BANNER CORP
Form 10-K
February 26, 2019

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

FORM 10-K

[X] ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 FOR THE FISCAL YEAR ENDED DECEMBER 31, 2018

OR

[ ] TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 FOR THE TRANSITION PERIOD FROM __________to__________

Commission File Number 0-26584

BANNER CORPORATION
(Exact name of registrant as specified in its charter)

Washington	91-1691604
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification Number)

10 South First Avenue, Walla Walla, Washington 99362
(Address of principal executive offices and zip code)
Registrant's telephone number, including area code: (509) 527-3636
Securities registered pursuant to Section 12(b) of the Act:

Common Stock, par value $.01 per share	The NASDAQ Stock Market LLC
(Title of Each Class)	(Name of Each Exchange on Which Registered)

Securities registered pursuant to section 12(g) of the Act:
None.
Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act Yes X No _
Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act Yes __No X

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

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files) Yes X No ____

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulations S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. ____

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

Large accelerated filer X	Accelerated filer ___	Non-accelerated filer _____	Smaller reporting company ____	Emerging growth company ____

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards pursuant to Section 13(a) of the Exchange Act. ____

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

The aggregate market value of the voting and non-voting common equity held by nonaffiliates of the registrant based on the closing sales price
of the registrant's common stock quoted on The NASDAQ Stock Market on June 30, 2018, was:
Common Stock – $1,914,245,405
(The exclusion from such amount of the market value of the shares owned by any person shall not be deemed an admission by the Registrant
that such person is an affiliate of the Registrant.)

The number of shares outstanding of the registrant's classes of common stock as of January 31, 2019:
Common Stock, $.01 par value – 35,106,227 shares
Non-voting Common Stock, $.01 par value – 74,933 shares
Documents Incorporated by Reference
Portions of Proxy Statement for Annual Meeting of Shareholders to be held April 25, 2019 are incorporated by reference into Part III.

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BANNER CORPORATION AND SUBSIDIARIES

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Forward-Looking Statements

Certain matters in this Form 10-K constitute forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. These statements relate to our financial condition, liquidity, results of operations, plans, objectives, future performance or business. Forward-looking statements are not statements of historical fact, are based on certain assumptions and are generally identified by use of the words “believes,” “expects,” “anticipates,” “estimates,” “forecasts,” “intends,” “plans,” “targets,” “potentially,” “probably,” “projects,” “outlook” or similar expressions o conditional verbs such as “may,” “will,” “should,” “would” and “could.” Forward-looking statements include statements with respect to our beliefs, plans, objectives, goals, expectations, assumptions and statements about future economic performance and projections of financial items. These forward-looking statements are subject to known and unknown risks, uncertainties and other factors that could cause actual results to differ materially from the results anticipated or implied by our forward-looking statements, including, but not limited to: expected revenues, cost savings, synergies and other benefits from the merger of Banner and Skagit Bancorp, Inc. (Skagit) might not be realized within the expected time frames or at all and costs or difficulties relating to integration matters, including but not limited to customer and employee retention, might be greater than expected; the credit risks of lending activities, including changes in the level and trend of loan delinquencies and write-offs and changes in estimates of adequacy of the allowance for loan losses and provisions for loan losses that may be impacted by deterioration in the housing and commercial real estate markets and may lead to increased losses and non-performing assets, and may result in the allowance for loan losses not being adequate to cover actual losses and require a material increase in reserves; results of examinations by regulatory authorities, including the possibility that any such regulatory authority may, among other things, require the writing down of assets or increases in the allowance for loan losses; the ability to manage loan delinquency rates; competitive pressures among financial services companies; changes in consumer spending or borrowing and spending habits; interest rate movements generally and the relative differences between short and long-term interest rates, loan and deposit interest rates, net interest margin and funding sources; the impact of repricing and competitors' pricing initiatives on loan and deposit products; fluctuations in the demand for loans, the number of unsold homes, land and other properties and fluctuations in real estate values; the ability to adapt successfully to technological changes to meet customers' needs and developments in the marketplace; the ability to access cost-effective funding; increases in premiums for deposit insurance; the ability to control operating costs and expenses; the use of estimates in determining fair value of certain assets and liabilities which estimates may prove to be incorrect and result in significant changes in valuation; staffing fluctuations in response to product demand or the implementation of corporate strategies that affect employees, and potential associated charges; disruptions, security breaches or other adverse events, failures or interruptions in, or attacks on information technology systems or on the third-party vendors who perform critical processing functions; changes in financial markets; changes in economic conditions in general and in Washington, Idaho, Oregon and California in particular; secondary market conditions for loans and the ability to originate loans for sale and sell loans in the secondary market; the costs effects and outcomes of litigation; legislation or regulatory changes or reforms, including changes in regulatory policies and principles, or the interpretation of regulatory capital or other rules, including changes related to Basel III; the impact of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 and the implementing regulations; results of safety and soundness and compliance examinations by the Board of Governors of the Federal Reserve System (the Federal Reserve), the Federal Deposit Insurance Corporation (the FDIC), the Washington State Department of Financial Institutions, Division of Banks (the Washington DFI) or other regulatory authorities, including the possibility that any such regulatory authority may, among other things, require restitution or institute an informal or formal enforcement action which could require an increase in reserves for loan losses, write-downs of assets, or changes in regulatory capital position or affect the ability to borrow funds, or maintain or increase deposits, or impose additional requirements and restrictions, any of which could adversely affect liquidity and earnings; the availability of resources to address changes in laws, rules, or regulations or to respond to regulatory actions; adverse changes in the securities markets; the inability of key third-party providers to perform their obligations; changes in accounting principles, policies or guidelines, including additional guidance and interpretation on accounting issues and details of the implementation of new accounting methods; the economic impact of war or any terrorist activities; other economic, competitive, governmental, regulatory, and technological factors affecting our operations, pricing, products and services; future acquisitions by Banner of other depository institutions or lines of business; and future goodwill impairment due to changes in Banner's business, changes in market conditions, or other factors; and other risks detailed from time to time in our filings with the U.S. Securities and Exchange Commission (SEC), including this report on Form 10-K. Any forward-looking statements are based upon management's beliefs and assumptions at the time they are made. We do not undertake and specifically disclaim any obligation to update any forward-looking statements included in this report or the reasons why actual results could differ from those contained in such statements, whether as a result of new information, future events or otherwise. These risks could cause our actual results to differ materially from those expressed in any forward-looking statements by, or on behalf of, us. In light of these risks, uncertainties and assumptions, the forward-looking statements discussed in this report might not occur, and you should not put undue reliance on any forward-looking statements.

As used throughout this report, the terms "we," "our," "us," or the "Company" refer to Banner Corporation and its consolidated subsidiaries, unless the context otherwise requires. All references to "Banner" refer to Banner Corporation and those to "the Banks" refer to its wholly-owned subsidiaries, Banner Bank and Islanders Bank, collectively.

PART 1

Item 1 – Business General

Banner Corporation (the Company) is a bank holding company incorporated in the State of Washington. We are primarily engaged in the business of planning, directing and coordinating the business activities of our wholly-owned subsidiaries, Banner Bank and Islanders Bank. Banner Bank is a Washington-chartered commercial bank that conducts business from its main office in Walla Walla, Washington and, as of December 31, 2018, its 179 branch offices located in Washington, Oregon, California and Idaho. Banner Bank also has 17 loan production offices located in Washington, Oregon, California, Idaho and Utah. Islanders Bank is also a Washington-chartered commercial bank that conducts business from three locations in San Juan County, Washington. Banner Corporation is subject to regulation by the Federal Reserve. Banner Bank and Islanders Bank (the Banks) are subject to regulation by the Washington DFI and the FDIC. As of December 31, 2018, we had total consolidated assets of $11.87 billion, net loans of $8.59 billion, total deposits of $9.48 billion and total shareholders' equity of $1.48 billion. Our voting common stock is traded on the NASDAQ Global Select Market under the ticker symbol "BANR."

Banner Bank is a regional bank which offers a wide variety of commercial banking services and financial products to individuals, businesses and public sector entities in its primary market areas. Islanders Bank is a community bank which offers similar banking services to individuals, businesses and public entities located primarily in the San Juan Islands. The Banks' primary business is that of traditional banking institutions, accepting deposits and originating loans in locations surrounding our offices in portions of Washington, Oregon, California and Idaho. Banner Bank is also an active participant in the secondary market, engaging in mortgage banking operations largely through the origination and sale of one- to four-family and multi-family residential loans. Lending activities include commercial business and commercial real estate loans, agriculture business loans, construction and land development loans, one- to four-family residential loans, small business administration (SBA) loans and consumer loans.

We continue to invest significantly in our delivery platform across the franchise with a primary emphasis on strengthening our presence in the higher growth regions of our markets including Puget Sound, greater Portland, Boise, Sacramento and Southern California. Recently, our acquisition activity included the acquisition of Skagit Bancorp, Inc. (Skagit), the holding company for Skagit Bank in 2018 which has strengthened our market presence along the I-5 corridor between Seattle and the Canadian border. The acquisition of Skagit, which closed on November 1, 2018, included 11 branches and approximately $915.8 million in assets, $632.4 million in loans and $810.2 million in deposits. In addition to our expansion efforts, we continue to improve the efficiency of our branch delivery channel with on-going branch consolidations and relocations and investments in streamlining the origination of new loan and deposit accounts.

In addition to bank acquisitions, relocations and consolidations, we also have focused on expanding our product offerings and invested heavily in marketing campaigns designed to significantly increase the brand awareness for Banner Bank. These investments have been significant elements in our strategy to grow customer relationships and have increased our market presence, allowing us to better serve existing and future customers. This has resulted in an elevated level of non-interest expense; however, we believe our branch network, broader product line and heightened brand awareness have created a franchise that is well positioned for growth and is allowing us to successfully execute on our super community bank model. That strategy is focused on delivering customers, including middle market and small businesses, business owners, their families and employees, a compelling value proposition by providing the financial sophistication and breadth of products of a regional bank while retaining the appeal, responsiveness, and superior service level of a community bank.

Banner Corporation's successful execution of its strategic initiatives and its super community bank model have delivered sustainable growth and solid profitability. We have made substantial progress on our goals to achieve and maintain the Company's moderate risk profile as well as to develop and continue strong earnings momentum. Highlights of this success have included continued strong asset quality, new client acquisitions, significantly increased non-interest-bearing deposit balances and strong revenue generation from core operations.

For the year ended December 31, 2018, our net income increased to $136.5 million, or $4.15 earnings per diluted share, compared to $60.8 million, or $1.84 earnings per diluted share, for the prior year. The prior year's net income was negatively impacted by a $42.6 million, or $1.29 per diluted share, revaluation of our net deferred tax asset as a result of the enactment of the Tax Cuts and Jobs Act (2017 Tax Act) in December 2017, which reduced the marginal federal corporate income tax rate from 35% to 21%. Current year results were positively impacted by growth in earnings assets, partially offset by acquisition-related expenses of $5.6 million in 2018. Banner had no acquisition-related expenses in 2017.

Our operating results depend primarily on our net interest income, which is the difference between interest income on interest-earning assets, consisting of loans and investment securities, and interest expense on interest-bearing liabilities, composed primarily of customer deposits, Federal Home Loan Bank of Des Moines (FHLB) advances, other borrowings and junior subordinated debentures. Net interest income is primarily a function of our interest rate spread, which is the difference between the yield earned on interest-earning assets and the rate paid on interest-bearing liabilities, as well as a function of the average balances of interest-earning assets, interest-bearing liabilities, and non-interest-bearing funding sources including non-interest-bearing deposits. Our net interest income before provision for loan losses increased 10% to $431.0 million for the year ended December 31, 2018, compared to $393.0 million for the year ended December 31, 2017. The increase in net interest income in 2018 was driven by renewed growth in interest-earning assets subsequent to the balance sheet restructuring carried out in the fourth quarter of 2017 to remain below $10.0 billion in assets at December 31, 2017. Remaining below $10.0 billion at year end 2017 had the beneficial effect of delaying the adverse impact from certain enhanced regulatory requirements and the Durbin Amendment cap on interchange revenues. For additional information regarding these regulatory consequences, see Item 1A, Risk Factors, "We may be subject to additional regulatory scrutiny since Banner Bank maintains total assets exceeding $10.0 billion."

Our net income also is affected by the level of our non-interest income, including deposit fees and service charges, results of mortgage banking operations, which includes loan origination and servicing fees and gains and losses on the sale of one- to four-family and multifamily loans, and gains and losses on the sale of securities, as well as our non-interest expenses, provisions for loan losses and income tax provisions. In addition, net income is affected by the net change in the value of certain financial instruments carried at fair value.

Our total revenues (net interest income before the provision for loan losses plus non-interest income) for 2018 increased $36.7 million, or 8%, to $515.0 million, compared to $478.2 million for 2017. Our total non-interest income, which is a component of total revenue and includes the net gain on sale of securities, changes in the value of financial instruments carried at fair value and gain on sale of branches including related loans and deposits, was $84.0 million for the year ended December 31, 2018, compared to $85.2 million for the year ended December 31, 2017. The year ended December 31, 2017 included a $12.2 million net gain on the sale of seven Utah branches including the related loans and deposits (the Utah Branch Sale).

Although our credit quality metrics continue to reflect our moderate risk profile, we recorded an $8.5 million provision for loan losses in the year ended December 31, 2018, primarily due to the organic growth in the loan portfolio, the renewal of acquired loans out of the discounted loan portfolios and net charge-offs, compared to an $8.0 million provision recorded in 2017. Non-performing loans decreased to $15.7 million at December 31, 2018, compared to $27.0 million a year earlier. Our allowance for loan losses at December 31, 2018 was $96.5 million, or 1.11% of total loans outstanding and 616% of non-performing loans. (See Note 5, Loans Receivable and the Allowance for Loan Losses, of the Notes to the Consolidated Financial Statements as well as “Asset Quality” below.)

Our non-interest expense increased 7% to $341.4 million for the year ended December 31, 2018, compared to $319.0 million for the year ended December 31, 2017. The year-over-year increase in non-interest expense was largely attributable to increased salary and employee benefits as compared to a year ago largely due to inclusion of the acquired Skagit operations for the last two months of 2018, and enhanced regulatory requirements attributable to compliance and risk management infrastructure build-out along with acquisition-related costs incurred in 2018.

Recent Developments and Significant Events

Acquisition of Skagit Bancorp, Inc.

Effective November 1, 2018, the Company acquired 100% of the outstanding common shares of Skagit and its wholly-owned subsidiary, Skagit Bank, a Washington State chartered commercial bank headquartered in Burlington, Washington, with 11 branches serving markets along the I-5 corridor from Seattle to the Canadian border. On that date, Skagit merged with and into Banner and Skagit Bank merged with and into Banner Bank. Pursuant to the previously announced terms of the merger, the equity holders of Skagit received an aggregate of 3.1 million shares of Banner voting common stock, plus cash in lieu of fractional shares and cash to buy out Skagit stock options for a total consideration paid of $180.0 million. The acquisition provided $915.8 million in assets, $632.4 million in loans and $810.2 million in deposits. See Note 3 of the Notes to the Consolidated Financial Statements for additional information.

Sale of Utah Branches

On October 6, 2017, Banner Bank completed the sale of its Utah branches and related assets and liabilities to People’s Intermountain Bank, a banking subsidiary of People’s Utah Bancorp (NASDAQ: PUB).

Under the terms of the purchase and assumption agreement, the sale included $253.8 million in loans, $160.3 million in deposits and all of Banner Bank's seven Utah branches, located in Provo, Orem, Salem, Springville, South Jordan, Salt Lake City and Woods Cross. The sale also included $4.0 million of property and equipment and $581,000 of accrued interest. In addition, Banner allocated an associated $1.9 million of goodwill and $1.1 million of other intangible assets with the divestiture, which constituted the disposal of a business. The deposit premium paid to Banner was $13.8 million based on average daily deposits for a period prior to closing. The net gain recorded on the Utah Branch Sale was $12.2 million.

Lending Activities

General: All of our lending activities are conducted through Banner Bank, its subsidiary, Community Financial Corporation, a residential construction lender located in Portland, Oregon, and Islanders Bank. We offer a wide range of loan products to meet the demands of our customers and our loan portfolio is very diversified by product type, borrower and geographic location within our market area. We originate loans for our own loan portfolio and for sale in the secondary market. Management's strategy has been to maintain a well-diversified portfolio with a significant percentage of assets in the loan portfolio having more frequent interest rate repricing terms or shorter maturities than traditional long-term fixed-rate mortgage loans. As part of this effort, we offer a variety of floating or adjustable interest rate products that correlate more closely with our cost of interest-bearing funds, particularly loans for commercial business and real estate, agricultural business, and construction and development purposes. However, in response to customer demand, we continue to originate fixed-rate loans, including fixed interest rate mortgage loans with terms of up to 30 years. The relative amount of fixed-rate loans and adjustable-rate loans that can be originated at any time is largely determined by the demand for each in a competitive environment. At December 31, 2018, our net loan portfolio totaled $8.59 billion compared to $7.51 billion at December 31, 2017.

Our lending activities are primarily directed toward the origination of real estate and commercial loans. Commercial real estate loans include owner-occupied, investment properties and multifamily residential real estate. Although our level of activity and investment in commercial real estate loans has been relatively stable for many years, we have experienced an increase in new originations in recent periods. We also originate construction, land and land development loans, a significant component of which is our residential one- to four-family construction loans. Originations of one- to four-family construction loans have increased in recent years as builders have expanded production and experienced strong sales in many of the markets we serve. Our origination of construction and development loans has been significant during this period and balances in this portion of the portfolio have increased in recent periods but not at the same pace of originations as brisk sales of new homes have produced rapid turnover through repayments. Our commercial business lending is directed toward meeting the credit and related deposit and treasury management needs of various small- to medium-sized business and agribusiness borrowers operating in our primary market areas. In recent years, our commercial business lending has also included participation in certain national syndicated loans. Reflecting the expanding economy of the western United States, demand for these types of commercial business loans has strengthened and our production levels have increased in recent periods. Our residential mortgage loan originations have been relatively strong in recent years, as exceptionally low interest rates have supported demand for loans to refinance existing debt as well as loans to finance home purchases; however, increases in market interest rates over the last year reduced residential mortgage loan originations in 2018. Most of the one- to four-family loans that we originate are sold in the secondary markets with net gains on sales and loan servicing fees reflected in our revenues from mortgage banking. Our consumer loan activity is primarily directed at meeting demand from our existing deposit customers. We have increased our emphasis on consumer lending in recent years primarily related to increased home equity lines of credit.

For additional information concerning our loan portfolio, see Item 7 of this report, “Management’s Discussion and Analysis of Financial Condition and Results of Operations—Comparison of Financial Condition at December 31, 2018 and 2017—Loans and Lending” including Tables 4 and 5, which sets forth the composition and geographic concentration of our loan portfolio, and Tables 6 and 7, which contain information regarding the loans maturing in our portfolio.

One- to Four-Family Residential Real Estate Lending: At both Banner Bank and Islanders Bank, we originate loans secured by first mortgages on one- to four-family residences in the markets we serve. Through our mortgage banking activities, we sell residential loans on either a servicing-retained or servicing-released basis. In recent years, we have generally sold a significant portion of our conventional residential mortgage originations and nearly all of our government insured loans in the secondary market. At December 31, 2018, $973.6 million, or 11% of our loan portfolio, consisted of permanent loans on one- to four-family residences.

We offer fixed- and adjustable-rate mortgages (ARMs) at rates and terms competitive with market conditions, primarily with the intent of selling these loans into the secondary market. Fixed-rate loans generally are offered on a fully amortizing basis for terms ranging from 10 to 30 years at interest rates and fees that reflect current secondary market pricing. Most ARM products offered adjust annually after an initial period ranging from one to five years, subject to a limitation on the annual adjustment and a lifetime rate cap. For a small portion of the portfolio, where the initial period exceeds one year, the first interest rate change may exceed the annual limitation on subsequent adjustments. Our ARM products most frequently adjust based upon the average yield on Treasury securities adjusted to a constant maturity of one year or certain London Interbank Offered Rate (LIBOR) indices plus a margin or spread above the index. ARM loans held in our portfolio may allow for interest-only payments for an initial period up to five years but do not provide for negative amortization of principal and carry no prepayment restrictions. The retention of ARM loans in our loan portfolio can help reduce our exposure to changes in interest rates. However, borrower demand for ARM loans versus fixed-rate mortgage loans is a function of the level of interest rates, the expectations of changes in the level of interest rates and the difference between the initial interest rates and fees charged for each type of loan. In recent years, borrower demand for ARM loans has been limited and we have chosen not to aggressively pursue ARM loans by offering minimally profitable, deeply discounted teaser rates or option-payment ARM products. As a result, ARM loans have represented only a small portion of our loans originated during recent periods.

Our residential loans are generally underwritten and documented in accordance with the guidelines established by the Federal Home Loan Mortgage Corporation (Freddie Mac or FHLMC) and the Federal National Mortgage Association (Fannie Mae or FNMA). Government insured loans are underwritten and documented in accordance with the guidelines established by the Department of Housing and Urban Development (HUD) and the Veterans Administration (VA). In the loan approval process, we assess the borrower's ability to repay the loan, the adequacy of the proposed security, the employment stability of the borrower and the creditworthiness of the borrower. For ARM loans, our standard practice provides for underwriting based upon fully indexed interest rates and payments. Generally, we will lend up to 95% of the lesser of the appraised value or purchase price of the property on conventional loans, although higher loan-to-value ratios are available on secondary market programs. We require private mortgage insurance on conventional residential loans with a loan-to-value ratio at origination exceeding 80%.

Construction and Land Lending: Historically, we have invested a significant portion of our loan portfolio in residential construction and land loans to professional home builders and developers. We also make construction loans to qualified owner occupants, which upon completion of the construction phase convert to long-term amortizing one- to four-family residential loans that are eligible for sale in the secondary market. We regularly monitor our construction and land loan portfolios and the economic conditions and housing inventory in each of our markets and increase or decrease this type of lending as we observe market conditions change. Our residential construction and land and land development lending has been recently increasing in select markets and has made a meaningful contribution to our net interest income and profitability. To a lesser extent, we also originate construction loans for commercial and multifamily real estate. Although well diversified with respect to sub-markets, price ranges and borrowers, our construction, land and land development loans are significantly concentrated in the greater Puget Sound region of Washington State and the Portland, Oregon market area. At December 31, 2018, construction, land and land development loans totaled $1.11 billion, or 13% of total loans; 65% of the balance was comprised of one- to four-family construction and residential land and land development loans, with the remaining balance comprised of commercial and multifamily real estate construction loans and commercial land or land development loans.

Construction and land lending affords us the opportunity to achieve higher interest rates and fees with shorter terms to maturity than are usually available on other types of lending. Construction and land lending, however, involves a higher degree of risk than other lending opportunities. We attempt to address these risks by adhering to strict underwriting policies, disbursement procedures and monitoring practices. For additional information concerning the risks associated with Construction and land lending, see Item 1A., "Risk Factors—Our loan portfolio includes loans with a higher risk of loss."

On a more limited basis, we also make land loans to developers, builders and individuals to finance the acquisition and/or development of improved lots or unimproved land. In making land loans, we follow underwriting policies and disbursement and monitoring procedures similar to those for construction loans. The initial term on land loans is typically one to three years with interest only payments, payable monthly, and provisions for principal reduction as lots are sold and released from the lien of the mortgage.

Commercial and Multifamily Real Estate Lending: We originate loans secured by multifamily and commercial real estate, including loans for construction of multifamily and commercial real estate projects. Commercial real estate loans are made for both owner-occupied and investor- owned properties. At December 31, 2018, our loan portfolio included $2.13 billion in non-owner-occupied commercial real estate loans, $1.43 billion in owner-occupied commercial real estate loans and $368.8 million in multifamily loans which in aggregate comprised 45% of our total loans. Multifamily and commercial real estate lending affords us an opportunity to receive interest at rates higher than those generally available from one- to four-family residential lending. In originating multifamily and commercial real estate loans, we consider the location, marketability and overall attractiveness of the properties. Our underwriting guidelines for multifamily and commercial real estate loans require an appraisal from a qualified independent appraiser and an economic analysis of each property with regard to the annual revenue and expenses, debt service coverage and fair value to determine the maximum loan amount. In the approval process we assess the borrowers' willingness and ability to manage the property and repay the loan and the adequacy of the collateral in relation to the loan amount. For information concerning the risks associated with commercial and multifamily real estate lending, see Item 1A., "Risk Factors—Our loan portfolio includes loans with a higher risk of loss."

Multifamily and commercial real estate loans originated by us are both fixed- and adjustable-rate loans with intermediate terms of generally five to ten years. A significant portion of our multifamily and commercial real estate loans are linked to various FHLB advance rates, certain prime rates, US Treasury rates, or other market rate indices. Rates on these adjustable-rate loans generally adjust with a frequency of one to five years after an initial fixed-rate period ranging from one to ten years. Our commercial real estate portfolio consists of loans on a variety of property types with no large concentrations by property type, location or borrower. At December 31, 2018, the average size of our commercial real estate loans was $657,000 and the largest commercial real estate loan, in terms of an outstanding balance, in our portfolio was approximately $16.4 million.

Commercial Business Lending: We are active in small- to medium-sized business lending and are engaged in agricultural lending primarily by providing crop production loans. Our commercial bankers are focused on local markets and devote a great deal of effort to developing customer relationships and providing these types of borrowers with a full array of products and services delivered in a thorough and responsive manner. Our experienced commercial bankers and senior credit staff help us meet our commitment to small business lending while also focusing on corporate lending opportunities for borrowers with credit needs generally in a $3 million to $25 million range. In addition to providing earning assets, commercial business lending has helped us increase our deposit base. In recent years, our commercial business lending has included modest participation in certain national syndicated loans, including shared national credits. We also originate smaller balance business loans principally through our retail branch network, using our Quick Step business loan program, which is closely aligned with our consumer lending operations and relies on centralized underwriting procedures. Quick Step business loans and lines of credit are available from $5,000 to $500,000 and owner-occupied real estate loans are available up to $1.0 million.

Commercial business loans may entail greater risk than other types of loans. Commercial business loans generally provide higher yields or related revenue opportunities than many other types of loans but also require more administrative and management attention. Loan terms, including the fixed or adjustable interest rate, the loan maturity and the collateral considerations, vary significantly and are negotiated on an individual loan basis. For information concerning the risks associated with commercial business lending, see Item 1A., "Risk Factors—Our loan portfolio includes loans with a higher risk of loss."

We underwrite our commercial business loans on the basis of the borrower's cash flow and ability to service the debt from earnings rather than on the basis of the underlying collateral value. We seek to structure these loans so that they have more than one source of repayment. The borrower is required to provide us with sufficient information to allow us to make a prudent lending determination. In most instances, this information consists of at least three years of financial statements, tax returns, a statement of projected cash flows, current financial information on any guarantor and information about the collateral. Loans to closely held businesses typically require personal guarantees by the principals. Our commercial business loan portfolio is geographically dispersed across the market areas serviced by our branch network and there are no significant concentrations by industry or products.

Our commercial business loans may be structured as term loans or as lines of credit. Commercial business term loans are generally made to finance the purchase of fixed assets and have maturities of five years or less. Commercial business lines of credit are typically made for the purpose of providing working capital and are usually approved with a term of one year. Adjustable- or floating-rate loans are primarily tied to various prime rate or LIBOR indices. At December 31, 2018, commercial business loans totaled $1.48 billion, or 17% of our total loans, including $149.2 million of shared national credits.

Agricultural Lending: Agriculture is a major industry in several of our markets. We make agricultural loans to borrowers with a strong capital base, sufficient management depth, proven ability to operate through agricultural cycles, reliable cash flows and adequate financial reporting. Payments on agricultural loans depend, to a large degree, on the results of operations of the related farm entity. The repayment is also subject to other economic and weather conditions as well as market prices for agricultural products, which can be highly volatile. At December 31, 2018, agricultural business loans, including collateral secured loans to purchase farm land and equipment, totaled $404.9 million, or 5% of our loan portfolio.

Agricultural operating loans generally are made as a percentage of the borrower's anticipated income to support budgeted operating expenses. These loans are secured by a blanket lien on all crops, livestock, equipment, accounts and products and proceeds thereof. In the case of crops, consideration is given to projected yields and prices from each commodity. The interest rate is normally floating based on the prime rate or a LIBOR index plus a negotiated margin. Because these loans are made to finance a farm or ranch's annual operations, they are usually written on a one-year review and renewable basis. The renewal is dependent upon the prior year's performance and the forthcoming year's projections as well as the overall financial strength of the borrower. We carefully monitor these loans and related variance reports on income and expenses compared to budget estimates. To meet the seasonal operating needs of a farm, borrowers may qualify for single payment notes, revolving lines of credit and/or non-revolving lines of credit.

In underwriting agricultural operating loans, we consider the cash flow of the borrower based upon the expected operating results as well as the value of collateral used to secure the loans. Collateral generally consists of cash crops produced by the farm, such as milk, grains, fruit, grass seed, peas, sugar beets, mint, onions, potatoes, corn and alfalfa or livestock. In addition to considering cash flow and obtaining a blanket security interest in the farm's cash crop, we may also collateralize an operating loan with the farm's operating equipment, breeding stock, real estate and federal agricultural program payments to the borrower.

We also originate loans to finance the purchase of farm equipment. Loans to purchase farm equipment are made for terms of up to seven years. On occasion, we also originate agricultural real estate loans secured primarily by first liens on farmland and improvements thereon located in our market areas, although generally only to service the needs of our existing customers. Loans are written in amounts ranging from 50% to 75% of the tax assessed or appraised value of the property for terms of five to 20 years. These loans generally have interest rates that adjust at least every five years based upon a Treasury index or FHLB advance rate plus a negotiated margin. Fixed-rate loans are granted on terms usually not to exceed five years. In originating agricultural real estate loans, we consider the debt service coverage of the borrower's cash flow, the appraised value of the underlying property, the experience and knowledge of the borrower, and the borrower's past performance with us and/or the market area. These loans normally are not made to start-up businesses and are reserved for existing customers with substantial equity and a proven history.

Among the more common risks to agricultural lending can be weather conditions and disease. These risks may be mitigated through multi-peril crop insurance. Commodity prices also present a risk, which may be reduced by the use of set price contracts. Normally, required beginning and projected operating margins provide for reasonable reserves to offset unexpected yield and price deficiencies. In addition to these risks, we also consider management succession, life insurance and business continuation plans when evaluating agricultural loans. For additional information concerning the risks associated with agricultural lending, see Item 1A., "Risk Factors—Our loan portfolio includes loans with a higher risk of loss."

Consumer and Other Lending: We originate a variety of consumer loans, including home equity lines of credit, automobile, boat and recreational vehicle loans and loans secured by deposit accounts. While consumer lending has traditionally been a small part of our business, with loans made primarily to accommodate our existing customer base, it has received consistent emphasis in recent years. Part of this emphasis includes a Banner Bank-owned credit card program. Similar to other consumer loan programs, we focus this credit card program on our existing customer base to add to the depth of our customer relationships. In addition to earning balances, credit card accounts produce non-interest revenues through interchange fees and other activity-based revenues. Our underwriting of consumer loans is focused on the borrower's credit history and ability to repay the debt as evidenced by documented sources of income. At December 31, 2018, we had $785.0 million, or 9% of our loan portfolio, in consumer related loans, including $569.0 million, or 7% of our loan portfolio, in consumer loans secured by one- to four-family residences. For information concerning the risks associated with consumer lending, see Item 1A., "Risk Factors—Our loan portfolio includes loans with a higher risk of loss."

