410	1,410
Total Real Estate Mortgage	7,513	207,364	214,877	15,573	181,792	197,365
	6,371	130,787	137,158	1,789	85,215	87,004

RE Construction and Development Loans						
Agricultural Loans	32	31,681	31,713	45	30,887	30,932
Installment Loans	700	11,102	11,802	48	9,282	9,330
Total Loans	$16,037	$441,882	$457,919	$18,132	$377,185	$395,317

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4. Premises and Equipment

The components of premises and equipment are as follows:

(In thousands)	December 31, 2014	December 31, 2013
Land	$968	$968
Buildings and improvements	14,731	14,613
Furniture and equipment	11,713	11,077
	27,412	26,658
Less accumulated depreciation and amortization	(15,862)	(14,536)
Total premises and equipment	$11,550	$12,122

Total depreciation expense on Company premises and equipment totaled $1,390,000 and $1,316,000 for the years ended December 31, 2014 and 2013, respectively, and is included in occupancy expense in the accompanying consolidated statements of operations.

5. Investment in Limited Partnership

The Bank owns limited interests in private limited partnerships that acquire affordable housing properties in California that generate Low Income Housing Tax Credits under Section 42 of the Internal Revenue Code of 1986, as amended. The Bank's limited partnership investment is accounted for under the equity method. The Bank's noninterest expense associated with the utilization and expiration of these tax credits for the years ended December 31, 2014 and 2013 was $39,000 and $253,000, respectively. These limited partnership investments are expected to generate tax credits of approximately $1.8 million over the life of the investment. The tax credits expire during 2015. No tax credits were available for income tax purposes for the years ended December 31, 2014 and 2013.

The Bank owns a 9.14% interest in a limited partnership which provides private capital for small to mid-sized businesses used to finance later stage growth, strategic acquisitions, ownership transitions, and recapitalizations, or mezzanine capital. The Company sold its $3,559,000 or 36% interest in a commercial real estate partnership in 2014 for a $691,000 gain on sale. At December 31, 2014, the total investment in limited partnerships was $871,000 .

6. Deposits

Deposits include the following:

(In thousands)	December 31, 2014	December 31, 2013
Noninterest-bearing deposits	$215,439	$214,317
Interest-bearing deposits:		
NOW and money market accounts	211,290	198,928
Savings accounts	60,499	45,758
Time deposits:		
Under $100,000	25,345	28,825
$100,000 and over	52,800	54,661
Total interest-bearing deposits	349,934	328,172
Total deposits	$565,373	$542,489

At December 31, 2014, the scheduled maturities of all certificates of deposit and other time deposits are as follows:

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(In thousands)	December 31, 2014
One year or less	$64,972
More than one year, but less than or equal to two years	9,900
More than two years, but less than or equal to three years	1,993
More than three years, but less than or equal to four years	1,168
More than four years, but less than or equal to five years	112
More than five years	—
	$78,145

The Company may utilize brokered deposits as an additional source of funding. At December 31, 2014 and 2013, the Company held brokered time deposits totaling $11,480,000 and $11,500,000, respectively. Of this balance at December 31, 2014, $10,320,000 is included in time deposits of $250,000 or more, and the remaining $$1,160,000 is included in time deposits of less than $250,000. Included in brokered time deposits at December 31, 2014 are balances totaling $3,815,000 maturing in three months or less, $7,211,000 maturing in 3 months to a year, and the remaining $453,000 maturing in 1 to 3 years.

Deposit balances representing overdrafts reclassified as loan balances totaled $215,000 and $157,000 as of December 31, 2014 and 2013, respectively.

Deposits of directors, officers and other related parties to the Bank totaled $8,658,000 and $6,943,000 at December 31, 2014 and 2013, respectively. The rates paid on these deposits were similar to those customarily paid to the Bank's customers in the normal course of business.

7. Short-term Borrowings/Other Borrowings

At December 31, 2014, the Company had collateralized lines of credit with the Federal Reserve Bank of San Francisco totaling $286,993,000, as well as Federal Home Loan Bank ("FHLB") lines of credit totaling $5,814,000. At December 31, 2014, the Company had an uncollateralized line of credit with Pacific Coast Bankers Bank ("PCBB") totaling $10,000,000. At December 31, 2014, and for the year then ended, the Company had no outstanding borrowing balances. These lines of credit generally have interest rates tied to the Federal Funds rate or are indexed to short-term U.S. Treasury rates or LIBOR. FHLB advances are collateralized by all of the Company's stock in the FHLB, investment securities, and certain qualifying mortgage loans. As of December 31, 2014, $6,106,000 in investment securities at FHLB were pledged as collateral for FHLB advances. Additionally, $406,358,000 in real estate-secured loans were pledged at December 31, 2014, as collateral for used and unused borrowing lines with the Federal Reserve Bank totaling $286,993,000. All lines of credit are on an "as available" basis and can be revoked by the grantor at any time.

The Company had collateralized lines of credit with the Federal Reserve Bank of San Francisco totaling $254,761,000, as well as Federal Home Loan Bank ("FHLB") lines of credit totaling $7,094,000 at December 31, 2013. At December 31, 2013, and for the year then ended, the Company had no outstanding borrowing balances.

8. Junior Subordinated Debt/Trust Preferred Securities

During July 2007, the Company formed USB Capital Trust II, a wholly-owned special purpose entity, for the purpose of issuing Trust Preferred Securities. USB Capital Trust II is a Variable Interest Entity (VIE) and a deconsolidated entity pursuant to ASC 810. On July 23, 2007, USB Capital Trust II issued $15 million in Trust Preferred securities. The securities have a thirty-year maturity and bear a floating rate of interest (repricing quarterly) of 1.29% over the three-month LIBOR rate (initial coupon rate of 6.65%). Interest will be paid quarterly. Concurrent with the issuance of the Trust Preferred securities, USB Capital Trust II used the proceeds of the Trust Preferred securities offering to purchase a like amount of junior subordinated debentures of the Company. The Company will pay interest on the junior subordinated debentures to USB Capital Trust II, which represents the sole source of dividend distributions to the holders of the Trust Preferred securities. The Company may redeem the junior subordinated debentures at anytime at par.

The Company elected the fair value measurement option for all the Company's new junior subordinated debentures issued under USB Capital Trust II.

Effective September 30, 2009 and beginning with the quarterly interest payment due October 1, 2009, the Company elected to defer interest payments on the Company's $15.0 million of junior subordinated debentures relating to its trust preferred

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securities. The terms of the debentures and trust indentures allow for the Company to defer interest payments for up to 20 consecutive quarters without default or penalty. During the period that the interest deferrals were elected, the Company continued to record interest expense associated with the debentures. As of June 30, 2014, the Company ended the extension period, paid all accrued and unpaid interest, and is currently making quarterly interest payments. At December 31, 2014 and 2013, the Company had $58,000 and $1,172,000, respectively, in accrued and unpaid interest on the junior subordinated debt.

At December 31, 2014, as with previous periods, the Company performed a fair value measurement analysis on its junior subordinated debt using a discounted cash flow valuation model approach to determine the present value of those cash flows. The cash flow model utilizes the forward 3-month LIBOR curve to estimate future quarterly interest payments due over the life of the debt instrument. These cash flows were discounted at a rate which incorporates a current market rate for similar-term debt instruments, adjusted for additional credit and liquidity risks associated with the junior subordinated debt. Although there is little market data in the current relatively illiquid credit markets, we believe the 6.87% discount rate used represents what a market participant would consider under the circumstances based on current market assumptions.

The fair value calculation performed resulted in a realized losses of $102,000 and $776,000 for the years ended December 31, 2014 and 2013, respectively. Fair value gains and losses are reflected as a component of noninterest income.

