ZIFFERER MORTON
Form 4
February 02, 2018

FORM 4

Check this box if no longer subject to Section 16. Form 4 or Form 5 obligations may continue. *See* Instruction 1(b).

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

STATEMENT OF CHANGES IN BENEFICIAL OWNERSHIP OF SECURITIES

Filed pursuant to Section 16(a) of the Securities Exchange Act of 1934, Section 17(a) of the Public Utility Holding Company Act of 1935 or Section 30(h) of the Investment Company Act of 1940

OMB APPROVAL
OMB Number: 3235-0287
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(Print or Type Responses)

1. Name and Address of Reporting Person *
ZIFFERER MORTON

(Last) (First) (Middle)

NEW STANDARD CORP., PO BOX 420

(Street)

MOUNT JOY, PA 17552-0420

(City) (State) (Zip)

2. Issuer Name **and** Ticker or Trading Symbol
TESSCO TECHNOLOGIES INC [TESS]

3. Date of Earliest Transaction (Month/Day/Year)
01/30/2018

4. If Amendment, Date Original Filed(Month/Day/Year)

5. Relationship of Reporting Person(s) to Issuer

(Check all applicable)

__X__ Director _____ 10% Owner
_____ Officer (give title below) _____ Other (specify below)

6. Individual or Joint/Group Filing(Check Applicable Line)
_X_ Form filed by One Reporting Person
___ Form filed by More than One Reporting Person

Table I - Non-Derivative Securities Acquired, Disposed of, or Beneficially Owned

1.Title of Security (Instr. 3)	2. Transaction Date (Month/Day/Year)	2A. Deemed Execution Date, if any (Month/Day/Year)	3. Transaction Code (Instr. 8)		4. Securities Acquired (A) or Disposed of (D) (Instr. 3, 4 and 5)			5. Amount of Securities Beneficially Owned Following Reported Transaction(s) (Instr. 3 and 4)	6. Ownership Form: Direct (D) or Indirect (I) (Instr. 4)	7. Nature of Indirect Beneficial Ownership (Instr. 4)
			Code	V	Amount	(A) or (D)	Price			
Common Stock	01/30/2018		S		3,018	D	$ 22.6	77,839	D	
Common Stock	01/30/2018		S		217	D	$ 22.6	77,622	D	
Common Stock	01/31/2018		S		2,474	D	$ 22.04	75,148	D	
Common Stock	01/31/2018		S		2,793	D	$ 22.04	72,355	D	
Common Stock	02/01/2018		S		1,498	D	$ 21.71	70,857	D	

Reminder: Report on a separate line for each class of securities beneficially owned directly or indirectly.

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SEC 1474 (9-02)

Table II - Derivative Securities Acquired, Disposed of, or Beneficially Owned
(*e.g.*, puts, calls, warrants, options, convertible securities)

1. Title of Derivative Security (Instr. 3)	2. Conversion or Exercise Price of Derivative Security	3. Transaction Date (Month/Day/Year)	3A. Deemed Execution Date, if any (Month/Day/Year)	4. Transaction Code (Instr. 8)		5. Number of Derivative Securities Acquired (A) or Disposed of (D) (Instr. 3, 4, and 5)		6. Date Exercisable and Expiration Date (Month/Day/Year)		7. Title and Amount of Underlying Securities (Instr. 3 and 4)		8. Price of Derivative Security (Instr. 5)	9. Nu Deriv Secur Bene Owne Follo Repo Trans (Instr
				Code	V	(A)	(D)	Date Exercisable	Expiration Date	Title	Amount or Number of Shares		

Reporting Owners

Reporting Owner Name / Address	Relationships			
	Director	10% Owner	Officer	Other
ZIFFERER MORTON NEW STANDARD CORP. PO BOX 420 MOUNT JOY, PA 17552-0420	X			

Signatures

Morton Zifferer by Aric Spitulnic by Power of Attorney	02/02/2018
**Signature of Reporting Person	Date

Explanation of Responses:

* If the form is filed by more than one reporting person, *see* Instruction 4(b)(v).

** Intentional misstatements or omissions of facts constitute Federal Criminal Violations. *See* 18 U.S.C. 1001 and 15 U.S.C. 78ff(a).

Note: File three copies of this Form, one of which must be manually signed. If space is insufficient, *see* Instruction 6 for procedure.
Potential persons who are to respond to the collection of information contained in this form are not required to respond unless the form displays a currently valid OMB number. >

Fair Value

Amortized Cost

Fair Value
Maturing in one year or less
$
767

$
771

$
1,270

$
1,281

Maturing after one year through five years
14,962

15,184

10,834

11,206

Maturing after five years through ten years
24,233

24,678

17,948

17,908

Maturing after ten years through twenty years
76,029

81,361

59,643

60,791

Maturing after twenty years
15,267

15,614

12,818

12,424

$
131,258

$
137,608

$
102,513

$
103,610

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Pledged Securities: The following table presents, as of December 31, 2014, investment securities which were pledged to secure borrowings, public deposits or other obligations as permitted or required by law (in thousands):

	Carrying Value	Amortized Cost	Fair Value
Purpose or beneficiary:			
State and local governments public deposits	$116,273	$116,242	$122,130
Interest rate swap counterparties	11,051	10,648	11,051
Retail repurchase transaction accounts	98,735	98,435	98,735
Other	248	248	248
Total pledged securities	$226,307	$225,573	$232,164

Interest Income from Securities and Cash Equivalents: The following table sets forth the composition of interest income from securities and cash equivalents for the periods indicated (in thousands):

	Years Ended December 31		
	2014	2013	2012
Mortgage-backed securities interest	$5,779	$5,168	$4,176
Other taxable interest income	3,101	3,601	5,087
Tax-exempt interest income	4,206	3,721	3,577
FHLB stock—dividend income	34	18	—
Total interest income from securities and cash equivalents	$13,120	$12,508	$12,840

Note 6: LOANS RECEIVABLE AND THE ALLOWANCE FOR LOAN LOSSES

Loans receivable, including loans held for sale, at December 31, 2014 and 2013 are summarized as follows (dollars in thousands):

	December 31, 2014		December 31, 2013	
	Amount	Percent of Total	Amount	Percent of Total
Commercial real estate:				
Owner-occupied	$546,783	14.3 %	$502,601	14.7 %
Investment properties	856,942	22.3	692,457	20.2
Multifamily real estate	167,524	4.4	137,153	4.0
Commercial construction	17,337	0.4	12,168	0.4
Multifamily construction	60,193	1.6	52,081	1.5
One- to four-family construction	219,889	5.7	200,864	5.9
Land and land development:				
Residential	102,435	2.7	75,695	2.2
Commercial	11,152	0.3	10,450	0.3
Commercial business	723,964	18.9	682,169	20.0
Agricultural business, including secured by farmland	238,499	6.2	228,291	6.7
One- to four-family residential	539,894	14.1	529,494	15.5
Consumer:				
Consumer secured by one- to four-family	222,205	5.8	173,188	5.1
Consumer—other	127,003	3.3	121,834	3.5
Total loans outstanding	3,833,820	100.0 %	3,418,445	100.0 %
Less allowance for loan losses	(75,907)		(74,258)	
Net loans	$3,757,913		$3,344,187	

Loan amounts are net of unearned, unamortized loan fees (and costs) of approximately $5.8 million at December 31, 2014 and approximately $8.3 million at December 31, 2013.

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The Company's loans by geographic concentration at December 31, 2014 were as follows (dollars in thousands):

	Washington	Oregon	Idaho	Other	Total
Commercial real estate:					
Owner-occupied	$383,950	$86,937	$56,348	$19,548	$546,783
Investment properties	523,806	124,604	60,053	148,479	856,942
Multifamily real estate	116,793	35,527	14,759	445	167,524
Commercial construction	15,599	—	1,738	—	17,337
Multifamily construction	50,931	8,850	412	—	60,193
One- to four-family construction	129,499	88,468	1,922	—	219,889
Land and land development:					
Residential	56,675	44,707	1,053	—	102,435
Commercial	5,781	2,529	2,842	—	11,152
Commercial business	397,103	125,235	85,580	116,046	723,964
Agricultural business, including secured by farmland	119,617	69,843	48,997	42	238,499
One- to four-family residential	341,944	172,974	24,223	753	539,894
Consumer:					
Consumer secured by one- to four-family	136,888	69,172	14,984	1,161	222,205
Consumer—other	79,520	40,803	6,243	437	127,003
Total loans	$2,358,106	$869,649	$319,154	$286,911	$3,833,820
Percent of total loans	61.5 %	22.7 %	8.3 %	7.5 %	100.0 %

The geographic concentrations of land and land development loans by state at December 31, 2014 were as follows (dollars in thousands):

	Washington	Oregon	Idaho	Total
Residential:				
Acquisition and development	$28,901	$24,378	$916	$54,195
Improved land and lots	21,703	17,262	137	39,102
Unimproved land	6,071	3,067	—	9,138
Commercial and industrial:				
Improved land and lots	3,750	478	1,783	6,011
Unimproved land	2,031	2,051	1,059	5,141
Total land and land development loans	$62,456	$47,236	$3,895	$113,587
Percent of land and land development loans	55.0 %	41.6 %	3.4 %	100.0 %

The Company originates both adjustable- and fixed-rate loans. At December 31, 2014 and 2013, the maturity and repricing composition of those loans, less undisbursed amounts and deferred fees and origination costs, were as follows (in thousands):

	December 31	
	2014	2013
Fixed-rate (term to maturity):		
Maturing in one year or less	$115,571	$122,313
Maturing after one year through three years	184,707	143,322
Maturing after three years through five years	180,449	187,279
Maturing after five years through ten years	240,742	209,869
Maturing after ten years	572,793	439,004
Total fixed-rate loans	1,294,262	1,101,787
Adjustable-rate (term to rate adjustment):		
Maturing or repricing in one year or less	1,468,316	1,390,579
Maturing or repricing after one year through three years	416,433	279,791
Maturing or repricing after three years through five years	566,371	541,529
Maturing or repricing after five years through ten years	87,506	99,503
Maturing or repricing after ten years	932	5,256
Total adjustable-rate loans	2,539,558	2,316,658
Total loans	$3,833,820	$3,418,445

The adjustable-rate loans have interest rate adjustment limitations and are generally indexed to various prime or LIBOR rates, FHLB advance rates or One- to Five-Year Constant Maturity Treasury Indices. Future market factors may affect the correlation of the interest rate adjustment with the rates the Banks pay on the short-term deposits that primarily have been utilized to fund these loans.

The Company's loans to directors, executive officers and related entities are on substantially the same terms and underwriting as those prevailing at the time for comparable transactions with unrelated persons and do not involve more than normal risk of collectability. Such loans had the following balances and activity during the years ended December 31, 2014 and 2013 (in thousands):

	Years Ended December 31	
	2014	2013
Balance at beginning of year	$15,976	$12,463
New loans or advances	38,241	39,921
Repayments and adjustments	(45,608)	(36,408)
Balance at end of period	$8,609	$15,976

Impaired Loans and the Allowance for Loan Losses: A loan is considered impaired when, based on current information and circumstances, the Company determines it is probable that it will be unable to collect all amounts due according to the contractual terms of the loan agreement, including scheduled interest payments. Impaired loans are comprised of loans on nonaccrual, TDRs that are performing under their restructured terms, and loans that are 90 days or more past due, but are still on accrual.