Loan Solicitation and Processing: We originate real estate loans in our market areas by direct solicitation of real estate brokers, builders, developers, depositors, walk-in customers and visitors to our Internet website. One- to four-family residential loan applications are taken by our mortgage loan officers or through our Internet website and are processed in branch or regional locations. In addition, we have specialized loan origination units, focused on construction and land development, commercial real estate and multifamily loans. Most underwriting and loan administration functions for our real estate loans are performed by loan personnel at central locations.

In addition to commercial real estate loans, our commercial bankers solicit commercial and agricultural business loans through call programs focused on local businesses and farmers. While commercial bankers are delegated reasonable commitment authority based upon their qualifications, credit decisions on significant commercial and agricultural loans are made by senior loan officers or in certain instances by the Board of Directors of Banner Bank and Islanders Bank.

We originate consumer loans and small business (including Quick Step) commercial business loans through various marketing efforts directed primarily toward our existing deposit and loan customers. Consumer loans and Quick Step commercial business loan applications are primarily underwritten and documented by centralized administrative personnel.

Loan Originations, Sales and Purchases

While we originate a variety of loans, our ability to originate each type of loan is dependent upon the relative customer demand and competition in each market we serve. For the years ended December 31, 2018 and 2017, we originated loans, net of repayments, including our participation in syndicated loans and loans held for sale of $1.31 billion and $1.1 billion, respectively. For additional information concerning origination of portfolio loans by type, see Item 7 in this report, "Management's Discussion and Analysis of Financial Condition—Comparison of Financial Condition at December 31, 2018 and 2017—Loans and Lending," and Table 3 contained therein.

We sell many of our newly originated one- to four-family residential mortgage loans and multifamily loans to secondary market purchasers as part of our interest rate risk management strategy. Originations of loans for sale increased to $896.5 million for the year ended December 31, 2018 from $807.1 million during 2017. Originations of loans for sale included $372.8 million and $292.3 million of multifamily held for sale loan production for the years ended December 31, 2018 and December 31, 2017, respectively. Sales of loans generally are beneficial to us because these sales may generate income at the time of sale, provide funds for additional lending and other investments, increase liquidity or reduce interest rate risk. During the year ended December 31, 2018, we sold $781.9 million of loans held for sale compared to $1.03 billion for the year ended December 31, 2017. The held for sale loans sold in 2018 and 2017 included $256.5 million and $475.7 million, respectively, of multifamily loans held for sale. In addition, we sold $2.5 million of portfolio multifamily loans in 2017, while no portfolio multifamily loans were sold in 2018. We sell loans on both a servicing-retained and a servicing-released basis. All loans are sold without recourse. The decision to hold or sell loans is based on asset liability management goals, strategies and policies and on market conditions. For additional information, see "Loan Servicing."

We periodically purchase whole loans and loan participation interests or participate in syndicates originating new loans, including shared national credits, primarily during periods of reduced loan demand in our primary market area and at times to support our Community Reinvestment Act lending activities. Any such purchases or loan participations are generally made on terms consistent with our underwriting standards; however, the loans may be located outside of our normal lending area. During the years ended December 31, 2018 and 2017, we purchased $33.7 million and $126.5 million, respectively, of loans and loan participation interests, principally commercial real estate loans.

Loan Servicing

We receive fees from a variety of institutional owners in return for performing the traditional services of collecting individual payments and managing portfolios of sold loans. At December 31, 2018, we were servicing $2.81 billion of loans for others. Loan servicing includes processing payments, accounting for loan funds and collecting and paying real estate taxes, hazard insurance and other loan-related items such as private mortgage insurance. In addition to earning fee income, we retain certain amounts in escrow for the benefit of the lender for which we incur no interest expense but are able to invest the funds into earning assets.

Mortgage Servicing Rights: We record mortgage servicing rights (MSRs) with respect to loans we originate and sell in the secondary market on a servicing-retained basis. The value of MSRs is capitalized and amortized in proportion to, and over the period of, the estimated future net servicing income. Management periodically evaluates the estimates and assumptions used to determine the carrying values of MSRs and the amortization of MSRs. MSRs generally are adversely affected by higher levels of current or anticipated prepayments resulting from decreasing interest rates. MSRs are evaluated for impairment based upon the fair value of the rights as compared to amortized cost. Impairment is recognized through a valuation allowance, to the extent that fair value is less than the capitalized carrying amount. At December 31, 2018, our MSRs were carried at a value of $14.6 million, net of amortization. For additional information see Note 17, Goodwill, Other Intangible Assets and Mortgage Servicing Rights, of the Notes to the Consolidated Financial Statements.

Asset Quality

Classified Assets: State and federal regulations require that the Banks review and classify their problem assets on a regular basis. In addition, in connection with examinations of insured institutions, state and federal examiners have authority to identify problem assets and, if appropriate, require them to be classified. Historically, we have not had any meaningful differences of opinion with the examiners with respect to asset classification. Banner Bank's Credit Policy Division reviews detailed information with respect to the composition and performance of the loan portfolios, including information on risk concentrations, delinquencies and classified assets for both Banner Bank and Islanders Bank. The Credit Policy Division approves all recommendations for new classified loans or, in the case of smaller-balance homogeneous loans including residential real estate and consumer loans, it has approved policies governing such classifications, or changes in classifications, and develops and monitors action plans to resolve the problems associated with the assets. The Credit Policy Division also approves recommendations for establishing the appropriate level of the allowance for loan losses. Significant problem loans are transferred to Banner Bank's Special Assets Department for resolution or collection activities. The Banks' and Banner Corporation's Boards of Directors are given a detailed report on classified assets and asset quality at least quarterly. For additional information regarding asset quality and non-performing loans, see Item 7 of this report, "Management's Discussion and Analysis of Financial Condition—Comparison of Financial Condition at December 31, 2018 and 2017—Asset Quality," and Table 12 contained therein.

Allowance for Loan Losses: In originating loans, we recognize that losses will be experienced and that the risk of loss will vary with, among other things, the type of loan being made, the creditworthiness of the borrower over the term of the loan, general economic conditions and, in the case of a secured loan, the quality of the security for the loan. As a result, we maintain an allowance for loan losses consistent with U.S. generally accepted accounting principles (GAAP) guidelines. We increase our allowance for loan losses by charging provisions for probable loan losses against our income. The allowance for loan losses is maintained at a level which, in management's judgment, is sufficient to provide for probable losses based on evaluating known and inherent risks in the loan portfolio and upon continuing analysis of the factors underlying the quality of the loan portfolio. In June 2016, Financial Accounting Standards Board issued ASU No. 2016-13, Measurement of Credit Losses on Financial Instruments, referred to as Current Expected Credit Loss, or CECL, that will be effective for Banner for our first fiscal year beginning after December 15, 2019. For additional information on CECL see Note 2, Accounting Standards Recently Issued or Adopted, of the Notes to the Consolidated Financial Statements. For additional information concerning our allowance for loan losses, see Item 7 of this report, “Management’s Discussion and Analysis of Financial Condition—Comparison of Results of Operations for the Years Ended December 31, 2018 and 2017—Provision and Allowance for Loan Losses,” and Tables 16 and 17 contained therein.

Real Estate Owned: Real estate owned (REO) is property acquired by foreclosure or receiving a deed in lieu of foreclosure, and is recorded at the estimated fair value of the property, less expected selling costs. Development and improvement costs relating to the property are capitalized to the extent they add value to the property. The carrying value of the property is periodically evaluated by management and, if necessary, allowances are established to reduce the carrying value to net realizable value. Gains or losses at the time the property is sold are credited or charged to operations in the period in which they are realized. The amounts we will ultimately recover from REO may differ substantially from the carrying value of the assets because of market factors beyond our control or because of changes in our strategies for recovering the investment. For additional information on REO, see Item 7 of this report, “Management’s Discussion and Analysis of Financial Condition—Comparison of Financial Condition at December 31, 2018 and 2017—Asset Quality” and Table 12 contained therein and Note 6, Real Estate Owned, Held for Sale, Net, of the Notes to the Consolidated Financial Statements.

Investment Activities

Investment Securities

Under Washington state law and FDIC regulation, banks are permitted to invest in various types of marketable securities. Authorized securities include but are not limited to Treasury obligations, securities of various federal agencies (including government-sponsored enterprises), mortgage-backed and asset-backed securities, certain certificates of deposit of insured banks and savings institutions, bankers’ acceptances, repurchase agreements, federal funds, commercial paper, corporate debt and equity securities and obligations of states and their political subdivisions. Our investment policies are designed to provide and maintain adequate liquidity and to generate favorable rates of return without incurring undue interest rate or credit risk. Our policies generally limit investments to U.S. Government and agency (including government-sponsored entities) securities, municipal bonds, certificates of deposit, corporate debt obligations and mortgage-backed securities. Investment in mortgage-backed securities may include those issued or guaranteed by Freddie Mac, Fannie Mae, Government National Mortgage Association (Ginnie Mae or GNMA) and investment grade privately-issued mortgage-backed securities, as well as collateralized mortgage obligations (CMOs). All of our investment securities, including those that have high credit ratings, are subject to market risk in so far as a change in market rates of interest or other conditions may cause a change in an investment’s earnings performance and/or market value.

At December 31, 2018, our consolidated investment portfolio totaled $1.90 billion and consisted principally of U.S. Government agency obligations, mortgage-backed securities, municipal bonds, corporate debt obligations, and asset-backed securities. From time to time, investment levels may be increased or decreased in order to manage balance sheet liquidity, interest rate risk, market risk and provide appropriate risk adjusted returns. The investment portfolio was increased in 2018 as a result of the Skagit acquisition along with the Company's renewed leveraging strategy as it crossed the $10 billion in total assets threshold.

For detailed information on our investment securities, see Item 7, “Management’s Discussion and Analysis of Financial Condition—Comparison of Financial Condition at December 31, 2018 and 2017—Investments,” and Tables 1 and 2 contained therein.

Derivatives

The Company, through its Banner Bank subsidiary, is party to various derivative instruments that are used for asset and liability management and customer financing needs. Derivative instruments are contracts between two or more parties that have a notional amount and an underlying variable, require no net investment and allow for the net settlement of positions. The notional amount serves as the basis for the payment provision of the contract and takes the form of units, such as shares or dollars. The underlying variable represents a specified interest rate, index, or other component. The interaction between the notional amount and the underlying variable determines the number of units to be exchanged between the parties and influences the market value of the derivative contract. We obtain dealer quotations to value our derivative contracts.

Our predominant derivative and hedging activities involve interest rate swaps related to certain term loans, interest rate lock commitments to borrowers, and forward sales contracts associated with mortgage banking activities. Generally, these instruments help us manage exposure to market risk and meet customer financing needs. Market risk represents the possibility that economic value or net interest income will be adversely affected by fluctuations in external factors such as market-driven interest rates and prices or other economic factors.

Derivatives Not Designated in Hedge Relationships

Interest Rate Swaps: Banner Bank uses an interest rate swap program for commercial loan customers, in which we provide the client with a variable rate loan and enter into an interest rate swap in which the client receives a fixed rate payment in exchange for a variable rate payment. We offset our risk exposure by entering into an offsetting interest rate swap with a dealer counterparty for the same notional amount and length of term as the client interest rate swap providing the dealer counterparty with a fixed rate payment in exchange for a variable rate payment. At December 31, 2018, Banner Bank had $272.4 million in notional amounts of these customer interest rate swaps outstanding that were not designated in hedge relationships, with an equal amount of offsetting third party swaps also in place. These swaps do not qualify as designated hedges; therefore, each swap is accounted for as a free standing derivative.

Mortgage Banking: In the normal course of business, the Company sells originated one- to four-family and multifamily mortgage loans into the secondary mortgage loan markets. During the period of loan origination and prior to the sale of the loans in the secondary market, the Company has exposure to movements in interest rates associated with written interest rate lock commitments with potential borrowers to originate one- to four-family loans that are intended to be sold and for closed one- to four-family and multifamily mortgage loans held for sale that are awaiting sale and delivery into the secondary market. The Company economically hedges the risk of changing interest rates associated with these mortgage loan commitments by entering into forward sales contracts to sell one- to four-family and multifamily mortgage loans or mortgage-backed securities to broker/dealers at specific prices and dates.
We are exposed to credit-related losses in the event of nonperformance by the counterparty to these agreements. Credit risk of the financial contract is controlled through the credit approval, limits, and monitoring procedures and we do not expect the counterparties to fail their obligations.
In connection with the interest rate swaps between Banner Bank and the dealer counterparties, the agreements contain a provision where if Banner Bank fails to maintain its status as a well/adequately capitalized institution, then the counterparty could terminate the derivative positions and Banner Bank would be required to settle its obligations. Similarly, we could be required to settle our obligations under certain of these agreements if specific regulatory events occur, such as a publicly issued prompt corrective action directive, cease and desist order, or a capital maintenance agreement that required Banner Bank to maintain a specific capital level. If we had breached any of these provisions at December 31, 2018 or 2017, we could have been required to settle our obligations under the agreements at the termination value. We generally post collateral against derivative liabilities in the form of government agency-issued bonds, mortgage-backed securities, or commercial mortgage-backed securities.
Derivative assets and liabilities are recorded at fair value on the balance sheet. Prior to 2018, the recorded derivative assets and liabilities on the balance sheet did not take into account the effects of master netting agreements. Master netting agreements allow us to settle all derivative contracts held with a single counterparty on a net basis and to offset net derivative positions with related collateral where applicable.

Derivatives Designated in Hedge Relationships

Our fixed-rate loans result in exposure to losses in value or net interest income as interest rates change. The risk management objective for hedging fixed-rate loans is to effectively convert the fixed rate received to a floating rate. Under a prior program that is now discontinued we hedged our exposure to changes in the fair value of certain fixed-rate loans through the use of interest rate swaps. As of December 31, 2018, Banner Bank was a party to $4.0 million in notional amounts of interest rate swaps designated in a hedge relationship. For a qualifying fair value hedge, changes in the value of the derivatives are recognized in current period earnings along with the corresponding changes in the fair value of the designated hedged item attributable to the risk being hedged.

Deposit Activities and Other Sources of Funds

General: Deposits, FHLB advances (or other borrowings) and loan repayments are our major sources of funds for lending and other investment purposes. Scheduled loan repayments are a relatively stable source of funds, while deposit inflows and outflows and loan prepayments are influenced by general economic, interest rate and money market conditions and may vary significantly. Borrowings may be used on a short-term basis to compensate for reductions in the availability of funds from other sources. Borrowings may also be used on a longer-term basis to fund loans and investments, as well as to manage interest rate risk.

We compete with other financial institutions and financial intermediaries in attracting deposits. There is strong competition for transaction balances and savings deposits from commercial banks, credit unions and non-bank corporations, such as securities brokerage companies, mutual funds and other diversified companies, some of which have nationwide networks of offices. Much of the focus of our acquisitions, branch relocations and renovation and advertising and marketing campaigns has been directed toward attracting additional deposit customer relationships and balances. In addition, our electronic and digital banking activities including debit card and automated teller machine (ATM) programs, on-line Internet banking services and, most recently, customer remote deposit and mobile banking capabilities are all directed at providing products and services that enhance customer relationships and result in growing deposit balances as well as fee income. Growing core deposits (non-interest-bearing checking and interest-bearing transaction and savings accounts) is a fundamental element of our business strategy. Core deposits were 86% of total deposits at December 31, 2018 compared to 88% a year earlier and 87% two years ago.

Deposit Accounts: We generally attract deposits from within our primary market areas by offering a broad selection of deposit instruments, including non-interest-bearing checking accounts, interest-bearing checking accounts, money market deposit accounts, regular savings accounts, certificates of deposit, treasury management services and retirement savings plans. Deposit account terms vary according to the minimum balance required, the time periods the funds must remain on deposit and the interest rate, among other factors. In determining the terms of deposit accounts, we consider current market interest rates, profitability to us, matching deposit and loan products and customer preferences and concerns. At December 31, 2018, we had $9.48 billion of deposits. For additional information concerning our deposit accounts, see Item 7 in this report, “Management’s Discussion and Analysis of Financial Condition—Comparison of Financial Condition at December 31, 2018 and 2017—Deposit Accounts,” including Table 8 contained therein, which sets forth the balances of deposits in the various types of accounts, and Table 9, which sets forth the amount of our certificates of deposit greater than $100,000 by time remaining until maturity as of December 31, 2018. In addition, see Note 8, Deposits of the Notes to the Consolidated Financial Statements.

Borrowings: While deposits are the primary source of funds for our lending and investment activities and for general business purposes, we also use borrowings to supplement our supply of lendable funds, to meet deposit withdrawal requirements and to more efficiently leverage our capital position. The FHLB serves as our primary borrowing source. The FHLB provides credit for member financial institutions such as Banner

Bank and Islanders Bank. As members, the Banks are required to own capital stock in the FHLB and are authorized to apply for advances on the security of that stock and certain of their mortgage loans and securities provided certain credit worthiness standards have been met. Limitations on the amount of advances are based on the financial condition of the member institution, the adequacy of collateral pledged to secure the credit, and FHLB stock ownership requirements. At December 31, 2018, we had $540.2 million of borrowings from the FHLB. At that date, Banner Bank was authorized by the FHLB to borrow up to $4.59 billion under a blanket floating lien security agreement, while Islanders Bank was approved to borrow up to $103.5 million under a similar agreement. The Federal Reserve Bank serves as an additional source of borrowing capacity. The Federal Reserve Bank provides credit based upon acceptable loan collateral, which includes certain loan types not eligible for pledging to the FHLB. At December 31, 2018, based upon our available unencumbered collateral, Banner Bank was eligible to borrow $1.15 billion from the Federal Reserve Bank, although at that date we had no funds borrowed under this arrangement. Although eligible to participate, Islanders Bank has not applied for approval to borrow from the Federal Reserve Bank. For additional information concerning our borrowings, see Item 7 in this report, "Management's Discussion and Analysis of Financial Condition—Comparison of Financial Condition at December 31, 2018 and 2017—Borrowings," and Table 11 contained therein, as well as Note 9, Advances from Federal Home Loan Bank of Des Moines and Note 10, Other Borrowings of the Notes to the Consolidated Financial Statements.

At December 31, 2018, Banner Bank had uncommitted federal funds line of credit agreements with other financial institutions totaling $110.0 million, while Islanders Bank had an uncommitted federal funds line of credit agreement with another financial institution totaling $5.0 million. No balances were outstanding under these agreements as of December 31, 2018. Availability of lines is subject to federal funds balances available for loan and continued borrower eligibility. These lines are intended to support short-term liquidity needs and the agreements may restrict consecutive day usage.

We issue retail repurchase agreements, generally due within 90 days, as an additional source of funds, primarily in connection with treasury management services provided to our larger deposit customers. At December 31, 2018, we had issued retail repurchase agreements totaling $119.0 million. We also may borrow funds through the use of secured wholesale repurchase agreements with securities brokers; at December 31, 2018, we had no borrowings outstanding under wholesale repurchase agreements. The retail and wholesale repurchase borrowings were secured by pledges of certain U.S. Government and agency notes and mortgage-backed securities with a market value of $154.0 million at December 31, 2018.

We have also issued $120.0 million of junior subordinated debentures in connection with the sale of trust preferred securities (TPS). The TPS were issued from 2002 through 2007 by special purpose business trusts formed by Banner Corporation and were sold in private offerings to pooled investment vehicles. In addition, Banner has $16.0 million of junior subordinated debentures that were acquired through acquisitions, for a total of $136.0 million in debentures at December 31, 2018. The junior subordinated debentures associated with the TPS have been recorded as liabilities and are reported at fair value on our Consolidated Statements of Financial Condition. As of December 31, 2018 the fair value of the junior subordinate debentures was $114.1 million. All of the debentures issued to the trusts, measured at their fair value, less the common stock of the trusts, qualified as Tier I capital as of December 31, 2018, under guidance issued by the Federal Reserve Board. We invested substantially all of the proceeds from the issuance of the TPS as additional paid in capital at Banner Bank. See Note 11, Junior Subordinated Debentures and Mandatorily Redeemable Trust Preferred Securities, of the Notes to the Consolidated Financial Statements.

Personnel

As of December 31, 2018, we had 2,187 full time equivalent employees. Banner Corporation has no employees except for those who are also employees of Banner Bank, its subsidiaries, and Islanders Bank. The employees are not represented by a collective bargaining unit. We believe our relationship with our employees is good.

Taxation

Tax-Sharing Agreement

Banner Corporation files its federal and state income tax returns on a consolidated basis under a tax-sharing agreement between the Company and each bank subsidiary. The Company prepares each subsidiary’s minimum income tax which would be required if the individual subsidiary were to file federal and state income tax returns as a separate entity. Each subsidiary pays to the Company an amount equal to the estimated income tax due if it were to file as a separate entity. The payment is made on or about the time the subsidiary would be required to make such tax payments to the United States Treasury or the applicable State Departments of Revenue. In the event the computation of the subsidiary’s federal or state income tax liability, after taking into account any estimated tax payments made, would result in a refund if the subsidiary were filing income tax returns as a separate entity, then the Company pays to the subsidiary an amount equal to the hypothetical refund. The Company is an agent for each subsidiary with respect to all matters related to the consolidated tax returns and refunds claims. If Banner's consolidated federal or state income tax liability is adjusted for any period, the liability of each party under the tax-sharing agreement is recomputed to give effect to such adjustments and any additional payments required as a result of the adjustments are made within a reasonable time after the corresponding additional tax payments are made or refunds are received.

Federal Taxation

General: For tax reporting purposes, we report our income on a calendar year basis using the accrual method of accounting on a consolidated basis. We are subject to federal income taxation in the same manner as other corporations with some exceptions, including particularly the reserve for bad debts. See Note 12, Income Taxes, of the Notes to the Consolidated Financial Statements for additional information concerning the income taxes payable by us.

State Taxation

Washington Taxation: We are subject to a Business and Occupation (B&O) tax which is imposed under Washington on gross receipts. Interest received on loans secured by mortgages or deeds of trust on residential properties, residential mortgage-backed securities, and certain U.S. Government and agency securities is not subject to this tax.

California, Oregon, Idaho, Montana and Utah Taxation: Corporations with nexus in the states of California, Oregon, Idaho, Montana and Utah are subject to a corporate level income tax. As our operations in these states increase, with the exception of our Utah operations which were sold in October 2017, the state income tax provision will have an increasing effect on our effective tax rate and results of operations.

Competition

We encounter significant competition both in attracting deposits and in originating loans. Our most direct competition for deposits comes from other commercial and savings banks, savings associations and credit unions with offices in our market areas. We also experience competition from securities firms, insurance companies, money market and mutual funds, and other investment vehicles. We expect continued strong competition from such financial institutions and investment vehicles in the foreseeable future, including competition from on-line Internet banking competitors and "FinTech" companies that rely on technology to provide financial services. Our ability to attract and retain deposits depends on our ability to provide transaction services and investment opportunities that satisfy the requirements of depositors. We compete for deposits by offering a variety of accounts and financial services, including electronic banking capabilities, with competitive rates and terms, at convenient locations and business hours, and delivered with a high level of personal service and expertise.

Competition for loans comes principally from other commercial banks, loan brokers, mortgage banking companies, savings banks and credit unions and for agricultural loans from the Farm Credit Administration. The competition for loans is intense as a result of the large number of institutions competing in our market areas. We compete for loans primarily by offering competitive rates and fees and providing timely decisions and excellent service to borrowers.

Regulation
Banner Bank and Islanders Bank

General: As state-chartered, federally insured commercial banks, Banner Bank and Islanders Bank (the Banks) are subject to extensive regulation and must comply with various statutory and regulatory requirements, including prescribed minimum capital standards. The Banks are regularly examined by the FDIC and the Washington DFI and file periodic reports concerning their activities and financial condition with these banking regulators. The Banks' relationship with depositors and borrowers also is regulated to a great extent by both federal and state law, especially in such matters as the ownership of deposit accounts and the form and content of mortgage and other loan documents.

Federal and state banking laws and regulations govern all areas of the operation of the Banks, including reserves, loans, investments, deposits, capital, issuance of securities, payment of dividends and establishment of branches. Federal and state bank regulatory agencies also have the general authority to limit the dividends paid by insured banks and bank holding companies if such payments should be deemed to constitute an unsafe and unsound practice and in other circumstances. The Federal Reserve and FDIC as the respective primary federal regulators of Banner Corporation and each of Banner Bank and Islanders Bank have authority to impose penalties, initiate civil and administrative actions and take other steps intended to prevent banks from engaging in unsafe or unsound practices.

The laws and regulations affecting banks and bank holding companies have changed significantly, particularly in connection with the enactment of The Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (Dodd-Frank Act). Among other changes, the Dodd-Frank Act established the Consumer Financial Protection Bureau (CFPB) as an independent bureau of the Federal Reserve. The CFPB assumed responsibility for the implementation of the federal financial consumer protection and fair lending laws and regulations and has authority to impose new requirements. Any change in applicable laws, regulations, or regulatory policies may have a material effect on our business, operations, and prospects. We cannot predict the nature or the extent of the effects on our business and earnings that any fiscal or monetary policies or new federal or state legislation may have in the future. For additional information concerning the Dodd-Frank Act and the CFPB, see Item 1A., “Risk Factors—We operate in a highly regulated environment and may be adversely affected by changes in federal and state laws and regulations that are expected to increase our costs of operation,” and “We will be subject to additional regulatory scrutiny since Banner Bank maintains total assets exceeding $10.0 billion.” We may also be affected by changes in accounting standards. See "2018 Reforms" below.

The following is a summary discussion of certain laws and regulations applicable to Banner and the Banks which is qualified in its entirety by reference to the actual laws and regulations.

State Regulation and Supervision: As a Washington state-chartered commercial bank with branches in the States of Washington, Oregon, Idaho and California, Banner Bank is subject not only to the applicable provisions of Washington law and regulations, but is also subject to Oregon, Idaho and California law and regulations. These state laws and regulations govern Banner Bank's ability to take deposits and pay interest thereon, to make loans on or invest in residential and other real estate, to make consumer loans, to invest in securities, to offer various banking services to its customers and to establish branch offices. In a similar fashion, Washington state laws and regulations for state-chartered commercial banks also apply to Islanders Bank.

Deposit Insurance: The Deposit Insurance Fund of the FDIC insures deposit accounts of each of the Banks up to $250,000 per separately insured deposit relationship category. As insurer, the FDIC imposes deposit insurance premiums and is authorized to conduct examinations of, and to require reporting by, FDIC-insured institutions.

Under the FDIC's rules the assessment base for a bank is equal to its total average consolidated assets less average tangible capital. As of December 31, 2018, assessment rates ranged from 3 to 30 basis points for all institutions, subject to adjustments for unsecured debt issued by the institution, unsecured debt issued by other FDIC-insured institutions, and brokered deposits held by the institution.
Under the current rules, when the reserve ratio for the prior assessment period is equal to, or greater than 2.0% and less than 2.5%, assessment rates will range from two basis points to 28 basis points and when the reserve ratio for the prior assessment period is greater than 2.5%, assessment rates will range from one basis point to 25 basis points (in each case subject to adjustments as described above for current rates). No institution may pay a dividend if it is in default on its federal deposit insurance assessment.
The FDIC conducts examinations of and requires reporting by state non-member banks, such as the Banks. The FDIC also may prohibit any insured institution from engaging in any activity determined by regulation or order to pose a serious risk to the deposit insurance fund.

The FDIC may terminate the deposit insurance of any insured depository institution if it determines after a hearing that the institution has engaged or is engaging in unsafe or unsound practices, is in an unsafe or unsound condition to continue operations, or has violated any applicable law, regulation, order or any condition imposed by an agreement with the FDIC. It also may suspend deposit insurance temporarily during the hearing process for the permanent termination of insurance if the institution has no tangible capital. If insurance of accounts is terminated, the accounts at the institution at the time of the termination, less subsequent withdrawals, shall continue to be insured for a period of six months to two years, as determined by the FDIC. Management is not aware of any existing circumstances which would result in termination of the deposit insurance of either Banner Bank or Islanders Bank.

Standards for Safety and Soundness: The federal banking regulatory agencies have prescribed, by regulation, guidelines for all insured depository institutions relating to internal controls, information systems and internal audit systems; loan documentation; credit underwriting; interest rate risk exposure; asset growth; asset quality; earnings; and compensation, fees and benefits. The guidelines set forth the safety and soundness standards that the federal banking agencies use to identify and address problems at insured depository institutions. Each insured depository institution must implement a comprehensive written information security program that includes administrative, technical, and physical safeguards appropriate to the institution's size and complexity and the nature and scope of its activities. The information security program must be designed to ensure the security and confidentiality of customer information, protect against any unanticipated threats or hazards to the security or integrity of such information, protect against unauthorized access to or use of such information that could result in substantial harm or inconvenience to any customer, and ensure the proper disposal of customer and consumer information. Each insured depository institution must also develop and implement a risk-based response program to address incidents of unauthorized access to customer information in customer information systems. If the FDIC determines that an institution fails to meet any of these guidelines, it may require an institution to submit to the FDIC an acceptable plan to achieve compliance.

Capital Requirements: Bank holding companies, such as Banner Corporation, and federally insured financial institutions, such as Banner Bank and Islanders Bank, are required to maintain a minimum level of regulatory capital.

Effective January 1, 2015 (with some changes transitioned into full effectiveness over several years), Banner Corporation and the Banks became subject to new capital regulations adopted by the Federal Reserve and the FDIC, which established minimum required ratios for common equity Tier 1 ("CET1") capital, Tier 1 capital, total capital and the leverage ratio; risk-weightings of certain assets and other items for purposes of the risk-based capital ratios, a required capital conservation buffer over the required capital ratios, and defined what qualifies as capital for purposes of meeting the capital requirements. These regulations implement the regulatory capital reforms required by the Dodd—Frank Act and the "Basel III" requirements.

Under the capital regulations, the minimum capital ratios are: (1) a CET1 capital ratio of 4.5% of risk-weighted assets; (2) a Tier 1 capital ratio of 6.0% of risk-weighted assets; (3) a total risk-based capital ratio of 8.0% of risk-weighted assets; and (4) a leverage ratio (the ratio of Tier 1 capital to average total consolidated assets) of 4.0%. CET1 generally consists of common stock; retained earnings; accumulated other comprehensive income ("AOCI") unless an institution elects to exclude AOCI from regulatory capital; and certain minority interests; all subject to applicable regulatory adjustments and deductions. Tier 1 capital generally consists of CET1 and noncumulative perpetual preferred stock. Tier 2 capital generally consists of other preferred stock and subordinated debt meeting certain conditions plus an amount of the allowance for loan and lease losses up to 1.25% of assets. Total capital is the sum of Tier 1 and Tier 2 capital.

There were a number of changes in what constitutes regulatory capital compared to the rules in effect prior to January 1, 2015, some of which are subject to transition periods. These changes include the phasing-out of certain instruments as qualifying capital and eliminate or significantly reduce the use of hybrid capital instruments, especially trust preferred securities, as regulatory capital. Trust preferred securities issued by a company, such as the Company, with total consolidated assets of less than $15 billion before May 19, 2010 and treated as regulatory capital are grandfathered, but any such securities issued later are not eligible as regulatory capital under the current regulations. If an institution grows above $15 billion as a result of an acquisition, the trust preferred securities are excluded from Tier 1 capital and instead included in Tier 2 capital. Mortgage servicing assets and deferred tax assets over designated percentages of CET1 are deducted from capital. In addition, Tier 1 capital includes AOCI, which includes all unrealized gains and losses on available for sale debt and equity securities. However, because of our asset size, we were eligible to elect, and did elect, to permanently opt out of the inclusion of unrealized gains and losses on available for sale debt and equity securities in our capital calculations.