9. Taxes on Income

The tax effects of significant items comprising the Company’s net deferred tax assets (liabilities) are as follows:

	December 31,	
(In thousands)	2014	2013
Deferred tax assets:		
Credit losses not currently deductible	$4,962	$4,927
Deferred compensation	1,976	1,920
Net operating losses	1,653	9,074
Depreciation	346	231
Accrued reserves	54	63
Write-down on other real estate owned	404	(97)
Unrealized gain on AFS	133	(211)
Interest on nonaccrual loans	43	36
Capitalized OREO expenses	778	1,079
Other	2,973	2,555
Total deferred tax assets	13,322	19,577
Deferred tax liabilities:		
State Tax	(1,681)	(2,640)
FHLB dividend	(53)	(53)
Loss on limited partnership investment	(1,077)	(1,808)
Deferred gain SFAS No. 159 – fair value option	(2,425)	(2,471)
Fair value adjustments for purchase accounting	(139)	(167)
Deferred loan costs	(750)	(570)
Prepaid expenses	(344)	(238)
Total deferred tax liabilities	(6,469)	(7,947)
Net deferred tax assets	$6,853	$11,630

The Company periodically evaluates its deferred tax assets to determine whether a valuation allowance is required based upon a determination that some or all of the deferred assets may not be ultimately realized. The Company did not record a valuation allowance at December 31, 2014 or December 31, 2013.

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Income tax expense (benefit) for the years ended December 31, consist of the following:

(In thousands)			
2014	Federal	State	Total
Current	$1,129	$(1,753)	$(624)
Deferred	1,994	2,822	4,816
	$3,123	$1,069	$4,192
2013			
Current	$1,059	$819	$1,878
Deferred	(1,055)	(718)	(1,773)
	$4	$101	$105

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A reconciliation of the statutory federal income tax rate to the effective income tax rate is as follows:

	Year Ended December 31,			
	2014		2013	
Statutory federal income tax rate	34.0	%	34.0	%
State franchise tax, net of federal income tax benefit	6.8		0.9	
Low Income Housing – federal credits	0.0		0.0	
Cash surrender value of life insurance	0.0		(2.4	)
Valuation Allowance	0.0		(33.0	)
Other	(0.5	)	1.9	
	40.3	%	1.4	%

During the year ended December 31, 2013, the Company reversed the remaining valuation allowance of $2,686,000. At December 31, 2014, the Company has no remaining federal net operating loss carry-forwards, and remaining state net operating loss carry-forwards totaling $27,404,000 which expire between 2015 and 2032. The Company anticipates that it will utilize the net operating loss carry-forwards expiring in 2015.

The Company periodically reviews its tax positions under the accounting standards related to uncertainty in income taxes, which defines the criteria that an individual tax position would have to meet for some or all of the income tax benefit to be recognized in a taxable entity's financial statements. Under the guidelines, an entity should recognize the financial statement benefit of a tax position if it determines that it is more likely than not that the position will be sustained on examination. The term, "more likely than not", means a likelihood of more than 50 percent. In assessing whether the more-likely-than-not criterion is met, the entity should assume that the tax position will be reviewed by the applicable taxing authority and all available information is known to the taxing authority.

The Company and its subsidiary file income tax returns in the U.S federal jurisdiction, and several states within the U.S. There are no filings in foreign jurisdictions. During 2014, the Company began the process to amend its state tax returns for the years 2009 through 2012 to file a combined report on a unitary basis with the Company and USB Investment Trust . The amended return for 2009 was filed during 2014 and the amended returns for 2010, 2011, and 2012 will be filed during 2015 once the FTB accepts the 2009 amended return.

The Company is not currently aware of any other tax jurisdictions where the Company or any subsidiary is subject to examination by federal, state, or local taxing authorities.

10. Stock Based Compensation

Options have been granted to officers and key employees at an exercise price equal to estimated fair value at the date of grant as determined by the Board of Directors. All options granted are service awards, and as such are based solely upon fulfilling a requisite service period (the vesting period). In May 2005, the Company's shareholders approved the adoption of the United Security Bancshares 2005 Stock Option Plan (2005 Plan). At the same time, all previous plans, including the 1995 Plan, were terminated. The 2005 Plan provides for the granting of up to 647,628 shares of authorized and unissued shares of common stock at option prices per share which must not be less than 100% of the fair market value per share at the time each option is granted.

The options granted (incentive stock options for employees and non-qualified stock options for Directors) have an exercise price at the prevailing market price on the date of grant. All options granted are exercisable 20% each year commencing one year after the date of grant and expire ten years after the date of grant.

Under the 2005 Plan, 142,562 granted shares are outstanding (111,402 incentive stock options and 31,160 nonqualified stock options) as of December 31, 2014, of which 114,375 are vested.

Options outstanding, exercisable, exercised and forfeited are as follows:

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	2005 Plan	Weighted Average Exercise Price
Options outstanding December 31, 2013	200,064	$10.19
Granted during the year	5,100	5.65
Exercised during the year	23,922	3.97
Forfeited during the year	38,680	13.99
Options outstanding December 31, 2014	142,562	$10.04

Included in total outstanding options at December 31, 2014, are 114,375 exercisable shares at a weighted average price of $11.48, a weighted average remaining contract term of 1.33 years and intrinsic value of $8,000.

Included in salaries and employee benefits for the years ended December 31, 2014 and 2013, is $28,000 and $29,000 of share-based compensation, respectively. The related tax benefit on share-based compensation recorded in the provision for income taxes was not material to either year.

As of December 31, 2014 and 2013, there was $85,000 and $64,000, respectively, of total unrecognized compensation expense related to non−vested stock options. This cost is expected to be recognized over a weighted average period of approximately 3.0 years. 5,202 options were exercised during 2013, while 23,922 options were exercised during 2014.

	December 31, 2014	December 31, 2013
Weighted average grant-date fair value of stock options granted	$3.33	$2.80
Total fair value of stock options vested	$31,440	$24,310
Total intrinsic value of stock options exercised	$39,711	$9,665

The Bank determines fair value at grant date using the Black-Scholes-Merton pricing model that takes into account the stock price at the grant date, the exercise price, the expected life of the option, the volatility of the underlying stock and the expected dividend yield and the risk-free interest rate over the expected life of the option.

The weighted average assumptions used in the pricing model are noted in the table below. The expected term of options granted is derived using the simplified method, which is based upon the average period between vesting term and expiration term of the options. The risk free rate for periods within the contractual life of the option is based on the U.S. Treasury yield curve in effect at the time of the grant. Expected volatility is based on the historical volatility of the Bank's stock over a period commensurate with the expected term of the options. The Company believes that historical volatility is indicative of expectations about its future volatility over the expected term of the options.

The Bank expenses the fair value of the option on a straight-line basis over the vesting period for each separately vesting portion of the award. The Bank estimates forfeitures and only recognizes expense for those shares expected to vest. Based upon historical evidence, the Company has determined that because options are granted to a limited number of key employees rather than a broad segment of the employee base, expected forfeitures, if any, are not material. The Company granted 5,100 shares and 25,502 shares in incentive stock options during 2014 and 2013, respectively. The assumptions used for the 2014 and 2013 stock option grant are as follows:

	Year Ended December 31, 2014	Year Ended December 31, 2013
Risk Free Interest Rate	1.70%	1.20%
Expected Dividend Yield	—%	—%
Expected Life in Years	5.5 years	5.5 years
Expected Price Volatility	67.02%	78.88%

The Black-Scholes-Merton option valuation model requires the input of highly subjective assumptions, including the expected life of the stock based award and stock price volatility. The assumptions listed above represent management's best estimates,

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but these estimates involve inherent uncertainties and the application of management judgment. As a result, if other assumptions had been used, the Bank's recorded stock-based compensation expense could have been materially different from that previously reported in proforma disclosures. In addition, the Bank is required to estimate the expected forfeiture rate and only recognize expense for those shares expected to vest. If the Bank's actual forfeiture rate is materially different from the estimate, the share-based compensation expense could be materially different.