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The amount of impaired loans and the related allocated reserve for loan losses at the dates indicated were as follows (in thousands):

	December 31, 2014		December 31, 2013	
	Loan Amount	Allocated Reserves	Loan Amount	Allocated Reserves
Impaired loans:				
Nonaccrual loans				
Commercial real estate:				
Owner-occupied	$1,365	$20	$2,466	$31
Investment properties	32	5	3,821	89
One- to four-family construction	—	—	269	—
Land and land development:				
Residential	1,275	—	924	6
Commercial business	537	46	724	104
Agricultural business, including secured by farmland	1,597	26	—	—
One- to four-family residential	8,507	35	12,532	250
Consumer:				
Consumer secured by one- to four-family	838	47	903	13
Consumer—other	411	—	269	1
Total nonaccrual loans	14,562	179	21,908	494
Loans 90 days past due and still accruing				
Agricultural business, including secured by farmland	—	—	105	8
One- to four-family residential	2,095	10	2,611	16
Consumer:				
Consumer secured by one- to four-family	80	—	13	—
Consumer—other	—	—	131	1
Total loans 90 days past due and still accruing	2,175	10	2,860	25
Troubled debt restructuring on accrual status:				
Commercial real estate:				
Owner-occupied	184	4	186	4
Investment properties	6,021	724	5,367	415
Multifamily real estate	786	86	5,744	1,139
One- to four-family construction	3,923	640	6,864	1,002
Land and land development:				
Residential	1,279	346	4,061	754
Commercial business	739	82	1,299	222
One- to four-family residential	15,792	987	23,302	1,355
Consumer:				
Consumer secured by one- to four-family	233	28	360	33
Consumer—other	197	6	245	34
Total troubled debt restructurings on accrual status	29,154	2,903	47,428	4,958
Total impaired loans	$45,891	$3,092	$72,196	$5,477

As of December 31, 2014 and 2013, the Company had commitments to advance funds up to an additional amount of $2.1 million and $225,000, respectively, related to TDRs.

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The following tables provide additional information on impaired loans with and without specific allowance reserves as of December 31, 2014 and December 31, 2013. Recorded investment includes the unpaid principal balance or the carrying amount of loans less charge-offs and net deferred loan fees (in thousands):

	At or For the Year Ended December 31, 2014				
	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized
Without a specific allowance reserve (1)					
Commercial real estate:					
Owner-occupied	$399	$449	$20	$526	$—
Investment properties	32	32	5	44	—
Commercial business	537	763	46	566	—
Agricultural business, including secured by farmland	853	853	26	1,122	—
One- to four-family residential	8,546	9,244	18	7,284	29
Consumer:					
Consumer secured by one- to four-family	783	888	11	838	3
Consumer—other	295	305	—	270	—
	11,445	12,534	126	10,650	32
With a specific allowance reserve (2)					
Commercial real estate:					
Owner-occupied	1,149	1,149	4	1,315	12
Investment properties	6,022	6,426	724	6,101	315
Multifamily real estate	786	786	86	795	45
One- to four-family construction	3,923	3,923	640	2,655	118
Land and land development:					
Residential	2,554	3,710	346	2,872	89
Commercial business	739	739	82	762	41
Agricultural business, including secured by farmland	744	744	—	744	—
One- to four-family residential	17,848	18,611	1,014	18,809	841
Consumer:					
Consumer secured by one- to four-family	368	368	64	410	16
Consumer—other	313	329	6	327	19
	34,446	36,785	2,966	34,790	1,496
Total					
Commercial real estate:					
Owner occupied	1,548	1,598	24	1,841	12
Investment properties	6,054	6,458	729	6,145	315
Multifamily real estate	786	786	86	795	45
One- to four-family construction	3,923	3,923	640	2,655	118
Land and land development:					
Residential	2,554	3,710	346	2,872	89
Commercial business	1,276	1,502	128	1,328	41
Agricultural business, including secured by farmland	1,597	1,597	26	1,866	—
One- to four-family residential	26,394	27,855	1,032	26,093	870
Consumer:					
Consumer secured by one- to four-family	1,151	1,256	75	1,248	19

Consumer—other	608	634	6	597	19
	$45,891	$49,319	$3,092	$45,440	$1,528

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	At or For the Year Ended December 31, 2013				
	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized
Without a specific allowance reserve (1)					
Commercial real estate:					
Owner-occupied	$534	$584	$31	$569	$—
Investment properties	429	974	89	624	—
Commercial business	724	1,040	104	896	—
Agricultural business, including secured by farmland	105	105	8	110	8
One- to four-family residential	8,611	9,229	42	8,889	31
Consumer:					
Consumer secured by one- to four-family	870	1,013	13	900	1
Consumer—other	276	285	2	287	8
	11,549	13,230	289	12,275	48
With a specific allowance reserve (2)					
Commercial real estate:					
Owner-occupied	2,118	2,118	4	2,192	12
Investment properties	8,759	10,395	415	8,353	241
Multifamily real estate	5,744	5,744	1,139	5,705	298
One- to four-family construction	7,133	7,213	1,002	5,870	239
Land and land development:					
Residential	4,985	6,140	760	6,053	221
Commercial business	1,298	1,298	222	1,340	59
One- to four-family residential	29,834	31,440	1,579	31,668	1,032
Consumer:					
Consumer secured by one- to four-family	406	407	33	503	24
Consumer—other	370	386	34	390	21
	60,647	65,141	5,188	62,074	2,147
Total					
Commercial real estate:					
Owner-occupied	2,652	2,702	35	2,761	12
Investment properties	9,188	11,369	504	8,977	241
Multifamily real estate	5,744	5,744	1,139	5,705	298
One- to four-family construction	7,133	7,213	1,002	5,870	239
Land and land development:					
Residential	4,985	6,140	760	6,053	221
Commercial business	2,022	2,338	326	2,236	59
Agricultural business, including secured by farmland	105	105	8	110	8
One- to four-family residential	38,445	40,669	1,621	40,557	1,063
Consumer:					
Consumer secured by one- to four-family	1,276	1,420	46	1,403	25
Consumer—other	646	671	36	677	29
	$72,196	$78,371	$5,477	$74,349	$2,195

(1) Loans without a specific allowance reserve have not been individually evaluated for impairment, but have been included in pools of homogeneous loans for evaluation of related allowance reserves.

(2) Loans with a specific allowance reserve have been individually evaluated for impairment using either a discounted cash flow analysis or, for collateral dependent loans, current appraisals to establish realizable value. These analyses may identify a specific impairment amount needed or may conclude that no reserve is needed. Any specific impairment that is identified is included in the category’s "Related Allowance" column.

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The following tables present TDRs at December 31, 2014 and 2013 (in thousands):

	December 31, 2014		
	Accrual Status	Nonaccrual Status	Total TDRs
Commercial real estate:			
Owner-occupied	$183	$109	$292
Investment properties	6,021	32	6,053
Multifamily real estate	786	—	786
One- to four-family construction	3,923	—	3,923
Land and land development:			
Residential	1,279	525	1,804
Commercial business	739	87	826
One- to four-family residential	15,793	1,363	17,156
Consumer:			
Consumer secured by one- to four-family	233	117	350
Consumer—other	197	116	313
	$29,154	$2,349	$31,503

	December 31, 2013		
	Accrual Status	Nonaccrual Status	Total TDRs
Commercial real estate:			
Owner-occupied	$186	$613	$799
Investment properties	5,367	1,630	6,997
Multifamily real estate	5,744	—	5,744
One- to four-family construction	6,864	269	7,133
Land and land development:			
Residential	4,061	174	4,235
Commercial business	1,299	164	1,463
One- to four-family residential	23,302	2,474	25,776
Consumer:			
Consumer secured by one- to four-family	360	252	612
Consumer—other	245	123	368
	$47,428	$5,699	$53,127

The following tables present new TDRs that occurred during the years ended December 31, 2014 and 2013 (dollars in thousands):

	Year Ended December 31, 2014		
	Number of Contracts	Pre-modification Outstanding Recorded Investment	Post-modification Outstanding Recorded Investment
Recorded Investment [1] [2]			
Commercial real estate:			
Owner-occupied	1	$203	$203
One- to four-family construction	10	2,153	2,153
Commercial business	1	100	100
One- to four-family residential	4	905	862
Consumer - other	1	9	9
	17	$3,370	$3,327

	Year Ended December 31, 2013		
	Number of Contracts	Pre-modification Outstanding Recorded Investment	Post-modification Outstanding Recorded Investment
Recorded Investment [1] [2]			
Commercial real estate:			
Owner-occupied	1	$1,246	$1,246
Multifamily real estate	1	375	375
One- to four-family construction	8	3,082	3,082
Land and land development:			
Residential	2	1,029	1,029
Commercial business	1	100	100
One- to four-family residential	10	2,726	2,726
	23	$8,558	$8,558

(1) Since most loans were already considered classified and/or on non-accrual status prior to restructuring, the modifications did not have a material effect on the Company's determination of the allowance for loan losses.

(2) The majority of these modifications do not fit into one separate type, such as: rate, term, amount, interest-only or payment; but instead are a combination of multiple types of modifications, therefore they are disclosed in aggregate.

The following table presents TDRs which incurred a payment default within the years ended December 31, 2014 and 2013, for which the payment default occurred within twelve months of the restructure date. A default on a restructured loan results in a transfer to nonaccrual status, a charge-off or a combination of both (in thousands):

	Years Ended December 31			
	2014		2013	
	Number of Loans	Amount	Number of Loans	Amount
Construction and land	—	$—	2	$483
Commercial business	—	—	2	321
One- to four-family residential	—	—	2	222
Total	—	$—	6	$1,026

Credit Quality Indicators: To appropriately and effectively manage the ongoing credit quality of the Company's loan portfolio, management has implemented a risk-rating or loan grading system for its loans. The system is a tool to evaluate portfolio asset quality throughout each applicable loan's life as an asset of the Company. Generally, loans and leases are risk rated on an aggregate borrower/relationship basis with individual loans sharing similar ratings. There are some instances when specific situations relating to individual loans will provide the basis for different risk ratings within the aggregate relationship. Loans are graded on a scale of 1 to 9. A description of the general characteristics of these categories is shown below:

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Overall Risk Rating Definitions: Risk-ratings contain both qualitative and quantitative measurements and take into account the financial strength of a borrower and the structure of the loan or lease. Consequently, the definitions are to be applied in the context of each lending transaction and judgment must also be used to determine the appropriate risk rating, as it is not unusual for a loan or lease to exhibit characteristics of more than one risk-rating category. Consideration for the final rating is centered in the borrower's ability to repay, in a timely fashion, both principal and interest. There were no material changes in the risk-rating or loan grading system in 2014.

Risk Rating 1: Exceptional
A credit supported by exceptional financial strength, stability, and liquidity. The risk rating of 1 is reserved for the Company's top quality loans, generally reserved for investment grade credits underwritten to the standards of institutional credit providers.

Risk Rating 2: Excellent
A credit supported by excellent financial strength, stability and liquidity. The risk rating of 2 is reserved for very strong and highly stable customers with ready access to alternative financing sources.

Risk Rating 3: Strong
A credit supported by good overall financial strength and stability. Collateral margins are strong, cash flow is stable although susceptible to cyclical market changes.

