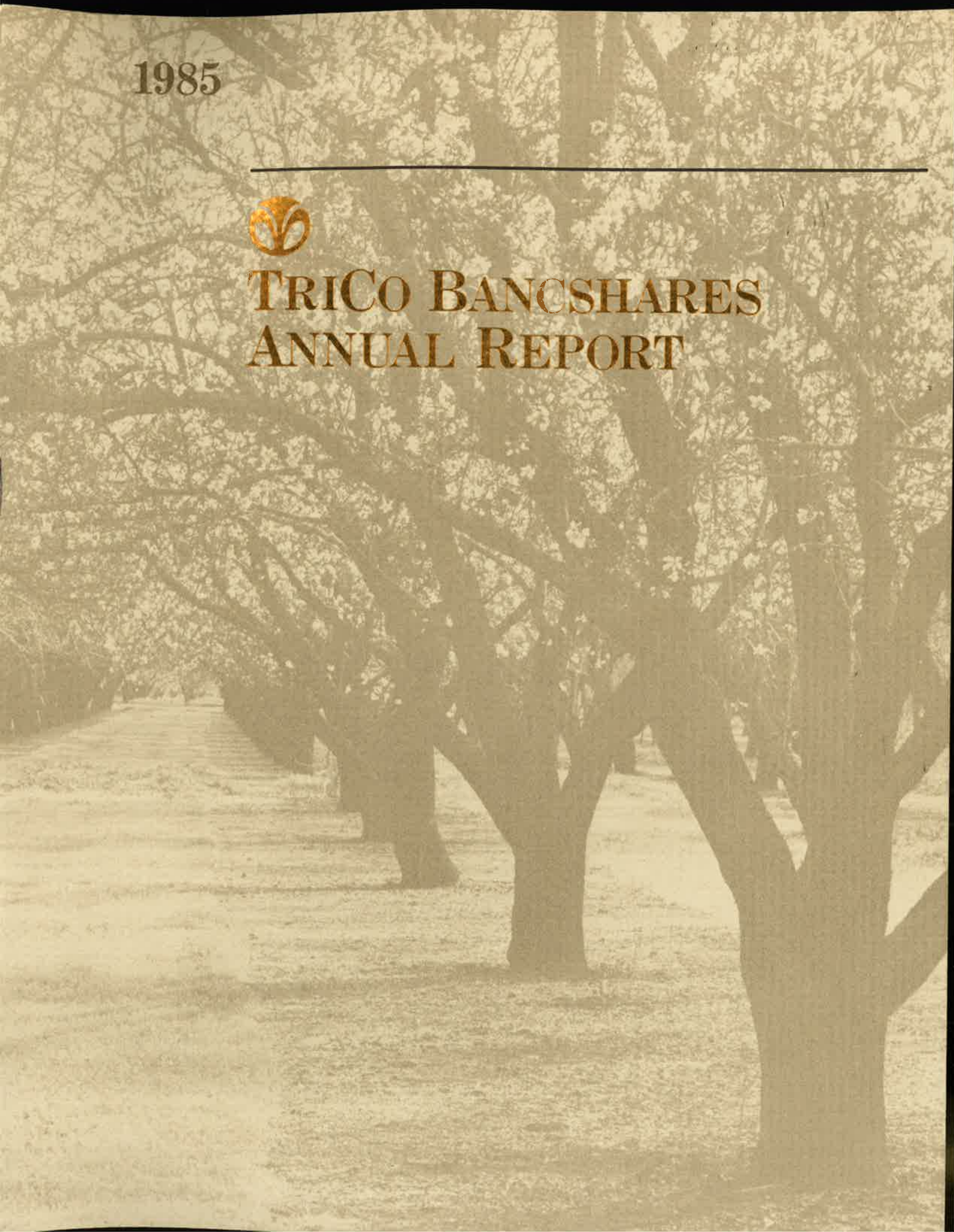
1985

TriCo Bancshares Annual Report



TRICO BANCSHARES (the "Company") is a bank holding company incorporated at the direction of the Board of Directors of Tri Counties Bank (the "Bank") on October 13, 1981. Pursuant to a corporate reorganization on September 7, 1982, the shareholders of the Bank became shareholders of the Company, and the Bank became the wholly-owned subsidiary of the Company. The Bank currently is the only subsidiary of the Company and the Company has not yet commenced any business operations independent of the Bank.

The Bank engages in the general commercial banking business in the California counties of Butte, Glenn and Shasta, as well as in portions of Tehama and Lassen counties. It opened its first banking office in Chico, California in 1975, followed by branch offices in Willows, Durham and Orland, California and a second branch office in Chico which opened in 1980. In 1981, the Bank acquired the assets of Shasta County Bank through a merger of that bank with and into the Bank and thereby acquired six additional branch offices located in the communities of Bieber, Burney, Cottonwood, Fall River Mills, Palo Cedro and Redding, California.

The Bank's operating policy since its inception has emphasized retail banking. Most of the Bank's customers are retail customers and small to medium-sized businesses. The business of the Bank emphasizes serving the needs of local businesses, farmers and ranchers, retired individuals and wage earners. The majority of the Bank's loans are direct loans made to individuals and businesses in the area, and most of the Bank's deposits are attracted from individuals and business-related sources. The Bank relies substantially on local promotional activity, personal contacts by its officers, directors, employees and shareholders, extended hours, personalized service and its reputation in the communities it serves, to compete with other financial institutions.

IN MEMORIAM

Gerald H. Compton

Founding Director,
Tri Counties Bank
and TriCo Bancshares

Jan. 27, 1934 – April 8, 1985

Financial Highlights

(in thousands, except net income per share)

	Years Ended December 31, 1985	1984	1983	1982	1981
Assets	**$173,684**	$152,508	$122,165	$106,116	$96,713
Securities investments	**29,422**	22,310	18,412	9,798	10,369
Loans, net	**108,352**	90,985	79,130	71,163	66,869
Deposits	**152,260**	132,800	108,588	93,074	83,555
Shareholders' equity	**11,756**	8,177	7,586	6,937	6,075
Interest income	**17,051**	15,675	13,444	12,434	10,990
Interest expense	**9,559**	9,047	7,039	6,775	5,893
Net income	**1,127**	476	544	218	535
Net income per share	**$1.30**	$0.57	$0.66	$0.28	$0.68
Stock dividend per share	**5.00%**	5.00%	–	–	10.00%
Return on total assets	**0.65%**	0.31%	0.44%	0.22%	1.17%
Return on common shareholders' equity	**13.65%**	5.82%	7.17%	3.33%	8.80%

Future Administrative Headquarters

Philadelphia Square, Chico, CA

Robert H. Steveson
President & Chief Executive Officer

Dear Shareholder:

It is my great pleasure to tell you TriCo Bancshares' earnings more than doubled in 1985! Net income for the year was $1,127,000 which is $1.30 per share. This is an increase from $476,000 and $0.57 per share in 1984.

The major improvement in earnings was accompanied by major improvements in other important areas.

Tri Counties Bank is now easily the largest community bank in the North Sacramento Valley/Intermountain Region. In fact, our gain in market share during 1985 gives us the second largest amount of total deposits in our marketing area.

The $19,460,000 gain in deposits during 1985 necessitated an increase in our capitalization. In July, we completed a combined preferred stock and subordinated debt offering of approximately $4,000,000. These funds together with retained earnings will provide the capital needed for continued growth.

Capital is certainly vital in the banking business, but equally important are people; people who are intelligent, honest, knowledgeable and experienced. I am proud to be part of such a team.

Your Board of Directors is composed of the men who founded Tri Counties Bank. Working through the various Board committees, these men guide the growth and profitability of TriCo Bancshares and Tri Counties Bank.

Your Management and Staff carry out the policies set down by the Board and do so with exceptional competence and devotion to duty. Each and every one of our 190 employees has made his or her contribution to these excellent 1985 results.

Sincerely,

Robert H. Steveson

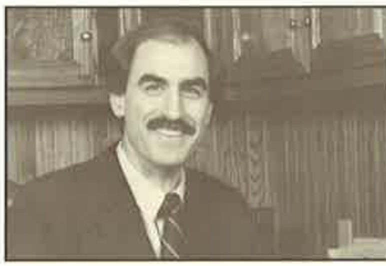
Robert H. Steveson
President and Chief
Executive Officer

Board of Directors

Robert H. Steveson
President and Chief Executive Officer, Tri Counties Bank and TriCo Bancshares, Chico

Alex A. Vereschagin, Jr.
Chairman of the Board. Secretary-Treasurer, Vereschagin Oil Company, petroleum distribution company, Orland

Everett B. Beich
Vice-Chairman of the Board. Owner, Beich Companies, mobile home park commercial development companies, Chico



Fred W. Hignell, III
Secretary of the Board. Principal Partner, Hignell & Hignell, Inc., investment and development company, Chico

Donald J. Casey, M.D.
Retired Physician, Chico

DeWayne E. Caviness, M.D.
Physician and Surgeon, Chico

Sankey M. Hall, Jr.
Owner-Director, Lambert Funeral Home, Roseville

Wendell J. Lundberg
Owner, Wehah Farms, rice and grain operations, Richvale

Wayne Meeks
Owner, Wayne Meeks Red Bluff Ford-Mercury, Red Bluff

Donald E. Murphy
Vice President & General Manager, J.H. McKnight Ranch, Nelson

Robert J. Stern
Retired President, R.J. Stern Co., Inc., Oroville

Administration Tri Counties Bank

Robert H. Steveson
President & Chief
Executive Officer

Joan Jones
Senior Vice President
& Cashier

James Mabry
Senior Vice President
& Loan Administrator

Lawrence Sparks
Vice President &
Loan Supervisor

Dave Raven
Regional Vice President

Carroll Taresh
Regional Vice President

Larry Hall
Vice President & Manager,
Data Processing Department

Janet K. Hannis
Assistant Vice President &
Sales Administrator

Ruth Irvine
Assistant Vice President &
Personnel Manager

Kathleen Pisani
Executive Secretary

Fred Drake
Auditor

Fred Bryant
Compliance Officer
& Credit Supervisor

Board of Directors and Shareholders
TriCo Bancshares and Subsidiaries
Chico, California

We have examined the consolidated balance sheets of TriCo Bancshares and subsidiaries at December 31, 1985 and 1984, and the related consolidated statements of income, changes in shareholders' equity and changes in financial position for each of the three years in the period ended December 31, 1985. Our examinations were made in accordance with generally accepted auditing standards and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the financial statements referred to above present fairly the consolidated financial position of TriCo Bancshares and subsidiaries at December 31, 1985 and 1984, and the consolidated results of their operations and the changes in their financial position for each of the three years in the period ended December 31, 1985, in conformity with generally accepted accounting principles applied on a consistent basis.