For purposes of determining risk-based capital, assets and certain off-balance sheet items are risk-weighted from 0% to 1,250%, depending on the risk characteristics of the asset or item. The regulations changed certain risk-weightings compared to the earlier capital rules, including a 150% risk weight (up from 100%) for certain high volatility commercial real estate acquisition, development and construction loans and for non-residential mortgage loans that are 90 days past due or otherwise in nonaccrual status; a 20% (up from 0%) credit conversion factor for the unused portion of a commitment with an original maturity of one year or less that is not unconditionally cancellable (up from 0%); and a 250% risk weight (up from 100%) for mortgage servicing and deferred tax assets that are not deducted from capital.

In addition to the minimum CET1, Tier 1, leverage ratio and total capital ratios, Banner and each of the Banks must maintain a capital conservation buffer consisting of additional CET1 capital greater than 2.5% of risk-weighted assets above the required minimum risk-based capital levels in order to avoid limitations on paying dividends, repurchasing shares, and paying discretionary bonuses. The new capital conservation buffer requirement was phased in beginning on January 1, 2016 when a buffer greater than 0.625% of risk-weighted assets was required, which amount increased each year by 0.625% until the buffer requirement was fully implemented on January 1, 2019.

To be considered "well capitalized," a bank holding company must have, on a consolidated basis, a total risk-based capital ratio of 10.0% or greater and a Tier 1 risk-based capital ratio of 6.0% or greater and must not be subject to an individual order, directive or agreement under which the FRB requires it to maintain a specific capital level. To be considered “well capitalized,” a depository institution must have a Tier 1 risk-based capital ratio of at least 8.0%, a total risk-based capital ratio of at least 10.0%, a CET1 capital ratio of at least 6.5% and a leverage ratio of at least 5.0% and not be subject to an individualized order, directive or agreement under which its primary federal banking regulator requires it to maintain a specific capital level.

Prompt Corrective Action: Federal statutes establish a supervisory framework for FDIC-insured institutions based on five capital categories: well capitalized, adequately capitalized, undercapitalized, significantly undercapitalized and critically undercapitalized. An institution's category depends upon where its capital levels are in relation to relevant capital measures. The well-capitalized category is described above. An institution that is not well capitalized is subject to certain restrictions on brokered deposits, including restrictions on the rates it can offer on its deposits generally. To be considered adequately capitalized, an institution must have the minimum capital ratios described above. Any institution which is neither well capitalized nor adequately capitalized is considered undercapitalized.

Undercapitalized institutions are subject to certain prompt corrective action requirements, regulatory controls and restrictions which become more extensive as an institution becomes more severely undercapitalized. Failure by either Banner Bank and Islanders Bank to comply with applicable capital requirements would, if unremedied, result in progressively more severe restrictions on its activities and lead to enforcement actions, including, but not limited to, the issuance of a capital directive to ensure the maintenance of required capital levels and, ultimately, the appointment of the FDIC as receiver or conservator. Banking regulators will take prompt corrective action with respect to depository institutions that do not meet minimum capital requirements. Additionally, approval of any regulatory application filed for their review may be dependent on compliance with capital requirements.

As of December 31, 2018, Banner Corporation and each of the Banks met the requirements to be "well capitalized" and the fully phased-in capital conservation buffer requirement. For additional information, see Note 16, Regulatory Capital Requirements, of the Notes to the Consolidated Financial Statements.

Commercial Real Estate Lending Concentrations: The federal banking agencies have issued guidance on sound risk management practices for concentrations in commercial real estate lending. The particular focus is on exposure to commercial real estate loans that are dependent on the cash flow from the real estate held as collateral and that are likely to be sensitive to conditions in the commercial real estate market (as opposed to real estate collateral held as a secondary source of repayment or as an abundance of caution). The purpose of the guidance is not to limit a bank's commercial real estate lending but to guide banks in developing risk management practices and capital levels commensurate with the level and nature of real estate concentrations. The guidance directs the FDIC and other bank regulatory agencies to focus their supervisory resources on institutions that may have significant commercial real estate loan concentration risk. A bank that has experienced rapid growth in commercial real estate lending, has notable exposure to a specific type of commercial real estate loan, or is approaching or exceeding the following supervisory criteria may be identified for further supervisory analysis with respect to real estate concentration risk:

- Total reported loans for construction, land development and other land represent 100% or more of the bank's total regulatory capital; or

- Total commercial real estate loans (as defined in the guidance) represent 300% or more of the bank's total regulatory capital or the outstanding balance of the bank's commercial real estate loan portfolio has increased 50% or more during the prior 36 months.

The guidance provides that the strength of an institution's lending and risk management practices with respect to such concentrations will be taken into account in supervisory guidance on evaluation of capital adequacy. As of December 31, 2018, Banner Bank's and Islanders Bank's aggregate recorded loan balances for construction, land development and land loans were 94% and 33% of total regulatory capital, respectively. In addition, at December 31, 2018, Banner Bank's and Islanders Bank's loans on commercial real estate were 310% and 219% of total regulatory capital, respectively.

Activities and Investments of Insured State-Chartered Financial Institutions: Federal law generally limits the activities and equity investments of FDIC insured, state-chartered banks to those that are permissible for national banks. An insured state bank is not prohibited from, among other things, (1) acquiring or retaining a majority interest in a subsidiary, (2) investing as a limited partner in a partnership the sole purpose of which is direct or indirect investment in the acquisition, rehabilitation or new construction of a qualified housing project, provided that such limited partnership investments may not exceed 2% of the bank's total assets, (3) acquiring up to 10% of the voting stock of a company that solely provides or re-insures directors', trustees' and officers' liability insurance coverage or bankers' blanket bond group insurance coverage for insured depository institutions, and (4) acquiring or retaining the voting shares of a depository institution if certain requirements are met.

Washington State has enacted laws regarding financial institution parity. These laws afford Washington-chartered commercial banks the same powers as Washington-chartered savings banks and provide that Washington-chartered commercial banks may exercise any of the powers that the Federal Reserve has determined to be closely related to the business of banking and the powers of national banks, subject to the approval of the Director in certain situations. Finally, the law provides additional flexibility for Washington-chartered banks with respect to interest rates on loans and other extensions of credit. Specifically, they may charge the maximum interest rate allowable for loans and other extensions of credit by federally-chartered financial institutions.

Environmental Issues Associated With Real Estate Lending: The Comprehensive Environmental Response, Compensation and Liability Act (CERCLA) is a federal statute that generally imposes strict liability on all prior and present “owners and operators” of sites containing hazardous waste. However, Congress acted to protect secured creditors by providing that the term “owner and operator” excludes a person whose ownership is limited to protecting its security interest in the site. Since the enactment of the CERCLA, this “secured creditor exemption” has been the subject of judicial interpretations which have left open the possibility that lenders could be liable for cleanup costs on contaminated property that they hold as collateral for a loan. To the extent that legal uncertainty exists in this area, all creditors, including Banner Bank and Islanders Bank, that have made loans secured by properties with potential hazardous waste contamination (such as petroleum contamination) could be subject to liability for cleanup costs, which costs often substantially exceed the value of the collateral property.

Federal Reserve System: The Federal Reserve requires that all depository institutions maintain reserves on transaction accounts or non-personal time deposits. These reserves may be in the form of cash or non-interest-bearing deposits with the regional Federal Reserve Bank. Interest-bearing checking accounts and other types of accounts that permit payments or transfers to third parties fall within the definition of transaction accounts and are subject to Regulation D reserve requirements, as are any non-personal time deposits at a bank. At December 31, 2018, the Banks' deposits with the Federal Reserve Bank and vault cash exceeded their reserve requirements.

Affiliate Transactions: Banner Corporation, Banner Bank and Islanders Bank are separate and distinct legal entities. Each Bank is an affiliate of the other and Banner Corporation (and any non-bank subsidiary of Banner Corporation) is an affiliate of both Banks. Federal laws strictly limit the ability of banks to engage in certain transactions with their affiliates. Transactions deemed to be a “covered transaction” under Section 23A of the Federal Reserve Act between a bank and an affiliate are limited to 10% of the bank's capital and surplus and, with respect to all affiliates, to an aggregate of 20% of the bank's capital and surplus. Further, covered transactions that are loans and extensions of credit generally are required to be secured by eligible collateral in specified amounts. Federal law also requires that covered transactions and certain other transactions listed in Section 23B of the Federal Reserve Act between a bank and its affiliates be on terms as favorable to the bank as transactions with non-affiliates.

Community Reinvestment Act: Banner Bank and Islanders Bank are subject to the provisions of the Community Reinvestment Act of 1977 (CRA), which requires the appropriate federal bank regulatory agency to assess a bank's performance under the CRA in meeting the credit needs of the community serviced by the bank, including low and moderate income neighborhoods. The regulatory agency's assessment of the bank's record is made available to the public. Further, a bank's CRA performance rating must be considered in connection with a bank's application to, among other things, establish a new branch office that will accept deposits, relocate an existing office or merge or consolidate with, or acquire the assets or assume the liabilities of, a federally regulated financial institution. Both Banner Bank and Islanders Bank received a “satisfactory” rating during their most recently completed CRA examinations.

Dividends: The amount of dividends payable by the Banks to the Company depends upon their earnings and capital position, and is limited by federal and state laws, regulations and policies, including the capital conservation buffer requirement. Federal law further provides that no insured depository institution may make any capital distribution (which includes a cash dividend) if, after making the distribution, the institution would be “undercapitalized,” as defined in the prompt corrective action regulations. Moreover, the federal bank regulatory agencies also have the general authority to limit the dividends paid by insured banks if such payments should be deemed to constitute an unsafe and unsound practice. In addition, under Washington law, no bank may declare or pay any dividend in an amount greater than its retained earnings without the prior approval of the Washington DFI. The Washington DFI also has the power to require any bank to suspend the payment of any and all dividends.

Privacy Standards: The Gramm-Leach-Bliley Financial Services Modernization Act of 1999 (GLBA) modernized the financial services industry by establishing a comprehensive framework to permit affiliations among commercial banks, insurance companies, securities firms and other financial service providers. Banner Bank and Islanders Bank are subject to FDIC regulations implementing the privacy protection provisions of the GLBA. These regulations require the Banks to disclose their privacy policy, including informing consumers of their information sharing practices and informing consumers of their rights to opt out of certain practices.

Anti-Money Laundering and Customer Identification: The Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act of 2001 (USA Patriot Act) was signed into law on October 26, 2001. The USA PATRIOT and Bank Secrecy Acts require financial institutions to develop programs to prevent financial institutions from being used for money laundering and terrorist activities. If such activities are detected, financial institutions are obligated to file suspicious activity reports with the U.S. Treasury’s Office of Financial Crimes Enforcement Network. These rules require financial institutions to establish procedures for identifying and verifying the identity of customers seeking to open new financial accounts, and, effective in 2018, the beneficial owners of accounts. Bank regulators are directed to consider an institution's effectiveness in combating money laundering when ruling on Bank Holding Company Act and Bank Merger Act applications. Banner Bank's and Islanders Bank's policies and procedures comply with the requirements of the USA Patriot Act.

Other Consumer Protection Laws and Regulations: The Dodd-Frank Act established the CFPB and empowered it to exercise broad regulatory, supervisory and enforcement authority with respect to both new and existing consumer financial protection laws. The quarter ended December 31, 2018, is the fourth consecutive quarter that Banner Bank will have reported assets exceeding $10 billion. Therefore, effective the second quarter of 2019 Banner Bank and its affiliates and subsidiaries will become subject to CFPB supervisory and enforcement authority. See Item 1A "Risk Factors—We will be subject to additional regulatory scrutiny since Banner Bank maintains total assets exceeding $10.0 billion."

The Banks are subject to a broad array of federal and state consumer protection laws and regulations that govern almost every aspect of their business relationships with consumers. While the list set forth below is not exhaustive, these include the Truth-in-Lending Act, the Truth in Savings Act, the Electronic Fund Transfers Act, the Expedited Funds Availability Act, the Equal Credit Opportunity Act, the Fair Housing Act, the Real Estate Settlement Procedures Act, the Home Mortgage Disclosure Act, the Fair Credit Reporting Act, the Right to Financial Privacy Act, the Home Ownership and Equity Protection Act, the Fair Credit Billing Act, the Homeowners Protection Act, the Check Clearing for the 21st Century Act, laws governing flood insurance, laws governing consumer protections in connection with the sale of insurance, federal and state laws prohibiting unfair and deceptive business practices, and various regulations that implement some or all of the foregoing. These laws and regulations mandate certain disclosure requirements and regulate the manner in which financial institutions must deal with customers when taking deposits, making loans, collecting loans, and providing other services. Failure to comply with these laws and regulations can subject the Banks to various penalties, including but not limited to, enforcement actions, injunctions, fines, civil liability, criminal penalties, punitive damages, and the loss of certain contractual rights.

2018 Reforms

In May 2018, the Economic Growth, Regulatory Relief and Consumer Protection Act (the “Economic Growth Act”) was enacted to modify or remove certain financial reform rules and regulations, including some of those implemented under the Dodd-Frank Act. While the Act maintains most of the regulatory structure established by the Dodd-Frank Act, it amends certain aspects of the regulatory framework for small depository institutions with assets of less than $10 billion and for large banks with assets of more than $50 billion.

The Economic Growth Act, among other matters, expands the definition of qualified mortgages which may be held by a financial institution and simplifies the regulatory capital rules for depository institutions and their holding companies with total consolidated assets of less than $10 billion by instructing the federal banking regulators to establish a single

“Community Bank Leverage Ratio” of between 8 and 10 percent. Any qualifying depository institution or its holding company that exceeds the “community bank leverage ratio” will be considered to have met generally applicable leverage and risk-based regulatory capital requirements and any qualifying depository institution that exceeds the new ratio will be considered to be “well capitalized” under the prompt corrective action rules.

In addition, the Economic Growth Act includes regulatory relief for community banks regarding regulatory examination cycles, call reports, the Volcker Rule (proprietary trading prohibitions), mortgage disclosures and risk weights for certain high-risk commercial real estate loans.

It is difficult at this time to predict when or how any new standards under the Economic Growth Act will ultimately be applied to us or what specific impact the Economic Growth Act and the yet-to-be-written implementing rules and regulations implementing the Economic Growth Act will have.

Current Expected Credit Loss, or CECL, that will be effective for Banner for our first fiscal year beginning after December 15, 2019. Upon adoption of CECL, a banking organization must record a one-time adjustment to its credit loss allowances as of the beginning of the fiscal year of adoption equal to the difference, if any, between the amount of credit loss allowances under the current methodology and the amount required under CECL. In 2018, the federal banking regulators (the Federal Reserve, the OCC and the FDIC) adopted a rule that gives a banking organization the option to phase in over a three-year period the day-one adverse effects of CECL on its regulatory capital.

Banner Corporation

General: Banner Corporation, as sole shareholder of Banner Bank and Islanders Bank, is a bank holding company registered with the Federal Reserve. Bank holding companies are subject to comprehensive regulation by the Federal Reserve under the Bank Holding Company Act of 1956, as amended, or the BHCA, and the regulations of the Federal Reserve. We are required to file quarterly reports with the Federal Reserve and provide additional information as the Federal Reserve may require. The Federal Reserve may examine us, and any of our subsidiaries, and charge us for the cost of the examination. The Federal Reserve also has extensive enforcement authority over bank holding companies, including, among other things, the ability to assess civil money penalties, to issue cease and desist or removal orders and to require that a holding company divest subsidiaries (including its bank subsidiaries). In general, enforcement actions may be initiated for violations of law and regulations and unsafe or unsound practices. Banner Corporation is also required to file certain reports with, and otherwise comply with the rules and regulations of the SEC.

The Bank Holding Company Act: Under the BHCA, Banner Corporation is supervised by the Federal Reserve. The Federal Reserve has a policy that a bank holding company is required to serve as a source of financial and managerial strength to its subsidiary banks and may not conduct its operations in an unsafe or unsound manner. In addition, the Dodd-Frank Act provides that a bank holding company must serve as a source of financial strength to its subsidiary banks. A bank holding company's failure to meet its obligation to serve as a source of strength to its subsidiary banks will generally be considered by the Federal Reserve to be an unsafe and unsound banking practice or a violation of the Federal Reserve's regulations or both. No regulations have yet been proposed by the Federal Reserve to implement the source of strength provisions of the Dodd-Frank Act. Banner Corporation and any subsidiaries that it may control are considered “affiliates” of the Banks within the meaning of the Federal Reserve Act, and transactions between Banner Bank and affiliates are subject to numerous restrictions. With some exceptions, Banner Corporation and its subsidiaries are prohibited from tying the provision of various services, such as extensions of credit, to other services offered by Banner Corporation or by its affiliates.

Acquisitions: The BHCA prohibits a bank holding company, with certain exceptions, from acquiring ownership or control of more than 5% of the voting shares of any company that is not a bank or bank holding company and from engaging in activities other than those of banking, managing or controlling banks, or providing services for its subsidiaries. Under the BHCA, the Federal Reserve may approve the ownership of shares by a bank holding company in any company, the activities of which the Federal Reserve has determined to be so closely related to the business of banking or managing or controlling banks as to be a proper incident thereto. These activities include: operating a savings institution, mortgage company, finance company, credit card company or factoring company; performing certain data processing operations; providing certain investment and financial advice; underwriting and acting as an insurance agent for certain types of credit-related insurance; leasing property on a full-payout, non-operating basis; selling money orders, travelers' checks and U.S. Savings Bonds; real estate and personal property appraising; providing tax planning and preparation services; and, subject to certain limitations, providing securities brokerage services for customers.

Federal Securities Laws: Banner Corporation's common stock is registered with the SEC under Section 12(b) of the Securities Exchange Act of 1934, as amended. We are subject to information, proxy solicitation, insider trading restrictions and other requirements under the Securities Exchange Act of 1934 (the Exchange Act).

The Dodd-Frank Act: On July 21, 2010, the Dodd-Frank Act was signed into law. The Dodd-Frank-Act imposes various restrictions and an expanded framework of regulatory oversight for financial institutions, including depository institutions, and implements certain capital regulations applicable to Banner Corporation and the Banks that are discussed above under the section entitled "Capital Requirements."

In addition, among other changes, the Dodd-Frank Act requires public companies, like Banner Corporation, to (i) provide their shareholders with a non-binding vote (a) at least once every three years on the compensation paid to executive officers and (b) at least once every six years on whether they should have a “say on pay” vote every one, two or three years; (ii) have a separate, non-binding shareholder vote regarding golden parachutes for named executive officers when a shareholder vote takes place on mergers, acquisitions, dispositions or other transactions that would trigger the parachute payments; (iii) provide disclosure in annual proxy materials concerning the relationship between the executive compensation paid and the financial performance of the issuer; and (iv) disclose the ratio of the Chief Executive Officer's annual total compensation to the median annual total compensation of all other employees.

The regulations to implement the provisions of Section 619 of the Dodd-Frank Act, commonly referred to as the Volcker Rule, contain prohibitions and restrictions on the ability of financial institutions holding companies and their affiliates to engage in proprietary trading and to hold certain interests in, or to have certain relationships with, various types of investment funds, including hedge funds and private equity funds. Banner Corporation is continuously reviewing its investment portfolio to determine if changes in its investment strategies are in compliance with the various provisions of the Volcker Rule regulations.

For certain of these changes, the implementing regulations have not been promulgated, so the full impact of the Dodd-Frank Act on public companies cannot be determined at this time. For information on the Economic Growth Act, which amended the Dodd-Frank Act, see "2018 Reforms" above.

Sarbanes-Oxley Act of 2002: As a public company that files periodic reports with the SEC, under the Securities Exchange Act of 1934, Banner Corporation is subject to the Sarbanes-Oxley Act of 2002 (Sarbanes-Oxley Act), which addresses, among other issues, corporate governance, auditing and accounting, executive compensation and enhanced and timely disclosure of corporate information. The Sarbanes-Oxley Act represents significant federal involvement in matters traditionally left to state regulatory systems, such as the regulation of the accounting profession, and to state corporate law, such as the relationship between a board of directors and management and between a board of directors and its committees. Our policies and procedures are designed to comply with the requirements of the Sarbanes-Oxley Act.

Interstate Banking and Branching: The Federal Reserve must approve an application of a bank holding company to acquire control of, or acquire all or substantially all of the assets of, a bank located in a state other than the holding company's home state, without regard to whether the transaction is prohibited by the laws of any state. The Federal Reserve may not approve the acquisition of a bank that has not been in existence for the minimum time period (not exceeding five years) specified by the statutory law of the host state. Nor may the Federal Reserve approve an application if the applicant (and its depository institution affiliates) controls or would control more than 10% of the insured deposits in the United States or 30% or more of the deposits in the target bank's home state or in any state in which the target bank maintains a branch. Federal law does not affect the authority of states to limit the percentage of total insured deposits in the state which may be held or controlled by a bank holding company to the extent such limitation does not discriminate against out-of-state banks or bank holding companies. Individual states may also waive the 30% state-wide concentration limit contained in the federal law.

The federal banking agencies are generally authorized to approve interstate merger transactions without regard to whether the transaction is prohibited by the law of any state. Interstate acquisitions of branches are permitted only if the law of the state in which the branch is located permits such acquisitions. Interstate mergers and branch acquisitions are subject to the nationwide and statewide insured deposit concentration amounts described above. Under the Dodd-Frank Act, the federal banking agencies may generally approve interstate de novo branching.

Dividends: The Federal Reserve has issued a policy statement on the payment of cash dividends by bank holding companies, which expresses its view that although there are no specific regulations restricting dividend payments by bank holding companies other than state corporate laws, a bank holding company must maintain an adequate capital position and generally should not pay cash dividends unless the company's net income for the past year is sufficient to fully fund the cash dividends and that the prospective rate of earnings appears consistent with the company's capital needs, asset quality, and overall financial condition. The Federal Reserve policy statement also indicates that it would be inappropriate for a company experiencing serious financial problems to borrow funds to pay dividends. As described above under “Capital Requirements,” the capital conversion buffer requirement can also restrict Banner Corporation’s and the Banks’ ability to pay dividends. Further, under Washington law, Banner Corporation is prohibited from paying a dividend if, after making such dividend payment, it would be unable to pay its debts as they become due in the usual course of business, or if its total liabilities, plus the amount that would be needed in the event Banner Corporation were to be dissolved at the time of the dividend payment, to satisfy preferential rights on dissolution of holders of preferred stock ranking senior in right of payment to the capital stock on which the applicable distribution is to be made, exceed our total assets.

Stock Repurchases: A bank holding company, except for certain “well-capitalized” and highly rated bank holding companies, is required to give the Federal Reserve prior written notice of any purchase or redemption of its outstanding equity securities if the gross consideration for the purchase or redemption, when combined with the net consideration paid for all such purchases or redemptions during the preceding twelve months, is equal to 10% or more of its consolidated net worth. The Federal Reserve may disapprove such a purchase or redemption if it determines that the proposal would constitute an unsafe or unsound practice or would violate any law, regulation, Federal Reserve order or any condition imposed by, or written agreement with, the Federal Reserve. During the year ended December 31, 2018, Banner Corporation repurchased 594,711 shares of its common stock at an average price of $57.82 per share.

Management Personnel
Executive Officers

The following table sets forth information with respect to the executive officers of Banner Corporation and Banner Bank as of December 31, 2018:

Name	Age	Position with Banner Corporation	Position with Banner Bank
Mark J. Grescovich	54	President, Chief Executive Officer, Director	President, Chief Executive Officer, Director
Richard B. Barton	75		Executive Vice President, Chief Credit Officer
Peter J. Conner	53	Executive Vice President Chief Financial Officer Treasurer	Executive Vice President, Chief Financial Officer
James P. Garcia	59		Executive Vice President, Chief Audit Executive
Kenneth W. Johnson	56		Executive Vice President Operations
Kayleen R. Kohler	46		Executive Vice President Human Resources
Kenneth A. Larsen	49		Executive Vice President, Mortgage Banking
James P. G. McLean	54		Executive Vice President, Commercial Real Estate Lending Division
Craig Miller	67	Executive Vice President General Counsel	Executive Vice President General Counsel
Cynthia D. Purcell	61		Executive Vice President, Retail Banking and Administration
M. Kirk Quillin	56		Executive Vice President, Commercial Executive
James T. Reed, Jr.	56		Executive Vice President, Commercial Banking West
Steven W. Rust	71		Executive Vice President, Chief Information Officer
Judith A. Steiner	56		Executive Vice President Chief Risk Officer
Gary W. Wagers	58		Executive Vice President, Retail Products and Services
Keith A. Western	63		Executive Vice President, Commercial Banking South

Biographical Information

Set forth below is certain information regarding the executive officers of Banner Corporation and Banner Bank. There are no family relationships among or between the directors or executive officers.

Mark J. Grescovich is President and Chief Executive Officer, and a director, of Banner Corporation and Banner Bank. Mr. Grescovich joined Banner Bank in April 2010 and became Chief Executive Officer in August 2010 following an extensive banking career specializing in finance, credit administration and risk management. Under his leadership, Banner has grown from $4.7 billion in assets in 2010 to more than $11 billion today through organic growth as well as selective acquisition. During that time, Mr. Grescovich has guided the expansion of the Company's footprint to nearly 200 locations in four states. Prior to joining the Bank, Mr. Grescovich was the Executive Vice President and Chief Corporate Banking Officer for Akron, Ohio-based FirstMerit Corporation and FirstMerit Bank N.A., a commercial bank with $14.5 billion in assets and over 200 branch offices in three states. He assumed the role and responsibility for FirstMerit's commercial and regional line of business in 2007, having served since 1994 in various commercial and corporate banking positions, including that of Chief Credit Officer. Prior to joining FirstMerit, Mr. Grescovich was a Managing Partner in corporate finance with Sequoia Financial Group, Inc. of Akron, Ohio and a commercial and corporate lending officer and credit analyst with Society National Bank of Cleveland, Ohio. He has a Bachelor of Business Administration degree in finance from Miami University and a Master of Business Administration degree, also in finance, from The University of Akron.

Richard B. Barton joined Banner Bank in 2002 as Chief Credit Officer. Mr. Barton’s banking career began in 1972 with Seafirst Bank and Bank of America, where he served in a variety of commercial lending and credit risk management positions. In his last positions at Bank of America before joining Banner Bank, he served as the senior real estate risk management executive for the Pacific Northwest and as the credit risk management executive for the west coast home builder division.

Peter J. Conner joined Banner Bank in 2015 upon the acquisition of AmericanWest Bank (AmericanWest). Prior to joining Banner, Mr. Conner was the Chief Financial Officer for SKBHC LLC, the holding company for Starbuck Bancshares, Inc. (Starbuck), the holding company for AmericanWest, and AmericanWest from 2010 until he joined Banner Bank in 2015. Mr. Conner has 29 years of experience in executive finance positions at Wells Fargo Bank as well as regional community banks. Additionally, he spent time as a managing director for FSI Group, where he evaluated and placed equity fund investments in community banks. He earned a B.S. in Quantitative Economics from the University of California at San Diego and a Master's of Business degree from the Haas School of Business at U.C. Berkeley.

James P. Garcia is the Chief Audit Executive responsible for proactively identifying and mitigating risks as well as providing internal audit services in the areas of financial compliance, IT Governance, and operations. He has more than 41 years of experience in the financial services industry. Prior to joining Banner in 2017, Mr. Garcia served for 16 years at the Bank of Hawaii, most recently as Executive Vice President and Chief Audit Executive, with prior positions as Vice President and Senior Audit Manager. Mr. Garcia also has 24 years of experience at Bank of America where he held several positions in consumer and commercial operations management and audit, including that of Audit Director. Mr. Garcia earned his bachelor's degree in management from St. Mary's College of California and is a graduate of the School of Mortgage Banking. He is a Certified Bank Auditor (CBA), holds a Certification in Risk Management Assurance (CRMA) and is a Certified Information Systems Auditor (CISA).

Kenneth W. Johnson has over 30 years of banking experience. Prior to joining Skagit Bank in 2015, Mr. Johnson held various executive positions with Chemical Financial Corporation, including production oversight of commercial, mortgage, consumer and deposit generation. In addition, while at Chemical, he served nine years as Executive Vice President, Director of Bank Operations, responsible for nine business units including the branch system, information technology, corporate marketing, loan operations, deposit operations, electronic banking, facilities/purchasing, card services, and customer care centers. Prior to Chemical, he held leadership roles in retail banking and operations at Shoreline Bank and as Vice President, Zone Manager for Michigan National Bank. Mr. Johnson holds a Bachelor of Arts Degree in Business Administration from Michigan State University. He is also a graduate of Stonier Graduate School of Banking.

Kayleen R. Kohler joined Banner Bank in 2016 as Executive Vice President of Human Resources. Ms. Kohler’s focus is on driving organizational design priorities at Banner Bank including: leadership development, talent acquisition, workforce planning, employee relations, compensation, benefits, diversity initiatives, payroll, and safety. Prior to joining Banner, Ms. Kohler served 20 years in progressive human resource leadership roles for Plum Creek Timber Company, now Weyerhaeuser. She holds bachelors’ degrees in Marketing as well as Business Management from Northwest Missouri State University and a master’s in Organizational Management from the University of Phoenix. Through continuing education, she maintains her certifications as a Senior Professional in Human Resources or SPHR and a Society of Human Resources Management Senior Certified Professional or SHRM-SCP.

Kenneth A. Larsen joined Banner Bank in 2005 as the Real Estate Administration Manager and was promoted to Mortgage Banking Director in 2010. Mr. Larsen is responsible for Banner Bank's mortgage banking activities from origination, administration, secondary marketing, through loan servicing. Mr. Larsen has had a 27-year career in mortgage banking, including holding positions in all facets of operations and management. A graduate of Eastern Washington University, he earned a Bachelor of Arts in Education with a degree in Social Science and earned certificates from the Pacific Coast Banking School and the School of Mortgage Banking. He is also a Certified Mortgage Banker, the highest designation recognized by the Mortgage Bankers Association. Mr. Larsen began his career at Action Mortgage/Sterling Savings, later moving to Peoples Bank of Lynden where he managed the mortgage banking operation. Mr. Larsen also served as the 90th President of the Seattle Mortgage Bankers Association. Formerly he was the Chairman of the Washington Mortgage Bankers Association and currently serves as a commissioner on the Washington State Housing Finance Commission. He was promoted to Executive Vice President in 2015.

James P.G. McLean joined Banner Bank in November 2010 and is Executive Vice President of the Commercial Real Estate Lending Division, leading teams within the Multifamily Lending Group, Commercial Real Estate Specialty Unit, Residential Construction and Income Property Divisions, as well as the loan administration functions related to this division. Mr. McLean has 28 years of real estate finance experience at large national commercial banks as well as community banks. This experience includes ten years in executive leadership roles and as a principal of a mid-sized regional commercial real estate development firm. Mr. McLean earned his bachelor's degree from the University of Washington. His community volunteering is focused on organizations that serve local youth, including the Boy Scouts of America, Lake Washington School District and numerous coaching positions.