Risk Rating 4: Acceptable
A credit supported by the borrower's adequate financial strength and stability. Assets and cash flow are reasonably sound and provide for orderly debt reduction. Access to alternative financing sources will be more difficult to obtain.

Risk Rating 5: Watch
A credit with the characteristics of an acceptable credit but one which requires more than the normal level of supervision and warrants formal quarterly management reporting. Credits in this category are not yet criticized or classified, but due to adverse events or aspects of underwriting require closer than normal supervision. Generally, credits should be watch credits in most cases for six months or less as the impact of stress factors are analyzed.

Risk Rating 6: Special Mention
A credit with potential weaknesses that deserves management's close attention is risk rated a 6. If left uncorrected, these potential weaknesses will result in deterioration in the capacity to repay debt. A key distinction between Special Mention and Substandard is that in a Special Mention credit, there are identified weaknesses that pose potential risk(s) to the repayment sources, versus well defined weaknesses that pose risk(s) to the repayment sources. Assets in this category are expected to be in this category no more than 9-12 months as the potential weaknesses in the credit are resolved.

Risk Rating 7: Substandard
A credit with well defined weaknesses that jeopardize the ability to repay in full is risk rated a 7. These credits are inadequately protected by either the sound net worth and payment capacity of the borrower or the value of pledged collateral. These are credits with a distinct possibility of loss. Loans headed for foreclosure and/or legal action due to deterioration are rated 7 or worse.

Risk Rating 8: Doubtful
A credit with an extremely high probability of loss is risk rated 8. These credits have all the same critical weaknesses that are found in a substandard loan; however, the weaknesses are elevated to the point that based upon current information, collection or liquidation in full is improbable. While some loss on doubtful credits is expected, pending

events may strengthen a credit making the amount and timing of any loss indeterminate. In these situations taking the loss is inappropriate until it is clear that the pending event has failed to strengthen the credit and improve the capacity to repay debt.

Risk Rating 9: Loss
A credit that is considered to be currently uncollectible or of such little value that it is no longer a viable Bank asset is risk rated 9. Losses are taken in the accounting period in which the credit is determined to be uncollectible. Taking a loss does not mean that a credit has absolutely no recovery or salvage value but, rather, it is not practical or desirable to defer writing off the credit, even though partial recovery may occur in the future.

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The following table shows Banner's portfolio of risk-rated loans and non-risk-rated loans by grade or other characteristic as of December 31, 2014 (in thousands):

	December 31, 2014							
	Commercial Real Estate	Multifamily Real Estate	Construction and Land	Commercial Business	Agricultural Business	One- to Four-Family Residential	Consumer	Total Loans
Risk-rated loans:								
Pass (Risk Ratings 1-5) [1]	$1,375,885	$166,712	$395,356	$691,143	$234,101	$527,384	$346,456	$3,737,037
Special mention	3,717	—	—	27,453	1,055	63	140	32,428
Substandard	24,123	812	15,650	5,368	3,343	12,447	2,601	64,344
Doubtful	—	—	—	—	—	—	11	11
Total loans	$1,403,725	$167,524	$411,006	$723,964	$238,499	$539,894	$349,208	$3,833,820
Performing loans	$1,402,328	$167,524	$409,731	$723,427	$236,902	$529,292	$347,880	$3,817,084
Non-performing loans [2]	1,397	—	1,275	537	1,597	10,602	1,328	16,736
Total loans	$1,403,725	$167,524	$411,006	$723,964	$238,499	$539,894	$349,208	$3,833,820

(1) The Pass category includes some performing loans that are part of homogenous pools which are not individually risk-rated. This includes all consumer loans, all one- to four-family residential loans and, as of December 31, 2014, in the commercial business category, $115 million of credit-scored small business loans. As loans in these pools become non-performing, they are individually risk-rated.

(2) Non-performing loans include loans on non-accrual status and loans more than 90 days delinquent, but still accruing interest.

The following table shows Banner's portfolio of risk-rated loans and non-risk-rated loans by grade or other characteristic as of December 31, 2013 (in thousands):

	December 31, 2013							
	Commercial Real Estate	Multifamily Real Estate	Construction and Land	Commercial Business	Agricultural Business	One- to Four-Family Residential	Consumer	Total Loans
Risk-rated loans:								
Pass (Risk Ratings 1-5) [1]	$1,160,921	$131,523	$332,150	$655,007	$225,329	$511,967	$291,992	$3,308,889
Special mention	6,614	—	350	10,484	561	—	106	18,115
Substandard	26,979	5,630	18,758	16,669	2,401	17,527	2,924	90,888
Doubtful	544	—	—	9	—	—	—	553
Total loans	$1,195,058	$137,153	$351,258	$682,169	$228,291	$529,494	$295,022	$3,418,445
Performing loans	$1,188,771	$137,153	$350,065	$681,445	$228,187	$514,351	$293,705	$3,393,677
Non-performing loans [2]	6,287	—	1,193	724	104	15,143	1,317	24,768
Total loans	$1,195,058	$137,153	$351,258	$682,169	$228,291	$529,494	$295,022	$3,418,445

(1) The Pass category includes some performing loans that are part of homogenous pools which are not individually risk-rated. This includes all consumer loans, all one- to four-family residential loans and, as of December 31,

2013, in the commercial business category, $94 million of credit-scored small business loans. As loans in these pools become non-performing, they are individually risk-rated.

(2) Non-performing loans include loans on non-accrual status and loans more than 90 days delinquent, but still accruing interest.

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The following tables provide additional detail on the age analysis of Banner's past due loans as of December 31, 2014 and 2013 (in thousands):

	December 31, 2014						
	30–59 Days Past Due	60–89 Days Past Due	90 Days or More Past Due	Total Past Due	Current	Total Loans	Loans 90 Days or More Past Due and Accruing
Commercial real estate:							
Owner-occupied	$—	$1,984	$—	$1,984	$544,799	$546,783	$—
Investment properties	639	—	—	639	856,303	856,942	—
Multifamily real estate	—	—	—	—	167,524	167,524	—
Commercial construction	—	—	—	—	17,337	17,337	—
Multifamily construction	—	—	—	—	60,193	60,193	—
One- to four-family construction	840	—	—	840	219,049	219,889	—
Land and land development:							
Residential	759	—	750	1,509	100,926	102,435	—
Commercial	—	—	—	—	11,152	11,152	—
Commercial business	775	35	100	910	723,054	723,964	—
Agricultural business, including secured by farmland	597	466	744	1,807	236,692	238,499	—
One- to four-family residential [(1)]	877	1,623	7,526	10,026	529,868	539,894	2,095
Consumer:							
Consumer secured by one- to four-family	59	60	139	258	221,947	222,205	80
Consumer—other	491	88	293	872	126,131	127,003	—
Total	$5,037	$4,256	$9,552	$18,845	$3,814,975	$3,833,820	$2,175

	December 31, 2013						
	30–59 Days Past Due	60–89 Days Past Due	90 Days or More Past Due	Total Past Due	Current	Total Loans	Loans 90 Days or More Past Due and Accruing
Commercial real estate:							
Owner-occupied	$883	$550	$813	$2,246	$500,355	$502,601	$—
Investment properties	—	—	—	—	692,457	692,457	—
Multifamily real estate	1,845	785	—	2,630	134,523	137,153	—
Commercial construction	—	—	—	—	12,168	12,168	—
Multifamily construction	—	—	—	—	52,081	52,081	—
One- to four-family construction	9	7	4	20	200,844	200,864	—
Land and land development:							
Residential	—	—	251	251	75,444	75,695	—

Commercial	—	—	—	—	10,450	10,450	—
Commercial business	2,001	2	299	2,302	679,867	682,169	—
Agricultural business, including secured by farmland	—	—	—	—	228,291	228,291	105
One- to four-family residential [(1)]	521	2,550	9,142	12,213	517,281	529,494	2,611
Consumer:							
Consumer secured by one- to four-family	723	93	918	1,734	171,454	173,188	13
Consumer—other	384	99	131	614	121,220	121,834	131
Total	$6,366	$4,086	$11,558	$22,010	$3,396,435	$3,418,445	$2,860

(1) One- to four-family loans are not considered past due until they exceed 30 days and are not reflected herein. One- to four-family loans exactly 30 days past due at December 31, 2014 and 2013 were $8 million and $6 million, respectively.

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The following tables provide additional information on the allowance for loan losses and loan balances individually and collectively evaluated for impairment at or for the year ended December 31, 2014 (in thousands):

	For the Year Ended December 31, 2014								
	Commercial Real Estate	Multifamily Real Estate	Construction and Land	Commercial Business	Agricultural Business	One- to Four-Family Residential	Consumer	Unallocated	Total
Allowance for loan losses:									
Beginning balance	$16,759	$ 5,306	$ 17,640	$ 11,773	$ 2,841	$ 11,486	$1,335	$7,118	$74,258
Provision for loan losses	1,757	(724)	6,336	626	(417)	(5,772)	90	(1,896)	—
Recoveries	1,507	—	1,776	988	1,576	618	528	—	6,993
Charge-offs	(1,239)	(20)	(207)	(1,344)	(179)	(885)	(1,470)	—	(5,344)
Ending balance	$18,784	$ 4,562	$ 25,545	$ 12,043	$ 3,821	$ 5,447	$483	$5,222	$75,907

	December 31, 2014								
	Commercial Real Estate	Multifamily Real Estate	Construction and Land	Commercial Business	Agricultural Business	One- to Four-Family Residential	Consumer	Unallocated	Total
Allowance individually evaluated for impairment	$728	$ 86	$ 986	$ 82	$ —	$ 1,014	$70	$—	$2,966
Allowance collectively evaluated for impairment	18,056	4,476	24,559	11,961	3,821	4,433	413	5,222	72,941
Total allowance for loan losses	$18,784	$ 4,562	$ 25,545	$ 12,043	$ 3,821	$ 5,447	$483	$5,222	$75,907

	December 31, 2014								
	Commercial Real Estate	Multifamily Real Estate	Construction and Land	Commercial Business	Agricultural Business	One- to Four-Family Residential	Consumer	Unallocated	Total
Loan balances:									
Loans individually evaluated for impairment	$7,171	$786	$6,477	$739	$744	$ 17,848	$681	$—	$34,446
Loans collectively evaluated for impairment	1,396,554	166,738	404,529	723,225	237,755	522,046	348,527	—	3,799,374
Total loans	$1,403,725	$167,524	$411,006	$723,964	$238,499	$ 539,894	$349,208	$—	$3,833,820

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Explanation of Responses:

The following tables provide additional information on the allowance for loan losses and loan balances individually and collectively evaluated for impairment at or for the year ended December 31, 2013 (in thousands):

	For the Year Ended December 31, 2013								
	Commercial Real Estate	Multifamily Real Estate	Construction and Land	Commercial Business	Agricultural Business	One- to Four-Family Residential	Consumer	Unallocated	Total
Allowance for loan losses:									
Beginning balance	$ 15,322	$ 4,506	$ 14,991	$ 9,957	$ 2,295	$ 16,475	$ 1,348	$ 11,865	$ 76,759
Provision for loan losses	1,639	800	2,195	1,925	97	(2,995)	1,086	(4,747)	—
Recoveries	2,367	—	2,275	1,673	697	145	340	—	7,497
Charge-offs	(2,569)	—	(1,821)	(1,782)	(248)	(2,139)	(1,439)	—	(9,998)
Ending balance	$ 16,759	$ 5,306	$ 17,640	$ 11,773	$ 2,841	$ 11,486	$ 1,335	$ 7,118	$ 74,258