11. Employee Benefit Plans

401K Plan

The Company has a Cash or Deferred 401(k) Stock Ownership Plan (the "401(k) Plan") organized under Section 401(k) of the Code. All employees of the Company are initially eligible to participate in the 401(k) Plan upon the first day of the month after date of hire. Under the terms of the plan, the participants may elect to make contributions to the 401(k) Plan as determined by the Board of Directors. Participants are automatically vested 100% in all employee contributions. Participants may direct the investment of their contributions to the 401(k) Plan in any of several authorized investment vehicles. The Company contributes funds to the Plan up to 4% of the employees' eligible annual compensation. Company contributions are immediately 100% vested at the time of contribution. During 2014 and 2013, the Company made matching contributions of $239,000 and $256,000 to the 401(k) Plan, respectively.

Salary Continuation Plan

The Company has an unfunded, non-qualified Salary Continuation Plan for senior executive officers and certain other key officers of the Company, which provides additional compensation benefits upon retirement for a period of 15 years. Future compensation under the Plan is earned by the employees for services rendered through retirement and vests over a period of 12 to 15 years. The Company accrues for the salary continuation liability based on anticipated years of service and vesting schedules provided under the Plan. The Company's current benefit liability is determined based upon vesting and the present value of the benefits at a corresponding discount rate. The discount rate used is an equivalent rate for high-quality investment-grade bonds with lives matching those of the service periods remaining for the salary continuation contracts, which averages approximately 20 years. At December 31, 2014 and 2013, $4,135,000 and $4,031,000, respectively, had been accrued to date, based on a discounted cash flow using an average discount rate of 2.69% and 3.39%, respectively, and is included in other liabilities. In connection with the implementation of the Salary Continuation Plans, the Company purchased single premium universal life insurance policies on the life of each of the key employees covered under the Plan. The Company is the owner and beneficiary of these insurance policies. The cash surrender value of the policies was $5,826,000 and $4,421,000 at December 31, 2014 and 2013, respectively, and is included on the consolidated balance sheet in cash surrender value of life insurance. Income on these policies, net of expense, totaled approximately $1,405,000 and $124,000 for the years ended December 31, 2014 and 2013, respectively. Although the Plan is unfunded, the Company intends to utilize the proceeds of such policies to settle the Plan obligations. Under Internal Revenue Service regulations, the life insurance policies are the property of the Company and are available to satisfy the Company's general creditors.

Pursuant to the guidance contained in ASC Topic 715 "Compensation," the Company is required to recognize in accumulated other comprehensive (loss) income, the amounts that have not yet been recognized as components of net periodic benefit costs. These unrecognized costs arise from changes in estimated interest rates used in the calculation of net liabilities under the plan.

As of December 31, 2014 and 2013, the Company had approximately $502,000 and $436,000, respectively in unrecognized net periodic benefit costs arising from changes in interest rates used in calculating the current post-retirement liability required under the plan. This amount represents the difference between the plan liabilities calculated under net present value calculations, and the net plan liabilities actually recorded on the Company's books at

December 31, 2014 and 2013.

Salary continuation expense is included in salaries and benefits expense, and totaled $143,000 and $160,000 for the years ended December 31, 2014 and 2013, respectively.

Officer Supplemental Life Insurance Plan

The Company owns single premium Bank-owned life insurance policies (BOLI) on certain officers with a portion of the death benefits available to the officers' beneficiaries. The BOLI's initial net cash surrender value is equivalent to the premium paid, and it adds income through non-taxable increases in its cash surrender value, net of the cost of insurance, plus any death benefits ultimately received by the Company. The cash surrender value of these insurance policies totaled $11,891,000 and $12,782,000 at December 31, 2014 and 2013, and is included on the consolidated balance sheet in cash surrender value of life

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insurance. These policies resulted in a net expense of approximately $493,000 and income, net of expense, totaling $398,000 for the years ended December 31, 2014 and 2013, respectively.

12. Commitments and Contingent Liabilities

Lease Commitments: The Company leases land and premises for its branch banking offices and administration facilities. The initial terms of these leases expire at various dates through 2023. Under the provisions of most of these leases, the Company has the option to extend the leases beyond their original terms at rental rates adjusted for changes reported in certain economic indices or as reflected by market conditions. The total expense on land and premises leased under operating leases was $718,000 and $652,000 during 2014 and 2013, respectively. Total rent expense for the years ended December 31, 2014 and 2013 included approximately $23,000 and $18,000 in reductions, respectively, related to adjustments made pursuant to ASC Topic 840, “Leases”. The adjustments represent the difference between contractual rent amounts paid and rent amounts actually expensed under the straight-line method pursuant to ASC 840.

Future minimum rental commitments under existing non-cancelable leases as of December 31, 2014 are as follows:

(In thousands):	
2015	$562
2016	415
2017	379
2018	375
2019	192
Thereafter	193
	$2,116

Financial Instruments with Off-Balance Sheet Risk: The Company is party to financial instruments with off-balance sheet risk which arise in the normal course of business. These instruments may contain elements of credit risk, interest rate risk and liquidity risk, and include commitments to extend credit and standby letters of credit. The credit risk associated with these instruments is essentially the same as that involved in extending credit to customers and is represented by the contractual amount indicated in the table below:

	Contractual amount – December 31,	
(In thousands)	2014	2013
Commitments to extend credit	$105,434	$63,271
Standby letters of credit	3,800	2,001

Commitments to extend credit are agreements to lend to a customer, as long as there is no violation of any condition established in the contract. Substantially all of these commitments are at floating interest rates based on the Prime rate, and most have fixed expiration dates. The Company evaluates each customer's creditworthiness on a case-by-case basis, and the amount of collateral obtained, if deemed necessary, is based on management's credit evaluation. Collateral held varies but includes accounts receivable, inventory, leases, property, plant and equipment, residential real estate and income-producing properties. Many of the commitments are expected to expire without being drawn upon and, as a result, the total commitment amounts do not necessarily represent future cash requirements of the Company.

Standby letters of credit are generally unsecured and are issued by the Company to guarantee the performance of a customer to a third party. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loans to customers. The Company’s letters of credit are short-term guarantees and generally have terms from less than one month to approximately 3 years. At December 31, 2014, the maximum potential amount of future undiscounted payments the Company could be required to make under outstanding standby letters of credit totaled $3,800,000.

In the ordinary course of business, the Company becomes involved in litigation arising out of its normal business activities. Management, after consultation with legal counsel, believes that the ultimate liability, if any, resulting from the disposition of such claims would not be material to the financial position of the Company.

13. Fair Value Measurements and Disclosure

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The following summary disclosures are made in accordance with the guidance provided by ASC Topic 825 “Fair Value Measurements and Disclosures” (formerly Statement of Financial Accounting Standards No. 107, “Disclosures about Fair Value of Financial Instruments,”) which requires the disclosure of fair value information about both on- and off-balance sheet financial instruments where it is practicable to estimate that value.

Generally accepted accounting guidance clarifies the definition of fair value, describes methods used to appropriately measure fair value in accordance with generally accepted accounting principles and expands fair value disclosure requirements. This guidance applies whenever other accounting pronouncements require or permit fair value measurements.

The fair value hierarchy prioritizes the inputs to valuation techniques used to measure fair value into three broad levels (Level 1, Level 2, and Level 3). Level 1 inputs are unadjusted quoted prices in active markets (as defined) for identical assets or liabilities that the reporting entity has the ability to access at the measurement date. Level 2 inputs are inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly. Level 3 inputs are unobservable inputs for the asset or liability, and reflect the reporting entity’s own assumptions about the assumptions that market participants would use in pricing the asset or liability (including assumptions about risk).