Craig Miller is the Executive Vice President and General Counsel for Banner Corporation and Banner Bank. He joined Banner in 2016 and is responsible for overseeing the company's legal functions. Mr. Miller had previously served as senior litigation partner at Davis Wright Tremaine LLP in Seattle. Mr. Miller earned his B.A. degree from Grinnell College and his J.D. degree from the University of Southern California Law School. His community involvement includes board service with the YMCA of Greater Seattle, Childhaven (past board president), King County Sexual Assault Resource Center, and the Meany Center for the Performing Arts.

Cynthia D. Purcell is the Executive Vice President for Retail Banking and Administration. Ms. Purcell is responsible for leading the Retail Banking business line including Branch Banking, Mortgage Banking, Business Banking and Digital delivery channels, as well as oversight of administrative and support functions for Banner Bank. She was formerly the Chief Financial Officer of Inland Empire Bank (now Banner Bank), which she joined in 1981. Over her banking career, Ms. Purcell has been deeply involved in advocating for the industry through leadership roles on various Boards and committees including State Banking Associations and the American Bankers Association (ABA). She has also taught banking courses throughout her career, including the ABA Graduate School of Bank Investments and Financial Management, the Northwest Intermediate Banking School, and the Oregon Bankers Association Directors College.
M. Kirk Quillin joined Banner Bank's commercial banking group in 2002 as a Senior Vice President and commercial banking manager for the Spokane, Washington, and Idaho markets. He was named the East Region Commercial Banking Executive in July 2012, responsible for commercial and specialty banking for all locations in Eastern Washington, Eastern Oregon and Idaho. Currently, he is overseeing a project that addresses both efficiency and scalability for Banner Bank. Mr. Quillin began his career in the banking industry in 1984 with Idaho First National Bank, which is now U.S. Bank. His career also included management positions in commercial lending with Washington Mutual. He earned a B.S. in Finance and Economics from Boise State University and was certified by the Pacific Coast Banking School and Northwest Intermediate Commercial Lending School.

James T. Reed, Jr. joined Towne Bank (now Banner Bank) as a Vice President and Commercial Branch Manager in July 1995 and was named to his current position as the West Region Commercial Banking Executive in July 2012. He is responsible for Commercial Banking in Western Washington and Western Oregon, as well as Treasury Management and Specialty Banking Services. Mr. Reed began his banking career with Rainier Bank, which later became Security Pacific Bank and later still West One Bank. He earned a Bachelor of Arts in Interdisciplinary Arts and Sciences from the University of Washington and earned certificates from Pacific Coast Banking School, Northwest Intermediate Banking School and Northwest Intermediate Commercial Lending School. Currently, Mr. Reed is a member of the University of Washington Bothell Advisory Board and the Association of Washington Business Board of Directors.

Steven W. Rust joined Banner Bank in October 2005 as Senior Vice President and Chief Information Officer and was named to his current position as Executive Vice President and Chief Information Officer in September 2007. Mr. Rust has over 39 years of relevant industry experience prior to joining Banner Bank and was founder and President of InfoSoft Technology, through which he worked for nine years as a technology consultant and interim Chief Information Officer for banks and insurance companies. He also worked 19 years with US Bank/West One Bancorp as Senior Vice President & Manager of Information Systems.
Judith A. Steiner joined Banner Bank in 2016 as Executive Vice President and Chief Risk Officer. In this role, Ms. Steiner is responsible for overseeing the company's risk and compliance functions as well as Banner Bank's interactions with industry regulators. Prior to joining Banner, Ms. Steiner spent 25 years with FirstMerit Corporation in executive leadership positions including Executive Vice President & Chief Risk Officer, Secretary, and General Counsel. Ms. Steiner earned her bachelor's degree from the University of Akron and her Juris Doctor degree (JD) from the Case Western Reserve University School of Law.

Gary W. Wagers joined Banner Bank as Senior Vice President, Consumer Lending Administration in 2002 and was named to his current position in Retail Products and Services in January 2008. Mr. Wagers began his banking career in 1982 at Idaho First National Bank. Prior to joining Banner Bank, his career included senior management positions in retail lending and branch banking operations with West One Bank and US Bank. Mr. Wagers earned his bachelor's degree from Whitman College and his Master's of Business degree from the University of Oregon. He is also a graduate of the ABA's Stonier School of Banking.

Keith A. Western is Executive Vice President, Commercial Banking South for Banner Bank, joining Banner upon the merger of AmericanWest and Banner Bank. Prior to the merger, Mr. Western was President of Northwest Banking for AmericanWest since 2011. Mr. Western has 41 years of banking experience across multiple markets including the western, eastern and mid-western United States and Canada. The bulk of Mr. Western's career was with Bank of America (approximately 15 years) and Citibank (approximately 12 years) in a variety of assignments including asset based lending, commercial and business banking, and credit risk management.

Corporate Information

Our principal executive offices are located at 10 South First Avenue, Walla Walla, Washington 99362. Our telephone number is (509) 527-3636. We maintain a website with the address www.bannerbank.com. The information contained on our website is not included as a part of, or incorporated by reference into, this Annual Report on Form 10-K. Other than an investor's own Internet access charges, we make available free of charge through our website our Annual Report on Form 10-K, quarterly reports on Form 10-Q and current reports on Form 8-K, and amendments to these reports, as soon as reasonably practicable after we have electronically filed such material with, or furnished such material to, the SEC.

Item 1A – Risk Factors

An investment in our common stock is subject to risks inherent in our business. Before making an investment decision, you should carefully consider the risks and uncertainties described below together with all of the other information included in this report. The risks described below are not the only ones we face. Additional risks and uncertainties not currently known to us or that we currently deem to be immaterial also may materially and adversely affect our business, financial condition, capital levels, cash flows, liquidity, results of operations and prospects. The market price of our common stock could decline significantly due to any of these identified or other risks, and you could lose some or all of your investment. The risks discussed below also include forward-looking statements, and our actual results may differ substantially from those discussed in these forward-looking statements. This report is qualified in its entirety by these risk factors.

Our business may be adversely affected by downturns in the national economy and the regional economies on which we depend.

Our operations are significantly affected by national and regional economic conditions. Weakness in the national economy or the economies of the markets in which we operate could have a material adverse effect on our financial condition, results of operations and prospects. We provide banking and financial services primarily to businesses and individuals in the states of Washington, Oregon, California and Idaho. All of our branches and most of our deposit customers are also located in these four states. Further, as a result of a high concentration of our customer base in the Puget Sound area and eastern Washington state regions, the deterioration of businesses in these areas, or one or more businesses with a large employee base in these areas, could have a material adverse effect on our business, financial condition, liquidity, results of operations and prospects. Weakness in the global economy has adversely affected many businesses operating in our markets that are dependent upon international trade and it is not known how changes in tariffs being imposed on international trade may also affect these businesses. In addition, adverse weather conditions as well as decreases in market prices for agricultural products grown in our primary markets can adversely affect agricultural businesses in our markets. As we expand our presence in areas such as San Diego and Sacramento, and throughout California, we will be exposed to concentration risks in those areas as well.

While real estate values and unemployment rates in the market areas we serve have generally improved, a deterioration in economic conditions in these markets, in particular the Puget Sound area of Washington State, the Portland, Oregon metropolitan area, Spokane, Washington, Boise, Idaho, Eugene and southwest Oregon, San Diego and Sacramento, California and the agricultural regions of the Columbia Basin, could result in the following consequences, any of which could have a material adverse effect on our business, financial condition, liquidity and results of operations:

- demand for our products and services may decline;
- loan delinquencies, problem assets and foreclosures may increase;
- we may increase our allowance for loan losses;
- collateral for loans, especially real estate, may decline in value, in turn reducing customers' borrowing power, reducing the value of assets and collateral associated with existing loans;
- the net worth and liquidity of loan guarantors may decline, impairing their ability to honor commitments to us; and
- the amount of our low-cost or non-interest-bearing deposits may decrease.

A decline in local economic conditions may have a greater effect on our earnings and capital than on the earnings and capital of larger financial institutions whose real estate loans are more geographically diverse. Many of the loans in our portfolio are secured by real estate. Deterioration in the real estate markets where collateral for a mortgage loan is located could negatively affect the borrower's ability to repay the loan and the value of the collateral securing the loan. Real estate values are affected by various other factors, including changes in general or regional economic conditions, governmental rules or policies and natural disasters such as earthquakes, flooding and tornadoes.

Adverse changes in the regional and general economy could reduce our growth rate, impair our ability to collect loans and generally have a negative effect on our financial condition and results of operations.

Our loan portfolio includes loans with a higher risk of loss.

In addition to first-lien one- to four -family residential real estate lending, we originate construction and land loans, commercial and multifamily mortgage loans, commercial business loans, agricultural mortgage loans and agricultural loans, and consumer loans, primarily within our market areas. We had $7.71 billion outstanding in these types of higher risk loans at December 31, 2018, compared to $6.75 billion at December 31, 2017. These loans typically present different risks to us for a number of reasons, including those discussed below:

- Construction and Land Loans. At December 31, 2018, construction and land loans were $1.11 billion, or 13% of our total loan portfolio. This type of lending is subject to the inherent difficulties in estimating both a property's value at completion of a project and the estimated cost (including interest) of the project. Because of the uncertainties inherent in estimating construction costs, as well as the market value of a completed project and the effects of governmental regulation on real property, it is relatively difficult to evaluate accurately the total funds required to complete a project and the completed project's loan-to-value ratio. If the estimate of construction cost proves to be inaccurate, we may be required to advance funds beyond the amount originally committed to ensure completion of the project. If our appraisal of the value of a completed project proves to be overstated, we may have inadequate security for the repayment of the loan upon completion of construction of the project and may incur a loss. Disagreements between borrowers and builders and the failure of builders to pay subcontractors may also jeopardize projects. This type of lending also typically involves higher loan principal amounts and may be concentrated with a small number of builders. A downturn in housing, or the real estate market, could increase delinquencies, defaults and foreclosures, and significantly impair the value of our collateral and our ability to sell the collateral upon foreclosure. Some of the builders we deal with have more than one loan outstanding with us. Consequently, an adverse development with respect to one loan or one credit relationship can expose us to a significantly greater risk of loss. In addition, during the term of some of our construction loans, no payment from the borrower is required since the accumulated interest is added to the principal of the loan through an interest reserve. Increases in market rates of interest may have a more pronounced effect on construction loans by rapidly increasing the end-purchaser's borrowing costs, thereby possibly reducing the homeowner's ability to finance the home upon completion or the overall demand for the project. Properties under construction are often difficult to sell and typically must be completed in order to be successfully sold which also complicates the process of managing our problem construction loans. This may require us to advance additional funds and/or contract with another builder to complete construction and assume the market risk of selling the project at a future market price, which may or may not enable us to fully recover unpaid loan funds and associated construction and liquidation costs. In addition, speculative construction loans to a builder are often associated with homes that are not pre-sold, and thus pose a greater potential risk to us than construction loans to individuals on their personal residences. Loans on land under development or held for future construction also pose additional risk because of the lack of income being produced by the property and the potential illiquid nature of the collateral. These risks can be significantly impacted by supply and demand. As a result, this type of lending often involves the disbursement of substantial funds with repayment dependent on the success of the ultimate project and the ability of the borrower to sell or lease the property or obtain permanent take-out financing, rather than the ability of the borrower or guarantor to independently repay principal and interest.

Construction loans made by us include those with a sales contract or permanent loan in place for the finished homes and those for which purchasers for the finished homes may not be identified either during or following the construction period. We actively monitor the number of unsold homes in our construction loan portfolio and local housing markets to attempt to maintain an appropriate balance between home sales and new loan originations. The maximum number of speculative loans (loans that are not pre-sold) approved for each builder is based on a combination of factors, including the financial capacity of the builder, the market demand for the finished product and the ratio of sold to unsold inventory the builder maintains. We have attempted to diversify the risk associated with speculative construction lending by doing business with a large number of small and mid-sized builders spread over a relatively large geographic region representing numerous sub-markets within our service area.

As a result of the recent improvement in real estate values in certain of our market areas, this category of lending has increased significantly in recent years and our investment in construction and land loans increased by $200.0 million or 22% in 2018. At December 31, 2018, construction and land loans that were non-performing were $3.2 million, or 20% of our total non-performing loans.

- Commercial and Multifamily Real Estate Loans. At December 31, 2018, commercial and multifamily real estate loans were $3.93 billion, or 45% of our total loan portfolio. These loans typically involve higher principal amounts than other types of loans and some of our commercial borrowers have more than one loan outstanding with us. Consequently, an adverse development with respect to one loan or one credit relationship can expose us to a significantly greater risk of loss compared to an adverse development with respect to a one- to four-family residential mortgage loan. Repayment of these loans is dependent upon income being generated from the property securing the loan in amounts sufficient to cover operating expenses and debt service, which may be adversely affected by changes in the economy or local market conditions. In addition, many of our commercial and multifamily real estate loans are not fully amortizing and contain large balloon payments upon maturity. Such balloon payments may require the borrower to either sell or refinance the underlying property in order to make the payment, which may increase the risk of default or non-payment. If we foreclose on a commercial or multifamily real estate loan, our holding period for the collateral typically is longer than for one-to-four family residential loans because there are fewer potential purchasers of the collateral. At December 31, 2018, commercial and multifamily real estate loans that were non-performing were $4.1 million, or 26% of our total non-performing loans.

Commercial Business Loans. At December 31, 2018, commercial business loans were $1.48 billion, or 17% of our total loan portfolio. Our commercial business loans are primarily made based on the cash flow of the borrower and secondarily on the underlying collateral provided by the borrower. A borrower's cash flow may prove to be unpredictable, and collateral securing these loans may fluctuate in value. Most often, this collateral includes accounts receivable, inventory, equipment or real estate. In the case of loans secured by accounts receivable, the availability of funds for the repayment of these loans may be substantially dependent on the ability of the borrower to collect amounts due from its customers. Other collateral securing loans may depreciate over time, may be difficult to appraise, may be illiquid and may fluctuate in value based on the success of the business. At December 31, 2018, commercial business loans that were non-performing were $2.9 million, or 19% of our total non-performing loans.

Agricultural Loans. At December 31, 2018, agricultural loans were $404.9 million, or 5% of our total loan portfolio. Agricultural lending involves a greater degree of risk and typically involves higher principal amounts than other types of loans. Repayment is dependent upon the successful operation of the business, which is greatly dependent on many things outside the control of either us or the borrowers. These factors include adverse weather conditions that prevent the planting of a crops or limit crop yields (such as hail, drought and floods), loss of livestock due to disease or other factors, declines in market prices for agricultural products (both domestically and internationally) and the impact of government regulations (including changes in price supports, subsidies, tariffs and environmental regulations). In addition, many farms are dependent on a limited number of key individuals whose injury or death may significantly affect the successful operation of the farm. If the cash flow from a farming operation is diminished, the borrower's ability to repay the loan may be impaired. Consequently, agricultural loans may involve a greater degree of risk than other types of loans, particularly in the case of loans that are unsecured or secured by rapidly depreciating assets such as farm equipment (some of which is highly specialized with a limited or no market for resale), or assets such as livestock or crops. In such cases, any repossessed collateral for a defaulted agricultural operating loan may not provide an adequate source of repayment of the outstanding loan balance as a result of the greater likelihood of damage, loss or depreciation or because the assessed value of the collateral exceeds the eventual realization value. At December 31, 2018, there were $1.8 million of agricultural loans that were non-performing, or 11% of total non-performing loans.

- Consumer Loans. At December 31, 2018, consumer loans were $785.0 million, or 9% of our total loan portfolio. Our consumer loans often entail greater risk than first-lien residential mortgage loans. Home equity lines of credit generally entail greater risk than do one- to four-family residential mortgage loans where we are in the first lien position. For those home equity lines secured by a second mortgage, it is less likely that we will be successful in recovering all of our loan proceeds in the event of default. Our foreclosure on these loans requires that the value of the property be sufficient to cover the repayment of the first mortgage loan, as well as the costs associated with foreclosure. In the case of consumer loans that are unsecured or secured by rapidly depreciating assets such as automobiles, any repossessed collateral for a defaulted consumer loan may not provide an adequate source of repayment of the outstanding loan balance as a result of the greater likelihood of damage, loss or depreciation. The remaining deficiency often does not warrant further substantial collection efforts against the borrower. In addition, consumer loan collections are dependent on the borrower's continuing financial stability, and thus are more likely to be adversely affected by job loss, divorce, illness or personal bankruptcy. Furthermore, the application of various federal and state laws, including federal and state bankruptcy and insolvency laws, may limit the amount which can be recovered on these consumer loans. Loans that we purchased, or indirectly originated, may also give rise to claims and defenses by a consumer loan borrower against an assignee of such loans such as us, and a borrower may be able to assert against the assignee claims and defenses that it has against the seller of the underlying collateral. At December 31, 2018, consumer loans that were non-performing were $1.5 million, or 10% of our total non-performing loans.

Our allowance for loan losses may prove to be insufficient to absorb losses in our loan portfolio, which would cause our results of operations, liquidity and financial condition to be adversely affected.

Lending money is a substantial part of our business and each loan carries a certain risk that it will not be repaid in accordance with its terms or that any underlying collateral will not be sufficient to assure repayment. This risk is affected by, among other things:

- cash flow of the borrower and/or the project being financed;
- in the case of a collateralized loan, the changes and uncertainties as to the future value of the collateral;
- the duration of the loan;
- the character and creditworthiness of a particular borrower;
- changes in economic and industry conditions; and
- the duration of the loan.

We maintain an allowance for loan losses, which is a reserve established through a provision for loan losses charged to expense, which we believe is appropriate to provide for probable losses in our loan portfolio. The amount of this allowance is determined by our management through periodic reviews and consideration of several factors, including, but not limited to:

- our general reserve, based on our historical default and loss experience, certain macroeconomic factors, regulatory requirements and management's expectations of future events;
- our specific reserve, based on our evaluation of non-performing loans and their underlying collateral; and
- an unallocated reserve to provide for other credit losses inherent in our portfolio that may not have been contemplated in the other loss factors.

The determination of the appropriate level of the allowance for loan losses inherently involves a high degree of subjectivity and requires us to make significant estimates of current credit risks and future trends, all of which may undergo material changes. If our estimates are incorrect, the allowance for loan losses may not be sufficient to cover losses inherent in our loan portfolio, resulting in the need for increases in our allowance for loan losses through the provision for losses on loans which is recorded as charged against income. Management also recognizes that significant new growth in loan portfolios, new loan products and the refinancing of existing loans can result in portfolios comprised of unseasoned loans that may not perform in a historical or projected manner and will increase the risk that our allowance may be insufficient to absorb losses without significant additional provisions.

Deterioration in economic conditions affecting borrowers, new information regarding existing loans, identification of additional problem loans and other factors, both within and outside of our control, may require an increase in the allowance for loan losses. If current conditions in the housing and real estate markets weaken, we expect we will experience increased delinquencies and credit losses.

The Financial Accounting Standards Board has adopted a new accounting standard referred to as Current Expected Credit Loss (CECL) which will require financial institutions to determine periodic estimates of lifetime expected credit losses on loans and recognize the expected credit losses as allowances for credit losses. This will change the current method of providing allowances for credit losses only when they have been incurred and are probable, which may require us to increase our allowance for loan losses, and may greatly increase the types of data we would need to collect and review to determine the appropriate level of the allowance for credit losses. This accounting pronouncement is expected to be applicable to us for our first fiscal year after December 15, 2019. We are evaluating the impact the CECL accounting model will have on our accounting, but expect to recognize a onetime cumulative-effect adjustment to the allowance for loan losses as of the beginning of the first reporting period in which the new standard is effective. We cannot yet determine the magnitude of any such one-time cumulative adjustment or of the overall impact of the new standard on our financial condition or results of operations. The federal banking regulators, including the Federal Reserve and the FDIC, have adopted a rule that gives a banking organization the option to phase in over a three-year period the day-one adverse effects of CECL on its regulatory capital.

In addition, bank regulatory agencies periodically review our allowance for loan losses and may require an increase in the provision for possible loan losses or the recognition of further loan charge-offs, based on judgments different than those of management. If charge-offs in future periods exceed the allowance for loan losses, we may need additional provisions to increase the allowance for loan losses. Any increases in the allowance for loan losses will result in a decrease in net income and, most likely, capital, and may have a material negative effect on our financial condition and results of operations.

We pursue a strategy of supplementing internal growth by acquiring other financial companies or their assets and liabilities that we believe will help us fulfill our strategic objectives and enhance our earnings. We may be adversely affected by risks associated with potential acquisitions.

As part of our general growth strategy, we have recently expanded our business through acquisitions. During the fourth quarter of 2018, we acquired Skagit, and expect system integration to be completed in the first quarter of 2019. Although our business strategy emphasizes organic expansion, we continue, from time to time in the ordinary course of business, to engage in preliminary discussions with potential acquisition targets. There can be no assurance that, in the future, we will successfully identify suitable acquisition candidates, complete acquisitions and successfully integrate acquired operations into our existing operations or expand into new markets. The consummation of any future acquisitions may dilute shareholder value or may have an adverse effect upon our operating results while the operations of the acquired business are being integrated into our operations. In addition, once integrated, acquired operations may not achieve levels of profitability comparable to those achieved by Banner's existing operations, or otherwise perform as expected. Further, transaction-related expenses may adversely affect our earnings. These adverse effects on our earnings and results of operations may have a negative impact on the value of Banner's stock. Acquiring banks, bank branches or businesses involves risks commonly associated with acquisitions, including:

- We may be exposed to potential asset quality issues or unknown or contingent liabilities of the banks, businesses, assets, and liabilities we acquire. If these issues or liabilities exceed our estimates, our results of operations and financial condition may be materially negatively affected;
- Higher than expected deposit attrition;
- Potential diversion of our management's time and attention;
- Prices at which acquisitions can be made fluctuate with market conditions. We have experienced times during which acquisitions could not be made in specific markets at prices we considered acceptable and expect that we will experience this situation in the future;
- The acquisition of other entities generally requires integration of systems, procedures and personnel of the acquired entity into our company to make the transaction economically successful. This integration process is complicated and time consuming and can also be disruptive to the customers of the acquired business. If the integration process is not conducted successfully and with minimal adverse effect on the acquired business and its customers, we may not realize the anticipated economic benefits of particular acquisitions within the expected time frame, and we may lose customers or employees of the acquired business. We may also experience greater than anticipated customer losses even if the integration process is successful;
- To finance an acquisition, we may borrow funds, thereby increasing our leverage and diminishing our liquidity, or raise additional capital, which could dilute the interests of our existing shareholders;
- We have completed various acquisitions in the past few years that enhanced our rate of growth. We may not be able to continue to sustain our past rate of growth or to grow at all in the future; and
- To the extent our costs of an acquisition exceed the fair value of the net assets acquired, the acquisition will generate goodwill. As discussed below under "-If the goodwill we have recorded in connection with acquisitions become

impaired, our earnings and capital could be reduced," we are required to assess our goodwill for impairment at least annually, and any goodwill impairment charge could have a material adverse effect on our results of operations and financial condition.

The required accounting treatment of loans we acquire through acquisitions including purchase credit impaired loans could result in higher net interest margins and interest income in current periods and lower net interest margins and interest income in future periods.

Under GAAP, we are required to record loans acquired through acquisitions, including purchase credit impaired loans, at fair value. Estimating the fair value of such loans requires management to make estimates based on available information and facts and circumstances as of the acquisition date. Actual performance could differ from management's initial estimates. If these loans outperform our original fair value estimates, the difference between our original estimate and the actual performance of the loan (the "discount") is accreted into net interest income. Thus, our net interest margins may initially increase due to the discount accretion. We expect the yields on our loans to decline as our acquired loan portfolio pays down or matures and the discount decreases, and we could experience downward pressure on our interest income to the extent that the runoff on our acquired loan portfolio is not replaced with comparable high-yielding loans. This could result in higher net interest margins and interest income in current periods and lower net interest rate margins and lower interest income in future periods.

We may be adversely affected by recent changes in U.S. tax laws.

Changes in tax laws contained in the 2017 Tax Act, which was enacted in December 2017, include a number of provisions that will have an impact on the banking industry, borrowers and the market for single-family residential real estate. Changes include (i) a lower limit on the deductibility of mortgage interest on single-family residential mortgage loans, (ii) limitations on interest deductions for home equity loans, (iii) a limitation on the deductibility of business interest expense and (iv) a limitation on the deductibility of property taxes and state and local income taxes. The recent changes in the tax laws may have an adverse effect on the market for, and valuation of, residential properties, and on the demand for such loans in the future and could make it harder for borrowers to make their loan payments. If home ownership becomes less attractive, demand for mortgage loans could decrease. The value of the properties securing loans in our loan portfolio may be adversely impacted as a result of the changing economics of home ownership, which could require an increase in our provision for loan losses, which would reduce our profitability and could materially adversely affect our business, financial condition and results of operations.

Severe weather, natural disasters, or other catastrophes could significantly impact our business.
Severe weather, natural disasters, widespread disease or pandemics, acts of war or terrorism or other adverse external events could have a significant impact on our ability to conduct business. In addition, such events could affect the stability of our deposit base, impair the ability of borrowers to repay outstanding loans and leases, impair the value of collateral securing loans, cause significant property damage, result in loss of revenue or cause us to incur additional expenses. The occurrence of any of these events in the future could have a material adverse effect on our business, financial condition or results of operations.
Our growth or future losses may require us to raise additional capital in the future, but that capital may not be available when it is needed or the cost of that capital may be very high.

We are required by federal regulatory authorities to maintain adequate levels of capital to support our operations. We may at some point, however, need to raise additional capital to support continued growth or be required by our regulators to increase our capital resources. Any capital we obtain may result in the dilution of the interests of existing holders of our common stock. Our ability to raise additional capital, if needed, will depend on conditions in the capital markets at that time, which are outside our control, and on our financial condition and performance. Accordingly, we cannot make assurances that we will be able to raise additional capital if needed on terms that are acceptable to us, or at all. If we cannot raise additional capital when needed, our ability to further expand our operations could be materially impaired and our financial condition and liquidity could be materially and adversely affected. In addition, if we are unable to raise additional capital when required by our bank regulators, we may be subject to adverse regulatory action.

If our investments in real estate are not properly valued or sufficiently reserved to cover actual losses, or if we are required to increase our valuation reserves, our earnings could be reduced.

We obtain updated valuations in the form of appraisals and broker price opinions when a loan has been foreclosed and the property taken in as REO and at certain other times during the assets holding period. Our net book value (NBV) in the loan at the time of foreclosure and thereafter is compared to the updated market value of the foreclosed property less estimated selling costs (fair value). A charge-off is recorded for any excess in the asset’s NBV over its fair value. If our valuation process is incorrect, or if property values decline, the fair value of the investments in real estate may not be sufficient to recover our carrying value in such assets, resulting in the need for additional write-downs. Significant write-downs to our investments in real estate could have a material adverse effect on our financial condition, liquidity and results of operations.

In addition, bank regulators periodically review our REO and may require us to recognize further write-downs. Any increase in our write-downs, as required by the bank regulators, may have a material adverse effect on our financial condition, liquidity and results of operations.

Our securities portfolio may be negatively impacted by fluctuations in market value and interest rates.

Our securities portfolio may be impacted by fluctuations in market value, potentially reducing accumulated other comprehensive income and/or earnings. Fluctuations in market value may be caused by changes in market interest rates, rating agency actions in respect of the securities, defaults by the issuer or with respect to the underlying securities, lower market prices for securities and limited investor demand. Our securities portfolio is evaluated for other-than-temporary impairment. If this evaluation shows impairment to the actual or projected cash flows associated with one or more securities, a potential loss to earnings may occur. Changes in interest rates can also have an adverse effect on our financial condition, as our available-for-sale securities are reported at their estimated fair value, and therefore are impacted by fluctuations in interest rates. We increase or decrease our shareholders' equity by the amount of change in the estimated fair value of the available-for-sale securities, net of taxes. There can be no assurance that the declines in market value will not result in other-than-temporary impairments of these assets, which would lead to accounting charges that could have a material adverse effect on our net income and capital levels.

An increase in interest rates, change in the programs offered by secondary market purchasers or our ability to qualify for their programs may reduce our mortgage banking revenues, which would negatively impact our non-interest income.

Our mortgage banking operations provide a significant portion of our non-interest income. We generate mortgage banking revenues primarily from gains on the sale of one- to four-family and multifamily mortgage loans. The one- to four-family mortgage loans are sold pursuant to programs currently offered by Fannie Mae, Freddie Mac, Ginnie Mae and non-Government Sponsored Enterprise (GSE) investors. These entities account for a substantial portion of the secondary market in residential one- to four-family mortgage loans. Multifamily mortgage loans are sold primarily to non-GSE investors.

Any future changes in the one- to four-family programs, our eligibility to participate in these programs, the criteria for loans to be accepted or laws that significantly affect the activity of such entities, or a reduction in the size of the secondary market for multifamily loans could, in turn, materially adversely affect our results of operations. Mortgage banking is generally considered a volatile source of income because it depends largely on the level of loan volume which, in turn, depends largely on prevailing market interest rates. In a rising or higher interest rate environment, our originations of mortgage loans may decrease, resulting in fewer loans that are available to be sold to investors. This would result in a decrease in mortgage banking revenues and a corresponding decrease in non-interest income. In addition, our results of operations are affected by the amount of non-interest expense associated with mortgage banking activities, such as salaries and employee benefits, occupancy, equipment and data processing expense and other operating costs. During periods of reduced loan demand, our results of operations may be adversely affected to the extent that we are unable to reduce expenses commensurate with the decline in loan originations. In addition, although we sell loans into the secondary market without recourse, we are required to give customary representations and warranties about the loans to the buyers. If we breach those representations and warranties, the buyers may require us to repurchase the loans and we may incur a loss on the repurchase.

Certain hedging strategies that we use to manage investment in mortgage servicing rights, mortgage loans held for sale and interest rate lock commitments may be ineffective to offset any adverse changes in the fair value of these assets due to changes in interest rates and market liquidity.

We use derivative instruments to economically hedge mortgage servicing rights, mortgage loans held for sale and interest rate lock commitments to offset changes in fair value resulting from changing interest rate environments. Our hedging strategies are susceptible to prepayment risk, basis risk, market volatility and changes in the shape of the yield curve, among other factors. In addition, hedging strategies rely on assumptions and projections regarding assets and general market factors. If these assumptions and projections prove to be incorrect or our hedging strategies do not adequately mitigate the impact of changes in interest rates, we may incur losses that would adversely impact earnings.

Our results of operations, liquidity and cash flows are subject to interest rate risk.

Our earnings and cash flows are largely dependent upon our net interest income. Interest rates are highly sensitive to many factors that are beyond our control, including general economic conditions and policies of various governmental and regulatory agencies and, in particular, the Federal Reserve. The Federal Reserve has steadily increased the targeted federal funds rate over the last three fiscal years to 2.50% at December 31, 2018. The Federal Reserve could make additional increases in interest rates during 2019 subject to economic conditions. If the Federal Reserve increases the targeted federal funds rates, overall interest rates will likely rise, which may negatively impact both the housing markets by reducing refinancing activity and new home purchases and the U.S. economic recovery.