	December 31, 2013								
	Commercial Real Estate	Multifamily Real Estate	Construction and Land	Commercial Business	Agricultural Business	One- to Four-Family Residential	Consumer	Unallocated	Total
Allowance individually evaluated for impairment	$ 419	$ 1,139	$ 1,762	$ 222	$ —	$ 1,579	$ 67	$ —	$ 5,188
Allowance collectively evaluated for impairment	16,340	4,167	15,878	11,551	2,841	9,907	1,268	7,118	69,070
Total allowance for loan losses	$ 16,759	$ 5,306	$ 17,640	$ 11,773	$ 2,841	$ 11,486	$ 1,335	$ 7,118	$ 74,258

	December 31, 2013								
	Commercial Real Estate	Multifamily Real Estate	Construction and Land	Commercial Business	Agricultural Business	One- to Four-Family Residential	Consumer	Unallocated	Total
Loan balances:									
Loans individually evaluated for impairment	$ 10,877	$ 5,744	$ 12,118	$ 1,298	$ —	$ 29,834	$ 776	$ —	$ 60,647
Loans collectively evaluated for impairment	1,184,181	131,409	339,140	680,871	228,291	499,660	294,246	—	3,357,798
Total loans	$ 1,195,058	$ 137,153	$ 351,258	$ 682,169	$ 228,291	$ 529,494	$ 295,022	$ —	$ 3,418,445

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Note 7: REAL ESTATE OWNED, HELD FOR SALE, NET

The following table presents the changes in real estate owned (REO), net of valuation allowance, for the years ended December 31, 2014, 2013 and 2012 (in thousands):

	Years Ended December 31		
	2014	2013	2012
Balance, beginning of period	$4,044	$15,778	$42,965
Additions from loan foreclosures	3,264	3,166	13,930
Additions from capitalized costs	30	348	300
Proceeds from dispositions of REO	(4,923)	(16,944)	(40,965)
Gain on sale of REO	973	2,481	4,725
Valuation adjustments in the period	(36)	(785)	(5,177)
Balance, end of period	$3,352	$4,044	$15,778

The following table shows REO by type and geographic location by state as of December 31, 2014 (dollars in thousands):

	Washington	Oregon	Idaho	Total
Land development—residential	259	1,271	32	1,562
One- to four-family real estate	1,435	355	—	1,790
Total REO	$1,694	$1,626	$32	$3,352
Percent of total REO	50.5%	48.5%	1.0%	100.0%

Note 8: PROPERTY AND EQUIPMENT, NET

Land, buildings and equipment owned by the Company and its subsidiaries at December 31, 2014 and 2013 are summarized as follows (in thousands):

	December 31	
	2014	2013
Land	$21,969	$19,974
Buildings and leasehold improvements	98,901	99,351
Furniture and equipment	72,152	65,912
	193,022	185,237
Less accumulated depreciation	(101,837)	(94,970)
Property and equipment, net	$91,185	$90,267

The Company’s depreciation expense related to property and equipment was $8.1 million, $7.5 million, and $7.8 million for the years ended December 31, 2014, 2013 and 2012, respectively. The Company’s rental expense was $7.6 million, $7.3 million, and $7.1 million for the years ended December 31, 2014, 2013 and 2012, respectively.

The Company’s obligations under long-term property leases are as follows:

Year	Amount
2015	$ 7.6 million
2016	5.7 million
2017	4.7 million
2018	4.2 million
2019	3.4 million
Thereafter	9.6 million
Total	$ 35.2 million

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Note 9: DEPOSITS

Deposits consist of the following at December 31, 2014 and 2013 (dollars in thousands):

	December 31					
	2014			2013		
	Amount	Percent of Total		Amount	Percent of Total	
Non-interest-bearing checking	$1,298,866	33.3	%	$1,115,346	30.8	%
Interest-bearing checking	439,480	11.3		422,910	11.7	
Regular savings accounts	901,142	23.1		798,764	22.1	
Money market accounts	488,946	12.5		408,211	11.3	
Total transaction and savings accounts	3,128,434	80.2		2,745,231	75.9	
Certificates of deposit:						
Up to 1.00%	643,065	16.5		723,891	20.0	
1.01% to 2.00%	87,661	2.3		95,663	2.6	
2.01% to 3.00%	32,184	0.8		43,062	1.2	
3.01% to 4.00%	3,024	0.1		6,663	0.2	
4.01% and greater	4,582	0.1		3,416	0.1	
Total certificates of deposit	770,516	19.8		872,695	24.1	
Total deposits	$3,898,950	100.0	%	$3,617,926	100.0	%
Included in total deposits:						
Public fund transaction accounts	$102,854	2.6	%	$87,521	2.4	%
Public fund interest-bearing certificates	35,346	0.9		51,465	1.4	
Total public deposits	$138,200	3.5	%	$138,986	3.8	%
Total brokered deposits	$4,799	0.1	%	$4,291	0.1	%

Deposits at December 31, 2014 and 2013 included deposits from the Company’s directors, executive officers and related entities totaling $6.2 million and $6.7 million, respectively.

Certificate of deposit accounts by total balance at December 31, 2014 and 2013 were as follows (in thousands):

	December 31	
	2014	2013
Certificates of deposit less than $100,000	$358,189	$386,745
Certificates of deposit $100,000 through $250,000	275,156	308,130
Certificates of deposit more than $250,000	137,171	177,820
Total certificates of deposit	$770,516	$872,695

Certificates of deposit of $250,000 and greater totaled $141 million and $184 million at December 31, 2014 and 2013, respectively.

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Scheduled maturities and weighted average interest rates of certificate accounts at December 31, 2014 and 2013 are as follows (dollars in thousands):

	December 31			
	2014		2013	
	Amount	Weighted Average Rate	Amount	Weighted Average Rate
Maturing in one year or less	$564,501	0.46 %	$660,394	0.47 %
Maturing after one year through two years	117,724	0.89	117,789	1.05
Maturing after two years through three years	46,378	1.19	47,362	1.34
Maturing after three years through four years	20,016	1.42	26,443	1.56
Maturing after four years through five years	17,338	1.22	17,075	1.34
Maturing after five years	4,559	2.09	3,632	1.78
Total certificates of deposit	$770,516	1.06 %	$872,695	0.65 %

The following table sets forth the deposit activities for the years ended December 31, 2014, 2013 and 2012 (in thousands):

	Years Ended December 31		
	2014	2013	2012
Balance at beginning of year	$3,617,926	$3,557,804	$3,475,654
Net increase before interest credited	273,446	50,385	67,043
Interest credited	7,578	9,737	15,107
Net increase in deposits	281,024	60,122	82,150
Balance at end of year	$3,898,950	$3,617,926	$3,557,804

Deposit interest expense by type for the years ended December 31, 2014, 2013 and 2012 was as follows (in thousands):

	Years Ended December 31		
	2014	2013	2012
Certificates of deposit [1]	$5,145	$6,836	$11,458
Demand, interest-bearing checking and money market accounts	1,123	1,329	1,824
Regular savings	1,310	1,572	1,825
	$7,578	$9,737	$15,107

(1) Interest expense on certificate of deposit accounts with balances of $100,000 or more totaled $3.1 million, $4.0 million, and $6.7 million for the years ended December 31, 2014, 2013 and 2012, respectively.

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Note 10: ADVANCES FROM FEDERAL HOME LOAN BANK OF SEATTLE

Utilizing a blanket pledge, qualifying loans receivable at December 31, 2014 and 2013, were pledged as security for FHLB borrowings and there were no securities pledged as collateral as of December 31, 2014 or 2013. At December 31, 2014 and 2013, FHLB advances were scheduled to mature as follows (dollars in thousands):

	December 31					
	2014			2013		
	Amount	Weighted Average Rate		Amount	Weighted Average Rate	
Maturing in one year or less	$32,000	0.27	%	$27,000	0.23	%
Maturing after one year through three years	—	—		—	—	
Maturing after three years through five years	—	—		—	—	
Maturing after five years	196	5.94		203	5.94	
Total FHLB advances, at par	32,196	0.27		27,203	0.27	
Fair value adjustment	54			47		
Total FHLB advances, carried at fair value	$32,250			$27,250		

The maximum, average outstanding and year-end balances (excluding fair value adjustments) and average interest rates on advances from the FHLB were as follows at or for the years ended December 31, 2014, 2013 and 2012 (dollars in thousands):

	At or For the Years Ended December 31					
	2014		2013		2012	
Maximum outstanding at any month end, at par	$105,450		$60,377		$10,216	
Average outstanding, at par	39,121		18,935		10,215	
Year-end outstanding, at par	32,196		27,203		10,210	
Weighted average interest rates:						
Annual	0.32	%	0.52	%	2.49	%
End of period	0.27	%	0.27	%	2.45	%
Interest expense during the period	$125		$99		$254	

As of December 31, 2014, Banner Bank has established a borrowing line with the FHLB to borrow up to 35% of its total assets, contingent on having sufficient qualifying collateral and ownership of FHLB stock. Islanders Bank has a similar line of credit, although it may borrow up to 25% of its total assets, also contingent on collateral and FHLB stock. At December 31, 2014, the maximum total FHLB credit line was $901 million and $23 million for Banner Bank and Islanders Bank, respectively.

Note 11: OTHER BORROWINGS

Other borrowings consist of retail repurchase agreements, other term borrowings and Federal Reserve Bank borrowings.

Retail Repurchase Agreements: At December 31, 2014, retail repurchase agreements carry interest rates ranging from 0.15% to 0.40%, and are secured by the pledge of certain mortgage-backed and agency securities with a carrying value of $99 million. Banner Bank has the right to pledge or sell these securities, but they must replace them with substantially the same security.

Federal Reserve Bank of San Francisco and Other Borrowings: Banner Bank periodically borrows funds on an overnight basis from the Federal Reserve Bank through the Borrower-In-Custody (BIC) program. Such borrowings are secured by a pledge of eligible loans. At December 31, 2014, based upon available unencumbered collateral,

Banner Bank was eligible to borrow $639 million from the Federal Reserve Bank, although, at that date, as well as at December 31, 2013, the Bank had no funds borrowed under this or other borrowing arrangements.

There were no wholesale repurchase agreements, other short-term borrowings, or any Fed Funds, outstanding as of December 31, 2014 and 2013.