Touche Ross & Co.

Certified Public Accountants
San Francisco, California
February 3, 1986

Consolidated Balance Sheets

December 31, 1985 and 1984
(in thousands, except share amounts)

Assets	1985	1984
Cash and due from banks	$ 10,961	$ 10,715
Federal funds sold	–	1,000
Investment securities (approximate market value: $29,695 and $21,979)	29,422	22,310
Loans held for sale	2,000	4,407
Loans:		
Commercial	50,336	38,992
Consumer installment	32,500	29,178
Real estate mortgages	19,259	20,007
Real estate construction	7,378	3,753
	109,473	91,930
Less: Allowance for loan losses	1,121	945
Net loans	108,352	90,985
Premises and equipment, net	6,974	6,611
Investment in real estate	10,144	8,037
Other real estate owned	1,659	3,701
Accrued interest receivable	1,691	1,714
Other assets	2,481	3,028
Total assets	$173,684	$152,508

Liabilities and shareholders' equity	1985	1984
Deposits:		
Non-interest bearing demand	$ 33,409	$ 27,524
Interest bearing demand	47,336	38,261
Savings	12,505	11,488
Time certificates, $100,00 and over	8,924	14,925
Other time certificates	50,086	40,602
Total deposits	152,260	132,800
Federal funds purchased	1,600	–
Mortgage loans payable	613	3,131
Accrued interest and other liabilities	2,478	2,400
Deferred income taxes	310	228
Long-term debt	4,667	5,772
Total liabilities	161,928	144,331
Commitments and contingencies (Note L)		
Shareholders' equity:		
Preferred stock, no par value; shares authorized 1,000,000; shares issued and outstanding 26,724 shares	2,544	–
Common stock, no par value; shares authorized 20,000,000; shares issued and outstanding 833,773 and 791,847 shares	7,155	6,674
Retained earnings	2,057	1,503
Total shareholders' equity	11,756	8,177
Total liabilities and shareholders' equity	$173,684	$152,508

See Notes to Consolidated Financial Statements

Consolidated Statements of Income

Years ended December 31, 1985, 1984 and 1983
(in thousands, except net income per share amounts)

	1985	1984	1983
Interest income:			
Interest and fees on loans	$14,868	$13,505	$11,945
Interest on investment securities	2,000	1,983	1,288
Interest on federal funds sold	183	187	211
Total interest income	17,051	15,675	13,444
Interest expense:			
Interest on money market, savings and time certificates of deposit	7,901	7,026	5,801
Interest on time certificates of deposit, $100,000 and over	949	1,309	872
Interest on short-term borrowing	45	56	15
Interest on long-term debt	664	656	351
Total interest expense	9,559	9,047	7,039
Net interest income	7,492	6,628	6,405
Provision for loan losses	698	750	983
Net interest income after provision for loan losses	6,794	5,878	5,422
Other income:			
Service charges and other income	1,537	1,529	1,465
Securities transactions	515	70	143
Total other income	2,052	1,599	1,608
Other expenses:			
Salaries and related expenses	3,720	3,449	3,246
Other	3,728	3,731	3,088
Total other expenses	7,448	7,180	6,334
Net income before taxes	1,398	297	696
Provision (credit) for income taxes	271	(179)	152
Net income	$ 1,127	$ 476	$ 544
Net income per share	$1.30	$0.57	$0.66

See Notes to Consolidated Financial Statements

Consolidated Statements of Changes in Shareholders' Equity

Years ended December 31, 1985, 1984 and 1983

(in thousands, except share amounts)

	Preferred Stock		Common Stock			
	Number of Shares	Amount	Number of Shares	Amount	Retained Earnings	Total
Balance, January 1, 1983	–	–	738,063	$5,932	$1,005	$ 6,937
Capital notes converted to common stock	–	–	9,222	128	–	128
Retirement of stock			(1,555)	(23)	–	(23)
Net income	–	–	–	–	544	544
Balance, December 31, 1983	–	–	745,730	6,037	1,549	7,586
Capital notes converted to common stock	–	–	9,602	126	–	126
5% stock dividend, less cash paid for fractional shares	–	–	36,515	511	(522)	(11)
Net Income	–	–	–	–	476	476
Balance, December 31, 1984	–	–	791,847	6,674	1,503	8,177
Capital notes converted to common stock	–	–	3,082	40	–	40
5% stock dividend, less cash paid for fractional shares	–	–	38,844	441	(449)	(8)
Preferred stock issue	26,724	$2,544	–	–	–	2,544
Preferred stock dividends	–	–	–	–	(124)	(124)
Net income	–	–	–	–	1,127	1,127
Balance, December 31, 1985	26,724	$2,544	833,773	$7,155	$2,057	$11,756

See Notes to Consolidated Financial Statements

Consolidated Statements of Changes in Financial Position

Years ended December 31, 1985, 1984 and 1983
(in thousands)

	1985	1984	1983
Financial resources were provided by (applied to):			
Operations:			
Net income	$ 1,127	$ 476	$ 544
Noncash items:			
Depreciation and amortization	780	676	414
Provision for loan losses	698	750	983
Provision for deferred income taxes	264	(257)	51
Gain on sale of loans and other real estate	–	–	(110)
Preferred stock, cash dividend	(123)	–	–
Financial resources provided by operations	2,746	1,645	1,882
Financing activities and shareholders' equity transactions:			
Series A preferred stock	2,672	–	–
14¼% subordinated capital notes	1,257	–	–
Public offering costs	(189)	–	–
Financial resources provided by public offering	3,740	–	–
Long-term debt incurred	–	2,500	–
Long-term debt retired	(2,356)	(341)	(401)
Capital notes converted to common stock	39	126	105
Net effect of stock dividend	(8)	(11)	–
	1,415	2,274	(296)
Deposits:			
Non-interest bearing	5,885	3,459	(111)
Interest bearing	13,575	20,753	15,625
	19,460	24,212	15,514
Other activities:			
Decrease (increase) in net non-earning assets:			
Cash and due from banks	(246)	(1,109)	(3,053)
Premises and equipment, net	(899)	(846)	(160)
Other real estate owned, net	2,042	309	(179)
Accrued interest receivable	23	(86)	294
Other	364	(90)	(74)
Increase (decrease) in liabilities:			
Federal funds purchased	1,600	–	–
Accrued interest payable and other liabilities	(110)	920	(55)
Mortgage loans payable	(2,518)	2,718	291
	256	1,816	(2,936)
Increase in financial resources invested in earning assets	$23,877	$29,947	$14,164
Increase (decrease) in earning assets:			
Federal funds sold	$(1,000)	1,000	(3,400)
Investment securities	7,112	3,898	8,614
Loans held for sale	(2,407)	4,407	–
Loans, net	18,065	12,605	8,950
Investment in real estate	2,107	8,037	–
Increase in earning assets	$23,877	$29,947	$14,164

See Notes to Consolidated Financial Statements

Note A – General Summary of Significant Accounting Policies:

Basis of Presentation

The consolidated financial statements include the accounts of TriCo Bancshares (the "Company"), its wholly owned subsidiary, Tri Counties Bank (the "Bank") and the wholly owned subsidiaries of the Bank. All significant intercompany accounts and transactions have been eliminated in consolidation.

Investment Securities

Investment securities are carried at cost, adjusted for the accretion of discounts and amortization of premium using the interest method. Gains and losses (determined on a specific identification basis) on sales of investment securities are presented separately in the statements of income.

Loans

Loans are stated net of undisbursed funds. Interest on loans is accrued principally on a simple-interest basis. Interest on loans is not accrued if, in management's judgement, principal amounts are considered doubtful of collection.

Loan Fees

Loan fees are recognized as income to the extent they represent reimbursements of loan origination costs.

Allowance for Loan Losses

The allowance for loan losses represents management's recognition of the assumed risks of extending credit and its evaluation of the overall quality of the loan portfolio. Although it is not possible to anticipate loan losses with complete accuracy, the evaluation of the quality of the loan portfolio includes such factors as the borrower's financial condition and repayment history, the value of any existing collateral, and the existence of third-party guarantees. Other factors considered by management include past loan loss experience and external business and economic conditions beyond the borrower's control.

The allowance for loan losses is increased by provisions for loan losses charged to operating expense and recoveries of previously charged-off loans, and is reduced for actual loans charged-off.

Intangible Assets

Intangible assets (included in other assets) represent the purchased deposit account base (core deposits) acquired in connection with the acquisition of Shasta County Bank. Core deposits represent the present value of the expected future benefits to be realized from the acquired bank's deposit base, comprised principally of demand and savings deposits. Core deposits are amortized over 10 years using the straight-line method.