We principally manage interest rate risk by managing our volume and mix of our earning assets and funding liabilities. Changes in monetary policy, including changes in interest rates, could influence not only the interest we receive on loans and investments and the amount of interest we pay on deposits and borrowings, but these changes could also affect (i) our ability to originate and/or sell loans and obtain deposits, (ii) the fair value of our financial assets and liabilities, which could negatively impact shareholders’ equity, and our ability to realize gains from the sale of such assets, (iii) our ability to obtain and retain deposits in competition with other available investment alternatives, (iv) the ability of our borrowers to repay adjustable or variable rate loans, and (v) the average duration of our investment securities portfolio and other interest-earning assets. In a changing interest rate environment, we may not be able to manage this risk effectively. If we are unable to manage interest rate risk effectively, our business, financial condition and results of operations could be materially affected.

Changes in interest rates could also have a negative impact on our results of operations by reducing the ability of borrowers to repay their current loan obligations or by reducing our margins and profitability. Our net interest margin is the difference between the yield we earn on our assets and the interest rate we pay for deposits and our other sources of funding. Changes in interest rates—up or down—could adversely affect our net interest margin and, as a result, our net interest income. Although the yield we earn on our assets and our funding costs tend to move in the same direction in response to changes in interest rates, one can rise or fall faster than the other, causing our net interest margin to expand or contract. Our liabilities tend to be shorter in duration than our assets, so they may adjust faster in response to changes in interest rates. As a result, when interest rates rise, our funding costs may rise faster than the yield we earn on our assets, causing our net interest margin to contract until the yield catches up. Changes in the slope of the "yield curve"—or the spread between short-term and long-term interest rates—could also reduce our net interest margin. Normally, the yield curve is upward sloping, meaning short-term rates are lower than long-term rates. Because our liabilities tend to be shorter in duration than our assets, when the yield curve flattens or even inverts, we could experience pressure on our net interest margin as our cost of funds increases relative to the yield we can earn on our assets. Also, interest rate decreases can lead to increased prepayments of loans and mortgage-backed securities as borrowers refinance their loans to reduce borrowing costs. Under these circumstances, we are subject to reinvestment risk as we may have to redeploy such repayment proceeds into lower yielding investments, which would likely hurt our income.

An increasing percentage of our deposits have been comprised of deposits bearing no or a relatively low rate of interest and having a shorter duration than our assets. We would incur a higher cost of funds to retain these deposits in a rising interest rate environment. If the interest rates paid on deposits and other borrowings increase at a faster rate than the interest rates received on loans and other investments, our net interest income, and therefore earnings, could be adversely affected.

In addition, a substantial amount of our loans have adjustable interest rates. As a result, these loans may experience a higher rate of default in a rising interest rate environment. Further, a significant portion of our adjustable rate loans have interest rate floors below which the loan's contractual interest rate may not adjust. Approximately 66% of our loan portfolio was comprised of adjustable or floating-rate loans at December 31, 2018, and approximately $2.81 billion, or 49%, of those loans contained interest rate floors, below which the loans' contractual interest rate may not adjust. At December 31, 2018, the weighted average floor interest rate of these loans was 4.71%. At that date, approximately $845.8 million, or 30%, of these loans were at their floor interest rate. The inability of our loans to adjust downward can contribute to increased income in periods of declining interest rates, although this result is subject to the risks that borrowers may refinance these loans during periods of declining interest rates. Also, when loans are at their floors, there is a further risk that our interest income may not increase as rapidly as our cost of funds during periods of increasing interest rates which could have a material adverse effect on our results of operations.

Changes in interest rates also affect the value of our interest-earning assets and in particular our securities portfolio. Generally, the fair value of fixed-rate securities fluctuates inversely with changes in interest rates. Unrealized gains and losses on securities available for sale are reported as a separate component of equity, net of tax. Decreases in the fair value of securities available for sale resulting from increases in interest rates could have an adverse effect on stockholders' equity.

Although management believes it has implemented effective asset and liability management strategies to reduce the potential effects of changes in interest rates on our results of operations, any substantial, unexpected, prolonged change in market interest rates could have a material adverse effect on our financial condition, liquidity and results of operations. Also, our interest rate risk modeling techniques and assumptions may not fully predict or capture the impact of actual interest rate changes on our balance sheet or projected operating results. For further discussion of how changes in interest rates could impact us, see "Part II, Item 7A. Quantitative and Qualitative Disclosures About Market Risk" for additional information about our interest rate risk management.

Uncertainty relating to the London Interbank Offered Rate (LIBOR) calculation process and potential phasing out of LIBOR may adversely affect our results of operations.

On July 27, 2017, the Chief Executive of the United Kingdom Financial Conduct Authority, which regulates LIBOR, announced that it intends to stop persuading or compelling banks to submit rates for the calibration of LIBOR to the administrator of LIBOR after 2021. The announcement indicates that the continuation of LIBOR on the current basis cannot and will not be guaranteed after 2021. It is impossible to predict whether and to what extent banks will continue to provide LIBOR submissions to the administrator of LIBOR or whether any additional reforms to LIBOR may be enacted in the United Kingdom or elsewhere. At this time, no consensus exists as to what rate or rates may become acceptable alternatives to LIBOR and it is impossible to predict the effect of any such alternatives on the value of LIBOR-based securities and variable rate loans, subordinated debentures, or other securities or financial arrangements, given LIBOR's role in determining market interest rates globally. Uncertainty as to the nature of alternative reference rates and as to potential changes or other reforms to LIBOR may adversely affect LIBOR rates and the value of LIBOR-based loans, and to a lesser extent, securities in our portfolio, and may impact the availability and cost of hedging instruments and borrowings, including the rates we pay on our subordinated debentures and trust preferred securities. If LIBOR rates are no longer available, and we are required to implement substitute indices for the calculation of interest rates under our loan agreements with our borrowers or our existing borrowings, we may incur significant expenses in effecting the transition, and may be subject to disputes or litigation with customers and creditors over the appropriateness or comparability to LIBOR of the substitute indices, which could have an adverse effect on our results of operations.

We will be subject to additional regulatory scrutiny since Banner Bank maintains total assets exceeding $10.0 billion.

Banner Bank's total assets were $11.58 billion at December 31, 2018, the fourth consecutive quarter where the total assets of Banner Bank exceeded $10 billion. As a result, Banner Bank and its affiliates will become subject to a number of additional requirements (such as general oversight by the CFPB) that will impose additional compliance costs on our business. As a result, there may also be additional higher expectations from regulators. The CFPB has supervision authority, including examination authority, over such institutions and their affiliates to assess compliance with federal consumer financial laws, to obtain information about the institutions' activities and compliance systems and procedures, and to detect and assess risks to consumers and markets.

Since Banner Bank has exceeded $10 billion in assets for four consecutive quarters, the method for determining its federal deposit insurance assessments will change from the method for smaller institutions (based on CAMELS ratings and certain financial ratios) to a scorecard method. The scorecard method uses a performance score and a loss severity score, which are combined and converted into an initial base assessment rate. The performance score is based on measures of the bank's ability to withstand asset-related stress and funding-related stress and weighted CAMELS ratings, which are ratings ascribed under the CAMELS supervisory rating system and assigned based on a supervisory authority's analysis of a bank's financial statements and on-site examinations. The loss severity score is a measure of potential losses to the FDIC in the event of the bank's failure. Under a formula, the performance score and loss severity score are combined and converted to a total score that determines the bank's initial base assessment rate. The FDIC has the discretion to alter the total score based on factors not captured by the scorecard. The resulting initial base assessment rate is also subject to adjustments downward based on long-term unsecured debt issued by the bank, to adjustment upward based on long-term unsecured debt held by the bank that is issued by other FDIC-insured institutions, and to further adjustment upward if the bank's brokered deposits exceed 10% of its domestic deposits.

The Dodd-Frank Act also requires publicly-traded bank holding companies with average assets of $10 billion or more for four consecutive quarters to establish a risk committee responsible for enterprise-wide risk management practices, comprised of independent directors, including one risk management expert.

As a result of the above, now that Banner's and Banner Bank's total assets exceed $10 billion deposit insurance assessments, expenses related to regulatory compliance are likely to increase, and interchange fee income will decrease, the cumulative effect of which may be significant.

Reductions in interchange income could negatively impact our earnings.

Banner Bank and Islanders Bank expect to be affected by the Durbin Amendment to the Dodd-Frank Act regarding limits on debit card interchange fees. The Durbin Amendment gave the Federal Reserve the authority to establish rules regarding interchange fees charged for electronic debit transactions by a payment card issuer that, together with its affiliates, has assets of $10 billion or more at year end and to enforce a new statutory requirement that such fees be reasonable and proportional to the actual cost of a transaction to the issuer. Banner and Banner Bank exceeded $10 billion in assets as of December 31, 2018 and therefore Banner Bank and Islanders Bank will be subject to the Durbin Amendment interchange fee limitation effective July 1, 2019. The Federal Reserve has adopted rules under this provision that limit the swipe fees that a debit card issuer can charge a merchant for a transaction to the sum of 21 cents and five basis points times the value of the transaction, plus up to one cent for fraud prevention costs. Based on current debit card volume, we believe we will experience a reduction of approximately $15 million a year in debit card related fee income and pre-tax earnings following the application of the Durbin Amendment to Banner Bank and and Islanders Bank beginning July 1, 2019.

Interchange income is derived from fees paid by merchants to the interchange network in exchange for the use of the network's infrastructure and payment facilitation. These fees are paid to card issuers to compensate them for the costs associated with issuance and operation. We earned interchange fees on card transactions from our debit cards, including $23.2 million during the year ended December 31, 2018. Merchants have attempted to negotiate lower interchange rates, and the Durbin Amendment to the Dodd-Frank Act, which we are subject to now that our total assets exceed $10.0 billion, limits the amount of interchange fees that may be charged for certain debit card transactions. See “We will be subject to additional regulatory scrutiny since Banner Bank maintains total assets exceeding $10.0 billion.” As the financial services industry evolves, consumers may find debit financial services to be less attractive than traditional or other financial services. Consumers might not use debit card financial services for any number of reasons, including the general perception of our industry. If consumers do not continue or increase their usage of debit cards, including making changes in the way debit cards are loaded, our operating revenues and debit card deposits may remain at current levels or decline. Any projected growth for the industry may not occur or may occur more slowly than estimated. If consumer acceptance of debit financial services does not continue to develop or develops more slowly than expected or if there is a shift in the mix of payment forms, such as cash, credit cards, traditional debit cards and debit cards, away from our products and services, it could have a material adverse effect on our financial position and results of operations. Merchants may also continue to pursue alternative payment platforms, such as Apple Pay, to lower their processing costs. Any such new payment system may reduce our interchange income. Our failure to comply with the operating regulations set forth by payment card networks, which may change, could subject us to penalties, fees or the termination of our license to use the networks. Any of these scenarios could have a material impact on our business, financial condition and results of operations.

Our business and financial results could be impacted materially by adverse results in legal proceedings.

Legal proceedings could result in judgments, significant time and attention from our management, or other adverse effects on our business and financial results. We establish estimated liabilities for legal claims when payments associated with claims become probable and the amount of loss can be reasonably estimated. We may still incur losses for a matter even if we have not established an estimated liability. In addition, the actual cost of resolving a legal claim may be substantially higher than any amounts accrued for that matter. The ultimate resolution of any legal proceeding, depending on the remedy sought and granted, could materially adversely affect our results of operations and financial condition.

New or changing tax, accounting, and regulatory rules and interpretations could significantly impact strategic initiatives, results of operations, cash flows, and financial condition.

The financial services industry is extensively regulated. Federal and state banking regulations are designed primarily to protect the deposit insurance funds and consumers, not to benefit our shareholders. These regulations may sometimes impose significant limitations on operations. Regulatory authorities have extensive discretion in connection with their supervisory and enforcement activities, including the imposition of restrictions on the operation of an institution, the classification of assets by the institution and the adequacy of an institution's allowance for loan losses. These bank regulators also have the ability to impose conditions in the approval of merger and acquisition transactions.

Additionally, actions by regulatory agencies or significant litigation against us and may lead to penalties that materially affect us. These regulations, along with the currently existing tax, accounting, securities, insurance, and monetary laws, regulations, rules, standards, policies, and interpretations control the methods by which financial institutions conduct business, implement strategic initiatives and tax compliance, and govern financial reporting and disclosures. These laws, regulations, rules, standards, policies, and interpretations are constantly evolving and may change significantly over time. Any new regulations or legislation, change in existing regulations or oversight, whether a change in regulatory policy or a change in a regulator's interpretation of a law or regulation, could have a material impact on our operations, increase our costs of regulatory compliance and of doing business and/or otherwise adversely affect us and our profitability. Further, changes in accounting standards can be both difficult to predict and involve judgment and discretion in their interpretation by us and our independent registered public accounting firm. These changes could materially impact, potentially even retroactively, how we report our financial condition and results of our operations as could our interpretation of those changes. We cannot predict what restrictions may be imposed upon us with future legislation.

Non-compliance with the USA PATRIOT Act, Bank Secrecy Act, or other laws and regulations could result in fines or sanctions and limit our ability to get regulatory approval of acquisitions.

The USA PATRIOT and Bank Secrecy Acts require financial institutions to develop programs to prevent financial institutions from being used for money laundering and terrorist activities. If such activities are detected, financial institutions are obligated to file suspicious activity reports with the U.S. Treasury’s Office of Financial Crimes Enforcement Network. These rules require financial institutions to establish procedures for identifying and verifying the identity of customers seeking to open new financial accounts. Failure to comply with these regulations could result in fines or sanctions and limit our ability to get regulatory approval of acquisitions. Recently several banking institutions have received large fines for non-compliance with these laws and regulations. While we have developed policies and procedures designed to assist in compliance with these laws and regulations, no assurance can be given that these policies and procedures will be effective in preventing violations of these laws and regulations.

Development of new products and services may impose additional costs on us and may expose us to increased operational risk.

Our financial performance depends, in part, on our ability to develop and market new and innovative services and to adopt or develop new technologies that differentiate our products or provide cost efficiencies, while avoiding increased related expenses. This dependency is exacerbated in the current “FinTech” environment, where financial institutions are investing significantly in evaluating new technologies, such as “Blockchain,” and developing potentially industry-changing new products, services and industry standards. The introduction of new products and services can entail significant time and resources, including regulatory approvals. Substantial risks and uncertainties are associated with the introduction of new products and services, including technical and control requirements that may need to be developed and implemented, rapid technological change in the industry, our ability to access technical and other information from our clients, the significant and ongoing investments required to bring new products and services to market in a timely manner at competitive prices and the preparation of marketing, sales and other materials that fully and accurately describe the product or service and its underlying risks. Our failure to manage these risks and uncertainties also exposes us to enhanced risk of operational lapses which may result in the recognition of financial statement liabilities. Regulatory and internal control requirements, capital requirements, competitive alternatives, vendor relationships and shifting market preferences may also determine if such initiatives can be brought to market in a manner that is timely and attractive to our clients. Failure to successfully manage these risks in the development and implementation of new products or services could have a material adverse effect on our business and reputation, as well as on our consolidated results of operations and financial condition.

If the goodwill we have recorded in connection with acquisitions become impaired, our earnings and capital could be reduced.

In accordance with GAAP, we record assets acquired and liabilities assumed at their fair value with the excess of the purchase consideration over the net assets acquired resulting in the recognition of goodwill. As a result, acquisitions typically result in recording goodwill. We perform a goodwill evaluation at least annually to test for goodwill impairment. As part of our testing, we first assess qualitative factors to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount. If we determine the fair value of a reporting unit is less than its carrying amount using these qualitative factors, we then compare the fair value of goodwill with its carrying amount and measure impairment loss by comparing the implied fair value of goodwill with the carrying amount of that goodwill. Adverse conditions in our business climate, including a significant decline in future operating cash flows, a significant change in our stock price or market capitalization, or a deviation from our expected growth rate and performance may significantly affect the fair value of our goodwill and may trigger additional impairment losses, which could be materially adverse to our operating results and financial position.

We cannot provide assurance that we will not be required to take an impairment charge in the future. Any impairment charge would have an adverse effect on our results of shareholders’ equity and financial results and could cause a decline in our stock price. The acquisitions of Skagit Bancorp, Inc, and its subsidiary, Skagit Bank have increased our goodwill.

Liquidity risk could impair our ability to fund operations and jeopardize our financial condition, growth and prospects.

Liquidity is essential to our business. We rely on a number of different sources in order to meet our potential liquidity demands. We require sufficient liquidity to meet customer loan requests, customer deposit maturities and withdrawals, payments on our debt obligations as they come due and other cash commitments under both normal operating conditions and other unpredictable circumstances, including events causing industry or general financial market stress. A tightening of the credit markets resulting in our inability to obtain adequate funding may negatively affect our liquidity, asset growth and, consequently, our earnings capability and capital levels. In addition to any deposit growth, and the sale of loans or investment securities, maturity of investment securities and loan payments, we rely from time to time on advances from the FHLB of Des Moines, and certain other wholesale funding sources to meet liquidity demands. Our liquidity position could be significantly constrained if we were unable to access funds from the FHLB of Des Moines or other wholesale funding sources. Factors that could detrimentally impact our access to liquidity sources include a decrease in the level of our business activity as a result of a downturn in the markets in which our loans are concentrated, negative operating results, or adverse regulatory action against us. Our ability to borrow could also be impaired by factors that are not specific to us, such as a disruption in the financial markets or negative views and expectations about the prospects for the financial services industry or deterioration in credit markets. Any decline in available funding in amounts adequate to finance our activities or on terms which are acceptable to us could adversely impact our ability to originate loans, invest in securities, meet our expenses, or fulfill obligations such as repaying our borrowings or meeting deposit withdrawal demands, any of which could, in turn, have a material adverse effect on our business, financial condition and results of operations

Additionally, our liquidity is affected by our collateralized public funds, which are bank deposits of state and local municipalities. These deposits are required to be secured by certain investment grade securities to ensure repayment, which on the one hand tends to reduce our contingent liquidity risk by making these funds somewhat less credit sensitive, but on the other hand reduces standby liquidity by restricting the potential liquidity of the pledged collateral. Although these funds historically have been a relatively stable source of funds for us, availability depends on the individual municipality's fiscal policies and cash flow needs.

We are dependent on key personnel and the loss of one or more of those key personnel may materially and adversely affect our prospects.

Competition for qualified employees and personnel in the banking industry is intense and there are a limited number of qualified persons with knowledge of, and experience in, the community banking industry where the Banks conduct their business. The process of recruiting personnel with the combination of skills and attributes required to carry out our strategies is often lengthy. Our success depends to a significant degree upon our ability to attract and retain qualified management, loan origination, finance, administrative, marketing and technical personnel and upon the continued contributions of our management and personnel. In particular, our success has been and continues to be highly dependent upon the abilities of key executives, including our President, and certain other employees. We could undergo a difficult transition period if we were to lose the services of any of these individuals. Our success also depends on the experience of our banking facilities' managers and bankers and on their relationships with the customers and communities they serve. In addition, our success has been and continues to be highly dependent upon the services of our directors, many of whom are at or nearing retirement age, and we may not be able to identify and attract suitable candidates to replace such directors. The loss of these key persons could negatively impact the affected banking operations.

Our operations rely on numerous external vendors.

We rely on numerous external vendors to provide us with products and services necessary to maintain our day-to-day operations. Accordingly, our operations are exposed to risk that these vendors will not perform in accordance with the contracted arrangements under service level agreements. The failure of an external vendor to perform in accordance with the contracted arrangements under service level agreements because of changes in the vendor's organizational structure, financial condition, support for existing products and services or strategic focus or for any other reason, could be disruptive to our operations, which in turn could have a material negative impact on our financial condition and results of operations. We also could be adversely affected to the extent such an agreement is not renewed by the third party vendor or is renewed on terms less favorable to us.

Any inaccurate assumptions in our analytical and forecasting models could cause us to miscalculate our projected revenue or losses, which could adversely affect us.

We use analytical and forecasting models to estimate the effects of economic conditions on our financial assets and liabilities as well as our mortgage servicing rights. Those models include assumptions about interest rates and consumer behavior that may be incorrect. If our model assumptions are incorrect, improperly applied or inadequate, we may record higher than expected losses or lower than expected revenues which could have a material adverse effect on our business, financial condition and results of operations.

Our business may be adversely affected by an increasing prevalence of fraud and other financial crimes.

Our loans to businesses and individuals and our deposit relationships and related transactions are subject to exposure to the risk of loss due to fraud and other financial crimes. Nationally, reported incidents of fraud and other financial crimes have increased. We have also experienced losses due to apparent fraud and other financial crimes. While we have policies and procedures designed to prevent such losses, there can be no assurance that such losses will not occur.

Managing reputational risk is important to attracting and maintaining customers, investors and employees.

Threats to our reputation can come from many sources, including adverse sentiment about financial institutions generally, unethical practices, employee misconduct, failure to deliver minimum standards of service or quality or operational failures due to integration or conversion challenges as a result of acquisitions we undertake, compliance deficiencies, and questionable or fraudulent activities of our customers. We have policies and procedures in place to protect our reputation and promote ethical conduct, but these policies and procedures may not be fully effective. Negative publicity regarding our business, employees, or customers, with or without merit, may result in the loss of customers, investors and employees, costly litigation, a decline in revenues and increased governmental regulation.

If our enterprise risk management framework is not effective at mitigating risk and loss to us, we could suffer unexpected losses and our results of operations could be materially adversely affected.

Our enterprise risk management framework seeks to achieve an appropriate balance between risk and return, which is critical to optimizing stockholder value. We have established processes and procedures intended to identify, measure, monitor, report, analyze and control the types of risk to which we are subject. These risks include liquidity risk, credit risk, market risk, interest rate risk, operational risk, legal and compliance risk, and reputational risk, among others. We also maintain a compliance program to identify, measure, assess, and report on our adherence to applicable laws, policies and procedures. While we assess and improve these programs on an ongoing basis, there can be no assurance that our risk management or compliance programs, along with other related controls, will effectively mitigate all risk and limit losses in our business. However, as with any risk management framework, there are inherent limitations to our risk management strategies as there may exist, or develop in the future, risks that we have not appropriately anticipated or identified. If our risk management framework proves ineffective, we could suffer unexpected losses and our business financial condition and results of operations could be materially adversely affected.

We are subject to certain risks in connection with our use of technology.

Our security measures may not be sufficient to mitigate the risk of a cyber attack. Communications and information systems are essential to the conduct of our business, as we use such systems to manage our customer relationships, our general ledger and virtually all other aspects of our business. Our operations rely on the secure processing, storage, and transmission of confidential and other information in our computer systems and networks. Although we take protective measures and endeavor to modify them as circumstances warrant, the security of our computer systems, software, and networks may be vulnerable to breaches, fraudulent or unauthorized access, denial or degradation of service attacks, misuse, computer viruses, malware or other malicious code and cyber-attacks that could have a security impact. If one or more of these events occur, this could jeopardize our or our customers' confidential and other information processed and stored in, and transmitted through, our computer systems and networks, or otherwise cause interruptions or malfunctions in our operations or the operations of our customers or counterparties. We may be required to expend significant additional resources to modify our protective measures or to investigate and remediate vulnerabilities or other exposures, and we may be subject to litigation and financial losses that are either not insured against or not fully covered through any insurance maintained by us. We could also suffer significant reputational damage.

Security breaches in our internet banking activities could further expose us to possible liability and damage our reputation. Increases in criminal activity levels and sophistication, advances in computer capabilities, new discoveries, vulnerabilities in third party technologies (including browsers and operating systems) or other developments could result in a compromise or breach of the technology, processes and controls that we use to prevent fraudulent transactions and to protect data about us, our clients and underlying transactions. Any compromise of our security could deter customers from using our internet banking services that involve the transmission of confidential information. We rely on standard internet security systems to provide the security and authentication necessary to effect secure transmission of data. Although we have developed and continue to invest in systems and processes that are designed to detect and prevent security breaches and cyber-attacks and periodically test our security, these precautions may not protect our systems from compromises or breaches of our security measures, and could result in losses to us or our customers, our loss of business and/or customers, damage to our reputation, the incurrence of additional expenses, disruption to our business, our inability to grow our online services or other businesses, additional regulatory scrutiny or penalties, or our exposure to civil litigation and possible financial liability, any of which could have a material adverse effect on our business, financial condition and results of operations.

Our security measures may not protect us from system failures or interruptions. While we have established policies and procedures to prevent or limit the impact of systems failures and interruptions, there can be no assurance that such events will not occur or that they will be adequately addressed if they do. In addition, we outsource certain aspects of our data processing and other operational functions to certain third-party providers. While we select third-party vendors carefully, we do not control their actions. If our third-party providers encounter difficulties including those resulting from breakdowns or other disruptions in communication services provided by a vendor, failure of a vendor to handle current or higher transaction volumes, cyber-attacks and security breaches or if we otherwise have difficulty in communicating with them, our ability to adequately process and account for transactions could be affected, and our ability to deliver products and services to our customers and otherwise conduct business operations could be adversely impacted. Replacing these third-party vendors could also entail significant delay and expense. Threats to information security also exist in the processing of customer information through various other vendors and their personnel.

We cannot assure you that such breaches, failures or interruptions will not occur or, if they do occur, that they will be adequately addressed by us or the third parties on which we rely. We may not be insured against all types of losses as a result of third party failures and insurance coverage may be inadequate to cover all losses resulting from breaches, system failures or other disruptions. If any of our third-party service providers experience financial, operational or technological difficulties, or if there is any other disruption in our relationships with them, we may be required to identify alternative sources of such services, and we cannot assure you that we could negotiate terms that are as favorable to us, or could obtain services with similar functionality as found in our existing systems without the need to expend substantial resources, if at all. Further, the occurrence of any systems failure or interruption could damage our reputation and result in a loss of customers and business, could subject us to additional regulatory scrutiny, or could expose us to legal liability. Any of these occurrences could have a material adverse effect on our financial condition and results of operations.

The board of directors oversees the risk management process, including the risk of cybersecurity breaches, and engages with management on cybersecurity issues.

We are subject to certain risks in connection with our data management or aggregation.

We are reliant on our ability to manage data and our ability to aggregate data in an accurate and timely manner to ensure effective risk reporting and management. Our ability to manage data and aggregate data may be limited by the effectiveness of our policies, programs, processes and practices that govern how data is acquired, validated, stored, protected and processed. While we continuously update our policies, programs, processes and practices, many of our data management and aggregation processes are manual and subject to human error or system failure. Failure to manage data effectively and to aggregate data in an accurate and timely manner may limit our ability to manage current and emerging risks, as well as to manage changing business needs.

We rely on dividends from Banner Bank for substantially all of our revenue at the holding company level.

We are an entity separate and distinct from our principal subsidiary, Banner Bank, and derive substantially all of our revenue at the holding company level in the form of dividends from that subsidiary. Accordingly, we are, and will be, dependent upon dividends from Banner Bank to pay the principal of and interest on our indebtedness, to satisfy our other cash needs and to pay dividends on our common stock. Banner Bank's ability to pay dividends is subject to its ability to earn net income and to meet certain regulatory requirements. In the event Banner Bank is unable to pay dividends to us, we may not be able to pay dividends on our common stock. Also, our right to participate in a distribution of assets upon a subsidiary's liquidation or reorganization is subject to the prior claims of the subsidiary's creditors.

Our articles of incorporation contain a provision which could limit the voting rights of a holder of our common stock.

Our charter provides that any person or group who acquires beneficial ownership of our common stock in excess of 10.0% of the outstanding shares may not vote the excess shares. Accordingly, if you acquire beneficial ownership of more than 10.0% of the outstanding shares of our common stock, your voting rights with respect to our common stock will not be commensurate with your economic interest in our company.

Anti-takeover provisions could negatively affect our shareholders.

Provisions in our articles of incorporation and bylaws, the corporate laws of the state of Washington and federal laws and regulations could delay or prevent a third party from acquiring us, despite the possible benefit to our shareholders, or otherwise negatively affect the market value of our stock. These provisions, among others, include: a prohibition on voting shares of our common stock beneficially owned in excess of 10.0% of total shares outstanding; advance notice requirements for nominations for election to our board of directors and for proposing matters that shareholders may act on at shareholder meetings; and staggered three-year terms for directors. Our articles of incorporation also authorize our board of directors to issue preferred or other stock, and preferred or other stock could be issued as a defensive measure in response to a takeover proposal. In addition, because we are a bank holding company, the ability of a third party to acquire us is limited by applicable banking laws and regulations. The Bank Holding Company Act requires any bank holding company to obtain the approval of the Federal Reserve before acquiring 5% or more of any class of our voting securities. Any entity that is a holder of 25% or more of any class of our voting securities, or in some circumstances a holder of a lesser percentage, is subject to regulation as a bank holding company under the Bank Holding Company Act. Under the Change in Bank Control Act of 1978, as amended, any person (or persons acting in concert), other than a bank holding company, is required to notify the Federal Reserve before acquiring 10% or more of any class of our voting securities.

Item 1B – Unresolved Staff Comments

None.

Item 2 – Properties

Banner Corporation maintains its administrative offices and main branch office, which is owned by us, in Walla Walla, Washington. In total, as of December 31, 2018, we have 182 branch offices located in Washington, Oregon, California, and Idaho. The 182 branches include 179 Banner Bank branches and three Islanders Bank branches. Geographically we have 93 branches are located in Washington, 43 in Oregon, 32 in California and 14 in Idaho. Of these branch locations, approximately half are owned and the other half are leased facilities. In addition to the branch locations, we also have 17 loan production offices, ten of which are located in Washington, three in California, two in Oregon, and one each in Idaho and Utah. All loan production offices are leased facilities. The lease terms for our branch and loan production offices are not individually material. Lease expirations range from one to 25 years. Administrative support offices are primarily in Washington, where we have ten facilities, of which we own six and lease two. Additionally, we have two leased administrative support offices in both Idaho and Oregon. In the opinion of management, all properties are adequately covered by insurance, are in a good state of repair and are appropriately designed for their present and future use.

Item 3 – Legal Proceedings

In the normal course of our business, we have various legal proceedings and other contingent matters pending. These proceedings and the associated legal claims are often contested and the outcome of individual matters is not always predictable. Furthermore, in some matters, it is difficult to assess potential exposure because the legal proceeding is still in the pretrial stage. We are not a party to any pending legal proceedings that we believe would have a material adverse effect on our financial condition, operations or cash flows.

Item 4 – Mine Safety Disclosures

Not applicable.

PART II

Item 5 – Market for Registrant’s Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities

Our voting common stock is principally traded on the NASDAQ Global Select Market under the symbol “BANR.” Shareholders of record as of December 31, 2018 totaled 2,141 based upon securities position listings furnished to us by our transfer agent. This total does not reflect the number of persons or entities who hold stock in nominee or “street” name through various brokerage firms.

Issuer Purchases of Equity Securities

The following table provides information about repurchases of common stock by the Company during the quarter ended December 31, 2018:

Period	Total Number of Common Shares Purchased	Average Price Paid per Common Share	Total Number of Shares Purchased as Part of Publicly Announced Plan	Maximum Number of Remaining Shares that May be Purchased at Period End under the Board Authorization
October 1, 2018 - October 31, 2018	2,833	$ 62.37	—	1,621,549
November 1, 2018 - November 30, 2018	137,975	59.86	137,975	1,483,574
December 1, 2018 - December 31, 2018	187,046	57.62	187,025	1,296,549
Total for quarter	327,854	58.60	325,000	1,296,549

On March 28, 2018, the Company announced that its Board of Directors had renewed its authorization to repurchase up to 5% of the Company's common stock, or 1,621,549 of the Company's outstanding shares. Under the authorization, shares may be repurchased by the Company in open market purchases. The extent to which the Company repurchases its shares and the timing of such repurchases will depend upon market conditions and other corporate considerations. During the quarter end December 31, 2018, the Company repurchased 325,000 shares under the 2018 stock repurchase authorization, leaving 1,296,549 shares available under this authorization for future repurchase. In addition, during the first quarter of 2018, the Company repurchased 269,711 shares under the previously announced 2017 stock repurchase authorization.