The table below is a summary of fair value estimates for financial instruments and the level of the fair value hierarchy within which the fair value measurements are categorized at the periods indicated:
December 31, 2014

(In thousands)	Carrying Amount	Estimated Fair Value	Quoted Prices In Active Markets for Identical Assets Level 1	Significant Other Observable Inputs Level 2	Significant Unobservable Inputs Level 3
Financial Assets:					
Cash and cash equivalents	$103,577	$103,577	$103,577	$—	$—
Interest-bearing deposits	1,522	1,522	—	1,522	—
Investment securities	48,301	48,301	3,823	44,478	—
Loans	446,824	441,186	—	—	441,186
Accrued interest receivable	1,927	1,927	—	1,927	—
Financial Liabilities:					
Deposits:					
Noninterest-bearing	215,439	215,439	215,439	—	—
NOW and money market	211,290	211,290	211,290	—	—
Savings	60,499	60,499	60,499	—	—
Time Deposits	78,145	78,239	—	—	78,239
Total Deposits	565,373	565,467	487,228	—	78,239
Junior Subordinated Debt	10,115	10,115	—	—	10,115
Accrued interest payable	40	40	—	40	—

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December 31, 2013

(In thousands)	Carrying Amount	Estimated Fair Value	Quoted Prices In Active Markets for Identical Assets Level 1	Significant Other Observable Inputs Level 2	Significant Unobservable Inputs Level 3
Financial Assets:					
Cash and cash equivalents	$135,212	$135,212	$135,212	$—	$—
Interest-bearing deposits	1,515	1,515	—	1,515	—
Investment securities	43,616	43,616	10,746	32,870	—
Loans	384,025	380,615	—	—	380,615
Accrued interest receivable	1,644	1,644	—	1,644	—
Financial Liabilities:					
Deposits:					
Noninterest-bearing	214,317	214,317	214,317	—	—
NOW and money market	198,928	198,928	198,928	—	—
Savings	45,758	45,758	45,758	—	—
Time Deposits	83,486	83,362	—	—	83,362
Total Deposits	542,489	542,365	459,003	—	83,362
Junior Subordinated Debt	11,125	11,125	—	—	11,125
Accrued interest payable	44	44	—	44	—

The Company performs fair value measurements on certain assets and liabilities as the result of the application of current accounting guidelines. Some fair value measurements, such as available-for-sale securities (AFS) and junior subordinated debt are performed on a recurring basis, while others, such as impairment of loans, other real estate owned, goodwill and other intangibles, are performed on a nonrecurring basis.

The following tables summarize the Company's assets and liabilities that were measured at fair value on a recurring and non-recurring basis as of December 31, 2014 (in 000's):

Description of Assets	December 31, 2014	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
AFS Securities (2):				
U.S. Government agencies	$12,496	$—	$12,495	$—
U.S Govt collateralized mortgage obligations	31,982	—	31,983	—
Mutual Funds	3,823	3,823	—	—
Total AFS securities	48,301	3,823	44,478	—
Impaired Loans (1):				
Commercial and industrial	—	—	—	—
Real estate mortgage	42	—	—	42
RE construction & development	—	—	—	—
Agricultural	—	—	—	—
Installment/Other	—	—	—	—
Total impaired loans	42	—	—	42

Other real estate owned (1)	—	—	—	—
Total	$48,343	$3,823	$44,478	$42

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Description of Liabilities	December 31, 2014	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Junior subordinated debt (2)	$ 10,115	$—	$—	$10,115
Total	$ 10,115	$—	$—	$10,115

(1)Nonrecurring
(2)Recurring

The following tables summarize the Company's assets and liabilities that were measured at fair value on a recurring and non-recurring basis as of December 31, 2013 (in 000's):

Description of Assets	December 31, 2013	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
AFS Securities (2):				
U.S. Government agencies	$ 14,501	$—	$14,501	$—
U.S Govt collateralized mortgage obligations	25,385	7,016	18,369	—
Mutual Funds	3,730	3,730	—	—
Total AFS securities	43,616	10,746	32,870	—
Impaired Loans (1):				
Commercial and industrial	—	—	—	—
Real estate mortgage	1,388	—	—	1,388
RE construction & development	—	—	—	—
Agricultural	—	—	—	—
Installment/Other	—	—	—	—
Total impaired loans	1,388	—	—	1,388
Other real estate owned (1)	3,889	—	—	3,889
Total	$ 48,893	$10,746	$32,870	$5,277

Description of Liabilities	December 31, 2013	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Junior subordinated debt (2)	$11,125	$—	$—	$11,125
Total	$11,125	$—	$—	$11,125

(1)Nonrecurring
(2)Recurring

The following table presents quantitative information about Level 3 fair value measurements for the Company's assets measured at fair value on a non-recurring basis at December 31, 2014:

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December 31, 2014

Financial Instrument	Fair Value	Valuation Technique	Unobservable Input	Range, Weighted Average
Impaired Loans:				
Real estate mortgage	$42	Sales Comparison Approach	Adjustment for difference between comparable sales	1%-16%, 13.2%

The following methods and assumptions were used in estimating the fair values of financial instruments:

Cash and Cash Equivalents - The carrying amounts reported in the balance sheets for cash and cash equivalents approximate their estimated fair values.

Interest-bearing Deposits – Interest bearing deposits in other banks consist of fixed-rate certificates of deposits. Accordingly, fair value has been estimated based upon interest rates currently being offered on deposits with similar characteristics and maturities.

Investments – Available for sale securities are valued based upon open-market price quotes obtained from reputable third-party brokers that actively make a market in those securities. Market pricing is based upon specific CUSIP identification for each individual security. To the extent there are observable prices in the market, the mid-point of the bid/ask price is used to determine fair value of individual securities. If that data is not available for the last 30 days, a Level 2-type matrix pricing approach based on comparable securities in the market is utilized. Level-2 pricing may include using a forward spread from the last observable trade or may use a proxy bond like a TBA mortgage to come up with a price for the security being valued. Changes in fair market value are recorded through other comprehensive loss as the securities are available for sale.

Loans - Fair values of variable rate loans, which reprice frequently and with no significant change in credit risk, are based on carrying values adjusted for credit risk. Fair values for all other loans, except impaired loans, are estimated using discounted cash flows over their remaining maturities, using interest rates at which similar loans would currently be offered to borrowers with similar credit ratings and for the same remaining maturities.

Impaired Loans - Fair value measurements for impaired loans are performed pursuant to authoritative accounting guidance and are based upon either collateral values supported by appraisals, observed market prices, or discounted cash flows. Changes are not recorded directly as an adjustment to current earnings or comprehensive income, but rather as an adjustment component in determining the overall adequacy of the loan loss reserve. Such adjustments to the estimated fair value of impaired loans may result in increases or decreases to the provision for credit losses recorded in current earnings. Collateral dependent loans are measured for impairment using the fair value of the collateral.

Other Real Estate Owned - Nonrecurring adjustments to certain commercial and residential real estate properties classified as other real estate owned (OREO) are measured at the lower of carrying amount or fair value, less costs to sell. Fair values are generally based on third party appraisals of the property, resulting in a Level 3 classification. In cases where the carrying amount exceeds the fair value, less costs to sell, an impairment loss is recognized.

Deposits – In accordance with authoritative accounting guidance, fair values for transaction and savings accounts are equal to the respective amounts payable on demand at December 31, 2014 and 2013 (i.e., carrying amounts). The Company believes that the fair value of these deposits is clearly greater than that prescribed under authoritative accounting guidance. Fair values of fixed-maturity certificates of deposit were estimated using the rates currently offered for deposits with similar remaining maturities.

Junior Subordinated Debt – The fair value of the junior subordinated debt was determined based upon a discounted cash flows model utilizing observable market rates and credit characteristics for similar debt instruments. In its analysis, the Company used characteristics that market participants generally use, and considered factors specific to (a) the liability, (b) the principal (or most advantageous) market for the liability, and (c) market participants with whom the reporting entity would transact in that market. For the year ended December 31, 2014, cash flows were discounted at a rate which incorporates a current market rate for similar-term debt instruments, adjusted for credit and liquidity risks associated with similar junior subordinated debt and circumstances unique to the Company. The Company believes that the subjective nature of theses inputs, due primarily to the current economic environment, require the junior subordinated debt to be classified as a Level 3 fair value.

Accrued Interest Receivable and Payable - The carrying value of these instruments is a reasonable estimate of fair value.