Premises and Equipment

Premises (including those acquired under capital lease) and equipment are stated at cost less accumulated depreciation and amortization. Land is carried at cost. Depreciation and amortization expenses are computed using the straight-line method over the shorter of the estimated useful life of the asset or lease term.

Investment in Real Estate

Investment in real estate is stated at the lower of cost or market and consists of properties either acquired or transferred from other real estate owned for the purpose of development or to be held as income earning assets.

Subsequent to acquisition or transfer, properties included in the investment in real estate account are periodically appraised. Any decline in value below the carrying amount of a property is charged to current operations by a provision for real estate losses. Income earned on the investment in real estate account, net of related expenses, is included in other expenses.

Other Real Estate

Other real estate is stated at the lower of cost or market and consists of properties acquired through foreclosure or in satisfaction of borrower obligations. These assets are recorded at the lower of the obligation satisfied or the property's fair market value determined as of the date of acquisition. Any required writedown to fair market value at the date of acquisition is charged to the allowance for loan losses.

Subsequent to acquisition, other real estate is periodically appraised. Any decline in value below the carrying amount of a property is charged to current operations by a provision for other real estate losses. The valuation allowance for such declines was $201,000 and $246,000 at December 31, 1985 and 1984.

Gains and losses on the disposition of other real estate, net of related expenses, are included in other expenses. Expenses prior to disposition are included in other expenses in the period the expenses are incurred.

Mortgage Loans Payable

In connection with the acquisition of other real estate and investment in real estate, the Company has incurred liabilities for the assumption of pre-existing mortgages. These mortgages bear interest rates that range between 8.5% and 9.0%. The Company's intent is to dispose of the properties and related debt within one year.

Income Taxes

The deferred income taxes include amounts attributable to timing differences between revenues and expenses reported for financial statement purposes and for income tax purposes. The principal timing differences result from the use of the cash method of accounting for tax purposes, recognition of gain or loss on sales of participation loans, and differences in the method of calculating or timing of the provisions for loan and other real estate losses. Investment tax credits reduce income tax expense using the flow-through method.

Net Income Per Share

Net income per share is computed based on the weighted average number of shares of common stock and common stock equivalents assumed outstanding during each year. The assumed conversion of the convertible capital notes results in elimination of the related interest expense, net of tax effect, in the computation of net income per share. In 1984 and 1983, the conversion of the capital notes was not assumed for computation purposes because the effect of such conversion would have been antidilutive. The weighted average number of shares used in the computation of net income per share were 983,073, 830,691 and 823,948 for 1985, 1984 and 1983. Fully diluted net income per share is not presented because such amounts would not differ materially from the reported net income per share amounts in any of the years presented.

Note B – Investment Securities:

The carrying amount and estimated market values of investment securities at December 31, 1985 and 1984 were as follows:

	1985		1984	
	Carrying Amount	**Market Value**	Carrying Amount	Market Value
	(in thousands)			
U.S. Treasury and other U.S. Government agencies and corporations	**$15,044**	**$15,267**	$17,123	$16,813
State and political subdivisions	**14,378**	**14,428**	5,187	5,166
	$29,422	**$29,695**	$22,310	$21,979

Investment securities with an aggregate carrying amount of $4,600,000 and $5,680,000 at December 31, 1985 and 1984, were pledged as collateral for public deposits as required by law.

The Bank generally intends to hold investment securities to maturity, and therefore, a valuation allowance is not provided for the excess of carrying amount over market value.

The investment securities included $14,368,000, $5,200,000 and $290,000 of nontaxable securities in 1985, 1984 and 1983. The interest on securities was as follows:

	Year ended December 31,		
	1985	1984	1983
	(in thousands)		
Taxable interest	**$1,172**	$1,920	$1,267
Nontaxable interest	**828**	63	21
	$2,000	$1,983	$1,288

Note C – Allowance for Loan Losses:

Transactions in the allowance for loan losses were as follows:

	Year Ended December 31,	
	1985	1984
	(in thousands)	
Balance, beginning of year	**$ 945**	$ 801
Provision charged to operations	**698**	750
Loans charged-off	**(628)**	(917)
Recoveries of loans previously charged-off	**106**	311
Balance, end of year	**$1,121**	$ 945

Loans classified as nonaccrual amounted to approximately $2,086,000 and $1,515,000 at December 31, 1985 and 1984. If interest on those loans had been accrued, such income would have approximated $320,000 and $315,000 in 1985 and 1984.

Note D – Premises and Equipment:

Premises and equipment are comprised of:

	Year Ended December 31,	
	1985	1984
	(in thousands)	
Premises (including $831,000 acquired under capital lease)	**$5,898**	$4,906
Furniture and equipment	**2,148**	2,236
	8,046	7,142
Less accumulated:		
Depreciation	**(2,040)**	(1,519)
Amortization of capital lease	**(155)**	(135)
	5,851	5,488
Land	**1,123**	1,123
	$6,974	$6,611

Depreciation and amortization of premises and equipment amounted to $555,000, $451,000 and $393,000 in 1985, 1984 and 1983.

Note E – Income Taxes:

The provision (credit) for income taxes is comprised of:	Year Ended December 31, 1985	1984	1983
		(in thousands)	
Tax expense (credit) applicable to income, net of tax credits:			
Federal	$ 122	$(199)	$ 79
State	149	20	73
	$ 271	$(179)	$ 152
Current:			
Federal	$ 10	$ –	$ –
State	179	78	73
	189	78	73
Deferred:			
Federal	72	(199)	79
State	10	(58)	–
	82	(257)	79
	$ 271	$(179)	$ 152

The components of deferred income tax expense are as follows:

	1985	1984	1983
Items applied to increase (reduce) deferred income taxes:			
Investment tax and other tax credits	$ 38	$(172)	$(155)
Cash basis reporting for tax purposes	102	(237)	(426)
Provision for loan losses	(22)	(19)	370
Provision for loss on other real estate	(77)	(68)	(40)
Amortization of core deposits	(112)	14	56
Use of accelerated depreciation methods for tax purposes	39	37	59
Capitalized leases	(11)	(9)	(15)
Direct financing leases	31	73	151
Restoration of deferred taxes, applicable to utilization of prior year tax operating loss carryovers	58	109	75
Other differences	36	15	4
	$ 82	$(257)	$ 79

A reconciliation of the federal statutory income tax rate to the Company's consolidated effective tax rate is as follows:

	1985	1984	1983
Federal statutory income tax rate	46.0%	46.0%	46.0%
Reduction of taxes previously provided, no longer required	(5.3)	(33.8)	–
State income taxes, net of federal tax benefit	5.8	5.9	6.3
Investment tax credits	(1.3)	(57.9)	(22.2)
Tax-exempt interest on municipal obligations	(24.5)	(10.7)	(6.2)
Tax bracket rate differential	(1.5)	(6.8)	(2.9)
Other	.1	(2.9)	.8
Effective tax rate	19.3%	(60.2)%	21.8%

Investment tax credits utilized to reduce the provision for federal income taxes for the years ended December 31, 1985, 1984 and 1983 were $18,000, $172,000 and $155,000.

The Company has tax credit carryforwards of $582,000 available to offset future federal income taxes on its federal income tax returns. The tax credit carryforwards expire in varying amounts between 1990 and 2000.

Investment tax credits include $135,000 and $143,000 which relate to leasing transactions that the Company entered into in 1984 and 1983.

Note F – Long-term Debt:

Long-term debt at December 31, 1985 and 1984 consisted of:

	1985	1984
	(in thousands)	
9½% convertible subordinated capital notes payable in annual installments of $400,000, including interest; balance due March 27, 1988. Notes are convertible into common stock of the Company at $12.53 per share as of December 31, 1985. Notes may be prepaid in whole or in part at par value any time prior to maturity, subject to the holder's prior right of conversion.	$1,884	$2,147
14¼% subordinated capital notes due on July 1, 1988 and July 1, 1992, in the amounts of $393,000 and $864,600, with interest payable monthly. Notes may be prepaid in whole or in part anytime after July 1, 1988.	$1,257	–
9% subordinated capital notes due April 1, 1989, with interest payable semiannually. Notes may be prepaid in whole or in part at any time.	150	150
Term loan agreement collateralized by 100% of Tri Counties Bank stock, with quarterly principal payments of $15,650 plus interest at prime plus 1 to 2 percent, through June 15, 1992. The agreement requires the Bank to maintain a net worth to total assets ratio of at least .07 to 1 and restricts payments of cash dividends or distribution of the Bank's assets to its shareholders.	407	2,500
10% mortgage payable in monthly installments of $4,000, including interest, through December 1, 2003, collateralized by a first deed of trust on certain Bank premises.	383	389
Capital lease obligation on premises; effective interest rate of 12%; payable monthly (interest only until 1986) in varying amounts through December 1, 2009.	586	586
	$4,667	$5,772

The aggregate maturities of long-term debt, excluding the capital lease obligation, are as follows:

	(in thousands)
1986	$ 290
1987	290
1988	1,907
1989	220
1990	70
1991 and after	1,304

Annual principal payments under the 9½% convertible subordinated capital notes are subject to the maintenance of certain capitalization levels and prior consent of the Bank's regulatory authorities under the laws of the California Financial Code and Federal Deposit Insurance Act. During 1985, approval for payment of the 1985 installment of principal on the 9½% convertible subordinated capital notes was received and such payment for $224,000 was made. The principal balance was further reduced during 1985 by conversions of notes into shares of common stock.