In addition, 2,854 shares were surrendered by employees to satisfy tax withholding obligations upon the vesting of restricted stock grants in the fourth quarter of 2018.

Equity Compensation Plan Information

The following table sets forth information about equity compensation plans that provide for the award of securities or the grant of options to purchase securities to employees and directors of Banner and its subsidiaries that were in effect at December 31, 2018:

	(A)	(B)	(C)

Plan category	Number of securities to be issued upon exercise of outstanding options or vesting of outstanding restricted stock and unit grants	Weighted average exercise price of outstanding options and rights	Number of securities remaining available for future issuance under equity compensation plans excluding securities reflected in column (A)
Equity compensation plans approved by security holders			
2012 Restricted Stock and Incentive Bonus Plan	8,014	n/a	30,137
2014 Omnibus Incentive Plan	307,287	n/a	376,260
2018 Omnibus Incentive Plan	—		—
	315,301		406,397
Equity compensation plans not approved by security holders	—		—
Total	315,301		406,397

There were no shares tendered in connection with option exercises during the years ended December 31, 2018 and 2017, respectively. Restricted shares canceled to pay withholding taxes totaled 27,653 and 29,579 during the years ended December 31, 2018 and 2017, respectively.

Performance Graph

The following graph compares the cumulative total shareholder return on Banner Corporation common stock with the cumulative total return on the NASDAQ (U.S. Stock) Index, a peer group of the SNL $5 Billion to $10 Billion Asset Bank Index and a peer group of the SNL NASDAQ Bank Index. Total return assumes the reinvestment of all dividends.

	Year Ended					
Index	12/31/13	12/31/14	12/31/15	12/31/16	12/31/17	12/31/18
Banner Corporation	100.00	97.70	105.76	130.72	133.67	133.73
NASDAQ Composite	100.00	114.75	122.74	133.62	173.22	168.30
SNL Bank $5B-$10B	100.00	103.01	117.34	168.11	167.48	151.57
SNL Bank NASDAQ	100.00	103.57	111.80	155.02	163.20	137.56

*Assumes $100 invested in Banner Corporation common stock and each index at the close of business on December 31, 2013 and that all dividends were reinvested. Information for the graph was provided by SNL Financial L.C. © 2019.

Our ability to pay dividends on our common stock depends primarily on dividends we receive from Banner Bank and Islanders Bank. The timing and amount of cash dividends paid on our common stock depends on our earnings, capital requirements, financial condition and other relevant factors, including required payments on our TPS, and is subject to the discretion of our board of directors. As a result of continued strong earnings, levels of capital, asset quality and financial condition during 2018, we increased our regular quarterly dividend to $0.35 per share for the first quarter of 2018 with a second increase to $0.38 per share for the third quarter of 2018 and declared a special dividend of $0.50 in the second quarter 2018. There can be no assurance that we will pay dividends on our common stock in the future. For additional information on our ability to pay dividends, see Item 1 of this report, “Business–Regulation–Banner Bank and Islanders Bank–Dividends” and “Banner Corporation–Dividends.”

Item 6 – Selected Financial Data

The following condensed consolidated statements of financial condition and operations and selected performance ratios as of December 31, 2018, 2017, 2016, 2015, and 2014 and for the years then ended have been derived from our audited consolidated financial statements.

The information below is qualified in its entirety by the detailed information included elsewhere herein and should be read along with “Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operations” and “Item 8, Financial Statement and Supplementary Data.”

FINANCIAL CONDITION DATA:

	December 31				
(In thousands)	2018	2017	2016	2015	2014
Total assets	$11,871,317	$9,763,209	$9,793,688	$9,796,298	$4,723,163
Cash and securities [(1)]	2,168,535	1,473,608	1,353,583	1,655,290	708,609
Loans receivable, net	8,588,110	7,509,856	7,365,151	7,236,496	3,755,127
Deposits	9,477,048	8,183,431	8,121,414	8,055,068	3,898,950
Borrowings	773,275	194,769	255,101	324,186	187,436
Common shareholders’ equity	1,478,595	1,272,626	1,305,710	1,300,059	582,888
Total shareholders’ equity	1,478,595	1,272,626	1,305,710	1,300,059	582,888
Shares outstanding	35,183	32,726	33,193	34,242	19,572

OPERATING DATA:

	For the Year Ended December 31				
(In thousands)	2018	2017	2016	2015	2014
Interest income	$463,632	$412,284	$391,477	$254,433	$190,661
Interest expense	32,659	19,250	16,408	12,154	10,789
Net interest income before provision for loan losses	430,973	393,034	375,069	242,279	179,872
Provision for loan losses	8,500	8,000	6,030	—	—
Net interest income	422,473	385,034	369,039	242,279	179,872
Deposit fees and other service charges	48,074	43,452	41,911	33,767	25,634
Mortgage banking operations revenue	21,343	20,880	25,552	17,720	10,249
Net change in valuation of financial instruments carried at fair value	3,775	(2,844)	(2,620)	(813)	1,374
All other non-interest income	10,816	23,712	11,382	4,778	12,815
Total non-interest income	84,008	85,200	76,225	55,452	50,072
REO operations expense (recoveries), net	804	(2,030)	175	397	(446)
All other non-interest expenses	340,567	321,000	315,449	229,363	149,268
Total non-interest expense	341,371	318,970	315,624	229,760	148,822
Income before provision for income tax expense	165,110	151,264	129,640	67,971	81,122
Provision for income tax expense	28,595	90,488	44,255	22,749	27,052
Net income	$136,515	$60,776	$85,385	$45,222	$54,070

(footnotes follow)

PER COMMON SHARE DATA:

	At or For the Years Ended December 31				
	2018	2017	2016	2015	2014
Net income:					
Basic	$4.16	$1.85	$2.52	$1.90	$2.79
Diluted	4.15	1.84	2.52	1.89	2.79
Common shareholders' equity per share(2)	42.03	38.89	39.34	37.97	29.78
Common shareholders' tangible equity per share(2)(9)	31.45	30.78	31.06	29.64	29.64
Cash dividends	1.96	2.00	0.88	0.72	0.72
Dividend payout ratio (basic)	47.12 %	108.11 %	34.92 %	37.89 %	25.78 %
Dividend payout ratio (diluted)	47.23 %	108.70 %	34.92 %	38.10 %	25.84 %

OTHER DATA:

	As of December 31				
	2018	2017	2016	2015	2014
Full time equivalent employees	2,187	2,078	2,078	2,063	1,150
Number of branches	182	178	190	202	93

(footnotes follow)

KEY FINANCIAL RATIOS:

	At or For the Years Ended December 31				
	2018	2017	2016	2015	2014
Performance Ratios:					
Return on average assets [3]	1.29 %	0.60 %	0.87 %	0.72 %	1.17 %
Return on average common equity [4]	10.45	4.57	6.41	5.56	9.59
Average common equity to average assets	12.37	13.09	13.54	12.87	12.20
Interest rate spread [5]	4.40	4.23	4.19	4.09	4.04
Net interest margin [6]	4.43	4.24	4.20	4.10	4.07
Non-interest income to average assets	0.80	0.84	0.78	0.88	1.08
Non-interest expense to average assets	3.23	3.14	3.21	3.64	3.22
Efficiency ratio [7]	66.29	66.70	69.94	77.17	64.72
Average interest-earning assets to funding liabilities	106.09	105.69	105.84	107.59	108.78
Selected Financial Ratios:					
Allowance for loan losses as a percent of total loans at end of period	1.11	1.17	1.15	1.07	1.98
Net (charge-offs) recoveries as a percent of average outstanding loans during the period	(0.01)	(0.07)	0.03	0.04	0.05
Non-performing assets as a percent of total assets	0.16	0.28	0.35	0.28	0.43
Allowance for loan losses as a percent of non-performing loans [8]	616.36	329.38	380.87	512.47	453.56
Common shareholders' tangible equity to tangible assets[9]	9.62	10.61	10.83	10.68	12.29
Consolidated Capital Ratios:					
Total capital to risk-weighted assets	13.12	13.81	13.40	13.63	16.80
Tier 1 capital to risk-weighted assets	12.12	12.77	12.41	12.65	15.54
Tier 1 capital to average leverage assets	10.98	11.34	11.83	11.06	13.41
Common equity tier I capital to risk-weighted assets	10.75	11.30	11.19	12.13	na

(1) Includes securities available-for-sale and held-to-maturity.

(2) Calculated using shares outstanding, excluding unearned restricted shares held in ESOP.

(3) Net income divided by average assets.

(4) Net income divided by average common equity.

(5) Difference between the average yield on interest-earning assets and the average cost of interest-bearing liabilities.

(6) Net interest income before provision for loan losses as a percent of average interest-earning assets.

(7) Non-interest expenses divided by the total of net interest income before loan losses and non-interest income.

(8) Non-performing loans consist of nonaccrual and 90 days past due loans still accruing interest.

(9) Common shareholders' tangible equity per share and the ratio of tangible common shareholders' equity to tangible assets are non-GAAP financial measures. We calculate tangible common equity by excluding the balance of goodwill and other intangible assets from shareholders' equity. We calculate tangible assets by excluding the balance of goodwill and other intangible assets from total assets. We believe that this is consistent with the treatment by our bank regulatory agencies, which exclude goodwill and other intangible assets from the calculation of risk-based capital ratios. Management believes that these non-GAAP financial measures provide information to investors that is useful in understanding the basis of our capital position. However, these non-GAAP financial measures are supplemental and are not a substitute for any analysis based on GAAP. Because not all companies use the same calculation of tangible common equity and tangible assets, this presentation may not be comparable to other similarly titled measures as calculated by other companies. For a reconciliation of these non–GAAP measures, see Item 7 of this report, "Management's Discussion and Analysis of Financial Condition and Results of Operations—Executive Overview."

Item 7 – Management’s Discussion and Analysis of Financial Condition and Results of Operations

Management’s discussion and analysis of results of operations is intended to assist in understanding our financial condition and results of operations. The information contained in this section should be read in conjunction with the Consolidated Financial Statements and accompanying Notes to the Consolidated Financial Statements of this Form 10-K.

Executive Overview

Banner Corporation's successful execution of its strategic plan and operating initiatives continued in 2018, as evidenced by our solid core operating results and profitability. We have made substantial progress on our goals to achieve and maintain the Company's moderate risk profile as well as to develop and continue consistent and sustainable earnings momentum. Highlights for the year included continued strong asset quality, outstanding client acquisition, strong revenue generation from core operations and the Skagit acquisition.

For the year ended December 31, 2018, our net income was $136.5 million, or $4.15 per diluted share, compared to net income of $60.8 million, or $1.84 per diluted share for the year ended December 31, 2017 and $85.4 million, or $2.52 per diluted share for the year ended December 31, 2016. Current year results were positively impacted by growth in interest-earning assets. Net income for both 2018 and 2017 were impacted by one-time tax adjustments primarily as a result of the enactment of the 2017 Tax Act, which reduced the marginal federal corporate income tax rate from 35% to 21%. Our net income for the year ended December 31, 2018, was increased by $5.5 million of tax benefit adjustments, which included the release of a $4.2 million valuation reserve previously recorded as a provisional amount related to the 2017 Tax Act. Our net income for 2017 was reduced by a $42.6 million, or $1.29 per diluted share, related to revaluation of our net deferred tax asset as a result of the 2017 Tax Act. In 2017, our results also included a net gain of $12.2 million as a result of the Utah Branch Sale. Our results for the years ended December 31, 2018 and 2016 were also impacted by $5.6 million and $11.7 million of acquisition-related expenses, respectively. There were no acquisition-related expenses in 2017.

Our operating results depend primarily on our net interest income, which is the difference between interest income on interest-earning assets, consisting of loans and investment securities, and interest expense on interest-bearing liabilities, composed primarily of customer deposits, FHLB advances, other borrowings and junior subordinated debentures. Net interest income is primarily a function of our interest rate spread, which is the difference between the yield earned on interest-earning assets and the rate paid on interest-bearing liabilities, as well as a function of the average balances of interest-earning assets and interest-bearing liabilities. Our net interest income before provision for loan losses increased 10% to $431.0 million for the year ended December 31, 2018, compared to $393.0 million for the prior year. This increase in net interest income reflects growth in average interest-earning assets, mostly loans, as well as increased yields. During the year ended December 31, 2018, our interest spread increased to 4.40% from 4.23% for the prior year while our net interest margin increased to 4.43% compared to 4.24% for the prior year. Our net interest margin was enhanced 10 basis points in both 2018 and 2017 by acquisition accounting adjustments, primarily the amortization of acquisition accounting discounts on purchased loans obtained from acquisitions, which are accreted into loan interest income.

Although our credit quality metrics continue to reflect our moderate risk profile, we recorded an $8.5 million provision for loan losses in the year ended December 31, 2018, primarily due to the organic growth in the loan portfolio, the renewal of acquired loans out of the discounted loan portfolios and net charge-offs, compared to an $8.0 million provision for loan losses recorded in 2017 and $6.0 million in 2016. Non-performing loans decreased to $15.7 million at December 31, 2018, compared to $27.0 million a year earlier. Our allowance for loan losses at December 31, 2018 was $96.5 million, representing 616% of non-performing loans. (See Note 5, Loans Receivable and the Allowance for Loan Losses, of the Notes to the Consolidated Financial Statements as well as “Asset Quality” below in this Form 10-K.)

Our net income also is affected by the level of our non-interest income, including deposit fees and other service charges, results of mortgage banking operations, which includes loan origination and servicing fees and gains and losses on the sale of loans, and gains and losses on the sale securities, as well as our non-interest expense and income tax provisions. In addition, our net income is affected by the net change in the value of certain financial instruments carried at fair value. Our total non-interest income was $84.0 million for the year ended December 31, 2018, compared to $85.2 million for the year ended December 31, 2017. For the year ended December 31, 2018, we recorded a net gain of $3.8 million for fair value adjustments and $837,000 in net losses on the sale of securities. In comparison, for the year ended December 31, 2017, we recorded a net loss of $2.8 million for fair value adjustments and $2.1 million in net losses on the sale of securities, offset by a $12.2 million gain on the Utah Branch Sale.

Our total revenues (net interest income before the provision for loan losses plus total non-interest income) for the year ended December 31, 2018 increased $36.7 million, or 8%, to $515.0 million, compared to $478.2 million for the same period a year earlier, largely as a result of increased interest income. Our total revenues from core operations (a non-GAAP financial measure), which excludes net gains and losses on sale of securities, fair value adjustments, and gains on sale of branches, including related loans and deposits, increased by $41.1 million, or 9%, to $512.0 million for the year ended December 31, 2018, compared to $471.0 million a year earlier.

For the year ended December 31, 2018, non-interest expense increased 7% to $341.4 million, compared to $319.0 million for the year ended December 31, 2017. The increase was largely attributable to the inclusion of acquired Skagit operations in the last two months of 2018, along with higher salary and employee benefits mostly due to the build-out of the Company's risk management and delivery platform infrastructure, and $5.6 million of merger and acquisition-related expenses in 2018.

Non-GAAP financial measures: Non-interest income, revenues and other earnings information excluding fair value adjustments, net gains or losses on sale of securities and, in certain periods gain on the sale of branches including related loans and deposits and acquisition-related costs, and non-interest expenses, excluding state/municipal business and occupational tax expense, CDI amortization, REO net gain or loss and acquisition-related costs, are non-GAAP financial measures. Management has presented these non-GAAP financial measures in this discussion and analysis because it believes that they provide useful and comparative information to assess trends in our core operations and in understanding our capital position. However, these non-GAAP financial measures are supplemental and are not a substitute for any analysis based on GAAP. Where applicable, we have also presented comparable earnings information using GAAP financial measures. For a reconciliation of these non-GAAP financial measures, see the tables below. Because not all companies use the same calculations, our presentation may not be comparable to other similarly titled measures as calculated by other companies. See “Comparison of Results of Operations for the Years Ended December 31, 2018 and 2017” for more detailed information about our financial performance.

The following tables set forth reconciliations of non-GAAP financial measures discussed in this report (dollars in thousands, except share and per share data):

	For the Years Ended December 31		
	2018	2017	2016
REVENUE FROM CORE OPERATIONS:			
Net interest income before provision for loan losses (GAAP)	$430,973	$393,034	$375,069
Total non-interest income	84,008	85,200	76,225
Total GAAP revenue	514,981	478,234	451,294
Exclude net loss (gain) on sale of securities	837	2,080	(843)
Exclude change in valuation of financial instruments carried at fair value	(3,775)	2,844	2,620
Exclude gain on sale of branches, including related loans and deposits	—	(12,189)	—
Revenue from core operations (non-GAAP)	$512,043	$470,969	$453,071
EARNINGS FROM CORE OPERATIONS:			
Net income (GAAP)	$136,515	$60,776	$85,385
Exclude net loss (gain) on sale of securities	837	2,080	(843)
Exclude change in valuation of financial instruments carried at fair value	(3,775)	2,844	2,620
Exclude gain on sale of branches, including related loans and deposits	—	(12,189)	—
Exclude acquisition related costs	5,607	—	11,733
Exclude related tax (benefit) expense	(426)	2,615	(4,857)
Exclude tax adjustments related to tax reform and valuation reserves	(4,207)	42,630	—
Total earnings from core operations (non-GAAP)	$134,551	$98,756	$94,038
Diluted earnings per share (GAAP)	$4.15	$1.84	$2.52
Diluted core earnings per share (non-GAAP)	$4.09	$2.99	$2.78

	December 31		
ADJUSTED EFFICIENCY RATIO:	2018	2017	2016
Non-interest expense (GAAP)	$341,371	$318,970	$315,624
Exclude acquisition-related costs	(5,607)	—	(11,733)
Exclude CDI amortization	(6,047)	(6,246)	(7,061)
Exclude state/municipal tax expense	(3,284)	(2,594)	(3,516)
Exclude REO (loss) gain	(804)	2,030	(175)
Adjusted non-interest expense (non-GAAP)	$325,629	$312,160	$293,139
Net interest income before provision for loan losses (GAAP)	$430,973	$393,034	$375,069
Non-interest income (GAAP)	84,008	85,200	76,225
Total revenue	514,981	478,234	451,294
Exclude net loss (gain) on sale of securities	837	2,080	(843)
Exclude net change in valuation of financial instruments carried at fair value	(3,775)	2,844	2,620
Exclude gain on sale of branches, including related loans and deposits	—	(12,189)	—
Adjusted revenue (non-GAAP)	$512,043	$470,969	$453,071
Efficiency ratio (GAAP)	66.29 %	66.70 %	69.94 %
Adjusted efficiency ratio (non-GAAP)	63.59 %	66.28 %	64.70 %

Common shareholders' tangible equity per share and the ratio of common shareholders' tangible equity to tangible assets referred to in footnote (9) to Item 6, Selected Financial Data above are also non-GAAP financial measures. We calculate common shareholders' tangible equity by excluding goodwill and other intangible assets from common shareholders' equity. We calculate tangible assets by excluding the balance of goodwill and other intangible assets from total assets. We believe that this is consistent with the treatment by our bank regulatory agencies, which exclude goodwill and other intangible assets from the calculation of risk-based capital ratios. Management believes that this non-GAAP financial measure provides information to investors that is useful in understanding our capital position (dollars in thousands).

	December 31		
	2018	2017	2016
Shareholders’ equity (GAAP)	$1,478,595	$1,272,626	$1,305,710
Exclude goodwill and other intangible assets, net	372,078	265,314	274,745
Common shareholders’ tangible equity (non-GAAP)	$1,106,517	$1,007,312	$1,030,965
Total assets (GAAP)	$11,871,317	$9,763,209	$9,793,668
Exclude goodwill and other intangible assets, net	372,078	265,314	274,745
Total tangible assets (non-GAAP)	$11,499,239	$9,497,895	$9,518,923
Common shareholders' equity to total assets (GAAP)	12.46 %	13.03 %	13.33 %
Common shareholders’ tangible equity to tangible assets (non-GAAP)	9.62 %	10.61 %	10.83 %
Common shares outstanding	35,182,772	32,726,485	33,193,387
Common shareholders' equity per share (GAAP)	$42.03	$38.89	$39.34
Common shareholders' tangible equity per share (non-GAAP)	$31.45	$30.78	$31.06

Management's Discussion and Analysis of Financial Condition and Results of Operations is intended to assist in understanding our financial condition and results of operations. The information contained in this section should be read in conjunction with the Consolidated Financial Statements and accompanying Notes to the Consolidated Financial Statements contained in Item IV of this Form 10-K.

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Critical Accounting Policies

In the opinion of management, the accompanying Consolidated Statements of Financial Condition and related Consolidated Statements of Operations, Comprehensive Income, Changes in Shareholders' Equity and Cash Flows reflect all adjustments (which include reclassification and normal recurring adjustments) that are necessary for a fair presentation in conformity with GAAP. The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect amounts reported in the financial statements.

Various elements of our accounting policies, by their nature, are inherently subject to estimation techniques, valuation assumptions and other subjective assessments. In particular, management has identified several accounting policies that, due to the judgments, estimates and assumptions inherent in those policies, are critical to an understanding of our financial statements. These policies relate to (i) the methodology for the recognition of interest income, (ii) determination of the provision and allowance for loan losses, (iii) the valuation of financial assets and liabilities recorded at fair value, including OTTI losses, (iv) the valuation of intangibles, such as goodwill, core deposit intangibles, favorable leasehold intangibles and mortgage servicing rights, (v) the valuation of real estate held for sale, (vi) the valuation of assets and liabilities acquired in business combinations and subsequent recognition of related income and expense, and (vii) the valuation of or recognition of deferred tax assets and liabilities. These policies and judgments, estimates and assumptions are described in greater detail below. Management believes the judgments, estimates and assumptions used in the preparation of the financial statements are appropriate based on the factual circumstances at the time. However, given the sensitivity of the financial statements to these critical accounting policies, the use of other judgments, estimates and assumptions could result in material differences in our results of operations or financial condition. Further, subsequent changes in economic or market conditions could have a material impact on these estimates and our financial condition and operating results in future periods. There have been no significant changes in our application of accounting policies since December 31, 2017. For additional information concerning critical accounting policies, see Notes 1, 3, 5, 12, 17 and 18 of the Notes to the Consolidated Financial Statements and the following:

Interest Income: (Notes 1 and 5) Interest on loans and securities is accrued as earned unless management doubts the collectability of the asset or the unpaid interest. Interest accruals on loans are generally discontinued when loans become 90 days past due for payment of interest and the loans are then placed on nonaccrual status. All previously accrued but uncollected interest is deducted from interest income upon transfer to nonaccrual status. For any future payments collected, interest income is recognized only upon management's assessment that there is a strong likelihood that the full amount of a loan will be repaid or recovered. Management's assessment of the likelihood of full repayment involves judgment including determining the fair value of the underlying collateral which can be impacted by the economic environment. A loan may be put on nonaccrual status sooner than this policy would dictate if, in management's judgment, the amounts owed, principal or interest, may be uncollectable. While less common, similar interest reversal and nonaccrual treatment is applied to investment securities if their ultimate collectability becomes questionable.

Provision and Allowance for Loan Losses: (Notes 1 and 5) The methodology for determining the allowance for loan losses is considered a critical accounting policy by management because of the high degree of judgment involved, the subjectivity of the assumptions used, and the potential for changes in the economic environment that could result in changes to the amount of the recorded allowance for loan losses. The provision for loan losses reflects the amount required to maintain the allowance loan for losses at an appropriate level based upon management's evaluation of the adequacy of general and specific loss reserves. Determining the amount of the allowance for loan losses involves a high degree of judgment. Among the material estimates required to establish the allowance for loan losses are: overall economic conditions; value of collateral; strength of guarantors; loss exposure at default; the amount and timing of future cash flows on impaired loans; and determination of loss factors to be applied to the various elements of the portfolio. All of these estimates are susceptible to significant change. We have established systematic methodologies for the determination of the adequacy of our allowance for loan losses. The methodologies are set forth in a formal policy and take into consideration the need for an overall general valuation allowance as well as specific allowances that are tied to individual problem loans. We increase our allowance for loan losses by charging provisions for probable loan losses against our income.

The allowance for loan losses is maintained at a level sufficient to provide for probable losses based on evaluating known and inherent risks in the loan portfolio and upon our continuing analysis of the factors underlying the quality of the loan portfolio. These factors include, among others, changes in the size and composition of the loan portfolio, delinquency rates, actual loan loss experience, current and economic conditions, detailed analysis of individual loans for which full collectability may not be assured, and determination of the existence and realizable value of the collateral and guarantees securing the loans. Realized losses related to specific assets are applied as a reduction of the carrying value of the assets and charged immediately against the allowance for loan loss reserve. Recoveries on previously charged off loans are credited to the allowance for loan losses. The reserve is based upon factors and trends identified by us at the time financial statements are prepared. Although we use the best information available, future adjustments to the allowance for loan losses may be necessary due to economic, operating, regulatory and other conditions beyond our control. The adequacy of general and specific reserves is based on our continuing evaluation of the pertinent factors underlying the quality of the loan portfolio as well as individual review of certain large balance loans. Loans are considered impaired when, based on current information and events, we determine that it is probable that we will be unable to collect all amounts due according to the contractual terms of the loan agreement. Factors involved in determining impairment include, but are not limited to, the financial condition of the borrower, the value of the underlying collateral less selling costs and the current status of the economy. Impaired loans are measured based on the present value of expected future cash flows discounted at the loan's effective interest rate or, as a practical expedient, at the loan's observable market price or the fair value of collateral if the loan is collateral dependent. We continue to assess the collateral of these loans and update our appraisals on large balance impaired loans on an annual basis. To the extent the property values continue to decline, there could be additional losses on these impaired loans, which may be material. Subsequent changes in the value of impaired loans are included within the provision for loan losses in the same manner in which impairment initially was recognized or as a reduction in the provision that would otherwise be reported. Large groups of smaller-balance homogeneous loans are collectively evaluated for impairment. Loans that are collectively evaluated for impairment include residential real estate and consumer loans and, as appropriate, smaller balance non-homogeneous loans. Larger balance non-homogeneous residential construction and land, commercial real estate, commercial business loans and unsecured loans are individually evaluated for impairment.

Our methodology for assessing the appropriateness of the allowance for loan losses consists of several key elements, which include specific allowances, an allocated formula allowance and an unallocated allowance. Losses on specific loans are provided for when the losses are probable and estimable. General loan loss reserves are established to provide for inherent loan portfolio risks not specifically provided for. The level of general reserves is based on analysis of potential exposures existing in our loan portfolio including evaluation of historical trends, current market conditions and other relevant factors identified by us at the time the financial statements are prepared. The formula allowance is calculated by applying loss factors to outstanding loans, excluding those loans that are subject to individual analysis for specific allowances. Loss factors are based on our historical loss experience adjusted for significant environmental considerations, including the experience of other banking organizations, which in our judgment affect the collectability of the loan portfolio as of the evaluation date. The unallocated allowance is based upon our evaluation of various factors that are not directly measured in the determination of the formula and specific allowances. This methodology may result in actual losses or recoveries differing significantly from the allowance for loan losses in the Consolidated Financial Statements.

While we believe the estimates and assumptions used in our determination of the adequacy of the allowance for loan losses are reasonable, there can be no assurance that such estimates and assumptions will not be proven incorrect in the future, or that the actual amount of future provisions will not exceed the amount of past provisions or that any increased provisions that may be required will not adversely impact our financial condition and results of operations. In addition, the determination of the amount of the Banks' allowance for loan losses is subject to review by bank regulators as part of the routine examination process, which may result in the adjustment of reserves based upon their judgment of information available to them at the time of their examination.

Fair Value Accounting and Measurement: (Notes 1 and 18) We use fair value measurements to record fair value adjustments to certain financial assets and liabilities and to determine fair value disclosures. We include in the Notes to the Consolidated Financial Statements information about the extent to which fair value is used to measure financial assets and liabilities, the valuation methodologies used and the impact on our results of operations and financial condition. Additionally, for financial instruments not recorded at fair value we disclose, where required, our estimate of their fair value. For more information regarding fair value accounting, please refer to Note 18 in the Notes to the Consolidated Financial Statements.

Business Combinations: (Notes 1 and 3) Business combinations are accounted for using the acquisition method of accounting and, accordingly, assets acquired and liabilities assumed, both tangible and intangible, and consideration exchanged are recorded at acquisition date fair values. The determination of the fair value of assets acquired and liabilities assumed involves a significant amount of judgment. The excess purchase consideration over the fair value of net assets acquired is recorded as goodwill. In the event that the fair value of net assets acquired exceeds the purchase price, including fair value of liabilities assumed, a bargain purchase gain is recorded on that acquisition. Expenses incurred in connection with a business combination are expensed as incurred. Changes in deferred tax asset valuation allowances related to acquired tax uncertainties are recognized in net income after the measurement period.

Acquired Loans: (Notes 3 and 5) Purchased loans, including loans acquired in business combinations, are recorded at their fair value at the acquisition date. Credit discounts are included in the determination of fair value; therefore, an allowance for loan losses is not recorded at the acquisition date. Establishing the fair value of acquired loans involves a significant amount of judgment, including determining the credit discount based upon historical data adjusted for current economic conditions and other factors. If any of these assumptions are inaccurate actual credit losses could vary significantly from the credit discount used to calculate the fair value of the acquired loans. Acquired loans are evaluated upon acquisition and classified as either purchased credit-impaired or purchased non-credit-impaired.

Purchased credit-impaired (PCI) loans reflect credit deterioration since origination such that it is probable at acquisition that the Company will be unable to collect all contractually required payments. The accounting for PCI loans is periodically updated for changes in cash flow expectations, and reflected in interest income over the life of the loans as accretable yield. Any subsequent decreases in expected cash flows attributable to credit deterioration are recognized by recording a provision for loan losses.

For purchased non-credit-impaired loans, the difference between the fair value and unpaid principal balance of the loan at the acquisition date is amortized or accreted to interest income over the life of the loans. Any subsequent deterioration in credit quality is recognized by recording a provision for loan losses.

Goodwill: (Notes 1 and 17) Goodwill represents the excess of the purchase consideration paid over the fair value of the assets acquired, net of the fair values of liabilities assumed in a business combination and is not amortized but is reviewed annually, or more frequently as current circumstances and conditions warrant, for impairment. The Company completes is annual review of goodwill as of December 31. An assessment of qualitative factors is completed to determine if it is more likely than not that the fair value of a reporting unit is less than its carrying amount. The qualitative assessment involves judgment by management on determining whether there have been any triggering events that have occurred which would indicate potential impairment. If the qualitative analysis concludes that further analysis is required, then a quantitative impairment test would be completed. The quantitative goodwill impairment test is used to identify the existence of impairment and the amount of impairment loss and compares the reporting unit's estimated fair value, including goodwill, to its carrying amount. If the fair value exceeds the carrying amount then goodwill is not considered impaired. If the carrying amount exceeds its fair value, an impairment loss would be recognized equal to the amount of excess, limited to the amount of total goodwill allocated to the reporting unit. The impairment loss would be recognized as a charge to earnings.