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Off-balance sheet Instruments - Off-balance sheet instruments consist of commitments to extend credit, standby letters of credit and derivative contracts. The contract amounts of commitments to extend credit and standby letters of credit are disclosed in Note 12. Fair values of commitments to extend credit are estimated using the interest rate currently charged to enter into similar agreements, taking into account the remaining terms of the agreements and the present counterparties' credit standing. There was no material difference between the contractual amount and the estimated value of commitments to extend credit at December 31, 2014 and 2013.

Fair values of standby letters of credit are based on fees currently charged for similar agreements. The fair value of commitments generally approximates the fees received from the customer for issuing such commitments. These fees are not material to the Company's consolidated balance sheet and results of operations.

The following tables provide a reconciliation of liabilities at fair value using significant unobservable inputs (Level 3) on a recurring basis during the period (in 000's):

Reconciliation of Liabilities:	December 31, 2014 Junior Subordinated Debt	December 31, 2013 Junior Subordinated Debt
Beginning balance	$11,125	$10,068
Total gains (losses) included in earnings (or changes in net assets)	(102)	(776)
Transfers in and/or out of Level 3 resulting from changes in unobservable input	(908)	281
Ending balance	$10,115	$9,573
The amount of total gains (losses) for the period included in earnings (or changes in net assets) attributable to the change in unrealized gains or losses and accrued interest relating to liabilities still held at the reporting date	$(102)	$(776)

The following table provides a description of the valuation technique, unobservable input, and qualitative information about the unobservable inputs for the Company's liabilities classified as Level 3 and measured at fair value on a recurring basis at December 31, 2014 and 2013:

December 31, 2014				December 31, 2013			
Financial Instrument	Valuation Technique	Unobservable Input	Weighted Average	Financial Instrument	Valuation Technique	Unobservable Input	Weighted Average
Subordinated Debt	Discounted cash flow	Discount Rate	6.87%	Subordinated Debt	Discounted cash flow	Discount Rate	8.19%

Management believes that the credit risk adjusted spread utilized in the fair value measurement of the junior subordinated debentures carried at fair value is indicative of the nonperformance risk premium a willing market participant would require under current market conditions, that is, the inactive market. Management attributes the change in fair value of the junior subordinated debentures during the period to market changes in the nonperformance expectations and pricing of this type of debt, and not as a result of changes to our entity-specific credit risk. The narrowing of the credit risk adjusted spread above the Company's contractual spreads has primarily contributed to the negative fair value adjustments. Generally, an increase in the credit risk adjusted spread and/or a decrease in the three month LIBOR swap curve will result in positive fair value adjustments (and decrease the fair value measurement). Conversely, a decrease in the credit risk adjusted spread and/or an increase in the three month LIBOR swap curve will result in negative fair value adjustments (and increase the fair value measurement).

14. Regulatory Matters

Regulatory Agreement with the Federal Reserve Bank of San Francisco

On March 23, 2010, United Security Bancshares (the "Company") and its wholly owned subsidiary, United Security Bank (the "Bank"), entered into a formal written agreement (the “Agreement”) with the Federal Reserve Bank of San Francisco (the “Federal Reserve”) as a result of a regulatory examination that was conducted by the Federal Reserve and the California Department of Financial Institutions (the “DFI”) in June 2009. That examination found significant increases in nonperforming assets, both classified loans and OREO, during 2008 and 2009, and heightened concerns about the Bank’s use of brokered and

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other wholesale funding sources to fund loan growth, which created increased risk to equity capital and potential volatility in earnings.

Under the terms of the Agreement, the Company and the Bank agreed, among other things: to maintain a sound process for determining, documenting, and recording an adequate allowance for loan and lease losses; to improve the management of the Bank's liquidity position and funds management policies; to maintain sufficient capital at the Company and Bank level; and to improve the Bank’s earnings and overall condition. The Company and Bank also agreed not to increase or guarantee any debt, purchase or redeem any shares of stock, declare or pay any cash dividends, or pay interest on the Company's junior subordinated debt or trust preferred securities, without prior written approval from the Federal Reserve. The Company generates no revenue of its own and, as such, relies on dividends from the Bank to pay its operating expenses and interest payments on the Company’s junior subordinated debt.

Effective November 19, 2014, the Federal Reserve terminated the Agreement with the Bank and the Company and replaced it with an informal supervisory agreement that requires, among other things, obtaining written approval from the Federal Reserve prior to the payment of dividends from the Bank to the Company or the payment of dividends by the Company or interest on the Company’s junior subordinated debt. The inability of the Bank to pay cash dividends to the Company may hinder the Company’s ability to meet its ongoing operating obligations.

Regulatory Order from the California Department of Business Oversight

On May 20, 2010, the DFI (now known as the Department of Business Oversight (the “DBO”)) issued a formal written order (the “Order”) pursuant to a consent agreement with the Bank as a result of the same June 2009 joint regulatory examination. The terms of the Order were essentially similar to the Federal Reserve’s Agreement, except for a few additional requirements.

On September 24, 2013, the Bank entered into an informal Memorandum of Understanding (the “MOU”) with the DBO and on October 15, 2013, the Order was terminated. The Order and the MOU require the Bank to maintain a ratio of tangible shareholder’s equity to total tangible assets equal to or greater than 9.0% and also requires the DBO’s approval for the Bank to pay a dividend to the Company.

Accordingly, reflecting the Company’s and the Bank’s improved financial condition and performance, as of November 19, 2014, the Bank and the Company have been relieved of all formal regulatory agreements. Some of the governance and procedures established by the Agreement and the Order remain in place, including submission of certain plans and reports to the Federal Reserve and DBO, the Bank’s obligation to maintain a 9.0% tangible shareholder’s equity ratio, and the requirement to seek approvals from the Federal Reserve and the DBO for either the Bank or the Company to pay dividends and for the Company to pay interest on its outstanding junior subordinated debt. While no assurances can be given as to future regulatory approvals, over the last three quarters the DBO and the Federal Reserve have been approving the Bank's payment of dividends to the Company to cover the Company's operating expenses and its interest payments and the Company's payment of quarterly interest on the junior subordinated debt.

Capital Adequacy - The Company (on a consolidated basis) and the Bank are subject to various regulatory capital requirements adopted by the Board of Governors of the Federal Reserve System (the “Board of Governors”). Failure to meet minimum capital requirements can initiate certain mandates and possible additional discretionary actions by regulators that, if undertaken, could have a direct material effect on the Company’s consolidated financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the consolidated Company and the Bank must meet specific capital guidelines that involve quantitative measures of their assets, liabilities, and certain off-balance sheet items as calculated under regulatory accounting practices. The capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings, and other factors. Prompt corrective action provisions are not applicable to bank holding companies.

Quantitative measures established by the capital adequacy guidelines require insured institutions to maintain a minimum leverage ratio of Tier 1 capital (the sum of common stockholders' equity, noncumulative perpetual preferred stock and minority interests in consolidated subsidiaries, minus intangible assets, identified losses and investments in certain subsidiaries, plus unrealized losses or minus unrealized gains on available for sale securities) to total assets. Institutions which have received the highest composite regulatory rating and which are not experiencing or anticipating significant growth are required to maintain a minimum leverage capital ratio of 3% of Tier 1 capital to total assets. All other institutions are required to maintain a minimum leverage capital ratio of at least 100 to 200 basis points above the 3% minimum requirement.

In addition to the general capital adequacy guidelines, pursuant to the DBO’s MOU the Bank is required to maintain a ratio of tangible shareholder’s equity to total tangible assets equal to or greater than 9.0%. For purposes of the MOU, “tangible

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shareholders' equity" is defined as shareholders' equity minus intangible assets. The Bank's ratio of tangible shareholders' equity to total tangible assets was 13.4% and 13.2% at December 31, 2014 and 2013, respectively.

The Company has adopted a capital plan that includes guidelines and trigger points to ensure sufficient capital is maintained at the Bank and the Company, and that capital ratios are maintained at a level deemed appropriate under regulatory guidelines given the level of classified assets, concentrations of credit, ALLL, current and projected growth, and projected retained earnings. The capital plan also contains contingency strategies to obtain additional capital as required to fulfill future capital requirements for both the Bank, as a separate legal entity, and the Company on a consolidated basis.