Future minimum annual lease payments under the capital lease obligation are as follows:

	(in thousands)
1986	$ 75
1987	75
1988	76
1989	77
1990	78
1991 and after	1,652
Net minimum lease payments	2,033
Less amount representing interest	1,447
Present value of net minimum lease payments	$ 586

Note G – Other Expenses:

The components of other expenses are as follows:

	Year Ended December 31,		
	1985	1984	1983
	(in thousands)		
Equipment and data processing	$ 861	$ 804	$ 687
Occupancy	556	494	425
Advertising	139	82	62
Stationery and supplies	233	211	170
Postage	158	143	143
Net real estate expense	307	448	93
Other	1,474	1,549	1,508
	$3,728	$3,731	$3,088

Note H – Retirement Plans:

In 1984 the Company terminated its defined benefit pension plan effective June 1984. At the date of termination, there were no unfunded vested benefits of the participants.

During 1984 the Company created a discretionary employee stock ownership plan and a discretionary profit-sharing plan. Substantially all the employees with at least one year's service as of the end of the calendar year participate in both the discretionary employee stock ownership plan and the discretionary profit-sharing plan. Contributions are made to each plan at the discretion of the Board of Directors. Contributions to the discretionary employee stock ownership plan were $132,000 and $96,000 in 1985 and 1984. No contributions were made to the discretionary profit-sharing plan in 1985 or 1984.

Note I – Preferred Stock:

On July 31, 1985, the Company issued 26,724 shares of Series A Preferred Stock.

The Company may redeem the preferred stock in whole or in part at its option on or after July 1, 1988 at $100 per share plus accrued and unpaid dividends. The preferred stock is nonvoting, has a dividend preference and has a liquidation preference of $100 per share plus accrued and unpaid dividends.

Note J – Restrictions on Subsidiary Bank Dividends:

The Bank is subject to legal limitations on the amount of dividends that can be paid without the prior approval of the State Superintendent of Banks. The limitation for a given year is the lesser of the Bank's retained earnings or its net income for the last three fiscal years, less the amount of any distributions made by the Bank during such period. As of December 31, 1985, the amount available for distribution by the Bank without the approval of the State Superintendent of Banks was $1,715,000. The Bank's net restricted assets as of December 31, 1985 were $11,362,000.

The Federal Deposit Insurance Corporation requested the Bank not to pay dividends except those required to meet obligations under the Term Loan Agreement, without prior written permission, if the Bank's capital and reserves to assets ratio is less than 7.5% before or after the dividend. At December 31, 1985, this ratio was 7.7%.

Note K – Related Party Transactions:

Certain directors and officers and companies with which they are associated, were customers of and had banking transactions with the Bank in the ordinary course of business. It is the Bank's policy that all loans and commitments to lend to officers and directors be made on substantially the same terms, including interest rates and collateral, as those prevailing at the time for comparable transactions with other borrowers. Such loans are summarized as follows:

	1985	1984
	(in thousands)	
Loans outstanding January 1	$2,029	$2,206
Loan proceeds disbursed	2,589	1,472
Loan repayments and other reductions	(1,371)	(1,649)
Loans outstanding December 31	$3,247	$2,029

Note L – Commitments and Contingencies:

In the normal course of business, the Bank makes various commitments and incurs certain contingent liabilities that are not presented in the accompanying financial statements. The commitments and contingent liabilities include various guarantees, commitments to extend credit, and standby letters of credit. At December 31, 1985, undisbursed commercial and real estate loans amounted to $12,544,000 and $2,990,000. Standby letters of credit and guarantees totaled $1,362,000 at December 31, 1985. The Bank does not anticipate any material losses as a result of the commitments and contingent liabilities.

The Bank is required to maintain an average cash reserve with the Federal Reserve Bank. At December 31, 1985, the amount was $716,000.

The Bank has available unused lines of credit totaling $9,000,000 for Federal Funds transactions.

The Bank is a defendant in legal actions arising from normal business activities. Management believes that these actions are without merit or that the ultimate liability, if any, resulting from them will not materially affect the Bank's financial position. During 1983, the Board of Directors of the Bank negotiated a stipulation and consent to the issuance of an order to change certain banking practices which, as of December 31, 1985, requires the Bank to maintain a ratio of adjusted capital and reserves to total adjusted assets of not less than 7.5% and to maintain a reserve for loan losses of not less than 1% of the Bank's total loans.

At December 31, 1985, minimum commitments under non-cancellable operating leases with initial or remaining terms of one year or more are as follows:

	(in thousands)
1986	$155
1987	14
1988	10
1989	10
1990	10
1991 and after	320
	$519

Rent expense under operating leases was $259,000, $253,000 and $193,000 in 1985, 1984 and 1983.

At December 31, 1985, the Company was committed to sell approximately $2,000,000 in conventional mortgage loans to the Federal Home Loan Mortgage Corporation.

Note M – TriCo Bancshares Financial Statements:

TriCo Bancshares (Parent Only) Balance Sheets

Assets	December 31, 1985	1984
	(in thousands)	
Cash	$ 1	$ 1
Investment in Tri Counties Bank	13,078	10,492
Other assets	66	16
Income tax benefit	316	182
Total assets	$13,461	$10,691

Liabilities and Shareholders' Equity	1985	1984
Liabilities:		
Long-term debt	$ 1,665	$ 2,500
Other liabilities	40	14
Shareholders' equity:		
Preferred Stock, no par value; shares authorized 1,000,000; shares issued and outstanding 26,724 shares	2,544	–
Common Stock, no par value ; shares authorized 20,000,000; shares issued and outstanding 833,773 shares	7,155	6,674
Retained earnings	2,057	1,503
Total shareholders' equity	11,756	8,177
Total liabilities and shareholders' equity	$13,461	$10,691

Statements of Income

	Year ended December 31, 1985	1984	1983
	(in thousands)		
Interest expense on long-term debt	$ 258	$297	$ –
Other income	(8)	–	–
Administration expense	7	63	85
Loss before equity in net income of Tri Counties Bank	257	360	85
Equity in net income of Tri Counties Bank	1,250	642	629
Provision (credit) for income taxes	(134)	(194)	–
Net income	$1,127	$476	$544

Statements of changes in financial position

	Year ended December 31, 1985	1984	1983
	(in thousands)		
Financial resources used:			
Operations:			
Net income	$1,127	$ 476	$ 544
Noncash items:			
Equity in net income of Tri Counties Bank	(1,251)	(642)	(629)
Provision for deferred income taxes	(134)	(182)	–
Amortization of organizational costs	6	6	6
Preferred stock, cash dividend	(123)	–	–
Financial resources used in operations	(375)	(342)	(79)
Financing activities and shareholders' equity transactions:			
Series A preferred stock	2,672	–	–
14¼% subordinated capital notes	1,257	–	–
Public offering costs	(189)	–	–
Financial resources provided by public offering	3,740	–	–
Long-term debt incurred	–	2,500	–
Long-term debt retired	(1,906)	–	–
Contributed capital to Tri Counties Bank	(1,800)	(2,500)	–
Dividend from Tri Counties Bank	503	303	–
Net effect of stock dividend	(8)	(11)	–
Retirement of stock	–	–	(23)
	529	292	(23)
	154	(50)	(102)
Resources provided:			
Cash	–	(38)	(102)
Other	154	(12)	–
	$ 154	$ (50)	$ (102)

Market Information. The Common Stock of the Company is not listed on any exchange nor is it listed with NASDAQ. There is only a limited trading market in the Company's Common Stock. The Company is not aware of any securities dealer which makes a market in the Common Stock of the Company. The following table summarizes those trades of which the Company has knowledge, setting forth the approximate high ask and low bid prices for the periods indicated. The prices indicated below may not necessarily represent actual transactions.

Quarter Ended:	Prices of the Company's Common Stock[1,2] High	Low	Approximate Trading Volume (in shares)
March 31, 1984	$12.70	$10.86	1,583
June 30, 1984	$12.70	$10.56	2,174
September 30, 1984	$ 9.98	$ 9.07	5,602
December 31, 1984	$11.79	$ 9.74	1,740
March 31, 1985	$11.00	$10.00	3,678
June 30, 1985	$10.50	$10.00	2,675
September 30, 1985	$10.50	$10.00	3,717
December 31, 1985	$10.50	$10.00	5,204

[1]As estimated by the Company, based upon trades of which the Company was aware. The Company is not aware of the price of some of the trades included in the Approximate Trading Volume.
[2]Figures adjusted to reflect the 5% stock dividends paid in each of 1985 and 1984.

Holders. As of December 31, 1985, there were approximately 1,548 holders of record of the Company's Common Stock.

Dividends. The Company has paid no cash dividends to date. On February 28, 1985 and March 19, 1984 the Company paid 5% stock dividends to its shareholders. The holders of common stock of the Company are entitled to receive cash dividends when and as declared by its Board of Directors, out of funds legally available therefor, subject to the restrictions set forth in the California General Corporation Law (the "Corporation Law"), the Term Loan Agreement and the dividend rights of the holders of the Series A Preferred Stock.

Pursuant to the terms of a Term Loan Agreement between the Company and First Interstate Bank of California in the amount of $407,000, the Company is restricted in its ability to pay cash dividends to its Common Stock shareholders. See Note F to Notes to Consolidated Financial Statements. The Certificate of Determination of Preferences of the Series A Preferred Stock prohibits the payment of dividends to the holders of Common Stock if the Company is not current in its payments of dividends to the Preferred Stock shareholders.

The Corporation Law provides that a corporation may make a distribution to its shareholders if the corporation's retained earnings equal at least the amount of the proposed distribution. The Corporation Law further provides that, if sufficient retained earnings are not available for the proposed distribution, a corporation may nevertheless make a distribution to its shareholders if immediately after giving effect to such dividend the corporation meets the following two conditions: (i) the corporation's assets equal at least 1¼ times its liabilities, and (ii) either the corporation's current assets equal at least its current liabilities or, if the average of the corporation's earnings before taxes on income and before interest expense for the two preceding fiscal years was less than the average of the corporation's interest expense for such fiscal years, the corporation's current assets equal at least 1¼ times its current liabilities.