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A summary of all other borrowings at December 31, 2014 and 2013 by the period remaining to maturity is as follows (dollars in thousands):

	At or for the Years Ended December 31					
	2014			2013		
	Amount	Weighted Average Rate		Amount	Weighted Average Rate	
Retail repurchase agreements:						
Maturing in one year or less	$77,185	0.20	%	$83,056	0.20	%
Maturing after one year through two years	—	—		—	—	
Maturing after two years	—	—		—	—	
Total year-end outstanding	$77,185	0.20		$83,056	0.20	
Average outstanding	$83,965	0.20		$84,877	0.23	
Maximum outstanding at any month-end	89,921	n/a		91,964	n/a	

The table below summarizes interest expense for other borrowings for the years ended December 31, 2014, 2013 and 2012 (in thousands):

	Years Ended December 31		
	2014	2013	2012
Retail repurchase agreements	$172	$192	$281
FDIC guaranteed debt	—	—	477
Total expense	$172	$192	$758

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NOTE 12: JUNIOR SUBORDINATED DEBENTURES AND MANDATORILY REDEEMABLE TRUST PREFERRED SECURITIES

At December 31, 2014, six wholly-owned subsidiary grantor trusts, Banner Capital Trust II, III, IV, V, VI and VII (BCT II, BCT III, BCT IV, BCT V, BCT VI and BCT VII (collectively, the Trusts)), established by the Company had issued $120 million of trust preferred securities to third parties, as well as $3.7 million of common capital securities, carried among other assets, which were issued to the Company. Trust preferred securities and common capital securities accrue and pay distributions periodically at specified annual rates as provided in the indentures. The Trusts used the proceeds from the offerings to purchase a like amount of junior subordinated debentures (the Debentures) of the Company. The Debentures are the sole assets of the Trusts. The Company's obligations under the debentures and related documents, taken together, constitute a full and unconditional guarantee by the Company of the obligations of the Trusts. The trust preferred securities are mandatorily redeemable upon the maturity of the Debentures, or upon earlier redemption as provided in the indentures. The Company has the right to redeem the Debentures in whole on or after specific dates, at a redemption price specified in the indentures plus any accrued but unpaid interest to the redemption date. All of the trust preferred securities issued by the Trusts qualified as Tier 1 capital as of December 31, 2014, under guidance issued by the Board of Governors of the Federal Reserve System. At December 31, 2014, the Trusts comprised $74.3 million, or 11.8% of the Company's total risk-based capital.

The following table is a summary of trust preferred securities at December 31, 2014 (dollars in thousands):

Name of Trust	Aggregate Liquidation Amount of Trust Preferred Securities	Aggregate Liquidation Amount of Common Capital Securities	Aggregate Principal Amount of Junior Subordinated Debentures	Stated Maturity	Current Interest Rate	Reset Period	Interest Rate Spread	Interest Deferral Period	Redemption Option
Banner Capital Trust II	$ 15,000	$ 464	$ 15,464	2033	3.58 %	Quarterly	Three-month LIBOR + 3.35%	20 Consecutive Quarters	On or after January 7, 2008
Banner Capital Trust III	15,000	465	15,465	2033	3.13	Quarterly	Three-month LIBOR + 2.90%	20 Consecutive Quarters	On or after October 8, 2008
Banner Capital Trust IV	15,000	465	15,465	2034	3.08	Quarterly	Three-month LIBOR + 2.85%	20 Consecutive Quarters	On or after April 7, 2009
Banner Capital Trust V	25,000	774	25,774	2035	1.80	Quarterly	Three-month LIBOR + 1.57%	20 Consecutive Quarters	On or after November 23, 2010
Banner Capital Trust VI	25,000	774	25,774	2037	1.86	Quarterly	Three-month LIBOR + 1.62%	20 Consecutive Quarters	On or after March 1, 2012
Banner Capital Trust VII	25,000	774	25,774	2037	1.62	Quarterly	Three-month LIBOR + 1.38%	20 Consecutive Quarters	On or after July 31, 2012
Total TPS liability at par	$ 120,000	$ 3,716	123,716		2.32 %				
Fair value adjustment			(45,715)						

Total TPS liability at fair value	$ 78,001

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Note 13: INCOME TAXES

The following table presents the components of the provision for income tax (benefit) expense included in the Consolidated Statement of Operations for the years ended December 31, 2014, 2013 and 2012 (in thousands):

	Years Ended December 31		
	2014	2013	2012
Current	$24,855	$12,121	$10,759
Deferred	1,365	10,407	841
Increase (decrease) in valuation allowance	—	—	(36,385)
Provision for (benefit from) income taxes	$26,220	$22,528	$(24,785)

The following tables present the reconciliation of the provision for income taxes computed at the federal statutory rate to the actual effective rate for the years ended December 31, 2014, 2013 and 2012 (dollars in thousands):

	Years Ended December 31		
	2014	2013	2012
Provision for (benefit from) income taxes computed at federal statutory rate	$28,134	$24,179	$14,034
Increase (decrease) in taxes due to:			
Tax-exempt interest	(2,084)	(1,633)	(1,710)
Investment in life insurance	(626)	(707)	(894)
State income taxes (benefit), net of federal tax offset	916	824	539
Tax credits	(661)	(636)	(788)
Valuation allowance	—	—	(36,385)
Other	541	501	419
Provision for (benefit from) income taxes	$26,220	$22,528	$(24,785)

	Years Ended December 31		
	2014	2013	2012
Federal income tax statutory rate	35.0 %	35.0 %	35.0 %
Increase (decrease) in tax rate due to:			
Tax-exempt interest	(2.6)	(2.4)	(4.3)
Investment in life insurance	(0.8)	(1.0)	(2.2)
State income taxes (benefit), net of federal tax offset	1.1	1.2	1.3
Tax credits	(0.8)	(0.9)	(2.0)
Valuation allowance	—	—	(90.7)
Other	0.7	0.7	1.1
Effective income tax rate	32.6 %	32.6 %	(61.8)%

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The following table reflects the effect of temporary differences that gave rise to the components of the net deferred tax asset as of December 31, 2014 and 2013 (in thousands):

	December 31	
	2014	2013
Deferred tax assets:		
REO and loan loss reserves	$26,536	$17,326
Deferred compensation	9,223	7,305
Net operating loss carryforward	17,577	27,639
Low income housing tax credits	3,676	3,676
State net operating losses	1,009	957
Other	1,344	1,235
Total deferred tax assets	59,365	58,138
Deferred tax liabilities:		
FHLB stock dividends	(4,805)	(5,875)
Depreciation	(4,479)	(4,074)
Deferred loan fees, servicing rights and loan origination costs	(7,843)	(6,444)
Intangibles	(975)	(833)
Financial instruments accounted for under fair value accounting	(15,611)	(15,118)
Loan discount	(1,190)	—
Total deferred tax liabilities	(34,903)	(32,344)
Deferred income tax asset	24,462	25,794
Unrealized loss on securities—available-for-sale	145	1,685
Deferred tax asset, net	$24,607	$27,479

At December 31, 2014, the Company has federal and state net operating loss carryforwards of approximately $50.2 million and $21.2 million, respectively, which will expire, if unused, by the end of 2033. The Company has federal general business credit carryforwards of $2.7 million, which will expire, if unused, by the end of 2031. The Company also has alternative minimum tax credit carryforwards of approximately $900,000, which are available to reduce future federal regular income taxes, if any, over an indefinite period. At December 31, 2013, the Company had federal and state net operating loss carryforwards of approximately $79.0 million and $20.4 million, respectively, and federal general business credits carryforwards of $2.7 million. The Company also had alternative minimum tax credit carryforwards of approximately $900,000.

As a consequence of our capital raise in June 2010, the Company experienced a change in control within the meaning of Section 382 of the Internal Revenue Code of 1986, as amended. Section 382 limits the ability of a corporate taxpayer to use net operating loss carryforwards, general business credit, and recognized built-in-losses incurred prior to the change in control against income earned after the change in control. As a result of the Section 382 limitation, the Company expects it will be able to utilize approximately $6.9 million of net operating loss carryforwards on an annual basis. Based on its analysis, the Company does not believe the change in control will impact its ability to utilize all of the available net operating loss carryforwards, general business credit, and recognized built-in-losses.

Retained earnings (accumulated deficits) at December 31, 2014 and 2013 include approximately $5.4 million in tax basis bad debt reserves for which no income tax liability has been booked. In the future, if this tax bad debt reserve is used for purposes other than to absorb bad debts or the Company no longer qualifies as a bank or is completely liquidated, the Company will incur a federal tax liability at the then-prevailing corporate tax rate, established as $1.9 million at December 31, 2014.

As of December 31, 2014, the Company had reduced its previous year's tax receivable by $9.8 million as a result of the approval of a closing agreement with the IRS related to amended 2006, 2008 and 2009 federal income tax returns.

Review of the amended federal returns was completed by the Internal Revenue Service (IRS) in 2013 and the Company signed a closing agreement with the IRS related to refund claims of $9.8 million, which was received in 2014.

Note 14: EMPLOYEE BENEFIT PLANS

Employee Retirement Plans: Substantially all of the Company's employees are eligible to participate in its 401(k)/Profit Sharing Plan, a defined contribution and profit sharing plan sponsored by the Company. Employees may elect to have a portion of their salary contributed to the plan in conformity with Section 401(k) of the Internal Revenue Code. At the discretion of the Company's Board of Directors, the Company may elect to make matching and/or profit sharing contributions for the employees' benefit. For the years ended December 31, 2014, 2013 and 2012, $1.4 million, $1.0 million and, $43,000 respectively, was expensed for 401(k) contributions. The Board of Directors has elected to make a 4% of eligible compensation matching contribution for 2015.

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Supplemental Retirement and Salary Continuation Plans: Through the Banks, the Company is obligated under various non-qualified deferred compensation plans to help supplement the retirement income of certain executives, including certain retired executives, selected by resolution of the Banks' Boards of Directors or in certain cases by the former directors of acquired banks. These plans are unfunded, include both defined benefit and defined contribution plans, and provide for payments after the executive's retirement. In the event of a participant employee's death prior to or during retirement, the Bank is obligated to pay to the designated beneficiary the benefits set forth under the plan. For the years ended December 31, 2014, 2013 and 2012, expense recorded for supplemental retirement and salary continuation plan benefits totaled $1.2 million, $1.5 million, and $879,000, respectively. At December 31, 2014 and 2013, liabilities recorded for the various supplemental retirement and salary continuation plan benefits totaled $14.2 million and $13.6 million, respectively, and are recorded in a deferred compensation liability account.

Deferred Compensation Plans and Rabbi Trusts: The Company and the Banks also offer non-qualified deferred compensation plans to members of their Boards of Directors and certain employees. The plans permit each participant to defer a portion of director fees, non-qualified retirement contributions, salary or bonuses for future receipt. Compensation is charged to expense in the period earned. In connection with its acquisitions, the Company also assumed liability for certain deferred compensation plans for key employees, retired employees and directors.

In order to fund the plans' future obligations, the Company has purchased life insurance policies or other investments, including Banner Corporation common stock, which in certain instances are held in irrevocable trusts commonly referred to as "Rabbi Trusts." As the Company is the owner of the investments and the beneficiary of the insurance policies, and in order to reflect the Company's policy to pay benefits equal to the accumulations, the assets and liabilities are reflected in the Consolidated Statements of Financial Condition. Banner Corporation common stock held for such plans is reported as a contra-equity account and was recorded at an original cost of $6.7 million at December 31, 2014 and $7.1 million at December 31, 2013. At December 31, 2014 and 2013, liabilities recorded in connection with deferred compensation plan benefits totaled $8.2 million ($6.7 million in contra-equity) and $8.5 million ($7.1 million in contra-equity), respectively, and are recorded in deferred compensation or equity as appropriate.