The following table shows the Company's and the Bank's regulatory capital and regulatory capital ratios at December 31, 2014 and 2013, as compared to the applicable capital adequacy guidelines:

	Actual			For Capital Adequacy Purposes			To Be Well Capitalized Under Prompt Corrective Action Provisions		
(In thousands)	Amount	Ratio		Amount	Ratio		Amount	Ratio	
As of December 31, 2014 (Company):									
Total Capital (to Risk Weighted Assets)	$91,935	17.29	%	$42,536	8.00	%	N/A	N/A	
Tier 1 Capital (to Risk Weighted Assets)	85,234	16.03	%	21,268	4.00	%	N/A	N/A	
Tier 1 Capital (to Average Assets)	85,234	12.49	%	27,295	4.00	%	N/A	N/A	
As of December 31, 2014 (Bank):									
Total Capital (to Risk Weighted Assets)	$89,889	16.91	%	$42,536	8.00	%	$53,170	10.00	%
Tier 1 Capital (to Risk Weighted Assets)	83,188	15.65	%	21,268	4.00	%	31,902	6.00	%
Tier 1 Capital (to Average Assets)	83,188	12.25	%	27,164	4.00	%	33,955	5.00	%
As of December 31, 2013 - (Company):									
Total Capital (to Risk Weighted Assets)	$77,530	15.49	%	$36,061	8.00	%	N/A	N/A	
Tier 1 Capital (to Risk Weighted Assets)	71,827	14.26	%	18,031	4.00	%	N/A	N/A	
Tier 1 Capital (to Average Assets)	71,827	10.66	%	25,672	4.00	%	N/A	N/A	
As of December 31, 2013 – (Bank):									
Total Capital (to Risk Weighted Assets)	$78,499	15.77	%	$36,061	8.00	%	$45,077	10.00	%
Tier 1 Capital (to Risk Weighted Assets)	72,796	14.54	%	18,031	4.00	%	27,046	6.00	%
Tier 1 Capital (to Average Assets)	72,796	10.95	%	25,484	4.00	%	31,855	5.00	%

The Board of Governors has also adopted a statement of policy, supplementing its leverage capital ratio requirements, which provides definitions of qualifying total capital (consisting of Tier 1 capital and Tier 2 supplementary capital, including the allowance for loan losses up to a maximum of 1.25% of risk-weighted assets) and sets forth minimum risk-based capital ratios of capital to risk-weighted assets. Insured institutions are required to maintain a ratio of qualifying total capital to risk weighted assets of 8%, at least one-half of which must be in the form of Tier 1 capital.

Under regulatory guidelines, the $15 million in Trust Preferred Securities issued by USB Capital Trust II in July of 2007 qualifies as Tier 1 capital up to 25% of Tier 1 capital. Any additional portion of Trust Preferred Securities qualifies as Tier 2 capital. As of December 31, 2014, the Company and the Bank meets all capital adequacy requirements to which they are subject.

The Federal Reserve and the Federal Deposit Insurance Corporation approved final capital rules in July 2013, that substantially amend the existing capital rules for banks. These new rules reflect, in part, certain standards initially adopted by the Basel Committee on Banking Supervision in December 2010 (which standards are commonly referred to as “Basel III”) as well as requirements contemplated by the Dodd-Frank Act.

Under the new capital rules, the Bank will be required to meet certain minimum capital requirements that differ from current capital requirements. The prompt corrective action rules are modified to include the common equity Tier 1 capital ratio and to increase the Tier 1 capital ratio requirements for the various thresholds. For example, the requirements for the Bank to be

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considered well-capitalized under the rules will be a 5.0% leverage ratio, a 6.5% common equity Tier 1capital ratio, an 8.0% Tier 1 capital ratio, and a 10.0% total capital ratio. To be adequately capitalized, those ratios are 4.0%, 4.5%, 6.0%, and 8.0%, respectively. The Bank is required to comply with the new capital rules on January 1, 2015, with a measurement date of March 31, 2015.

Dividends – Cash dividends, if any, paid to shareholders are paid by the Company, subject to restrictions set forth in the California Corporations Code and the terms of the Federal Reserve informal supervisory agreement. All dividends paid by the Company during 2014 and 2013 were in the form of stock dividends rather than cash dividends.

The primary source of funds with which cash dividends are paid to shareholders comes from cash dividends received by the Company from the Bank. The Bank's ability to pay dividends is subject to the restrictions set forth in the California Financial Code and the informal agreements the Bank has entered into with the Federal Reserve and the DBO. Under the Financial Code, the Bank may not pay cash dividends in an amount which exceeds the lesser of the retained earnings of the Bank or the Bank's net income for the last three fiscal years (less the amount of distributions to shareholders during that period of time). If the above test is not met, cash dividends may only be paid with the prior approval of the DBO, in an amount not exceeding the greater of: (i) the Bank's retained earnings; (ii) its net income for the last fiscal year; or (iii) its net income for the current fiscal year. During the year ended December 31, 2014, the Bank's cash dividends of $1,519,000 paid to the Company were approved by the Federal Reserve and the DBO and funded the Company's operating costs and payments of interest on its junior subordinated debentures.

Cash Restrictions - The Bank is required to maintain average reserve balances with the Federal Reserve. In prior years, the Bank implemented a deposit reclassification program, which allows the Bank to reclassify a portion of its transaction accounts to non-transaction accounts for reserve purposes. The deposit reclassification program was provided by a third-party vendor, and has been approved by the Federal Reserve Bank.

15. Supplemental Cash Flow Disclosures

	Year Ended December 31,		
(In thousands)	2014	2013	
Cash paid (received) during the period for:			
Interest	$2,462	$1,356	
Income Taxes	—	(3,679	)
Noncash investing activities:			
Loans transferred to foreclosed property	1,308	437	
Financed OREO	—	2,328	

16. Common Stock Dividend

The Company declared one-percent (1)% common stock dividends during each of the four quarters ended December 31, 2014, September 30, 2014, June 30, 2014, and March 31, 2014. All 1% stock dividends were considered "small stock dividends" resulting in a transfer between retained earnings and common stock an amount equal to the number of shares issued in the stock dividend multiplied by the stock's closing price at the date of declaration. Other than for earnings-per-share calculations, shares issued for the stock dividend have been treated prospectively for financial reporting purposes. For purposes of earnings per share calculations, the Company's weighted average shares outstanding and potentially dilutive shares used in the computation of earnings per share have been restated after giving retroactive effect to a 1% stock dividend to shareholders for all periods presented.

The Company declared one-percent (1)% common stock dividends during each of the four quarters ended December 31, 2013, September 30, 2013, June 30, 2012, and March 31, 2013. All 1% stock dividends were considered "small stock dividends" resulting in a transfer between retained earnings and common stock an amount equal to the number of shares issued in the stock dividend multiplied by the stock's closing price at the date of declaration. Other than for earnings-per-share calculations, shares issued for the stock dividend have been treated prospectively for financial reporting purposes. For purposes of earnings per share calculations, the Company's weighted average shares outstanding and potentially dilutive shares used in the computation of earnings per share have been restated after giving retroactive effect to a 1% stock dividend to shareholders for all periods presented.

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17. Net Income Per Share

The following table provides a reconciliation of the numerator and the denominator of the basic EPS computation with the numerator and the denominator of the diluted EPS computation. (Weighted average shares have been adjusted to give retroactive recognition for the 1% stock dividend for each of the quarters since the third quarter ended September 30, 2008):

	Year Ended December 31,	
(In thousands, except earnings per share data)	2014	2013
Net income available to common shareholders	$6,216	$7,269
Weighted average shares outstanding	15,410,733	15,398,911
Add: dilutive effect of stock options	4,931	605
Weighted average shares outstanding adjusted for potential dilution	15,415,664	15,399,516
Basic earnings per share	$0.40	$0.49
Diluted earnings per share	$0.40	$0.49
Anti-dilutive shares excluded from earnings per share calculation	138,000	195,000

18. Common Stock Repurchase Plan

On May 16, 2007, the Company’s Board of Directors approved a plan to repurchase, as conditions warrant, up to 781,384 shares of the Company's common stock on the open market or in privately negotiated transactions. The repurchase plan represents approximately 5.00% of the Company's currently outstanding common stock. The duration of the program is open-ended and the timing of purchases will depend on market conditions. As of December 31, 2014, there were 676,503 shares available for repurchase.