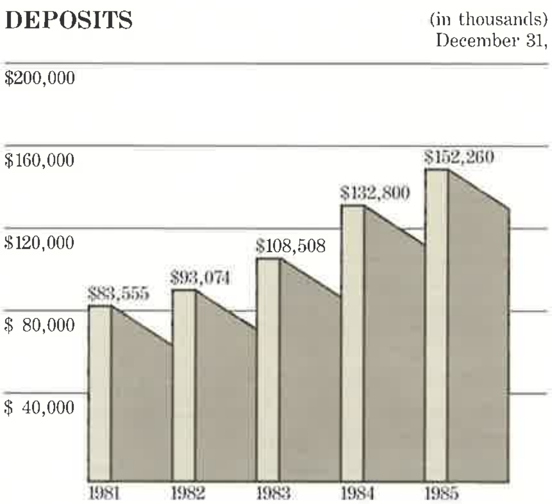
The Company, as sole shareholder of the Bank, is entitled to dividends when and as declared by the Bank's Board of Directors, out of funds legally available therefor, subject to the powers of the Federal Deposit Insurance Corporation (the "FDIC") and the restrictions set forth in the California Financial Code (the "Financial Code") and the Term Loan Agreement. The Financial Code provides that a bank may not make any distributions to its shareholders in excess of the lesser of: (i) the bank's retained earnings, or (ii) the bank's net income for its last three fiscal years, less the amount of any distributions made by the bank to its shareholders during such period. However, a bank may, with the prior approval of the California Superintendent of Banks (the "Superintendent"), make a distribution to its shareholders of up to the amount of its net income for its last fiscal year. If the Superintendent determines that the shareholders' equity of a bank is inadequate or that a distribution by the bank to its shareholders would be unsafe or unsound, the Superintendent may order a bank to refrain from making a proposed distribution. The FDIC has advised the Bank that it should not pay any dividends to the Company except those required to meet obligations under the Term Loan Agreement, if the Bank's capital to assets ratio is less than 7.5% before or after the dividend payment, unless the Bank has obtained the FDIC's prior written consent. See Note J to Notes to Consolidated Financial Statements. As of December 31, 1985, the capital to assets ratio of the Bank was 7.7%. The FDIC may also order a bank to refrain from making a

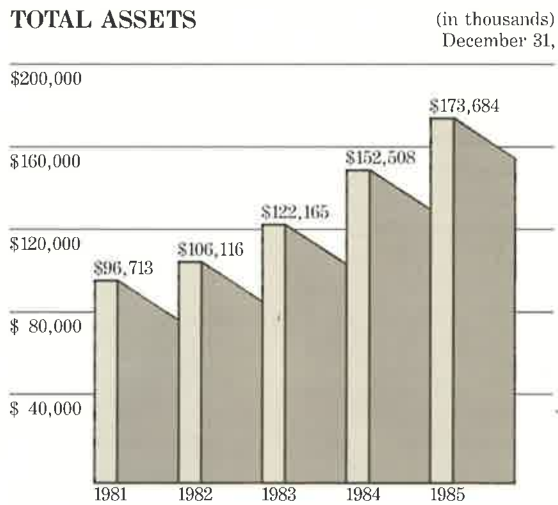
Common Stock Information
(Continued)

proposed distribution when, in its opinion, the payment of such would be an unsafe or unsound practice. The Bank paid cash dividends in the aggregate amount of $503,698 in 1985. The Term Loan Agreement restricts the dividends that the Bank may pay to the Company.

The Federal Reserve Act limits the loans and advances that the Bank may make to its affiliates. For purposes of such Act, the Company is an affiliate of the Bank. The Bank may not make any loans, extensions of credit or advances to the Company if the aggregate amount of such loans, extensions of credit, advances and any repurchase agreements and investments exceeds 10% of the capital stock and surplus of the Bank. Any such permitted loan or advance by the Bank must be secured by collateral of a type and value set forth in the Federal Reserve Act.

Financial Highlights





As the Company has not commenced any business operations independent of the Bank, its only subsidiary, the following discussion pertains primarily to the activities of the Bank.

(A) Results of Operations.

The following is a summary of operations for the five years ended December 31, 1985 and management's discussion and analysis of the significant changes in income and expense accounts presented therein for the most recent two years – each as compared with its respective prior period. This information should be read in conjunction with the financial statements and notes related thereto appearing elsewhere in this Annual Report.

	Years ended December 31,				
	1985[1]	1984[1]	1983[1]	1982[1]	1981[1]
	(in thousands, except net income per share amounts)				
Interest income:					
Interest and fees on loans	$14,868	$13,505	$11,945	$11,349	$ 9,720
Interest on investment securities[2]	2,710	2,046	1,288	1,032	1,169
Interest on time deposits and federal funds sold	183	187	211	53	101
Total interest income	17,761	15,738	13,444	12,434	10,990
Interest expense:					
Interest on deposits	8,850	8,335	6,673	6,269	5,399
Interest on short-term borrowing	45	56	15	87	182
Interest on long-term debt	664	656	351	419	312
Total interest expense	9,559	9,047	7,039	6,775	5,893
Net interest income	8,202	6,691	6,405	5,659	5,097
Less provision for loan losses	698	750	983	860	530
Net interest income after provision for loan losses	7,504	5,941	5,422	4,799	4,567
Other income:					
Gain on security transactions	515	70	143	268	89
Service charges and other	1,537	1,529	1,465	1,120	967
Total other income	2,052	1,599	1,608	1,388	1,056
Other expenses:					
Salaries and employee benefits	3,720	3,449	3,246	3,133	2,430
Other operating expenses	3,728	3,731	3,088	2,756	2,498
Total other expenses	7,448	7,180	6,334	5,889	4,928
Income before provision for income taxes	2,108	360	696	298	695
Provision (credit) for income taxes – actual	271	(179)	152	80	160
Tax equivalent adjustment	710	63			
Net Income	$ 1,127	$ 476	$ 544	$ 218	$ 535
Net income per share	$1.30	$ .57	$ .66	$ .28	$ .68
Selected Balance Sheet Information					
Total assets	$173,684	$152,508	$122,165	$106,116	$ 96,713
Long-term obligations	$ 4,667	$ 5,772	$ 3,613	$ 4,014	$ 4,862
Preferred Stock	$ 2,544	–	–	–	–

[1]Certain reclassifications have been made in the 1984, 1983, 1982 and 1981 summary of operations to conform to classifications in 1985.
[2]Interest on tax free securities is reported on a tax equivalent basis of 1.85.

Management's Discussion and Analysis of Financial Condition and Results of Operations

(A) Results of Operations. (Continued)

Net Interest Income

The major component of income, net interest income, continued to increase in 1985. Net interest income increased to $8,202,000 in 1985 from $6,691,000 in 1984. This 22% increase reflects an increase in net interest margin, an increase in the net yield on earning assets, and an increase in volume of both interest bearing assets and interest bearing liabilities. Net interest income increased in 1984 compared to 1983 as a result of an increased volume of interest bearing assets and an increased rate of interest.

Net interest income is the most significant contributor to the Bank's earnings. Net interest income represents the excess of interest and fees earned on interest earning assets (loans, investment securities and federal funds sold) over the

Table One: Analysis of Change in Net Yield on Earning Assets

	1985			1984		
Assets	**Average Balance**[1]	**Income/ Expense**	**Yield/ Rate**	Average Balance[1]	Income/ Expense	Yield Rate
			(amounts in thousands)			
Earning assets:						
Loans[2,3]	$102,709	$14,868	14.48%	$ 85,285	$13,505	15.84%
Investment Securities[4]	22,284	2,710	12.16%	19,975	2,046	10.24%
Federal funds sold	2,211	183	8.28%	1,665	187	11.23%
Total earning assets	127,204	17,761	13.96%	106,925	15,738	14.72%
Cash and due from banks	8,909			8,209		
Premises and equipment	7,027			6,481		
Other assets	16,891			12,608		
Less: Allowance for loan losses	(1,015)			(795)		
Total	$159,016			$133,428		
Liabilities and shareholders' equity						
Interest bearing liabilities:						
Demand deposits (interest bearing)	$ 44,872	3,103	6.92%	$ 36,511	3,039	8.32%
Savings deposits	11,443	631	5.51%	11,351	637	5.61%
Time deposits	54,913	5,116	9.32%	43,964	4,659	10.60%
Federal funds purchased	540	45	8.33%	487	56	11.50%
Long-term debt and mortgages	5,160	664	12.87%	5,695	656	11.52%
Total interest bearing liabilities	116,928	9,559	8.18%	98,008	9,047	9.23%
Demand deposits	28,919			25,550		
Other liabilities	3,202			1,887		
Shareholders' equity	9,967			7,882		
Total	$159,016			$133,327		
Net interest income		$ 8,202			$ 6,691	
Net interest margin			5.78%			5.49%
Net yield on earning assets[5]			6.45%			6.26%

[1]Average balances are computed principally on the basis of daily balances.
[2]Nonaccrual loans are included.
[3]Interest income on loans includes fees on loans of $1,224,000 in 1985 and $994,000 in 1984.
[4]Interest income is stated on a tax equivalent basis of 1.85.
[5]Net yield on interest earning assets is computed by dividing net interest earnings by total interest earning assets. Net interest earnings is the difference between the total interest earned and the total interest paid.

(A) Results of Operations.
(Continued)

interest paid on deposits and borrowed funds.