Other Intangible Assets: (Notes 1 and 17) Other intangible assets consists primarily of core deposit intangibles (CDI), which are amounts recorded in business combinations or deposit purchase transactions related to the value of transaction-related deposits and the value of the customer relationships associated with the deposits. Core deposit intangibles are being amortized on an accelerated basis over a weighted average estimated useful life of eight years. The determination of the estimated useful life of the core deposit intangible involves judgment by management. The actual life of the core deposit intangible could vary significantly from the estimated life. These assets are reviewed at least annually for events or circumstances that could impact their recoverability. These events could include loss of the underlying core deposits, increased competition or adverse changes in the economy. To the extent other identifiable intangible assets are deemed unrecoverable, impairment losses are recorded in other non-interest expense to reduce the carrying amount of the assets.

Other intangibles also include favorable leasehold intangibles (LHI). LHI represents the value assigned to leases assumed in an acquisition in which the lease terms are favorable compared to a market lease at the date of acquisition. LHI is amortized over the underlying lease term and is reviewed at least annually for events or circumstances that could impair the value.

Mortgage Servicing Rights: (Note 17) Mortgage servicing rights (MSRs) are recognized as separate assets when rights are acquired through purchase or through sale of loans. Generally, purchased MSRs are capitalized at the cost to acquire the rights. For sales of mortgage loans, the value of the MSR is estimated and capitalized. Fair value is based on market prices for comparable mortgage servicing contracts. The fair value of the MSRs includes an estimate of the life of the underlying loans which is affected by estimated prepayment speeds. The estimate of prepayment speeds is based on current market conditions. Actual market conditions could vary significantly from current conditions which could result in the estimated life of the underlying loans being different which would change the fair value of the MSR. Capitalized MSRs are reported in other assets and are amortized into non-interest income in proportion to, and over the period of, the estimated future net servicing income of the underlying financial assets.

Real Estate Owned Held for Sale: (Notes 1 and 6) Property acquired by foreclosure or deed in lieu of foreclosure is recorded at the estimated fair value of the property, less expected selling costs. Development and improvement costs relating to the property may be capitalized, while other holding costs are expensed. The carrying value of the property is periodically evaluated by management, property values are influenced by current economic and market conditions, changes in economic conditions could result in a decline in property value. To the extent that property values decline, allowances are established to reduce the carrying value to net realizable value. Gains or losses at the time the property is sold are charged or credited to operations in the period in which they are realized. The amounts the Banks will ultimately recover from real estate held for sale may differ substantially from the carrying value of the assets because of market factors beyond the Banks' control or because of changes in the Banks' strategies for recovering the investment.

Income Taxes and Deferred Taxes: (Note 12) The Company and its wholly-owned subsidiaries file consolidated U.S. federal income tax returns, as well as state income tax returns in Oregon, California, Idaho, Utah and Montana. Income taxes are accounted for using the asset and liability method. Under this method a deferred tax asset or liability is determined based on the enacted tax rates which are expected to be in effect when the differences between the financial statement carrying amounts and tax basis of existing assets and liabilities are expected to be reported in the Company's income tax returns. The effect on deferred taxes of a change in tax rates is recognized in income in the period that includes the enactment date. The Company assesses the appropriate tax treatment of transactions and filing positions after considering statutes, regulations, judicial precedent and other pertinent information and maintain tax accruals consistent with its evaluation. Changes in the estimate of accrued taxes occur periodically due to changes in tax rates, interpretations of tax laws, the status of examinations by the tax authorities and newly enacted statutory, judicial and regulatory guidance that could impact the relative merits of tax positions. These changes, when they occur, impact accrued taxes and can materially affect our operating results. A valuation allowance is required to be recognized if it is “more likely than not” that all or a portion of our deferred tax assets will not be realized. The evaluation pertaining to the tax expense and related deferred tax asset and liability balances involves a high degree of judgment and subjectivity around the measurement and resolution of these matters. The ultimate realization of the deferred tax assets is dependent upon the existence, or generation, of taxable income in the periods when those temporary differences and net operating loss and credit carryforwards are deductible.

In December 2017, the federal government enacted the 2017 Tax Act, which among other provisions, reduced the federal marginal corporate income tax rate from 35% to 21%. As a result of the passage of the 2017 Tax Act, the Company recorded a $42.6 million charge for the revaluation of its net deferred tax to account for the future impact of the decrease in the corporate income tax rate and other provisions of the legislation. The charge was recorded as an increase to tax expense and reduction of the net deferred asset for the year ended December 31, 2017. The Company’s 2017 financial results reflected the income tax effects of the 2017 Tax Act for which the accounting was complete and provisional amounts for those specific income tax effects of the 2017 Tax Act for which the accounting was incomplete but a reasonable estimate could be determined. The $42.6 million charge recorded in 2017 by the Company included $4.2 million of provisional income tax expense related to Alternative Minimum Tax (AMT) credits that are limited under Internal Revenue Code of 1986 (Code) Section 383, which resulted in a reduction in the AMT deferred tax asset. The utilization of the limited AMT credits under the refundable AMT credit law was uncertain as of December 31, 2017. Subsequently, in 2018 the Company determined it could use the AMT credits and reversed the previously recorded $4.2 million provisional tax expense.

Legal Contingencies: In the normal course of our business, we have various legal proceedings and other contingent matters pending. We determine whether an estimated loss from a contingency should be accrued by assessing whether a loss is deemed probable and can be reasonably estimated. We assess our potential liability by analyzing our litigation and regulatory matters using available information. We develop our views on estimated losses in consultation with outside counsel handling our defense in these matters, which involves an analysis of potential results, assuming a combination of litigation and settlement strategies. The estimated losses often involve a level of subjectivity and usually are a range of reasonable losses and not an exact number, in those situations we accrue the best estimate within the range or the low end of the range if no estimate within the range is better than another.

Accounting Standards Recently Adopted or Issued - See Note 2 of the Notes to the Consolidated Financial Statements for a description of recently adopted and new accounting pronouncements, including the respective dates of adoption and expected effects on the Company's financial position and results of operations.

Comparison of Financial Condition at December 31, 2018 and 2017

General. Total assets increased to $11.87 billion at December 31, 2018, compared to $9.76 billion at December 31, 2017. The increase in assets in 2018 reflects the assets acquired in the Skagit acquisition as well as the re-leveraging of the investment portfolio and organic loan and deposit growth.

Net loans receivable (gross loans less deferred fees and discounts, and allowance for loan losses and excluding loans held for sale) increased $1.08 billion, or 14%, to $8.59 billion at December 31, 2018, from $7.51 billion at December 31, 2017. The increase in loans receivable in 2018 included $631.7 million of portfolio loans acquired in the Skagit acquisition as well as $454.0 million of organic loan growth. The increase in net loans included increases of $339.4 million in commercial real estate loans, $203.7 million in commercial business loans, $200.0 million in construction loans, $125.3 million in one- to four-family loans, $66.5 million in agricultural loans and $54.6 million in multifamily real estate loans. The increase in construction loans was particularly helpful to the net interest margin as interest rates, loan fees and the velocity of turnover in this lending activity are generally higher than for most other categories of loans. Loans held for sale increased to $171.0 million at December 31, 2018, compared to $40.7 million at December 31, 2017, principally as a result of multifamily loan originations exceeding multifamily loan sales. Loans held for sale at December 31, 2018 included $130.7 million of multifamily loans and $40.3 million of one- to four-family loans.

Securities increased to $1.90 billion at December 31, 2018, from $1.20 billion at December 31, 2017, and the aggregate total of securities and interest-bearing deposits increased $673.9 million, or 53%, to $1.94 billion at December 31, 2018, compared to $1.26 billion a year earlier. The increase in securities balances reflects securities acquired from Skagit along with securities purchases in 2018 to re-leverage the balance sheet following the sales of securities during the fourth quarter of 2017 as the Company deleveraged the balance sheet consistent with its strategy to remain below $10 billion in assets at December 31, 2017. The average effective duration of Banner's securities portfolio was approximately 3.5 years at December 31, 2018. The fair value of our trading securities was $1.3 million less than their amortized cost at December 31, 2018. In addition, fair value adjustments for securities designated as available-for-sale reflected a decrease of $6.5 million for the year ended December 31, 2018, which was included as a component of other comprehensive income and largely occurred as a result of slightly increased market interest rates. Periodically, we also acquire securities (primarily municipal bonds) which are designated as held-to-maturity and this portfolio decreased by $26.1 million from the prior year-end balance. (See Notes 4 and 18 of the Notes to the Consolidated Financial Statements.)

Goodwill increased $96.5 million to $339.2 million at December 31, 2018, compared to $242.7 million at December 31, 2017 as a result of the Skagit acquisition. Other intangibles increased $10.3 million to $32.9 million at December 31, 2018, compared to $22.7 million at December 31, 2017, primarily due to CDI recorded in the Skagit acquisition, partially offset by scheduled amortization of CDI and leasehold intangibles.

Deposits increased $1.29 billion, or 16%, to $9.48 billion at December 31, 2018, from $8.18 billion at December 31, 2017, largely as a result of $810.2 million of deposits acquired in the Skagit acquisition as well as organic growth in deposits. Core deposits were 86% of total deposits at December 31, 2018, compared to 88% of total deposits one year earlier. Non-interest-bearing deposits increased by $392.3 million, or 12%, to $3.66 billion from $3.27 billion at December 31, 2017, interest-bearing transaction and savings accounts increased by $548.0 million, to $4.50 billion at December 31, 2018 from $3.95 billion at December 31, 2017, and certificates of deposit increased $353.3 million, or

37%, to $1.32 billion at December 31, 2018 from $966.9 million at December 31, 2017. Brokered deposits increased to $377.3 million at December 31, 2018, compared to $57.2 million a year earlier. Brokered deposits increased during 2018 in connection with our re-leveraging strategy as higher yielding investment securities were purchased along with organic and seasonal growth in loan outstandings.

FHLB advances increased $540.0 million, to $540.2 million at December 31, 2018 from $202,000 at December 31, 2017, as borrowings were used to fund a portion of the growth in the securities and loan portfolios. Other borrowings, consisting of retail and wholesale repurchase agreements primarily related to customer cash management accounts, increased $23.1 million to $119.0 million at December 31, 2018, compared to $95.9 million at December 31, 2017. Junior subordinated debentures, which are carried at fair value, increased $15.4 million to $114.1 million at December 31, 2018 from $98.7 million a year ago, primarily due to changes in the fair value. For more information, see Notes 9, 10 and 11 of the Notes to the Consolidated Financial Statements.

Total shareholders’ equity increased $206.0 million, to $1.48 billion at December 31, 2018, compared to $1.27 billion at December 31, 2017. The increase in equity primarily reflects 3.1 million of common shares issued in connection with the Skagit acquisition and net income of $136.5 million, partially offset by the accrual of $64.8 million of dividends to common shareholders and the repurchase of $34.4 million of common stock. In the year ended December 31, 2018, we repurchased 594,711 shares of our common stock at an average price of $57.82 per share. Tangible common shareholders' equity, which excludes goodwill and other intangible assets was $1.11 billion, or 9.62% of tangible assets at December 31, 2018, compared to $1.01 billion, or 10.61% at December 31, 2017. Banner's tangible book value per share was $31.45 at December 31, 2018, compared to $30.78 per share a year ago.

Investments. At December 31, 2018, our consolidated investment securities portfolio totaled $1.90 billion and consisted principally of U.S. Government and agency obligations, mortgage-backed and mortgage-related securities, municipal bonds, corporate debt obligations, and asset-backed securities. From time to time, our investment levels may be increased or decreased depending upon yields available on investment alternatives and management’s projections as to the demand for funds to be used in our loan origination, deposit and other activities. During the year ended December 31, 2018, our aggregate investment in securities increased $694.3 million, as we purchased securities in connection with our renewed leveraging strategy following the sale of securities during the fourth quarter of 2017 to reduce assets below $10 billion at December 31, 2017. Holdings of mortgage-backed securities increased $591.7 million, U.S. Government and agency obligations increased $76.6 million and municipal bonds increased $35.8 million. Partially offsetting these increases was a decrease in asset-backed securities of $5.8 million.

U.S. Government and Agency Obligations: Our portfolio of U.S. Government and agency obligations had a carrying value of $150.1 million (with an amortized cost of $152.0 million) at December 31, 2018, a weighted average contractual maturity of 13.5 years and a weighted average coupon rate of 4.18%. Many of the U.S. Government and agency obligations we own include call features which allow the issuing agency the right to call the securities at various dates prior to the final maturity.

Mortgage-Backed Obligations: At December 31, 2018, our mortgage-backed and mortgage-related securities had a carrying value of $1.40 billion ($1.41 billion at amortized cost, with a net fair value adjustment of $11.4 million). The weighted average coupon rate of these securities was 3.36% and the weighted average contractual maturity was 20.4 years, although we receive principal payments on these securities each month resulting in a much shorter expected average life. As of December 31, 2018, 90% of the mortgage-backed and mortgage-related securities pay interest at a fixed rate and 10% pay at an adjustable interest rate.

Municipal Bonds: The carrying value of our tax-exempt bonds at December 31, 2018 was $240.6 million ($239.3 million at amortized cost), comprised of general obligation bonds (i.e., backed by the general credit of the issuer) and revenue bonds (i.e., backed by revenues from the specific project being financed) issued by cities and counties and various housing authorities, and hospital, school, water and sanitation districts. We also had taxable bonds in our municipal bond portfolio, which at December 31, 2018 had a carrying value of $53.9 million (also $53.9 million at amortized cost). Many of our qualifying municipal bonds are not rated by a nationally recognized credit rating agency due to the smaller size of the total issuance and a portion of these bonds have been acquired through direct private placement by the issuers. We have not experienced any defaults or payment deferrals on our current portfolio of municipal bonds. Our combined municipal bond portfolio is geographically diverse, with the majority within Washington, Oregon, Idaho and California. At December 31, 2018, our municipal bond portfolio, including taxable and tax-exempt, had a weighted average maturity of approximately 11.3 years and a weighted average coupon rate of 4.07%.

Corporate Bonds: Our corporate bond portfolio had a carrying value of $33.1 million ($34.5 million at amortized cost, with a net fair value adjustment of $1.4 million) at December 31, 2018. Long-term adjustable-rate capital securities issued by financial institutions make up over half of our corporate bond portfolio. (See “Critical Accounting Policies” above and Note 18 of the Notes to the Consolidated Financial Statements.) At December 31, 2018, the portfolio had a weighted average maturity of 16.9 years and a weighted average coupon rate of 4.04%.

Asset-Backed Securities: At December 31, 2018, our asset-backed securities portfolio had a carrying value of $21.9 million (with an amortized cost of $22.0 million), and was comprised of securitized pools of student loans issued or guaranteed by the Student Loan Marketing Association (SLMA) and credit card receivables. The weighted average coupon rate of these securities was 2.97% and the weighted average contractual maturity was 6.0 years. Approximately 55% of these securities have adjustable interest rates tied to three-month LIBOR while the remaining securities have fixed interest rates.

The following tables set forth certain information regarding carrying values and percentage of total carrying values of our portfolio of securities—trading and securities—available-for-sale, both carried at estimated fair market value, and securities—held-to-maturity, carried at amortized cost as of December 31, 2018, 2017 and 2016 (dollars in thousands):

Table 1: Securities

	December 31					
	2018		2017		2016	
	Carrying Value	Percent of Total	Carrying Value	Percent of Total	Carrying Value	Percent of Total
Trading						
U.S. Government and agency obligations	$—	— %	$—	— %	$1,326	5.4 %
Municipal bonds	—	—	100	0.5	335	1.4
Corporate bonds	25,896	100.0	22,058	98.8	21,143	86.0
Mortgage-backed or related securities	—	—	—	—	1,641	6.7
Equity securities	—	—	160	0.7	123	0.5
Total securities—trading	$25,896	100.0%	$22,318	100.0%	$24,568	100.0%
Available-for-Sale						
U.S. Government and agency obligations	$149,112	9.1 %	$72,466	7.9 %	$56,978	7.1 %
Municipal bonds	117,822	7.2	68,733	7.5	109,853	13.6
Corporate bonds	3,495	0.2	5,393	0.6	10,283	1.3
Mortgage-backed or related securities	1,343,861	82.1	739,557	80.4	594,712	73.7
Asset-backed securities	21,933	1.4	27,758	3.0	28,993	3.6
Equity securities	—	—	5,578	0.6	5,609	0.7
Total securities—available-for-sale	$1,636,223	100.0%	$919,485	100.0%	$806,428	100.0%
Held-to-Maturity						
U.S. Government and agency obligations	$1,006	0.4 %	$1,024	0.4 %	$1,065	0.4 %
Municipal bonds	176,663	75.5	189,860	73.0	196,989	73.5
Corporate bonds	3,736	1.6	3,978	1.5	3,876	1.5
Mortgage-backed or related securities	52,815	22.5	65,409	25.1	65,943	24.6
Total securities—held-to-maturity	$234,220	100.0%	$260,271	100.0%	$267,873	100.0%
Estimated market value	$232,537		$262,188		$270,528	

The following table shows the maturity or period to repricing of our consolidated portfolio of securities as of December 31, 2018 (dollars in thousands):

Table 2: Securities—Maturity/Repricing and Rates

	December 31, 2018											
	One Year or Less		After One to Five Years		After Five to Ten Years		After Ten to Twenty Years		After Twenty Years		Total	
	Carrying Value	Weighted Average Yield	Carrying Value	Weighted Average Yield	Carrying Value	Weighted Average Yield	Carrying Value	Weighted Average Yield	Carrying Value	Weighted Average Yield	Carrying Value	W Av Yi
U.S. Government and agency obligations:												
Fixed-rate	$4,097	2.48 %	$7,126	2.21 %	$19,568	2.64 %	$18,621	2.67 %	$—	— %	$49,412	2.5
Adjustable-rate	100,706	3.18	—	—	—	—	—	—	—	—	100,706	3.1
	104,803	3.15	7,126	2.21	19,568	2.64	18,621	2.67	—	—	150,118	2.9
Municipal bonds:												
Fixed-rate taxable	662	0.02	27,760	1.93	20,819	3.15	4,187	3.74	—	—	53,428	2.5
Fixed-rate tax exempt	8,016	1.42	27,382	1.80	57,766	2.69	114,330	2.91	32,270	2.72	239,764	2.6
Adjustable-rate taxable	490	0.03	—	—	—	—	—	—	—	—	490	0.0
Adjustable-rate tax exempt	—	—	803	0.04	—	—	—	—	—	—	803	0.0
	9,168	1.25	55,945	1.84	78,585	2.81	118,517	2.94	32,270	2.72	294,485	2.6
Corporate bonds:												
Fixed-rate	748	1.19	1,834	2.02	—	—	—	—	1,936	—	4,518	1.0
Adjustable-rate	28,609	5.38	—	—	—	—	—	—	—	—	28,609	5.3
	29,357	5.28	1,834	2.02	—	—	—	—	1,936	—	33,127	4.8
Mortgage-backed or related securities:												
Fixed-rate	—	—	46,759	2.61	291,268	3.08	77,278	3.02	837,219	2.89	1,252,524	2.9
Adjustable-rate	49,314	2.97	45,913	3.03	48,925	3.60	—	—	—	—	144,152	3.2
	49,314	2.97	92,672	2.82	340,193	3.15	77,278	3.02	837,219	2.89	1,396,676	2.9
Asset-backed securities:												
Fixed-rate	—	—	9,912	1.65	—	—	—	—	—	—	9,912	1.6
Adjustable-rate	12,021	3.23	—	—	—	—	—	—	—	—	12,021	3.2
	12,021	3.23	9,912	1.65	—	—	—	—	—	—	21,933	2.5
Equity securities	—	—	—	—	—	—	—	—	—	—	—	—
Total securities—carrying value	$204,663	3.34	$167,489	2.39	$438,346	3.07	$214,416	2.94	$871,425	2.88	$1,896,339	2.9
Total securities—estimated market value	$204,640		$166,940		$438,769		$214,844		$869,815		$1,895,008	

Loans and Lending. Loans are our most significant and generally highest yielding earning assets. We attempt to maintain a portfolio of loans in a range of 90% to 95% of total deposits to enhance our revenues, while adhering to sound underwriting practices and appropriate diversification guidelines in order to maintain a moderate risk profile. At December 31, 2018, our net loan portfolio totaled \$8.59 billion compared to \$7.51 billion at December 31, 2017. Our total loan portfolio increased \$1.09 billion, or 14%, during the year ended December 31, 2018, compared to an increase of \$147.7 million, or 2.0%, during the year ended December 31, 2017. The increase included \$631.7 million of portfolio loans acquired in the Skagit acquisition as well as organic loan growth. While we originate a variety of loans, our ability to originate each type of loan is dependent upon the relative customer demand and competition in each market we serve. We have implemented strategies designed to capture more market share and achieve increases in targeted loans resulting in strong loan originations in 2018 and 2017. Nonetheless, looking forward, new loan originations and portfolio balances will continue to be significantly affected by the course of economic activity and changes in interest rates. For the years ended December 31, 2018, 2017 and 2016, we originated loans, net of repayments and charge-offs, of \$1.31 billion, \$1.10 billion and \$1.14 billion, respectively. The level of net originations during all three years was significantly impacted by a substantial amount of loan repayments.

Originations of loans for sale increased to \$896.5 million for the year ended December 31, 2018 from \$807.1 million during 2017. Originations of loans for sale included \$372.8 million and \$292.3 million of multifamily held-for-sale loan production for the years ended December 31, 2018 and December 31, 2017, respectively. We generally sell a significant portion of our newly originated one- to four-family residential mortgage loans and multifamily loans to secondary market purchasers. Proceeds from sales of loans for the years ended December 31, 2018, 2017 and 2016 totaled \$791.7 million, \$1.05 billion and \$1.07 billion, respectively. See “Loan Servicing Portfolio” below. Loans held for sale increased \$130.3 million to \$171.0 million at December 31, 2018, compared to \$40.7 million at December 31, 2017. The increase in loans held for sale was primarily due to the increased volume of originations of multifamily loans held-for-sale, which exceeded sales during the year.

The following table shows loan origination (excluding loans held for sale) activity for the years ended December 31, 2018 and 2017 (in thousands):

Table 3: Loan Origination

	Years Ended	
	Dec 31, 2018	Dec 31, 2017
Commercial real estate	\$536,784	\$537,825
Multifamily real estate	25,771	77,409
Construction and land	1,460,536	1,216,227
Commercial business	839,290	647,079
Agricultural business	123,702	117,186
One-to four- family residential	177,332	249,558
Consumer	331,661	344,407
Total loan originations (excluding loans held for sale)	\$3,495,076	\$3,189,691

The loan origination table above includes loan participations and loan purchases. During the years ended December 31, 2018, and 2017 , we purchased \$33.7 million and \$126.5 million, respectively, of loans. The loan purchases in 2018 were one- to four-family loans compared to the loan purchases in 2017 which included both one- to four-family and commercial real estate loans.

One- to Four-Family Residential Real Estate Lending: At December 31, 2018, \$973.6 million, or 11% of our loan portfolio, consisted of permanent loans on one- to four-family residences. Our residential mortgage loan originations have been relatively strong in recent years, as interest rates have supported demand for loans to finance home purchases as well as loans to refinance existing debt, although starting in 2017 refinance activity declined as interest rates have increased. We are active originators of one- to four-family residential loans in most communities where we have established offices in Washington, Oregon, California and Idaho. Most of the one- to four-family loans that we originate are sold in the secondary markets with net gains on sales and loan servicing fees reflected in our revenues from mortgage banking. Our balance of loans for one- to four-family residences increased by $125.3 million in 2018, largely as a result of us holding a larger percentage of our originations for our portfolio.

Construction and Land Lending: Our construction loan originations have increased in recent years as builders have expanded production and experienced strong sales in many markets where we operate. As a result, one-to four-family construction loans have increased by $97.2 million in 2016, $39.6 million in 2017 and $119.4 million in 2018, to total $534.7 million at December 31, 2018. During the year ended December 31, 2018, land and land development loans (both residential and commercial) increased by $26.7 million to $215.8 million at December 31, 2018. At December 31, 2018, construction, land and land development loans totaled $1.11 billion (including $534.7 million of one- to four-family construction loans, $188.5 million of residential land or land development loans, $357.0 million of commercial and multifamily real estate construction loans and $27.3 million of commercial land or land development loans), or 13% of total loans, compared to $907.5 million, or 12%, at December 31, 2017.

Commercial and Multifamily Real Estate Lending: We also originate loans secured by commercial and multifamily real estate. Commercial and multifamily real estate loans originated by us are both fixed- and adjustable-rate loans with intermediate terms of generally five to ten years. Our commercial real estate portfolio consists of loans on a variety of property types with no significant concentrations by property type, borrowers or locations. At December 31, 2018, our loan portfolio included $3.56 billion of commercial real estate loans, or 41% of the total loan portfolio, compared to $3.22 billion, or 42%, at December 31, 2017. Our portfolio of multifamily real estate loans was $368.8 million, or 4% of total loans at December 31, 2018, compared to $314.2 million, or 4%, at December 31, 2017. The increases in commercial real estate loans and multifamily real estate loans during 2018 were due to $292.2 million of commercial and multifamily loans acquired in the Skagit acquisition as well as organic growth.

Commercial Business Lending: Our commercial business lending is directed toward meeting the credit and related deposit needs of various small- to medium-sized business and agribusiness borrowers operating in our primary market areas. In addition to providing earning assets, this type of lending has helped increase our deposit base. At December 31, 2018, commercial business loans totaled $1.48 billion, or 17% of total loans, compared to $1.28 billion, or 17%, at December 31, 2017. This increase was due to $93.4 million of commercial business loans acquired in the Skagit acquisition as well as organic growth. In recent years our commercial lending has also included participation in certain national syndicated loans, including shared national credits, which totaled $149.2 million at December 31, 2018.

Agricultural Lending: Agriculture is a major industry in many Washington, Oregon, California and Idaho locations in our service area. While agricultural loans are not a large part of our portfolio, we routinely make agricultural loans to borrowers with a strong capital base, sufficient management depth, proven ability to operate through agricultural cycles, reliable cash flows and adequate financial reporting. Payments on agricultural loans depend, to a large degree, on the results of operation of the related farm entity. The repayment is also subject to other economic and weather conditions as well as market prices for agricultural products, which can be highly volatile at times. At December 31, 2018, agricultural loans totaled $404.9 million, or 5% of the loan portfolio, compared to $338.4 million, or 4%, at December 31, 2017.

Consumer and Other Lending: Consumer lending has traditionally been a modest part of our business with loans made primarily to accommodate our existing customer base. Outstanding balances increased during 2018 due to $77.4 million of consumer loans acquired in the Skagit acquisition as well as organic loan growth. At December 31, 2018, our consumer loans increased $96.2 million to $785.0 million, or 9% of our loan portfolio, compared to $688.8 million, or 9%, at December 31, 2017. As of December 31, 2018, 72% of our consumer loans were secured by one- to four-family real estate, including home equity lines of credit. Credit card balances totaled $39.0 million at December 31, 2018 compared to $37.1 million a year earlier.

Loan Servicing Portfolio: At December 31, 2018, we were servicing $2.81 billion of loans for others and held $11.7 million in escrow for our portfolio of loans serviced for others. The loan servicing portfolio at December 31, 2018 was composed of $1.14 billion of Freddie Mac residential mortgage loans, $1.05 billion of Fannie Mae residential mortgage loans, $327.0 million of Oregon Housing residential mortgage loans and $286.0 million of other loans serviced for a variety of investors. The portfolio included loans secured by property located primarily in the states of Washington, Oregon, Idaho and California. For the year ended December 31, 2018, we recognized $2.7 million of loan servicing fees in our results of operations, which was net of $3.9 million of amortization for MSRs and included no impairment charges or reversals for a valuation adjustment to MSRs.

Mortgage Servicing Rights: For the years ended December 31, 2018, 2017 and 2016, we capitalized $3.6 million, $3.4 million, and $6.0 million, respectively, of MSRs relating to loans sold with servicing retained. Amortization of MSRs for the years ended December 31, 2018, 2017 and 2016 was $3.9 million, $4.0 million, and $4.0 million, respectively. Management periodically evaluates the estimates and assumptions used to determine the carrying values of MSRs and the amortization of MSRs. At December 31, 2018, our MSRs were carried at a value of $14.6 million, net of amortization, compared to $14.7 million at December 31, 2017.

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The following table sets forth the composition of the Company's loan portfolio, net of discounts and deferred fees and costs, by type of loan as of the dates indicated (dollars in thousands):

Table 4: Loan Portfolio Analysis

	December 31									
	2018		2017		2016		2015		2014	
	Amount	Percent of Total	Amount	Percent of Total	Amount	Percent of Total	Amount	Percent of Total	Amount	Percen of Tot
Commercial real estate:										
Owner-occupied	$1,430,097	16.4 %	$1,284,363	16.9 %	$1,352,999	18.1 %	$1,327,807	18.2 %	$546,783	14.3
Investment properties	2,131,059	24.5	1,937,423	25.5	1,986,336	26.7	1,765,353	24.1	856,942	22.3
Multifamily real estate	368,836	4.2	314,188	4.1	248,150	3.3	472,976	6.5	167,524	4.4
Commercial construction	172,410	2.0	148,435	2.0	124,068	1.7	72,103	1.0	17,337	0.5
Multifamily construction	184,630	2.1	154,662	2.0	124,126	1.7	63,846	0.9	60,193	1.6
One- to four-family construction	534,678	6.2	415,327	5.5	375,704	5.0	278,469	3.8	219,889	5.7
Land and land development:										
Residential	188,508	2.2	164,516	2.2	170,004	2.3	126,773	1.7	102,435	2.7
Commercial	27,278	0.3	24,583	0.3	29,184	0.4	33,179	0.5	11,152	0.3
Commercial business	1,483,614	17.1	1,279,894	16.8	1,207,879	16.2	1,207,944	16.5	723,964	18.9
Agricultural business, including secured by farmland	404,873	4.7	338,388	4.4	369,156	5.0	376,531	5.1	238,499	6.2
One- to four-family real estate	973,616	11.2	848,289	11.2	813,077	10.9	952,633	13.0	537,108	14.0
Consumer secured by one- to four-family real estate	568,979	6.6	522,931	6.9	493,211	6.6	478,420	6.5	222,205	5.8
Consumer—other	216,017	2.5	165,885	2.2	157,254	2.1	158,470	2.2	127,003	3.3
Total loans outstanding	8,684,595	100.0%	7,598,884	100.0%	7,451,148	100.0%	7,314,504	100.0%	3,831,034	100.0
Less allowance for loan losses	(96,485)		(89,028)		(85,997)		(78,008)		(75,907)	
Net loans	$8,588,110		$7,509,856		$7,365,151		$7,236,496		$3,755,127	

The following table sets forth the Company's loans by geographic concentration at December 31, 2018, 2017 and 2016 (dollars in thousands):

Table 5: Loans by Geographic Concentration

	December 31, 2018		December 31, 2017		December 31, 2016	
	Amount	Percent	Amount	Percent	Amount	Percent
Washington	$4,324,588	49.8 %	$3,508,542	46.2 %	$3,433,617	46.1 %
Oregon	1,636,152	18.8	1,590,233	20.9	1,505,369	20.2
California	1,596,604	18.4	1,415,076	18.6	1,239,989	16.6
Idaho	521,026	6.0	492,603	6.5	495,992	6.7
Utah	57,318	0.7	73,382	1.0	283,890	3.8
Other	548,907	6.3	519,048	6.8	492,291	6.6
Total	$8,684,595	100.0%	$7,598,884	100.0%	$7,451,148	100.0%

The following table sets forth certain information at December 31, 2018 regarding the dollar amount of loans maturing in our portfolio based on their contractual terms to maturity, but does not include scheduled payments or potential prepayments. Demand loans, loans having no stated schedule of repayments and no stated maturity, and overdrafts are reported as due in one year or less. Loan balances are net of unamortized premiums and discounts, and exclude loans held for sale and the allowance for loan losses (in thousands):

Table 6: Loans by Maturity

	Maturing in One Year or Less	Maturing After One to Three Years	Maturing After Three to Five Years	Maturing After Five to Ten Years	Maturing After Ten Years	Total
Commercial real estate:						
Owner-occupied	$58,823	$91,268	$207,181	$767,751	$305,074	$1,430,097
Investment properties	82,465	119,179	319,643	1,046,254	563,518	2,131,059
Multifamily real estate	7,443	20,748	41,068	148,263	151,314	368,836
Commercial construction	90,292	37,601	662	37,167	6,688	172,410
Multifamily construction	121,403	59,487	—	—	3,740	184,630
One- to four-family construction	498,576	30,853	216	161	4,872	534,678
Land and land development:						
Residential	119,097	61,909	3,113	4,389	—	188,508
Commercial	10,734	9,542	2,056	4,223	723	27,278
Commercial business	531,846	254,643	288,488	228,566	180,071	1,483,614
Agricultural business, including secured by farmland	145,557	43,265	49,112	142,776	24,163	404,873
One- to four-family real estate	12,316	7,654	13,379	68,997	871,270	973,616
Consumer secured by one- to four-family real estate	5,723	5,974	14,444	32,032	510,806	568,979
Consumer—other	37,785	21,288	38,117	42,421	76,406	216,017
Total loans	$1,722,060	$763,411	$977,479	$2,523,000	$2,698,645	$8,684,595

Contractual maturities of loans do not necessarily reflect the actual life of such assets. The average life of loans typically is substantially less than their contractual maturities because of principal repayments and prepayments. In addition, due-on-sale clauses on certain mortgage loans generally give us the right to declare loans immediately due and payable in the event that the borrower sells the real property subject to the mortgage and the loan is not repaid. The average life of mortgage loans tends to increase however when current mortgage loan market rates are substantially higher than rates on existing mortgage loans and, conversely, decreases when rates on existing mortgage loans are substantially higher than current mortgage loan market rates.