The Banks have purchased, or acquired through mergers, life insurance policies in connection with the implementation of certain executive supplemental retirement, salary continuation and deferred compensation retirement plans, as well as additional policies not related to any specific plan. These policies provide protection against the adverse financial effects that could result from the death of a key employee and provide tax-exempt income to offset expenses associated with the plans. It is the Banks' intent to hold these policies as a long-term investment. However, there will be an income tax impact if the Banks choose to surrender certain policies. Although the lives of individual current or former management-level employees are insured, the Banks are the owners and sole or partial beneficiaries. At December 31, 2014 and 2013, the cash surrender value of these policies was $63.8 million and $61.9 million, respectively. The Banks are exposed to credit risk to the extent an insurance company is unable to fulfill its financial obligations under a policy. In order to mitigate this risk, the Banks use a variety of insurance companies and regularly monitor their financial condition.

Note 15: EMPLOYEE STOCK OWNERSHIP PLAN AND TRUST

In 1995, the Company established an ESOP and related trust for eligible employees of Banner Bank as of January 1, 1995 and eligible employees of the Banks or Company employed after such date. The ESOP borrowed $8.7 million from the Company in order to purchase the common stock. The loan was repaid principally from the Company's contributions to the ESOP. Shares were released to participants for allocation based on the cumulative debt service paid to the Company by the ESOP divided by cumulative debt service paid to date plus the scheduled debt service remaining. No ESOP contributions were made for the years ended December 31, 2014, 2013 or 2012 and no payments were made on the loan in those years. On December 17, 2013, the Company's Board of Directors elected to

terminate the ESOP effective January 1, 2014. The allocated shares held by the ESOP were distributed to the participants of the plan during 2014. The unallocated shares held by the ESOP were forfeited and redeemed and the outstanding balance of the loan was canceled. Termination of the ESOP had no impact on the net equity position of the Company or its current and future operating results.

Note 16: STOCK-BASED COMPENSATION PLANS

The Company operates the following stock-based compensation plans as approved by the shareholders: the 1996 Stock Option Plan, the 1998 Stock Option Plan and 2001 Stock Option Plan (collectively, SOPs), the 2012 Restricted Stock and Incentive Bonus Plan, and the 2014 Omnibus Incentive Plan. In addition, the Board approved in 2006 the Banner Corporation Long-Term Incentive Plan. The purpose of these plans is to promote the success and enhance the value of the Company by providing a means for attracting and retaining highly skilled employees, officers and directors of Banner Corporation and its affiliates and linking their personal interests with those of the Company's shareholders. Under these plans the Company currently has outstanding restricted stock grants, stock options and stock appreciation rights.

Restricted Stock Grants: Under the 2012 Restricted Stock and Incentive Bonus Plan, which was initially approved on April 24, 2012, the Company is authorized to issue up to 300,000 shares of its common stock to provide a means for attracting and retaining highly skilled officers of Banner Corporation and its affiliates. Shares granted under the Plan have a minimum vesting period of three years. The Plan will continue in effect for a term of ten years, after which no further awards may be granted. The 2012 Restricted Stock and Incentive Bonus Plan was amended on April 23, 2013 to provide for the ability to grant (1) cash-denominated incentive-based awards payable in cash or common stock, including those that are eligible to qualify as qualified performance-based compensation for the purposes of Section 162(m) of the IRS Code and (2) restricted stock awards that qualify as qualified performance-based compensation for the purposes of Section 162(m) of the IRS Code. Vesting requirements may include time-based conditions, performance-based conditions, or market-based conditions. As of December 31, 2014, the Company had granted 266,778 shares of restricted stock, net of forfeitures, from the 2012 Restricted Stock and Incentive Bonus Plan, of which 81,241 shares had vested and 185,537 shares remain unvested.

Banner Corporation 2014 Omnibus Incentive Plan: The 2014 Plan was approved by shareholders on April 22, 2014. The 2014 Plan provides for the grant of incentive stock options, non-qualified stock options, stock appreciation rights, restricted stock, restricted stock units, performance shares, performance units, other stock-based awards and other cash awards, and provides for vesting requirements which may include time-based or performance-based conditions. The Company has reserved 900,000 shares of its common stock for issuance under the 2014 Plan in connection with exercise of awards. As of December 31, 2014, 9,352 shares had been granted to directors under the 2014 Omnibus Incentive Plan.

The expense associated with all restricted stock grants was $2.7 million, $1.5 million and $434,000, respectively, for the years ended December 31, 2014, 2013 and 2012. Unrecognized compensation expense for these awards as of December 31, 2014 was $3.9 million and will be amortized over the next 30 months.

A summary of the Company's Restricted Stock award activity during the years ended December 31, 2012, 2013 and 2014 follows:

	Shares	Weighted Average Grant-Date Fair Value
Unvested at December 31, 2011	28,735	$14.50
Granted	92,035	21.77
Vested	(11,419)	14.60
Forfeited	(1,500)	21.94
Unvested at December 31, 2012	107,851	20.59
Granted	98,891	30.81
Vested	(42,250)	19.85
Forfeited	—	—
Unvested at December 31, 2013	164,492	26.94
Granted	90,181	40.07
Vested	(56,307)	24.81
Forfeited	(3,260)	31.00
Unvested at December 31, 2014	195,106	32.83

Stock Options: Under the SOPs, Banner reserved 2,284,186 shares for issuance pursuant to the exercise of stock options to be granted to directors and employees. Authority to grant additional options under the 1998 Stock Option Plan terminated on July 24, 2008 with all options having been granted. Authority to grant additional options under the 2001 Stock Option Plan terminated on April 20, 2011. The exercise price of the stock options is set at 100% of the fair market value of the stock price on the date of grant. Options granted vest at a rate of 20% per year from the date of grant and any unexercised incentive stock options will expire ten years after date of grant or 90 days after employment or service ends.

During the years ended December 31, 2014, 2013 and 2012, the Company did not grant any stock options. Additionally, there were no significant modifications made to any stock option grants during the period. The fair values of stock options granted are amortized as compensation expense on a straight-line basis over the vesting period of the grant.

For the years ended December 31, 2014 and 2013, there were no stock option compensation expenses recorded. For the year ended December 31, 2012, stock-based compensation costs related to the SOPs was $7,000. The SOPs' stock option grant compensation costs are generally based on the fair value calculated from the Black-Scholes option pricing on the date of the grant award. The Black-Scholes model assumes an expected stock price volatility based on

the historical volatility at the date of the grant and an expected term based on the remaining contractual life of the vesting period. The Company bases the estimate of risk-free interest rate on the Treasury's Constant Maturities Indices in effect at the time of the grant. The dividend yield is based on the current quarterly dividend in effect at the time of the grant.

The Company is required to estimate potential forfeitures of stock option grants and adjust compensation cost recorded accordingly. The estimate of forfeitures is adjusted over the requisite service period to the extent that actual forfeitures differ, or are expected to differ, from such estimates. Changes in estimated forfeitures are recognized through a cumulative catch-up adjustment in the period of change and also impact the amount of stock compensation expense to be recognized in future periods.

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A summary of the Company's stock option award activity for the years ended December 31, 2012, 2013 and 2014 follows:

	Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term, In Years	Aggregate Intrinsic Value
Outstanding at December 31, 2011	51,729	$168.98	2.40	n/a
Granted	—	—		
Exercised	—	—		
Forfeited	(9,208)	145.97		
Outstanding at December 31, 2012	42,521	173.98	1.75	n/a
Granted	—	—		
Exercised	—	—		
Forfeited	(16,157)	121.29		
Outstanding at December 31, 2013	26,364	206.27	1.58	n/a
Granted	—	—		
Exercised	—	—		
Forfeited	(15,700)	206.44		
Outstanding at December 31, 2014	10,664	206.03	1.90	n/a
Outstanding at December 31, 2014, net of expected forfeitures	—	—	n/a	n/a
Exercisable at December 31, 2014	10,664	206.03	1.90	

The intrinsic value of stock options is calculated as the amount by which the market price of Banner's common stock exceeds the exercise price at the time of exercise or the end of the period as applicable.

At December 31, 2014, financial data pertaining to outstanding stock options was as follows:

Exercise Price	Weighted Average Exercise Price of Option Shares Granted	Number of Option Shares Granted	Weighted Average Option Shares Vested and Exercisable	Weighted Average Exercise Price of Option Shares Exercisable	Remaining Contractual Life
$0.00 to $184.00	$176.72	2,593	2,593	$176.72	0.1 years
$184.01 to $220.00	212.96	8,071	8,071	212.96	1.8 years
	206.44	10,664	10,664	206.27	

During the year ended December 31, 2014, there were no exercises of stock options. Cash was not used to settle any equity instruments previously granted. The Company issues shares from authorized but unissued shares upon the exercise of stock options. The Company does not currently expect to repurchase shares from any source to satisfy such obligations under the SOPs.

The following are the stock-option compensation costs recognized in the Company's consolidated statements of operations for the years ended December 31, 2014, 2013 and 2012 (in thousands):

	Years Ended December 31		
	2014	2013	2012
Salary and employee benefits	$—	$—	$11
Decrease in provision for income taxes	—	—	(4)
Decrease in equity, net	$—	$—	$7

Banner Corporation Long-Term Incentive Plan: In June 2006, the Board of Directors adopted the Banner Corporation Long-Term Incentive Plan effective July 1, 2006. The Plan is an account-based type of benefit, the value of which is directly related to changes in the value of Company common stock, dividends declared on Company common stock and changes in Banner Bank's average earnings rate, and is considered a stock appreciation right (SAR). Each SAR entitles the holder to receive cash, upon vesting, equal to the excess of the fair market value of a share of

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the Company's common stock on the date of maturity of the SAR over the fair market value of such share on the date granted plus, for some grants, the dividends declared on the stock from the date of grant to the date of vesting. The primary objective of the Plan is to create a retention incentive by allowing officers who remain with the Company or the Banks for a sufficient period of time to share in the increases in the value of Company stock. The Company re-measures the fair value of SARs each reporting period until the award is settled and recognizes changes in fair value and vesting in compensation expense. The Company recognized compensation expense of $89,000, $1.0 million, and $314,000, respectively, for the years ended December 31, 2014, 2013 and 2012 related to the increase in the fair value of SARs and additional vesting during the period. At December 31, 2014, the aggregate liability related to SARs was $1.1 million and is included in deferred compensation.

Note 17: PREFERRED STOCK AND RELATED WARRANT

On November 21, 2008, as part of the Capital Purchase Program established by the U.S. Treasury under the Emergency Economic Stabilization Act of 2008 (the EESA), the Company entered into a Purchase Agreement with Treasury pursuant to which the Company issued and sold to Treasury 124,000 shares of Series A Preferred Stock, having a liquidation preference of $1,000 per share ($124 million liquidation preference in the aggregate), and as more fully explained below, a ten-year warrant to purchase up to 243,998 shares (post reverse-split) of the Company's common stock, par value $0.01 per share, at an initial exercise price of $76.23 per share (post reverse-split), for an aggregate purchase price of $18.6 million in cash. The warrant issued is immediately exercisable, in whole or in part, has a ten-year term and the number of shares is subject to certain customary anti-dilution and other adjustments. The warrant is not subject to any contractual restrictions on transfer. The Company has granted the warrant holder piggyback registration rights for the warrant and the common stock underlying the warrant and has agreed to take such other steps as may be reasonably requested to facilitate the transfer of the warrant and the common stock underlying the warrant. The holder of the warrant is not entitled to any common stockholder rights.