The accompanying tables analyze the changes in net interest income for 1985 and 1984. The first table provides an analysis of change in net yield on earning assets setting forth average assets, liabilities and shareholders' equity; interest income earned and interest expense paid; average rates earned and paid; and the net interest margin. The second table presents an analysis of volume and rate changes on net interest income and expense.

Table Two: Analysis of Volume and Rate Changes on Net Interest Income and Expense

	1985 over 1984			1984 over 1983		
	Volume	**Yield/ Rate**	**Total**	Volume	Yield/ Rate	Total
			(in thousands)			
Increase (decrease) in interest income:						
Loans[1]	$2,523	(1,160)	$1,363	$1,028	$ 532	$1,560
Investment securities[2]	81	583	664	700	58	758
Federal funds sold	45	(49)	(4)	(85)	61	(24)
Total	2,649	(626)	2,023	1,643	651	2,294
Increase (decrease) in interest expense:						
Demand deposits (interest bearing)	579	(515)	64	36	66	102
Savings deposits	5	(11)	(6)	(128)	21	(107)
Time deposits	1,020	(563)	457	1,104	563	1,667
Short-term borrowings	4	(15)	(11)	37	4	41
Long-term borrowings	(69)	77	8	208	97	305
Total	1,539	(1,027)	512	1,257	751	2,008
Increase (decrease) in net interest income	$1,110	$ 401	$1,511	$ 386	$ (100)	$ 286

[1] Nonaccrual loans are included.
[2] Interest income is stated on a tax equivalent basis of 1.85.

Net Yield on Earning Assets

The net yield on earning assets increased to 6.45% in 1985 from 6.26% in 1984. This increase, the first increase in two years, is due to two factors: rate differential, that is, the interest rate on interest bearing liabilities decreased more than the interest rate on interest earning assets; and, continued shift of time deposits with a higher interest rate to money market accounts with a lower interest rate. The net yield on earning assets declined to 6.26% in 1984 from 6.79% in 1983. The change resulted primarily from the increased rate differential; that is, interest on interest bearing liabilities increased more than interest on interest earning assets.

Interest Income

Interest income increased 13% to $17,761,000 in 1985 from $15,738,000 in 1984 due to a 19% growth in the volume of interest bearing assets and an increased rate in interest from securities.

The total increase in interest income from loans was $1,363,000. An increased volume of loans resulted in an increase in interest income of $2,523,000; reduction in interest rates on loans offset that amount by $1,160,000. In 1984, the increase of 17% in interest income was due to both an increased volume of loans and an increase in interest rates on loans.

The Bank continued to increase its holding of investment securities in 1985. Tax free securities increased to $14,368,000 in 1985 from $5,200,000 in 1984. This resulted in tax free income from securities of $828,000 in 1985. Income on securities is restated to reflect the tax benefit. This tax benefit is $710,000 in 1985 and $63,000 in 1984.

Fees on loans increased 23% and 52% in 1985 and 1984. Commercial and real estate loan fees provided the major portion of the increase.

Interest Expense

Interest expense in 1985 increased a total of $512,000. Increased volume of interest bearing liabilities caused an increase in interest expense of $1,677,000, offset by a reduction of $1,165,000, as a result of reduced interest rates in 1985. Interest expense increased $2,008,000 in 1984 compared to 1983, primarily due to an increased volume of time deposits and an increased rate of interest. Average savings deposits increased slightly in 1985 following a decrease of 17% in 1984. Management believes the savings deposits will continue to increase slightly in 1986.

Interest expense on short term borrowing decreased $11,000 in 1985 compared to an increase of $41,000 in 1984. The decrease in expense in 1985 was primarily due to a reduction in interest rates; the increase in 1984 was primarily due to an increase of volume of short term borrowing.

Total long term debt decreased in 1985 as a result of the partial repayment of the Term Loan Agreement. Interest expense increased by $8,000, primarily due to the issuance of subordinated Capital Notes with a higher interest rate. See "Public Offering of Preferred Stock and Long Term Debt." In 1984, long term debt increased primarily due to the $2,500,000 Term Loan Agreement entered into by the Company.

Provision for Loan Losses

The provision for loan losses decreased 7% in 1985, following a decrease of 24% in 1984. Management expects the provision to decrease slightly in 1986 due to the continued decrease in charge-offs in 1985.

Other Income

Income from service charges totaled $1,251,000, $1,242,000, and $1,120,000 in 1985, 1984 and 1983. The increase is due primarily to an increased volume of accounts.

Securities Transactions

Net gains from security transactions were $515,000, $70,000, and $143,000 in 1985, 1984 and 1983. The Bank does not actively trade in the securities market but does elect, for liquidity purposes, to sell certain securities when it is to its advantage during periods of declining interest rates.

Other Expenses

Salaries and benefits increased 8% in 1985 and 9% in 1984, primarily due to annual salary adjustments and increased insurance costs.

Other operating expenses remained constant in 1985. Net real estate expense decreased to $307,000 in 1985 from $448,000 in 1984. Other expenses, as well as salary and benefit expenses, increased in 1985 in part due to general increased costs. Other expenses increased in 1984, primarily due to increased expense on other real estate owned.

Provision (Credit) for Income Taxes

The effective tax rate on income is 19% in 1985. The effective tax rate is less than the statutory tax rate because of tax free securities income of $828,000. The effective tax rate on income was a credit of 60.2% in 1984. Two factors caused this credit, investment tax credits of $172,000 and a reduction of income taxes previously provided and no longer required.

Return on Assets and Equity

The following sets forth certain ratios for the Company for the last two years.

	1985	1984
Return on assets	.65%	.31%
Return on shareholders' equity	11.31%	6.04%
Shareholders' equity to assets	6.27%	5.94%

In 1985, the return on assets increased primarily due to $1,127,000 of income offset by a $21,176,000 increase in assets. The return on shareholders' equity increased primarily due to $1,127,000 of income offset by the increase of $2,544,000 in shareholders' equity arising from the issue of preferred stock.

The ratio of shareholders' equity to assets increased due to two factors: the increase of $1,127,000 in income; and, the addition of $2,544,000 due to the issuance of the preferred stock, offset by an increase of $21,176,000 in assets. In 1984 the return on assets and equity decreased primarily due to an increase of $30,343,000 in assets.

(B) Balance Sheet Analysis.

Loans

Total average loans increased 20% in 1985, following an increase of 8% in 1984. The mix of loans also changed. Commercial loans, including leases, increased to 46% of the total loans in 1985 as compared to 32% in 1984. Real estate construction increased to 7% of the loans in 1985 compared to 4% in 1984. Consumer installment dropped slightly to 30% in 1985 compared to 32% in 1984.

Loan Portfolio Composite

The composition of the loan portfolio at the end of each of the last two years is reflected in the following table:

	December 31, 1985	December 31, 1984
	(in thousands)	
Commercial, financial and agricultural	**$ 48,040**	$36,003
Consumer installment	**32,500**	29,178
Real estate mortgage	**19,259**	20,007
Real estate construction	**7,378**	3,753
Lease financing	**2,296**	2,989
Total loans	**$109,473**	$91,930

Nonaccrual, Past Due and Restructured Loans

The table below sets forth the nonaccrual loans and loans carried on an accrual basis but past due more than 90 days, as of December 31, 1985 and 1984. There were no loans, the terms of which had been restructured, at December 31, 1985 and 1984.

	December 31, 1985	December 31, 1984
	(in thousands)	
Nonaccrual loans	**$2,086**	$1,515
Past due loans (90 days or more)	**1,812**	1,475
Total	**$3,898**	$2,990

Nonperforming loans increased slightly to 3.6% of total loans in 1985 compared to 3.3% in 1984. Commercial, real estate (other than 1-4 single family dwellings), and consumer loans are reviewed on an individual basis for reclassification to nonaccrual status when any one of the following occurs: the loan becomes 90 days past due as to interest or principal, the full and timely collection of additional interest or principal becomes uncertain, the loan is classified doubtful by internal auditors or bank regulatory agencies, or a portion of the principal balance has been charged off. Approximately $320,000 of additional interest income would have been recorded if loans classified as non-accrual had been current in 1985. The reclassification of loans as nonperforming does not necessarily reflect management's judgment as to collectibility.

Allowance for Loan Losses Activity

One percent has been determined by management to be adequate in relation to the risk of future losses inherent in the loan portfolio. In determining the adequacy of the loan loss allowance, management relies primarily on its ongoing review of the loan portfolio, both to ascertain whether there are probable losses to be written off and to assess the loan portfolio in the aggregate. Problem loans are examined on an individual basis to determine estimated probable loss. In addition, management considers current and projected loan mix and loan volumes, historical net loan loss experience for each loan category, and current and anticipated economic conditions affecting each loan category. The Bank has agreed with the FDIC to maintain a minimum of one percent of loans as an allowance for loan loss. The Bank takes into consideration the judgments of internal auditors, independent auditors and bank regulatory agencies that review the loan portfolio as a part of the regular bank examination process.

The Bank's total charge-offs decreased by 32% to $628,000 in 1985 from $917,000 in 1984. Total charge-offs in 1986 are expected to continue to decrease, primarily in commercial loans; real estate and consumer loan charge-offs are expected to remain the same.

Allowance for Loan Losses Activity

The following table summarizes, for the years indicated, the activity in the allowance for loan losses:

	December 31, 1985	1984
	(in thousands)	
Balance, beginning of year	$ 945	$ 801
Provision charged to operations	698	750
Loans charged off:		
Commercial, financial and agricultural	(332)	(518)
Consumer installment	(292)	(379)
Real estate mortgage	(4)	(20)
Real estate construction	–	–
Total loans charged off	(628)	(917)
Recoveries:		
Commercial, financial, and agricultural	65	266
Consumer installment	34	45
Real estate mortgage	7	–
Real estate construction	–	–
Total recoveries	106	311
Net loans charged off	(522)	(606)
Balance, end of year	1,121	945
Average total loans	$102,709	$85,285
Ratios:		
Net charge-offs during period to average loans outstanding during period	.61%	.71%
Provision for loan losses to average loans outstanding	.68%	.88%
Allowance to loans at year-end	1.02%	1.03%

Loans Held For Sale

At December 31, 1985, the Bank was committed to sell approximately $2,000,000 in conventional real estate mortgage loans to the Federal Home Loan Mortgage Corporation to provide increased liquidity. The sale was completed in 1986.