The following table sets forth the dollar amount of all loans maturing after December 31, 2019 which have fixed interest rates and floating or adjustable interest rates (in thousands):

Table 7: Loans Maturing after One Year

	Fixed Rates	Floating or Adjustable Rates	Total
Commercial real estate:			
Owner-occupied	$324,835	$1,046,439	$1,371,274
Investment properties	486,729	1,561,865	2,048,594
Multifamily real estate	160,073	201,320	361,393
Commercial construction	18,755	63,363	82,118
Multifamily construction	50,674	12,553	63,227
One- to four-family construction	6,025	30,077	36,102
Land and land development:			
Residential	5,538	63,873	69,411
Commercial	5,191	11,353	16,544
Commercial business	568,671	383,097	951,768
Agricultural business, including secured by farmland	87,555	171,761	259,316
One- to four-family real estate	672,728	288,572	961,300
Consumer secured by one- to four-family real estate	17,318	545,938	563,256
Consumer—other	124,203	54,029	178,232
Total loans maturing after one year	$2,528,295	$4,434,240	$6,962,535

Deposits. We compete with other financial institutions and financial intermediaries in attracting deposits and we generally attract deposits within our primary market areas. Much of the focus of our expansion and current marketing efforts have been directed toward attracting additional deposit customer relationships and balances. This effort has been particularly directed towards increasing transaction and savings accounts which has contributed to us being very successful in increasing these core deposit balances. The long-term success of our deposit gathering activities is reflected not only in the growth of deposit balances, but also in increases in the level of deposit fees, service charges and other payment processing revenues.

One of our key strategies is to strengthen our franchise by emphasizing core deposit activity in non-interest-bearing and other transaction and savings accounts with less reliance on higher cost certificates of deposit. Increasing core deposits is a fundamental element of our business strategy. This strategy continues to help control our cost of funds and increase the opportunity for deposit fee revenues, while stabilizing our funding base. Total deposits increased $1.29 billion, or 16%, to $9.48 billion at December 31, 2018 from $8.18 billion at December 31, 2017. Deposit growth for 2018 included $810.2 million of deposits acquired in the Skagit acquisition and a $320.1 million increase in brokered deposits, as well as organic deposit growth. Non-interest-bearing deposits increased by $392.3 million, or 12%, to $3.66 billion at year end from $3.27 billion at December 31, 2017. Interest-bearing transaction and savings accounts increased by $548.0 million, to $4.50 billion at December 31, 2018 compared to $3.95 billion a year earlier. Certificates of deposit increased $353.3 million, or 37%, to $1.32 billion at December 31, 2018 from $966.9 million at December 31, 2017. The increase in certificate balances in 2018 was largely due to the $320.1 million increase in brokered deposits to $377.3 million at December 31, 2018.

The following table sets forth the balances of deposits in the various types of accounts offered by the Banks at the dates indicated (dollars in thousands):

Table 8: Deposits

	December 31							
	2018			2017			2016	
	Amount	Percent of Total	Increase (Decrease)	Amount	Percent of Total	Increase (Decrease)	Amount	Percent of Total
Non-interest-bearing checking	$3,657,817	38.6 %	$392,273	$3,265,544	39.9 %	$125,093	$3,140,451	38.6 %
Interest-bearing checking	1,191,016	12.6	219,879	971,137	11.9	56,653	914,484	11.3
Regular savings	1,842,581	19.4	285,081	1,557,500	19.0	34,109	1,523,391	18.8
Money market	1,465,369	15.5	43,056	1,422,313	17.4	(75,442)	1,497,755	18.4
Total interest-bearing transaction and savings accounts	4,498,966	47.5	548,016	3,950,950	48.3	15,320	3,935,630	48.5
Certificates maturing:								
Within one year	1,001,206	10.6	315,614	685,592	8.4	(79,814)	765,406	9.4
After one year, but within two years	201,919	2.1	103,662	98,257	1.2	(61,179)	159,436	2.0
After two years, but within five years	114,893	1.2	(65,993)	180,886	2.2	63,804	117,082	1.4
After five years	2,247	—	45	2,202	—	(1,207)	3,409	—
Total certificate accounts	1,320,265	13.9	353,328	966,937	11.8	(78,396)	1,045,333	12.9
Total Deposits	$9,477,048	100.0%	$1,293,617	$8,183,431	100.0%	$62,017	$8,121,414	100.0%

Included in Total Deposits:								
Public transaction accounts	$217,401	2.3%	$18,682	$198,719	2.5%	$(23,046)	$221,765	2.7%
Public interest-bearing certificates	30,089	0.3	6,404	23,685	0.3	(1,965)	25,650	0.3
Total public deposits	$247,490	2.6%	$25,086	$222,404	2.8%	$(25,011)	$247,415	3.0%
Total brokered deposits	$377,347	4.0%	$320,119	$57,228	0.7%	$23,154	$34,074	0.4%

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The following table indicates the amount of the Banks' certificates of deposit with balances equal to or greater than $100,000 by time remaining until maturity as of December 31, 2018 (in thousands):

Table 9: Maturity Period—$100,000 or greater CDs

	Certificates of Deposit $100,000 or Greater
Maturing in three months or less	$ 123,775
Maturing after three months through six months	60,326
Maturing after six months through twelve months	101,430
Maturing after twelve months	152,388
Total	$ 437,919

The following table provides additional detail on geographic concentrations of our deposits at December 31, 2018 (in thousands):

Table 10: Geographic Concentration of Deposits

	December 31, 2018		December 31, 2017		December 31, 2016	
	Amount	Percent	Amount	Percent	Amount	Percent
Washington	$5,674,328	59.9 %	$4,506,249	55.0 %	$4,347,644	53.6 %
Oregon	1,891,145	20.0	1,797,147	22.0	1,708,973	21.0
California	1,434,033	15.1	1,432,819	17.5	1,469,748	18.1
Idaho	477,542	5.0	447,216	5.5	447,019	5.5
Utah	—	—	—	—	148,030	1.8
Total deposits	$9,477,048	100.0%	$8,183,431	100.0%	$8,121,414	100.0%

Borrowings. The FHLB-Des Moines serves as our primary borrowing source. To access funds, we are required to own a sufficient level of capital stock in the FHLB-Des Moines and may apply for advances on the security of such stock and certain of our mortgage loans and securities provided that certain creditworthiness standards have been met. At December 31, 2018, we had $540.2 million of FHLB advances outstanding at a weighted average rate of 2.64%, an increase of $540.0 million compared to a year earlier. Also, at December 31, 2018, we had an investment of $32.0 million in FHLB capital stock. At that date, Banner Bank was authorized by the FHLB-Des Moines to borrow up to $4.59 billion under a blanket floating lien security agreement, while Islanders Bank was approved to borrow up to $103.5 million under a similar agreement.

The following table provides additional detail on our FHLB advances as of December 31, 2018 and 2017 (dollars in thousands):

Table 11: FHLB Advances Outstanding

	December 31			
	2018		2017	
	Amount	Weighted Average Rate	Amount	Weighted Average Rate
Maturing in one year or less	$540,000	2.64 %	$—	— %
Maturing after one year through three years	—	—	—	—
Maturing after three years through five years	—	—	—	—

Maturing after five years	189	5.94		202	5.94	
Total FHLB advances	$540,189	2.64	%	$202	5.94	%

At certain times the Federal Reserve Bank has also served as an important source of borrowings. The Federal Reserve Bank provides credit based upon acceptable loan collateral, which includes certain loan types not eligible for pledging to the FHLB-Des Moines. At December 31, 2018, based upon our available unencumbered collateral, Banner Bank was eligible to borrow $1.15 billion from the Federal Reserve Bank; however, at that date we had no funds borrowed under this arrangement.

We also issue retail repurchase agreements to customers that are primarily related to customer cash management accounts and in the past have borrowed funds through the use of secured wholesale repurchase agreements with securities brokers. In each case, the repurchase agreements are generally due within 90 days. At December 31, 2018, retail and wholesale repurchase agreements totaling $119.0 million, with a weighted average rate of 0.21%, were secured by pledges of certain mortgage-backed securities and agency securities. Retail repurchase agreement balances, which are primarily associated with customer sweep account arrangements, increased $28.1 million, or 31%, from the 2017 year-end balance. We had no and $5.0 million of borrowings under wholesale repurchase agreements at December 31, 2018 and December 31, 2017, respectively.

We have an aggregate of $136.0 million, net of repayments, of TPS. This includes $120.0 million issued by us and $16.0 million acquired in our bank acquisitions. The junior subordinated debentures associated with the TPS have been recorded as liabilities on our Consolidated Statements of Financial Condition, although the TPS qualifies as Tier 1 capital for regulatory capital purposes. The junior subordinated debentures are carried at fair value on our Consolidated Statements of Financial Condition and had an estimated fair value of $114.1 million at December 31, 2018. At December 31, 2018, the TPS had a weighted average rate of 4.71%. See Note 11, Junior Subordinated Debentures and Mandatorily Redeemable Trust Preferred Trust Preferred Securities, of the Notes to the Consolidated Financial Statements for additional information with respect to the TPS.

Asset Quality. Achieving and maintaining a moderate risk profile by employing appropriate underwriting standards, avoiding excessive asset concentrations and aggressively managing troubled assets has been and will continue to be a primary focus for us. During 2018, we continued to be actively engaged with our borrowers in resolving remaining problem assets and with the effective management of real estate owned as a result of foreclosures.

Non-performing assets decreased to $18.9 million, or 0.16% of total assets, at December 31, 2018, from $27.5 million, or 0.28% of total assets, at December 31, 2017, and from $33.8 million, or 0.35% of total assets, at December 31, 2016. At December 31, 2018, our allowance for loan losses was $96.5 million, or 616% of non-performing loans, compared to $89.0 million, or 329% of non-performing loans at December 31, 2017 and $86.0 million, or 381% of non-performing loans at December 31, 2016. We continue to believe our level of non-performing loans and assets is manageable and further believe that we have sufficient capital and human resources to manage the collection of our non-performing assets in an orderly fashion.

Loans are reported as restructured when we grant concessions to a borrower experiencing financial difficulties that we would not otherwise consider. As a result of these concessions, restructured loans, or troubled debt restructures (TDRs), are considered impaired as the Banks will not collect all amounts of principal and interest due in accordance with the terms of the original loan agreement. If any restructured loan becomes delinquent or other matters call into question the borrower's ability to repay full interest and principal in accordance with the restructured terms, the restructured loan(s) would be reclassified as nonaccrual. At December 31, 2018, we had $13.4 million of restructured loans currently performing under their restructured terms.

The loans acquired in Banner's merger transactions that are determined to have deteriorated credit quality for which it is probable that all contractual payments will not be collected are accounted for as purchased credit-impaired pools. Typically this would include loans that were considered non-performing or restructured as of the acquisition date. Accordingly, subsequent to acquisition, loans included in the purchased credit-impaired pools are not reported as non-performing loans based upon their individual performance status, so the categories of nonaccrual, impaired and 90 day past due and accruing do not include any purchased credit-impaired loans. Purchased credit-impaired loans were $14.4 million at December 31, 2018, compared to $21.3 million at December 31, 2017.

The following table sets forth information with respect to our non-performing assets and restructured loans, at the dates indicated (dollars in thousands):

Table 12: Non-Performing Assets

	December 31				
	2018	2017	2016	2015	2014
Nonaccrual loans: (1)					
Secured by real estate:					
Commercial	$4,088	$10,646	$8,237	$3,751	$1,132
Construction/land	3,188	798	1,748	2,260	1,275
One- to four-family	1,544	3,264	2,263	4,700	8,834
Commercial business	2,936	3,406	3,074	2,159	537
Agricultural business, including secured by farmland	1,751	6,132	3,229	697	1,597
Consumer	1,241	1,297	1,875	703	1,187
	14,748	25,543	20,426	14,270	14,562
Loans more than 90 days delinquent, still on accrual:					
Secured by real estate:					
Commercial	—	—	701	—	—
Multifamily	—	—	147	—	—
Construction/land	—	298	—	—	—
One- to four-family	658	1,085	1,233	899	2,095
Commercial business	1	18	—	8	—
Agricultural business, including secured by farmland	—	—	—	—	—
Consumer	247	85	72	45	79
	906	1,486	2,153	952	2,174
Total non-performing loans	15,654	27,029	22,579	15,222	16,736
REO assets held for sale, net (2)	2,611	360	11,081	11,627	3,352
Other repossessed assets held for sale, net	592	107	166	268	76
Total non-performing assets	$18,857	$27,496	$33,826	$27,117	$20,164
Total non-performing loans to net loans before allowance for loan losses	0.18 %	0.36 %	0.30 %	0.21 %	0.44 %
Total non-performing loans to total assets	0.13 %	0.28 %	0.23 %	0.16 %	0.35 %
Total non-performing assets to total assets	0.16 %	0.28 %	0.35 %	0.28 %	0.43 %
Restructured loans (3)	$13,422	$16,115	$18,907	$21,777	$29,154
Loans 30-89 days past due and on accrual	$25,108	$29,278	$11,571	$18,834	$8,387

(1) Includes $317,000 of nonaccrual restructured loans as of December 31, 2018.

(2) Real estate acquired by us as a result of foreclosure or by deed-in-lieu of foreclosure is classified as real estate held for sale until it is sold. When property is acquired, it is recorded at the lower of the estimated fair value of the property, less expected selling costs, or the carrying value of the defaulted loan. Subsequent to foreclosure, the property is carried at the lower of the foreclosed amount or net realizable value. Upon receipt of a new appraisal and market analysis, the carrying value is written down through the establishment of a specific reserve to the anticipated sales price, less selling and holding costs.

(3) These loans were performing under their restructured terms.

In addition to the non-performing loans noted in Table 12 and purchased credit-impaired loans as of December 31, 2018 and 2017, we had other classified loans with an aggregate outstanding balance of $68.6 million and $80.8 million, respectively, that are not on nonaccrual status with respect to which known information concerning possible credit problems with the borrowers or the cash flows of the properties securing the respective loans has caused management to be concerned about the ability of the borrowers to comply with present loan repayment terms. This may result in the future inclusion of such loans in the nonaccrual loan category.

The following table presents the REO activity for the years ended December 31, 2018, 2017 and 2016 (in thousands):

Table 13: REO

	For the years ended December 31,		
	2018	2017	2016
Balance, beginning of the period	$360	$11,081	$11,627
Additions from loan foreclosures	641	46	8,909
Additions from acquisitions	2,593	—	400
Additions from capitalized costs	—	54	—
Proceeds from dispositions of REO	(838)	(13,474)	(10,812)
Gain on sale of REO	242	2,909	1,833
Valuation adjustments in period	(387)	(256)	(876)
Balance, end of period	$2,611	$360	$11,081

REO increased $2.3 million, to $2.6 million at December 31, 2018 compared to $360,000 at December 31, 2017 and $11.1 million at December 31, 2016. The increase during 2018 primarily reflects REO properties acquired in the Skagit acquisition.

From time to time, non-recurring fair value adjustments to REO are recorded to reflect partial write-downs based on an observable market price or current appraised value of property. The individual carrying values of these assets are reviewed for impairment at least annually and any additional impairment charges are expensed to operations.

Comparison of Results of Operations for the Years Ended December 31, 2018 and 2017

For the year ended December 31, 2018, we had net income of $136.5 million, or $4.15 per diluted share. This compares to net income of $60.8 million, or $1.84 per diluted share, for the year ended December 31, 2017. The 2018 results primarily reflect growth in average interest-earning assets from re-leveraging our investment portfolio, organic loan and deposit growth and to a lesser extent the acquisition of Skagit. Net income for both 2018 and 2017 were impacted by one-time tax adjustments primarily as a result of the enactment of the 2017 Tax Act, which reduced the marginal federal corporate income tax rate from 35% to 21%. Our net income for the year ended December 31, 2018, was positively impacted by $5.5 million of tax benefit adjustments, which included the release of a $4.2 million valuation reserve previously recorded as a provisional amount related to the 2017 Tax Act, while 2017 was negatively impacted by a $42.6 million, or $1.29 per diluted share, revaluation of our net deferred tax asset as a result of the 2017 Tax Act. In 2017, our results also included a net gain of $12.2 million as a result of the Utah Branch Sale. Our results for the year ended December 31, 2018 included $5.6 million of acquisition-related expenses. There were no acquisition-related expenses in 2017.

Our operating results depend largely on our net interest income which increased by $37.9 million to $431.0 million, primarily reflecting growth in both the loan and investment securities portfolios as well increased yields on interest-earning assets. Our operating results for the year ended December 31, 2018 also reflected a decrease in non-interest income, as the $4.6 million increase in deposit fees and other service charges and positive changes in the fair value of financial instruments carried at fair value in 2018 were offset by the absence of a similar $12.2 million gain from the Utah Branch Sale in 2017. The increase in net interest income contributed to an increase of $41.1 million, or 9%, in revenue from core operations to $512.0 million for the year ended December 31, 2018 compared to $471.0 million for the year ended December 31, 2017. Non-interest expense increased to $341.4 million for the year ended December 31, 2018 compared with $319.0 million for the year ended December 31, 2017, largely as a result of higher salary and employee benefits related primarily to enhanced regulatory requirements attributable to compliance and risk management infrastructure build-out, acquisition-related expenses, higher REO operations expenses, and other expenses associated with operating the branches acquired in the Skagit acquisition.

Net Interest Income. Net interest income before provision for loan losses increased by $37.9 million, or 10%, to $431.0 million for the year ended December 31, 2018, compared to $393.0 million one year earlier, largely reflecting organic client acquisition and to a lesser extent the contribution from the Skagit acquisition in the fourth quarter of 2018. Our net interest margin was enhanced by the amortization of acquisition accounting discounts on purchased loans acquired from bank acquisitions, which are accreted into loan interest income. The net interest margin of 4.43% for the year ended December 31, 2018 was 19 basis points higher than the prior year and both 2018 and 2017 included ten basis points from acquisition accounting adjustments. The average yield on interest-earning assets of 4.76% for the year ended December 31, 2018 increased 31 basis points compared to the prior year due to higher contractual yields on loans and securities. Funding costs were higher, as the average cost of funding liabilities increased by 14 basis points to 0.36% as compared to the prior year. As a result, the net interest spread increased to 4.40% for the year ended December 31, 2018 compared to 4.23% for the prior year.

Interest Income. Interest income for the year ended December 31, 2018 was $463.6 million, compared to $412.3 million for the prior year, an increase of $51.3 million, or 12%. The increase in interest income occurred as a result of increases in both the average balances and yields of interest-earning assets. The average balance of interest-earning assets was $9.73 billion for the year ended December 31, 2018, an increase of

$473.4 million, or 5%, compared to $9.26 billion one year earlier. The yield on average interest-earning assets was 4.76% for the year ended December 31, 2018, compared to 4.45% for the year ended December 31, 2017. The increased yield on interest-earning assets reflects improvement in yields on loans and securities. Loan yields increased 34 basis points to 5.21% for the year ended December 31, 2018 compared to 4.87% in the preceding year, reflecting the positive impact of increases in the prime rate, LIBOR and other market rates on adjustable-rate and recently originated loans and a one basis point increase in acquisition accounting loan discount accretion to 13 basis points in 2018 from 12 basis points in 2017. Average loans receivable for the year ended December 31, 2018 increased $251.9 million, or 3%, to $7.94 billion, compared to $7.69 billion for the prior year. Interest income on loans increased by $38.9 million, or 10%, to $413.4 million for the year ended December 31, 2018, from $374.4 million for the prior year, reflecting the impact of the $251.9 million increase in average loan balances and the 34 basis point increase in the average yield on total loans.

The combined average balance of mortgage-backed securities, other investment securities, daily interest-bearing deposits and FHLB stock increased to $1.80 billion for the year ended December 31, 2018 (excluding the effect of fair value adjustments), compared to $1.57 billion for the year ended December 31, 2017, contributing to the $12.4 million increase in interest and dividend income compared to the prior year. The average yield on the combined portfolio increased to 2.80% for the year ended December 31, 2018, from 2.40% for the prior year. Portfolio yields improved primarily as a result of security purchases in 2018 at higher yields than our existing portfolio. For the year ended December 31, 2018, the average yield on mortgage-backed securities increased 46 basis points to 2.81% compared to the prior year, while the yield on other securities increased 17 basis points to 2.85% compared to the prior year.

Interest Expense. Interest expense for the year ended December 31, 2018 was $32.7 million, compared to $19.3 million for the prior year, an increase of $13.4 million, or 70%. The increase in interest expense occurred as a result of a $413.8 million, or 5%, increase in average funding liabilities and a 14 basis point increase in the average cost of all funding liabilities to 0.36% for the year ended December 31, 2018, compared to 0.22% for the year ended December 31, 2017. This increase in average funding liabilities reflects increases in core deposits, including non-interest-bearing deposits and interest-bearing transaction and savings accounts, as well as increases in FHLB advances. Our strong base of non-interest-bearing deposits and other core deposits have lessened the impact of the increases in market interest rates resulting from changes in Federal Reserve monetary policy actions during 2018 and 2017.

Deposit interest expense increased $8.4 million, or 68%, to $20.6 million for the year ended December 31, 2018 compared to $12.3 million for the prior year as a result of a $314.7 million, or 4%, increase in the average balance of deposits and a nine basis point increase in the average cost of deposits. Average deposit balances increased to $8.67 billion for the year ended December 31, 2018, from $8.36 billion for the year ended December 31, 2017, while the average rate paid on deposit balances increased to 0.24% in the current year from 0.15% for the prior year. The cost of interest-bearing deposits increased by 15 basis points to 0.39% for the year ended December 31, 2018 compared to 0.24% in the prior year. The $177.1 million increase in the average balance of non-interest-bearing accounts during 2018 reduced the increase in total deposit costs. Deposit costs are significantly affected by changes in the level of market interest rates; however, changes in the average rate paid for interest-bearing deposits frequently tend to lag changes in market interest rates.

Average total borrowings increased to $502.6 million for the year end December 31, 2018, compared to $403.4 million for the prior year. The increase in average total borrowings was largely due to a $102.4 million increase in average FHLB advances. The average rate paid on total borrowings increased 66 basis points to 2.39% from 1.73% reflecting the 99 basis point increase in the average cost for our junior subordinated debentures (which reprice every three months based on changes in the three-month LIBOR index) and a 96 basis point increase in the average cost of FHLB advances reflecting increases to the Fed Funds target rate over the last two years. The increase in the average cost of total borrowings was the primary reason for the $5.0 million increase in the related interest expense to $12.0 million for the year ended December 31, 2018, from $7.0 million in the prior year.

Table 14, Analysis of Net Interest Spread, presents, for the periods indicated, our condensed average balance sheet information, together with interest income and yields earned on average interest-earning assets and interest expense and rates paid on average interest-bearing liabilities. Average balances are computed using daily average balances. (See the footnotes to the tables for more information on average balances.)

The following table provides an analysis of our net interest spread for the last three years (dollars in thousands):
Table 14: Analysis of Net Interest Spread

	Year Ended December 31, 2018			Year Ended December 31, 2017			Year Ended December 31, 2016		
	Average Balance	Interest and Dividends	Yield/ Cost (3)	Average Balance	Interest and Dividends	Yield/ Cost (3)	Average Balance	Interest and Dividends	Yield/ Cost (3)
Interest-earning assets:									
Held for sale loans	$81,873	$3,926	4.80 %	$128,480	$5,245	4.08 %	$107,018	$3,984	3.72 %
Mortgage loans	6,188,279	320,264	5.18	5,932,300	290,132	4.89	5,700,379	278,435	4.88
Commercial/agricultural loans	1,519,871	79,605	5.24	1,485,985	70,266	4.73	1,485,390	68,405	4.61
Consumer and other loans	149,184	9,575	6.42	140,500	8,806	6.27	141,460	8,788	6.21
Total loans (1)	7,939,207	413,370	5.21	7,687,265	374,449	4.87	7,434,247	359,612	4.84
Mortgage-backed securities	1,247,758	35,076	2.81	1,043,599	24,535	2.35	931,111	19,328	2.08
Other securities	468,416	13,332	2.85	464,680	12,448	2.68	454,977	11,814	2.60
Interest-bearing deposits with banks	59,031	1,080	1.83	49,573	583	1.18	94,456	395	0.42
FHLB stock	20,496	774	3.78	16,379	269	1.64	16,119	328	2.03
Total investment securities	1,795,701	50,262	2.80	1,574,231	37,835	2.40	1,496,663	31,865	2.13
Total interest-earning assets	9,734,908	463,632	4.76	9,261,496	412,284	4.45	8,930,910	391,477	4.38
Non-interest-earning assets	828,184			892,052			904,181		
Total assets	$10,563,092			$10,153,548			$9,835,091		
Deposits:									
Interest-bearing checking accounts	$1,048,327	$1,200	0.11	$933,978	$850	0.09	$859,621	$767	0.09
Savings accounts	1,665,608	3,944	0.24	1,559,042	2,138	0.14	1,370,014	1,796	0.13
Money market accounts	1,421,161	4,107	0.29	1,515,854	2,638	0.17	1,575,877	3,098	0.20
Certificates of deposit	1,127,612	11,391	1.01	1,116,304	6,647	0.60	1,208,702	5,444	0.45
Total interest-bearing deposits	5,262,708	20,642	0.39	5,125,178	12,273	0.24	5,014,214	11,105	0.22
Non-interest-bearing deposits	3,411,010	—	—	3,233,889	—	—	3,033,604	—	—
Total deposits	8,673,718	20,642	0.24	8,359,067	12,273	0.15	8,047,818	11,105	0.14
Other interest-bearing liabilities:									
FHLB advances	253,661	5,636	2.22	151,295	1,908	1.26	141,885	953	0.67
Other borrowings	108,730	245	0.23	111,903	317	0.28	108,427	310	0.29
Junior subordinated debentures	140,212	6,136	4.38	140,212	4,752	3.39	140,212	4,040	2.88
Total borrowings	502,603	12,017	2.39	403,410	6,977	1.73	390,524	5,303	1.36
Total funding liabilities	9,176,321	32,659	0.36	8,762,477	19,250	0.22	8,438,342	16,408	0.19
Other non-interest-bearing liabilities (2)	79,901			61,592			65,508		

Total liabilities	9,256,222				8,824,069				8,503,850		
Shareholders' equity	1,306,870				1,329,479				1,331,241		
Total liabilities and shareholders' equity	$10,563,092				$10,153,548				$9,835,091		
Net interest income/rate spread		$430,973	4.40	%		$393,034	4.23	%		$375,069	4.19	%
Net interest margin			4.43	%			4.24	%			4.20	%
Average interest-earning assets / average interest-bearing liabilities			168.85	%			167.52	%			165.24	%
Average interest-earning assets / average funding liabilities			106.09	%			105.69	%			105.84	%

(footnotes follow)

(1) Average balances include loans accounted for on a nonaccrual basis and loans 90 days or more past due. Amortization of net deferred loan fees/costs is included with interest on loans.
(2) Average other non-interest-bearing liabilities include fair value adjustments related to FHLB advances and junior subordinated debentures.
(3) Yields and costs have not been adjusted for the effect of tax-exempt interest.

The following table sets forth the effects of changing rates and volumes on our net interest income during the periods shown (in thousands). Information is provided with respect to (i) effects on interest income attributable to changes in volume (changes in volume multiplied by prior rate) and (ii) effects on interest income attributable to changes in rate (changes in rate multiplied by prior volume). Effects on interest income attributable to changes in rate and volume (changes in rate multiplied by changes in volume) have been allocated between changes in rate and changes in volume (in thousands):

Table 15: Rate/Volume Analysis

	Year Ended December 31, 2018 Compared to Year Ended December 31, 2017 Increase (Decrease) in Income/Expense Due to			Year Ended December 31, 2017 Compared to Year Ended December 31, 2016 Increase (Decrease) in Income/Expense Due to		
	Rate	Volume	Net	Rate	Volume	Net
Interest-earning assets:						
Mortgage loans	$18,384	$10,429	$28,813	$610	$12,348	$12,958
Commercial/agricultural loans	7,707	1,632	9,339	1,834	27	1,861
Consumer and other loans	215	554	769	78	(60)	18
Total loans (1)	26,306	12,615	38,921	2,522	12,315	14,837
Mortgage-backed securities	5,271	5,270	10,541	2,725	2,483	5,208
Other securities	784	100	884	379	254	633
Interest-bearing deposits with banks	370	127	497	447	(259)	188
FHLB stock	350	155	505	(63)	4	(59)
Total investment securities	6,775	5,652	12,427	3,488	2,482	5,970
Total net change in interest income on interest-earning assets	33,081	18,267	51,348	6,010	14,797	20,807
Interest-bearing liabilities:						
Deposits (2)	8,259	110	8,369	1,412	(244)	1,168
FHLB advances	1,974	1,754	3,728	888	67	955
Other borrowings	(63)	(9)	(72)	(3)	10	7
Junior subordinated debentures	1,384	—	1,384	712	—	712
Total borrowings	3,295	1,745	5,040	1,597	77	1,674
Total net change in interest expense on interest-bearing liabilities	11,554	1,855	13,409	3,009	(167)	2,842
Net change in net interest income	$21,527	$16,412				