On March 29, 2012, the Company's $124 million of Series A Preferred Stock was sold by the Treasury as part of its efforts to manage and recover its investments under the Troubled Assets Relief Program (TARP). While the sale of these preferred shares to new owners did not result in any proceeds to the Company and did not change the Company's capital position or accounting for these securities, it did eliminate restrictions put in place by the Treasury on TARP recipients. During the year ended December 31, 2012, the Company repurchased or redeemed its Series A Preferred Stock. The related warrants to purchase up to $18.6 million in Banner common stock (243,998 shares) were sold by the Treasury at public auction in June 2013. That sale did not change the Company's capital position and did not have any impact on the financial accounting and reporting for these securities.

Note 18: REGULATORY CAPITAL REQUIREMENTS

Banner Corporation is a bank holding company registered with the Federal Reserve. Bank holding companies are subject to capital adequacy requirements of the Federal Reserve under the Bank Holding Company Act of 1956, as amended (BHCA), and the regulations of the Federal Reserve. Banner Bank and Islanders Bank, as state-chartered federally insured commercial banks, are subject to the capital requirements established by the FDIC. The Federal Reserve requires Banner to maintain capital adequacy that generally parallels the FDIC requirements.

Federal statutes establish a supervisory framework 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, which include a risk-based capital measure, a leverage ratio capital measure and certain other factors. The federal banking agencies have adopted regulations that implement this statutory framework. Under these regulations, an institution is treated as well capitalized if its ratio of total capital to risk-weighted assets is 10% or more, its ratio of core capital to risk-weighted assets is 6% or more, its ratio of core capital to adjusted total assets (leverage ratio) is 5% or more, and it is not subject

to any federal supervisory order or directive to meet a specific capital level. In order to be adequately capitalized, an institution must have a total risk-based capital ratio of not less than 8%, a core capital to risk-weighted assets ratio of not less than 4%, and a leverage ratio of not less than 4%. 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 their respective 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.

FDIC regulations recognize two types, or tiers, of capital: core (Tier 1) capital and supplementary (Tier 2) capital. Tier 1 capital generally includes common stockholders' equity and qualifying noncumulative perpetual preferred stock, less most intangible assets. Tier 2 capital, which is recognized up to 100% of Tier 1 capital for risk-based capital purposes (after any deductions for disallowed intangibles and disallowed deferred tax assets), includes such items as qualifying general loan loss reserves (up to 1.25% of risk-weighted assets), cumulative perpetual preferred stock, long-term preferred stock, certain perpetual preferred stock, hybrid capital instruments including mandatory convertible debt, term subordinated debt, intermediate-term preferred stock (original average maturity of at least five years), and net unrealized holding gains on equity securities (subject to certain limitations); provided, however, the amount of term subordinated debt and intermediate term preferred stock that may be included in Tier 2 capital for risk-based capital purposes is limited to 50% of Tier 1 capital.

The FDIC currently measures an institution's capital using a leverage limit together with certain risk-based ratios. The FDIC's minimum leverage capital requirement specifies a minimum ratio of Tier 1 capital to average total assets. Most banks are required to maintain a minimum leverage

ratio of at least 3% to 4% of total assets. The FDIC retains the right to require a particular institution to maintain a higher capital level based on an institution's particular risk profile.

FDIC regulations also establish a measure of capital adequacy based on ratios of qualifying capital to risk-weighted assets. Assets are placed in one of four categories and given a percentage weight—0%, 20%, 50% or 100%—based on the relative risk of the category. In addition, certain off-balance-sheet items are converted to balance-sheet credit equivalent amounts, and each amount is then assigned to one of the four categories. Under the guidelines, the ratio of total capital (Tier 1 capital plus Tier 2 capital) to risk-weighted assets must be at least 8%, and the ratio of Tier 1 capital to risk-weighted assets must be at least 4%. In evaluating the adequacy of a bank's capital, the FDIC may also consider other factors that may affect the bank's financial condition. Such factors may include interest rate risk exposure, liquidity, funding and market risks, the quality and level of earnings, concentration of credit risk, risks arising from nontraditional activities, loan and investment quality, the effectiveness of loan and investment policies, and management's ability to monitor and control financial operating risks.

FDIC capital requirements are designated as the minimum acceptable standards for banks whose overall financial condition is fundamentally sound, which are well-managed and have no material or significant financial weaknesses. The FDIC capital regulations state that, where the FDIC determines that the financial history or condition, including off-balance-sheet risk, managerial resources and/or the future earnings prospects of a bank are not adequate and/or a bank has a significant volume of assets classified substandard, doubtful or loss or otherwise criticized, the FDIC may determine that the minimum adequate amount of capital for the bank is greater than the minimum standards established in the regulation.

The following table shows the regulatory capital ratios of the Company and the Banks and the minimum regulatory requirements (dollars in thousands):

	Actual			Minimum for Capital Adequacy Purposes			Minimum to be Categorized as "Well-Capitalized" Under Prompt Corrective Action Provisions		
	Amount	Ratio		Amount	Ratio		Amount	Ratio	
December 31, 2014:									
The Company—consolidated:									
Total capital to risk-weighted assets	$684,583	16.80	%	$326,071	8.00	%	n/a	n/a	
Tier 1 capital to risk-weighted assets	633,317	15.54		163,036	4.00		n/a	n/a	
Tier 1 leverage capital to average assets	633,317	13.41		188,885	4.00		n/a	n/a	
Banner Bank:									
Total capital to risk- weighted assets	605,997	15.53		312,220	8.00		$390,274	10.00	%
Tier 1 capital to risk- weighted assets	556,897	14.27		156,110	4.00		234,165	6.00	
Tier 1 leverage capital to average assets	556,897	12.42		179,304	4.00		224,130	5.00	
Islanders Bank:									
Total capital to risk- weighted assets	36,590	19.92		14,693	8.00		18,367	10.00	
Tier 1 capital to risk- weighted assets	34,332	18.69		7,347	4.00		11,020	6.00	
Tier 1 leverage capital to average assets	34,332	13.68		10,040	4.00		12,550	5.00	
December 31, 2013:									
The Company—consolidated:									
Total capital to risk-weighted assets	$631,674	16.99	%	$297,493	8.00	%	n/a	n/a	

Tier 1 capital to risk-weighted assets	584,838	15.73	148,747	4.00	n/a	n/a	
Tier 1 leverage capital to average assets	584,838	13.64	171,553	4.00	n/a	n/a	
Banner Bank:							
Total capital to risk- weighted assets	557,253	15.75	282,984	8.00	$353,730	10.00	%
Tier 1 capital to risk- weighted assets	512,689	14.49	141,192	4.00	212,238	6.00	
Tier 1 leverage capital to average assets	512,689	12.65	162,174	4.00	202,707	5.00	
Islanders Bank:							
Total capital to risk- weighted assets	34,795	18.73	14,859	8.00	18,574	10.00	
Tier 1 capital to risk- weighted assets	32,469	17.48	7,430	4.00	11,144	6.00	
Tier 1 leverage capital to average assets	32,469	13.60	9,553	4.00	11,941	5.00	

At December 31, 2014, Banner Corporation and the Banks each exceeded all regulatory capital adequacy requirements. There have been no conditions or events since December 31, 2014 that have materially adversely changed the Tier 1 or Tier 2 capital of the Company or the Banks. However, events beyond the control of the Banks, such as weak or depressed economic conditions in areas where the Banks have most

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of their loans, could adversely affect future earnings and, consequently, the ability of the Banks to meet their respective capital requirements. The Company may not declare or pay cash dividends on, or repurchase, any of its shares of common stock if the effect thereof would cause equity to be reduced below applicable regulatory capital maintenance requirements or if such declaration and payment would otherwise violate regulatory requirements.

On July 2, 2013, the Federal Reserve approved a final rule (Final Rule) to establish a new comprehensive regulatory capital framework for all U.S. financial institutions and their holding companies. On July 9, 2013, the Final Rule was approved as an interim final rule by the FDIC. The Final Rule implements the "Basel III" regulatory capital reforms and changes required by the Dodd-Frank Act. The final rule includes new risk-based capital and leverage ratios, which are effective January 1, 2015 and revise the definition of what constitutes "capital" for purposes of calculating those ratios.

Effective January 1, 2015 (with some changes transitioned into full effectiveness over two to four years), Banner and the Banks became subject to the new capital requirements adopted by the Federal Reserve and the FDIC. These new requirements create a new required ratio for common equity Tier 1 ("CET1") capital, increase the leverage and Tier 1 capital ratios, change the risk-weights of certain assets for purposes of the risk-based capital ratios, create an additional capital conservation buffer over the required capital ratios and change what qualifies as capital for purposes of meeting these various capital requirements. Beginning in 2016, failure to maintain the required capital conservation buffer will limit our ability and the ability of our bank subsidiary to pay dividends, repurchase shares or pay discretionary bonuses. Under the new capital regulations, the minimum capital ratios applicable to Banner and the Banks are: (i) a CETI capital ratio of 4.5%; (ii) a Tier 1 capital ratio of 6% (increased from 4%); (iii) a total capital ratio of 8% (unchanged from prior rules); and (iv) a Tier 1 leverage ratio of 4% for all institutions. CET1 generally consists of common stock; retained earnings; accumulated other comprehensive income ("AOCI"), explained below, unless we elect to exclude AOCI from regulatory capital, as discussed below; and certain minority interests; all subject to applicable regulatory adjustments and deductions. There are a number of changes in what constitutes regulatory capital, some of which are subject to transition periods. These changes include the phasing-out of certain instruments as qualifying capital. Banner and the Banks do not have any of these instruments. Under the new requirements for total capital, Tier 2 capital is no longer limited to the amount of Tier 1 capital included in total capital. Mortgage servicing rights, certain deferred tax assets and investments in unconsolidated subsidiaries over designated percentages of CET1 will be deducted from capital. In addition, Tier 1 capital will include AOCI, which includes all unrealized gains and losses on available for sale debt and equity securities. Because of our asset size, we have the one-time option of deciding in the first quarter of 2015 whether to permanently opt-out of the inclusion of accumulated other comprehensive income in our capital calculations. We are planning to take advantage of this opt-out to reduce the impact of market volatility on our regulatory capital levels.

The new requirements also include changes in the risk-weights of assets to better reflect credit risk and other risk exposures. These include 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 non-accrual 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 (currently set at 0%); a 250% risk weight (up from 100%) for mortgage servicing and deferred tax assets that are not deducted from capital; and increased risk-weights (0% to 600%) for equity exposures.

In addition to the minimum CET1, Tier 1 and total capital ratios, Banner and the Banks will have to maintain a capital conservation buffer consisting of additional CET1 capital greater than 2.5% of risk-weighted assets above the required minimum levels in order to avoid limitations on paying dividends, engaging in share repurchases, and paying discretionary bonuses based on percentages of eligible retained income that could be utilized for such actions. This new capital conservation buffer requirement will be phased in beginning in January 2016 at 0.625% of risk-weighted assets and increasing each year until fully implemented in January 2019.

Note 19: CONTINGENCIES

In the normal course of business, the Company and/or its subsidiaries have various legal proceedings and other contingent matters outstanding. These proceedings and the associated legal claims are often contested and the outcome of individual matters is not always predictable. These claims and counter-claims typically arise during the course of collection efforts on problem loans or with respect to action to enforce liens on properties in which the Banks hold a security interest. Based upon the information known to management at this time, the Company and the Banks are not a party to any legal proceedings that management believes would have a material adverse effect on the results of operations or consolidated financial position at December 31, 2014.