Investment in Real Estate

At December 31, 1985, $10,144,000 of property was held by a subsidiary of the Bank for the purposes of development or to be held as income earning assets pending receipt of necessary approvals from the State Banking Department.

Deposits

Deposit accounts increased to $152,260,000 in 1985 from $132,800,000 in 1984. There were changes in the mix of deposits in 1985. Interest bearing demand deposits increased to 31% of deposits in 1985 from 28% in 1984. Total time deposits decreased to 38% of total deposits in 1985 from 42% of deposits in 1984. Non-interest bearing demand deposits increased slightly and savings deposits decreased slightly. The Bank concentrated on time deposits under $100,000 by offering more competitive interest rates on those deposits. As a result, time deposits under $100,000 increased to $50,086,000 in 1985 from $40,602,000 in 1984. Time deposits over $100,000 decreased to $8,924,000 in 1985 from $14,025,000 in 1984.

Public Offering of Preferred Stock and Long-term Debt

The Company completed an offering of Series A Preferred Stock and 14¼% Subordinated Capital Notes on July 31, 1985. The Company contributed $1,800,000 of the proceeds to the Bank as a capital contribution. The remainder of the net proceeds, $1,941,418, was used to prepay the principal and the accrued interest of the Term Loan Agreement between the Company and First Interstate Bank. See Note F to Notes to Consolidated Financial Statement for additional information.

In 1984, the Federal Deposit Insurance Corporation requested the Bank not to pay further dividends except those required to meet obligations under the Term Loan Agreement, without prior written permission, if the Bank's capital and reserves to asset ratio (as defined by the FDIC) is less than 7.5% before or after the dividend. At December 31, 1984, this ratio was 6.8%. At December 31, 1985, the ratio had increased to 7.7% as a result of the capital contribution from the Company and the Bank's net income.

Liquidity

Liquidity relates to the Company and the Bank's ability to generate adequate cash to meet their respective needs. The principal cash requirements of the Bank are to cover downward fluctuations in its deposit accounts and unexpected loan demand.

Another indication of potential demand on the Bank's liquidity is the maturity distribution of certificates of deposit in denominations of $100,000 or more which is set forth in the following table. These deposits are generally more rate sensitive than other deposits and therefore more likely to be withdrawn to obtain higher yields elsewhere if available.

(B) Balance Sheet Analysis. (Continued)

Certificates of Deposit in Denominations of $100,000 or More –

	Amount as of December 31, 1985	1984
	(in thousands)	
Time remaining until maturity:		
Less than three months	$6,070	$ 9,380
3 months to 6 months	2,654	4,233
6 months to 12 months	100	1,111
More than 12 months	100	201
Total	$8,924	$14,925

Management believes that the Bank's investment portfolio, together with the Bank's lines of credit with other institutions and the surplus funds due to increased deposits, is sufficiently liquid to cover potential fluctuations in deposit accounts and loan demand. The Bank has maintained a quality portfolio and has selected maturities to provide a proper balance of liquidity and attractive yields. The maturity distribution of the portfolio is presented in the following tables:

Investment Securities Maturities – December 31, 1985

	Within One Year	After One but within 5 Years	After 5 but within 10 Years	After 10 Years	Total
	(amounts in thousands)				
U.S. Treasury and other U.S. Government agencies and corporations	$5,849	$ 9,195	–	–	$15,044
State and political subdivisions	1,500	3,014	4,551	5,313	14,378
Total book value	$7,349	$12,209	$4,551	$5,313	$29,422
Average Yield[1]	8.29%	10.40%	15.06%	15.79%	11.57%

Investment Securities Maturities – December 31, 1984

	Within One Year	After One but within 5 Years	After 5 but within 10 Years	After 10 Years	Total
	(amounts in thousands)				
U.S. Treasury and other U.S. Government agencies and corporations	$4,490	$ 7,260	$4,055	$1,317	$17,122
State and political subdivisions	–	10	4,078	1,100	5,188
Total book value	$4,490	$7,270	$8,133	$2,417	$22,310
Average Yield[1]	9.97%	10.35%	12.87%	14.80%	11.72%

[1]Yields are computed on a tax equivalent basis.

Information pertaining to certain of the tax-free securities held December 31, 1985 follows:

	Book Value	Market Value	Basis	Yield[1]	Rating[2]
	(amounts in thousands)				
Covina Redevelopment Agency Multi-family Housing	$1,250	$1,275	8.25%	15.04%	AAA
Orange County Multi-family Housing	1,547	1,488	8.50%	14.79%	AAA
Redevelopment Agency of the City of Pittsburg, CA	1,000	955	5.75%	10.48%	AAA
Redevelopment Agency of the City of Pittsburg, CA	250	254	8.50%	14.54%	AAA

[1]Yields are computed on a tax equivalent basis.
[2]Standard and Poor.

Loan demands also affect the Bank's liquidity position. The following tables present the maturities and sensitivity to changes in interest rates of commercial and real estate construction loans at December 31, 1985 and 1984:

Loan Maturities – December 31, 1985

	Within One Year	After One but within 5 Years	After 5 Years	Total
	(in thousands)			
Commercial loans	$17,138	$17,528	$15,670	$50,336
Real estate construction loans	7,378	–	–	7,378
Total	$24,516	$17,528	$15,670	$57,714
Loans with predetermined interest rates		$11,220	$ 3,859	
Loans tied to Bank's base commercial loan rate		6,308	11,811	
Total		$17,528	$15,670	

(B) Balance Sheet Analysis.
(Continued)

Loan Maturities – December 31, 1984

	Within One Year	After One but within 5 Years	After 5 Years	Total
	(in thousands)			
Commercial loans	$20,076	$10,640	$ 8,276	$38,992
Real estate construction loans	3,623	130	–	3,753
Total	$23,699	$10,770	$ 8,276	$42,745
Loans with predetermined interest rates		$ 8,315	$ 1,842	
Loans tied to Bank's base commercial loan rate		2,455	6,434	
Total		$10,770	$ 8,276	

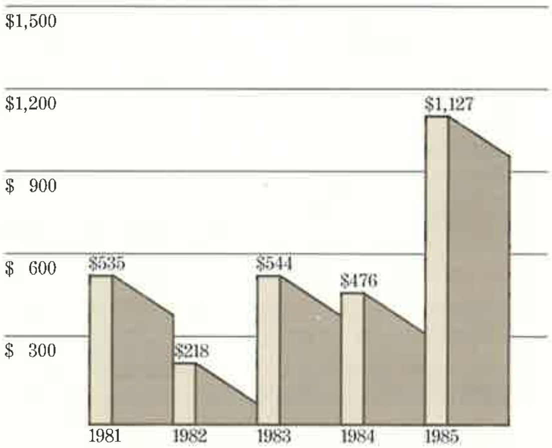
The principal cash requirements of the Company are servicing the Term Loan Agreement of $407,000, paying interest on 14¼% Subordinated Capital Notes and dividends on Series A Preferred Stock. The Company is dependent upon the payment of cash dividends by the Bank to service its commitments.

The Company expects that the cash dividends paid by the Bank to the Company will be sufficient to meet this repayment schedule. See "Common Stock Information – Dividends" and Note J to Notes to Consolidated Financial Statements.