As a condition of the MOU entered into with the Federal Reserve Bank of San Francisco (FRB) on November 19, 2014, and the MOU entered into with the California Department of Business Oversight (DBO) on September 24, 2013, the Company may not repurchase any of its common stock without prior approval of the FRB and the DBO. The Company did not repurchase any common shares during the years ended December 31, 2014 and 2013.

19. Goodwill and Intangible Assets

At December 31, 2014, the Company had $4,488,000 of goodwill and no core deposit intangibles. The following table summarizes the carrying value of those assets at December 31, 2014 and 2013.

(In thousands)	December 31, 2014	December 31, 2013
Goodwill	$4,488	$4,488
Core deposit intangible assets	—	62
Total goodwill and intangible assets	$4,488	$4,550

Core deposit intangibles and other identified intangible assets are amortized over their useful lives, while goodwill is not amortized. The Company conducts periodic impairment analysis on goodwill and intangible assets and goodwill at least annually or more often as conditions require. The following table summarizes the amortization expense and impairment losses recorded on the Company’s intangible assets and goodwill for the years ended December 31, 2014 and 2013.

(In thousands)	December 31, 2014	December 31, 2013
Amortization expense - core deposit intangibles	$62	$187
Amortization expense - other intangibles	—	—
Total amortization expense	$62	$187
Impairment losses - core deposit intangibles	$—	$—
Impairment losses - goodwill	—	—

Total impairment losses	$—	$—

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Goodwill: The largest component of goodwill is related to the Legacy merger (Campbell reporting unit) completed during February 2007 and totaled approximately $2.9 million at December 31, 2014. The Company completed a "Step 0" analysis for the Campbell reporting unit as of March 31, 2014, and a "Step 1" at March 31, 2013, with no goodwill impairment.

The first step in impairment testing is to identify potential impairment, which involves determining and comparing the fair value of the operating unit with its carrying value. If the fair value of the reporting unit exceeds its carrying value, goodwill is not impaired. If the carrying value exceeds fair value, there is an indication of possible impairment and the second step is performed to determine the amount of the impairment, if any. The fair value determined in the step one testing is determined based on a discounted cash flow methodology using estimated market discount rates and projections of future cash flows for the Campbell reporting unit. In addition to projected cash flows, the Company also utilizes other market metrics including industry multiples of earnings and price-to-book ratios to estimate what a market participant would pay for the operating unit in the current business environment. Determining the fair value involves a significant amount of judgment, including estimates of changes in revenue growth, changes is discount rates, competitive forces within the industry, and other specific industry and market valuation conditions. If at the conclusion of the step 1 analysis, the Company concludes that the potential for goodwill impairment exists, step-two testing will be required to determine goodwill impairment and the amount of goodwill that might be impaired, if any. The second step in impairment analysis compares the fair value of the Campbell reporting unit to the aggregate fair values of its individual assets, liabilities and identified intangibles. Based on the results of the first step of the impairment analysis at December 31, 2014, the Company concluded that that the fair value of the reporting unit exceeds it carrying value; therefore, goodwill was not impaired.

Core Deposit Intangibles: The core deposit intangible asset, which totaled $3.0 million at the time of merger, is being amortized over an estimated life of approximately seven years. The Company recognized no amortization expense related to the Legacy operating unit during the year ended December 31, 2014. At December 31, 2014, there was no remaining carrying value of the core deposit intangible related to the Legacy Bank merger. At December 31, 2014 and 2013, there was $0 and $62,000, respectively, in remaining carrying value of core deposit intangible related to the Taft branch acquisitions completed in April, 2004.

20. Parent Company Only Financial Statements

The following are the condensed financial statements of United Security Bancshares and should be read in conjunction with the consolidated financial statements:

United Security Bancshares – (parent only)
Balance Sheets - December 31, 2014 and 2013

(In thousands)	2014	2013
Assets		
Cash and equivalents	$224	$66
Investment in bank subsidiary	93,170	87,775
Other assets	1,975	2,298
Total assets	95,369	90,139
Liabilities & Shareholders' Equity		
Liabilities:		
Junior subordinated debt securities (at fair value)	10,114	11,125
Deferred taxes	2,429	2,471
Total liabilities	12,543	13,596
Shareholders' Equity:		

Common stock, no par value 20,000,000 shares authorized, 15,425,086 and 14,799,888 issued and outstanding, in 2014 and 2013	49,271	45,778
Retained earnings	33,730	30,884
Accumulated other comprehensive (loss) income	(175)	(119)
Total shareholders' equity	82,826	76,543
Total liabilities and shareholders' equity	$95,369	$90,139

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United Security Bancshares – (parent only) Income Statements	Year ended December 31,	
(In thousands)	2014	2013
Income		
Loss on fair value option of financial assets	$(102)	$(776)
Dividends from subsidiary	1,519	—
Total (loss) income	1,417	(776)
Expense		
Interest expense	241	281
Other expense	101	159
Total expense	342	440
(Loss) Income before taxes and equity in undistributed income of subsidiary	1,075	(1,216)
Income tax benefit	(182)	(500)
Undistributed income of subsidiary	4,959	7,985
Net Income	$6,216	$7,269

United Security Bancshares – (parent only) Statement of Cash Flows	Year ended December 31,	
(In thousands)	2014	2013
Cash Flows From Operating Activities		
Net income	$6,216	$7,269
Adjustments to reconcile net income to cash provided by operating activities:		
Equity in undistributed income of subsidiary	(4,959)	(7,985)
Provision for deferred income taxes	(42)	1,232
Loss on fair value option of financial liability	102	776
Increase in income tax receivable	(140)	(1,732)
Net change in other assets/liabilities	(1,114)	198
Net cash provided by (used in) operating activities	63	(242)
Cash Flows From Financing Activities		
Proceeds from exercise of stock options	95	12
Net cash provided by financing activities	95	12
Net increase (decrease) in cash and cash equivalents	158	(230)
Cash and cash equivalents at beginning of year	66	296
Cash and cash equivalents at end of year	$224	$66
Supplemental cash flow disclosures		
Non-cash financing activities:		
Dividends declared not paid	$—	$—

21. Subsequent Events

Subsequent events are events or transactions that occur after the balance sheet date but before financial statements are issued. Recognized subsequent events are events or transactions that provide additional evidence about conditions that existed at the date of the balance sheet, including the estimates inherent in the process of preparing financial statements. Nonrecognized subsequent events are events that provide evidence about conditions that did not exist at the date of the balance sheet but arose after that date. Management has reviewed events occurring through the date the financial statements were issued and no subsequent events occurred requiring accrual or disclosure.

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Item 9 - Changes in and Disagreements with Accountants on Accounting and Financial Disclosure
None.

Item 9A. Controls and Procedures

CONCLUSION REGARDING THE EFFECTIVENESS OF DISCLOSURE CONTROLS AND PROCEDURES

As of the end of the period covered by this report, the Company carried out an evaluation, under the supervision and with the participation of the Company's management, including the Chief Executive Officer and the Chief Financial Officer, of the effectiveness of the design and operation of the Company's disclosure controls and procedures, as defined in the Securities and Exchange Act Rule 13(a)-15(e). Based on that evaluation and the remediation of the material weaknesses in the Company's internal control over financial reporting above under the caption "Management's Report on Internal Control Over Financial Reporting" in Item 8 of this report ," the Chief Executive Officer and Chief Financial Officer have concluded that the Company's disclosure controls and procedures were effective at December 31, 2014 to ensure that information required to be disclosed in its reports that the Company files or submits to the Securities and Exchange Commission under the Exchange Act is recorded, processed, summarized and reported on a timely basis. The Company's Chief Executive Officer and Chief Financial Officer have certified that, based on their knowledge, the Company's Consolidated Financial Statements included in this report fairly present in all material respects the Company's financial condition, results of operations and cash flows for the periods presented in this report.