Financial Highlights

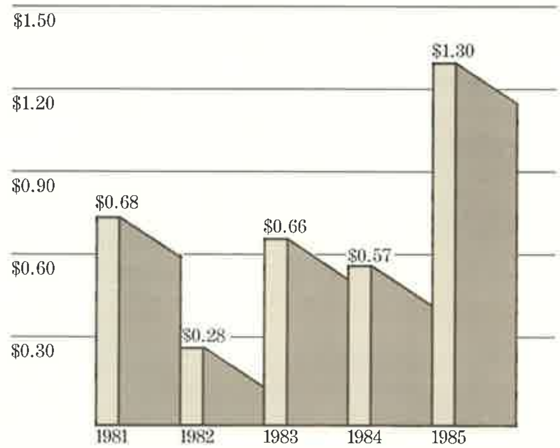
NET INCOME

(in thousands)
December 31,



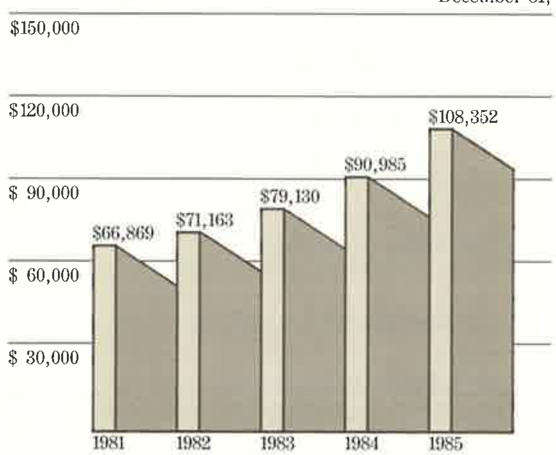
NET INCOME PER SHARE

(in thousands)
December 31,



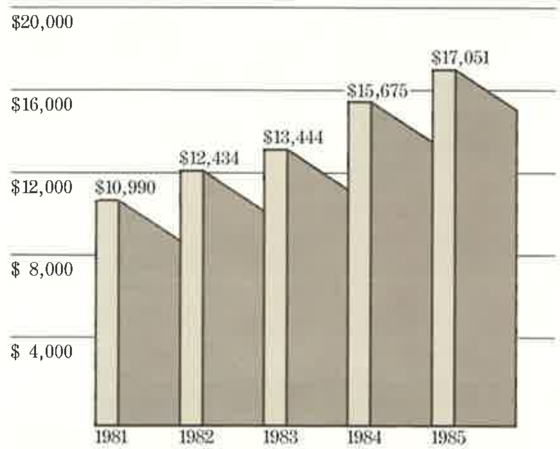
LOANS, NET

(in thousands)
December 31,



INTEREST INCOME

(in thousands)
December 31,



TriCo Bancshares Executive Officers

Robert H. Steveson
President & Chief Executive Officer

Joan Jones
Vice President & Chief Financial Officer

Fred W. Hignell, III
Secretary

Administration Tri Counties Bank

Robert H. Steveson
President & Chief Executive Officer

Joan Jones
Senior Vice President & Cashier

James Mabry
Senior Vice President & Loan Administrator

Lawrence Sparks
Vice President & Loan Supervisor

Dave Raven
Regional Vice President

Carroll Taresh
Regional Vice President

Ruth Irvine
Assistant Vice President & Personnel Manager

Kathleen Pisani
Executive Secretary

Janet K. Hannis
Assistant Vice President & Sales Administrator

Larry Hall
Vice President & Manager, Data Processing Department

Fred Bryant
Compliance Officer & Credit Supervisor

Fred Drake
Auditor

Form 10-K

The Company will provide to any interested party, without charge, a copy of the Company's Annual Report on Form 10-K for the year ended December 31, 1985, as filed with the Securities and Exchange Commission, including the financial statements and schedules thereto. The report may be obtained by written request to: **Corporate Secretary, TriCo Bancshares, P.O. Box 2207, Chico, CA 95927.**

Managers Tri Counties Bank

Park Plaza Branch/Chico
Ty Thresher
Manager

Palo Cedro Branch
Julie Jones
Facility Manager

Pillsbury Branch/Chico
Jim Burnell
Manager

Redding Branch
Dan Herbert
Manager

Durham Branch
Walter Bender
Manager

Burney Branch
Robert Jones
Manager

Orland Branch
Erika Bender
Manager

Fall River Valley Branch
Robert Jones
Manager

Bieber Branch
Stella Griner
Facility Manager

Cottonwood Branch
Larry Lewis
Manager

Department Managers Tri Counties Bank

Data Processing
Chico
Larry Hall
Vice President & Manager

Real Estate Department
Redding
Ron Bee
Manager

SBA Department
Redding
Debbie Gibson
Manager

Purchasing Department
Chico
Beverly London
Manager

Locations

Administrative Office & Park Plaza Branch
780 Mangrove Avenue
P.O. Box 2207
Chico, CA 95927
(916) 345-5151

Pillsbury Branch
2171 Pillsbury Road
P.O. Box 1130
Chico, CA 95927
(916) 345-5151

Durham Branch
The Midway
P.O. Box 190
Durham, CA 95938
(916) 343-3735

Orland Branch
100 East Walker Street
P.O. Box 188
Orland, CA 95963
(916) 865-5524

Willows Branch
210 North Tehama
P.O. Box 1158
Willows, CA 95988
(916) 934-2191

Cottonwood Branch
3349 Main Street
Cottonwood, CA 96022
(916) 347-3751

Palo Cedro Branch
3751 Deschutes Rd.
Palo Cedro, CA 96073
(916) 547-4494

Redding Branch
1810 Market Street
Redding, CA 96001
(916) 244-4700

Burney Branch
1275 Main Street
Burney, CA 96013
(916) 335-2215

Fall River Valley Branch
Highway 299 East
Fall River Mills, CA 96028
(916) 336-6291

Bieber Branch
Bridge & Market Sts.
Bieber, CA 96009
(916) 294-5211

Tri Counties Bank Managers

Ty Thresher
Park Plaza Branch

Jim Burnell
Pillsbury Branch

Walter Bender
Durham Branch

Erika Bender
Orland Branch

Larry Lewis
Cottonwood Branch

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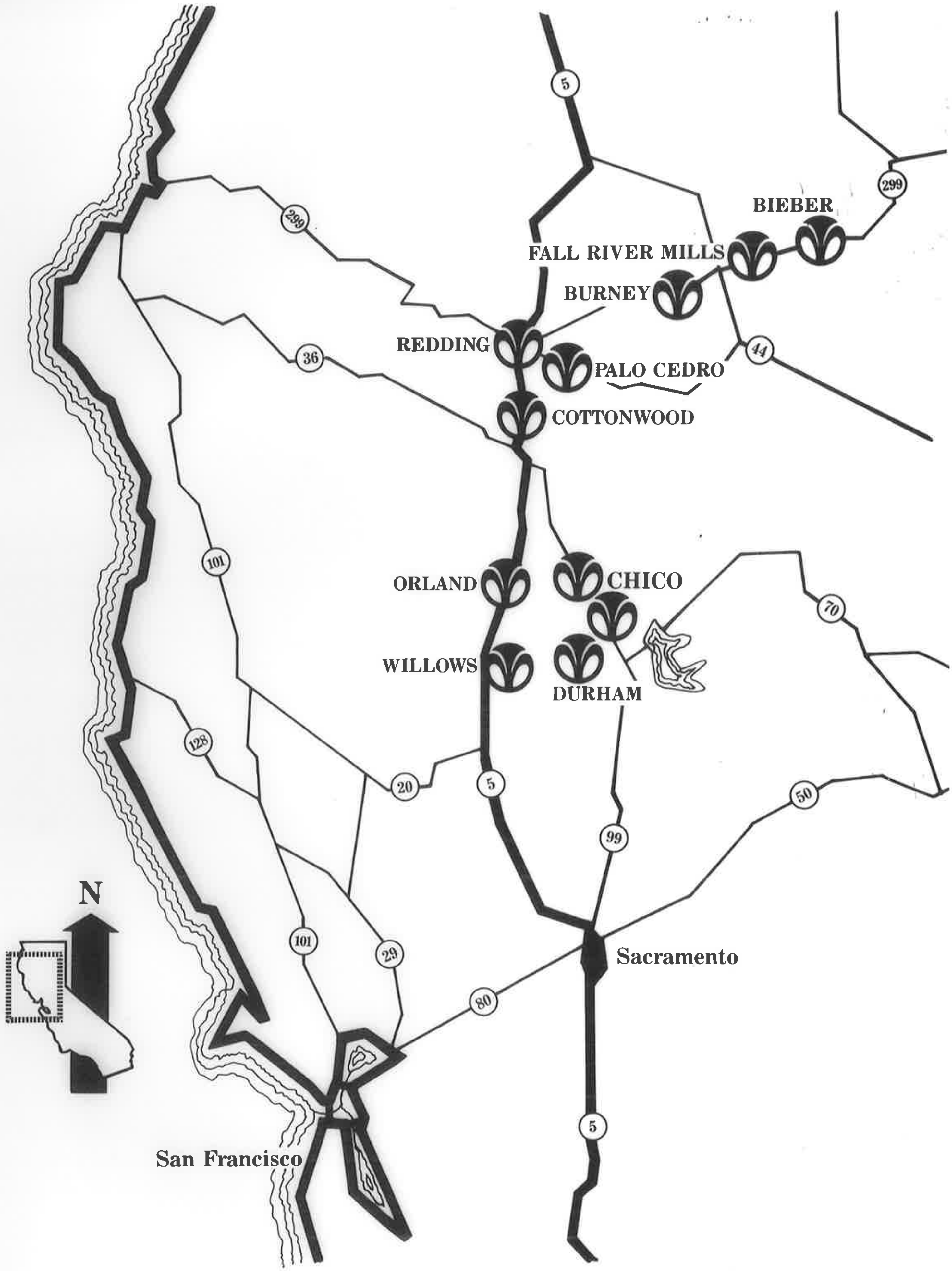
Bieber Branch



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299
BIEBER
FALL RIVER MILLS
BURNEY
REDDING
PALO CEDRO
44
36
COTTONWOOD
101
ORLAND
CHICO
70
WILLOWS
DURHAM
128
20
5
50
99
N
Sacramento
101
29
80
5
San Francisco

Tri Counties Bank Marketing Area

THE ELEVEN Tri Counties Bank offices serve the North Sacramento Valley and adjoining Intermountain Area of California with a population of approximately 350,000 residents. Tri Counties Bank has more than 10% market share of deposits.

Five Tri Counties Bank offices are in or near Chico, approximately 90 miles north of Sacramento and 175 miles northeast of San Francisco. Chico is the largest city in rural Butte County. Agriculture and food processing are the county's major source of income. Almonds, walnuts, prunes, peaches, rice and wheat are the principal crops.

California State University, Chico, the second oldest campus in the state system, attracts its 12,000 students from all over the state.

Six Tri Counties Bank offices are in or near Redding, approximately 160 miles north of Sacramento and 222 miles north of San Francisco. Redding is the largest city and county seat of Shasta County. Recreation and tourism are major industries. Shasta Lake, Trinity Lake, Whiskeytown Lake and Lassen National Park are nearby. Surrounding forests provide timber for several lumber mills.

The beautiful scenery, the clean air, the pure and abundant water and the many recreational opportunities have made the entire marketing area extremely popular for those retiring from the San Francisco Bay Area as well as from Southern California. The medical facilities are excellent.

TRICO BANCSHARES

Administrative Headquarters

780 Mangrove Avenue
P.O. Box 2207
Chico, CA 95927

916/345-5151