Pursuant to Section 404 of the Sarbanes-Oxley Act of 2002, the Company has included a report of management's assessment of the design and operating effectiveness of its internal controls as part of this report.

CHANGES IN INTERNAL CONTROL OVER FINANCIAL REPORTING

There have not been any changes in the Company's internal control over financial reporting that occurred during the year ended December 31, 2014, that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

The Company does not expect that its disclosure controls and procedures and internal control over financial reporting will prevent all error and fraud. A control procedure, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control procedure are met. Because of the inherent limitations in all control procedures, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within the Company have been detected. These inherent limitations include the realities that judgments in decision-making can be faulty, and that breakdowns in controls or procedures can occur because of simple error or mistake. Additionally, controls can be circumvented by the individual acts of some persons, by collusion of two or more people, or by management override of the control. The design of any control procedure is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions; over time, controls become inadequate because of changes in conditions, or the degree of compliance with the policies or procedures may deteriorate. Because of the inherent limitations in a cost-effective control procedure, misstatements due to error or fraud may occur and not be detected.

Item 9B. Other Information

None

PART III

Item 10 – Directors, Executive Officers, and Corporate Governance

Pursuant to Instruction G, the information required by this item is hereby incorporated herein by reference from the captions entitled "Election of Directors and Executive Officers" and “Corporate Governance Principles and Board Matters” set forth in the Company's definitive Proxy Statement for its 2015 Annual Meeting of Shareholders ("Proxy Statement").

Item 11 - Executive Compensation

Pursuant to Instruction G, the information required by this item is hereby incorporated herein by reference from the captions entitled "Executive Compensation" and “Director Compensation” set forth in the Company's definitive Proxy Statement for its 2015 Annual Meeting of Shareholders ("Proxy Statement").

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Item 12 - Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters

Pursuant to Instruction G, the information required by this item is hereby incorporated herein by reference from the caption entitled "Shareholdings of Certain Beneficial Owners and Management" set forth in the Company's definitive Proxy Statement for its 2015 Annual Meeting of Shareholders ("Proxy Statement").

Item 13 - Certain Relationships and Related Transactions, and Director Independence

Pursuant to Instruction G, the information required by this item is hereby incorporated herein by reference from the captions entitled "Certain Transactions" and “Corporate Governance Principles” set forth in the Company's definitive Proxy Statement for its 2015 Annual Meeting of Shareholders ("Proxy Statement").

Item 14 - Principal Accounting Fees and Services

Pursuant to Instruction G, the information required by this item is hereby incorporated herein by reference from the caption entitled "Independent Accountant Fees and Services" set forth in the Company's definitive Proxy Statement for its 2015 Annual Meeting of Shareholders ("Proxy Statement").

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PART IV

Item 15 – Exhibits and Financial Statement Schedules

(a)(1) Financial Statements

The Consolidated Financial Statements and related documents set forth in "Item 8. Financial Statements and Supplementary Data" of this report are filed as part of this report.

(a)(2) Financial Statement Schedules

All financial statement schedules are omitted because they are not applicable or not required or because the information is included in the financial statements or notes thereto or is not material.

(a)(3) Exhibits

3.1	Articles of Incorporation of Registrant (1)
3.2	Bylaws of Registrant (1)
4.1	Specimen common stock certificate of United Security Bancshares (1)
10.1	Amended and Restated Executive Salary Continuation Agreement for Dennis Woods (4)
10.2	Amended and Restated Employment Agreement for Dennis R. Woods (4)
10.3	Amended and Restated Executive Salary Continuation Agreement for Kenneth Donahue (4)
10.4	Amended and Restated Change in Control Agreement for Kenneth Donahue (4)
10.5	Amended and Restated Executive Salary Continuation Agreement for David Eytcheson (4)
10.6	Amended and Restated Change in Control Agreement for David Eytcheson (4)
10.7	Amended and Restated Executive Salary Continuation Agreement for Rhodlee Braa (4)
10.8	Amended and Restated Change in Control Agreement for Rhodlee Braa (4)
10.9	Amended and Restated Executive Salary Continuation Agreement for William F. Scarborough (4)
10.10	Amended and Restated Change in Control Agreement for William F. Scarborough (4)
10.11	USB 2005 Stock Option Plan. Filed as Exhibit B to the Company's 2005 Schedule 14A Definitive Proxy filed April 18, 2005 and incorporated herein by reference.
10.12	Stock Option Agreement for William F. Scarborough dated August 1, 2005 (2)
10.13	Stock Option Agreement for Dennis R. Woods dated February 6, 2006 (3)
10.14	Written Agreement between United Security Bancshares, United Security Bank, and the Federal Reserve Bank of San Francisco dated March 23, 2010 (5)
10.15	Stock Option Agreement for Richard B. Shupe dated February 7, 2010 (6)
11.1	Computation of earnings per share.

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See Note 19 to Consolidated Financial Statements and related documents set forth in "Item 8. Financial Statements and Supplementary Data" of this report are filed as part of this report.

21	Subsidiaries of the Company
23.1	Consent of Moss Adams LLP, Independent Registered Public Accounting Firm
31.1	Certification of the Chief Executive Officer of United Security Bancshares pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification of the Chief Financial Officer of United Security Bancshares pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Certification of the Chief Executive Officer of United Security Bancshares pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
32.2	Certification of the Chief Financial Officer of United Security Bancshares pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

(1) Previously filed on April 4, 2001 as an exhibit to the Company's filing on Form S-4 (file number 333-58256).
(2) Previously filed on March 15, 2006 as an exhibit to the Company's filing on Form 10-K for the year ended December 31, 2006 (file number 000-32897).
(3) Previously filed on November 7, 2006 as an exhibit to the Company's filing on Form 10-Q/A for the period ended March 31, 2006 (file number 000-32897).
(4) Previously filed on March 17, 2007 as an exhibit to the Company's filing on Form 10-K for the year ended December 31, 2007 (file number 000-32897).
(5) Previously filed on March 25, 2010 as an exhibit to the Company's filing on Form 8-K (file number 000-32897).
(6) Previously filed on April 4, 2011 as an exhibit to the Company's filing on Form 10-K for the year ended December 31, 2010 (file number 000-32897)..

(b) Exhibits filed:

See Exhibit Index under Item 15(a)(3) above for the list of exhibits required to be filed by Item 601 of regulation S-K with this report.

(c) Financial statement schedules filed:

See Item 15(a)(2) above.

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Signatures

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this report on Form 10-K for the year ended December 31, 2014 to be signed on its behalf by the undersigned thereunto duly authorized, in Fresno, California, on the 17th day of March 2015.

United Security Bancshares

March 17, 2015	/S/ Dennis R. Woods Dennis R. Woods President and Chief Executive Officer
March 17, 2015	/S/ Kenneth L. Donahue Kenneth L. Donahue Executive Vice President and Acting Chief Financial Officer

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Signatures

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities on the date indicated:

Date:	March 17, 2015	/s/ Robert G. Bitter Director
Date:	March 17, 2015	/s/ Stanley J. Cavalla Director
Date:	March 17, 2015	/s/ Tom Ellithorpe Director
Date:	March 17, 2015	/s/ Kenneth D. Newby Director
Date:	March 17, 2015	/s/ Ronnie D. Miller Director
Date:	March 17, 2015	/s/ Robert M. Mochizuki Director
Date:	March 17, 2015	/s/ Walter Reinhard Director
Date:	March 17, 2015	/s/ John Terzian Director
Date:	March 17, 2015	/s/ Mike Woolf Director