In connection with certain asset sales, the Banks typically make representations and warranties about the underlying assets conforming to specified guidelines. If the underlying assets do not conform to the specifications, the Bank may have an obligation to repurchase the assets or indemnify the purchaser against any loss. The Banks believe that the potential for material loss under these arrangements is remote. Accordingly, the fair value of such obligations is not material.

In February 2009, for the first time in its history, the State of Washington's Public Deposit Protection Commission assessed all Qualified Public Depositories participating in the State's public deposit program an amount that, in aggregate, covered the uninsured portion of the public funds on deposit at a failed Washington bank. Generally, the maximum liability should any member(s) of the State's public deposit program default on its uninsured public funds is limited to 10% of the public funds held by the Banks. A similar program is also in place in Oregon, where Banner Bank also holds public deposits. Should other bank failures occur in either state, the Banks could be subject to additional assessments; however, the rules for participation have been revised to require 100% collateralization of these deposits in the State of Washington and a range of 50% to 110% in the State of Oregon, depending of an institution's CAMEL rating, which serves to significantly limit the contingent liability that currently exists for Qualified Public Depositories. As a result of these collateralization requirements, the Banks have generally sought to

reduce their reliance on public funds since February 2009. Public funds totaled $138 million at December 31, 2014 as compared to $139 million at December 31, 2013.

Note 20: INTEREST RATE RISK

The financial condition and operation of the Company are influenced significantly by general economic conditions, including the absolute level of interest rates as well as changes in interest rates and the slope of the yield curve. The Company's profitability is dependent to a large extent on its net interest income, which is the difference between the interest received from its interest-earning assets and the interest expense incurred on its interest-bearing liabilities.

The activities of the Company, like all financial institutions, inherently involve the assumption of interest rate risk. Interest rate risk is the risk that changes in market interest rates will have an adverse effect on the institution's earnings and underlying economic value. Interest rate risk is determined by the maturity and repricing characteristics of an institution's assets, liabilities and off-balance-sheet contracts. Interest rate risk is measured by the variability of financial performance and economic value resulting from changes in interest rates. Interest rate risk is the primary market risk impacting the Company's financial performance.

The greatest source of interest rate risk to the Company results from the mismatch of maturities or repricing intervals for rate-sensitive assets, liabilities and off-balance-sheet contracts. Additional interest rate risk results from mismatched repricing indices and formula (basis risk and yield curve risk), product caps and floors, and early repayment or withdrawal provisions (option risk), which may be contractual or market driven, that are generally more favorable to customers than to the Company.

The Company's primary monitoring tool for assessing interest rate risk is asset/liability simulation modeling, which is designed to capture the dynamics of balance sheet, interest rate and spread movements, and to quantify variations in net interest income and economic value of equity resulting from those movements under different rate environments. Another monitoring tool used by the Company to assess interest rate risk is gap analysis. The matching of repricing characteristics of assets and liabilities may be analyzed by examining the extent to which such assets and liabilities are interest sensitive and by monitoring the Company's interest sensitivity gap. Management is aware of the sources of interest rate risk and in its opinion actively monitors and manages it to the extent possible, and considers that the Company's current level of interest rate risk is reasonable.

Note 21: INTANGIBLE ASSETS AND MORTGAGE SERVICING RIGHTS

Intangible Assets: At December 31, 2014, intangible assets consisted 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.

The Company amortizes CDI over its estimated useful life and reviews it at least annually for events or circumstances that could impair its value. The CDI assets shown in the table below represent the value ascribed to the long-term deposit relationships acquired in three separate bank acquisitions during 2007, a single branch acquisition in 2013, and the Branch Acquisition in 2014. These intangible assets are being amortized using an accelerated method over estimated useful lives of three to eight years. The CDI assets are not estimated to have a significant residual value. Other intangible assets are amortized over their estimated useful lives and are also reviewed for impairment.

The following table summarizes the changes in the Company's CDI and other intangibles for the years ended December 31, 2012, 2013 and 2014 (in thousands):

	CDI	Other	Total
Balance, December 31, 2011	$6,322	$9	$6,331

Amortization	(2,092)	(9)	(2,101)
Balance, December 31, 2012	4,230	—	4,230
Additions through acquisition	160	—	160
Amortization	(1,941)	—	(1,941)
Balance, December 31, 2013	2,449	—	2,449
Additions through acquisition	2,372	—	2,372
Amortization	(1,990)	—	(1,990)
Balance, December 31, 2014	$2,831	$—	$2,831

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Estimated amortization expense in future years with respect to existing intangibles as of December 31, 2014 (in thousands):

Year Ended:	CDI
December 31, 2015	$1,007
December 31, 2016	353
December 31, 2017	321
December 31, 2018	296
Thereafter	854
Net carrying amount	$2,831

Mortgage servicing rights are reported in other assets. Mortgage servicing rights are initially reported at fair value and are amortized in proportion to, and over the period of, the estimated future net servicing income of the underlying financial assets. Mortgage servicing rights are subsequently evaluated for impairment based upon the fair value of the rights compared to the amortized cost (remaining unamortized initial fair value). If the fair value is less than the amortized cost, a valuation allowance is created through an impairment charge to servicing fee income. However, if the fair value is greater than the amortized cost, the amount above the amortized cost is not recognized in the carrying value. In 2014, the Company did not record any impairment charges or recoveries against mortgage servicing rights. In 2013, the Company recorded a recovery of $1.3 million in previously recognized impairment charges against mortgage servicing rights. In 2012, the Company recorded $400,000 in impairment charges against mortgage servicing rights. Loans serviced for others totaled $1.391 billion and $1.216 billion at December 31, 2014 and 2013, respectively. Custodial accounts maintained in connection with this servicing totaled $6.7 million and $5.7 million at December 31, 2014 and 2013, respectively.

An analysis of the mortgage servicing rights for the years ended December 31, 2014, 2013 and 2012 is presented below (in thousands):

	Years Ended December 31		
	2014	2013	2012
Balance, beginning of the year	$8,086	$6,244	$5,584
Amounts capitalized	3,023	2,913	3,662
Amortization [1]	(2,079)	(2,371)	(2,602)
Valuation adjustments in the period	—	1,300	(400)
Balance, end of the year [2]	$9,030	$8,086	$6,244

(1) Amortization of mortgage servicing rights is recorded as a reduction of loan servicing income and any unamortized balance is fully written off if the loan repays in full.

(2) Balances as of December 31, 2014 and 2013 are net of no valuation allowances, and as of December 31, 2012 are net of a $1.3 million valuation allowance.

Note 22: FAIR VALUE OF FINANCIAL INSTRUMENTS

The Company has elected to record certain assets and liabilities at fair value. Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date (that is, not a forced liquidation or distressed sale). GAAP (ASC 820, Fair Value Measurements) establishes a consistent framework for measuring fair value and disclosure requirements about fair value measurements. Among other things, the standard requires us to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. Observable inputs reflect market data obtained from independent sources, while unobservable inputs reflect the Company's estimates for market assumptions. These two types of inputs create the following fair value hierarchy:

- Level 1 – Quoted prices in active markets for identical instruments. An active market is a market in which transactions occur with sufficient frequency and volume to provide pricing information on an ongoing basis. A quoted price in an active market provides the most reliable evidence of fair value and shall be used to measure fair value whenever available.

- Level 2 – Observable inputs other than Level 1 including quoted prices in active markets for similar instruments, quoted prices in less active markets for identical or similar instruments, or other observable inputs that can be corroborated by observable market data. Our use of Level 2 measurements for these securities is generally based upon a matrix pricing model from an investment reporting and valuation service. Matrix pricing is a mathematical technique used principally to value debt securities without relying exclusively on quoted prices for the specific securities, but rather by relying on the securities' relationship to other benchmark quoted securities.

- Level 3 – Unobservable inputs supported by little or no market activity for financial instruments whose value is determined using pricing models, discounted cash flow methodologies, or similar techniques, as well as instruments for which the determination of fair value requires significant management judgment or estimation; also includes observable inputs from non-binding single dealer quotes not

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corroborated by observable market data. In developing Level 3 measurements, management incorporates whatever market data might be available and uses discounted cash flow models where appropriate. These calculations include projections of future cash flows, including appropriate default and loss assumptions, and market based discount rates.

The estimated fair value amounts of financial instruments have been determined by the Company using available market information and appropriate valuation methodologies. However, considerable judgment is required to interpret data to develop the estimates of fair value. Accordingly, the estimates presented herein are not necessarily indicative of the amounts the Company could realize in a current market exchange. The use of different market assumptions and/or estimation methodologies may have a material effect on the estimated fair value amounts. In addition, reasonable comparability between financial institutions may not be likely due to the wide range of permitted valuation techniques and numerous estimates that must be made given the absence of active secondary markets for many of the financial instruments. This lack of uniform valuation methodologies also introduces a greater degree of subjectivity to these estimated fair values. Transfers between levels of the fair value hierarchy are deemed to occur at the end of the reporting period.

Items Measured at Fair Value on a Recurring Basis

Banner records trading account securities, securities available-for-sale, FHLB advances, junior subordinated debentures and certain derivative transactions at fair value on a recurring basis.

- Investment securities primarily consist of U.S. Government and agency obligations, municipal bonds, corporate bonds, single issue trust preferred securities (TPS), pooled trust preferred collateralized debt obligation securities (TRUP CDO), mortgage-backed securities, asset-backed securities, equity securities and certain other financial instruments.

From mid-2008 through the current year, the lack of active markets and market participants for certain securities resulted in an increase in Level 3 measurements. In particular, the market for our TRUP CDO securities has been generally inactive during this period. This was evidenced first by a significant widening of the bid-ask spread in the brokered markets in which TRUP CDOs trade and then by a significant decrease in the volume of trades relative to historical levels. The new issue market is also inactive as almost no new TRUP CDOs have been issued since 2007. There are still very few market participants who are willing and/or able to transact for these securities. Thus, a low market price for a particular bond may only provide evidence of lack of an active market rather than being an indicator of credit problems with a particular issuer or of the fair value of the security. As of December 31, 2014, Banner owned $10 million in current par value of these securities.

Given these conditions and the absence of observable transactions in the secondary and new issue markets, management determined that for the TRUP CDOs at December 31, 2014 and 2013:

- The few observable transactions and market quotations that were available were not reliable for purposes of determining fair value,
- An income valuation approach technique (present value technique) that maximizes the use of relevant observable inputs and minimizes the use of unobservable inputs was equally or more representative of fair value than the market approach valuation technique, and
- The Company’s TRUP CDOs should be classified exclusively within Level 3 of the fair value hierarchy because of the significant assumptions required to determine fair value at the measurement date.

The TRUP CDO valuations were derived using input from independent third parties who used proprietary cash flow models for analyzing collateralized debt obligations. Their approaches to determining fair value involve considering the credit quality of the collateral, assuming a level of defaults based on the probability of default of each underlying

trust preferred security, creating expected cash flows for each TRUP CDO security and discounting that cash flow at an appropriate risk-adjusted rate plus a liquidity premium.

Where appropriate, management reviewed the valuation methodologies, and assumptions used by the independent third party providers and for certain securities determined that the fair value estimates were reasonable and utilized those estimates in the Company’s reported financial statements, while for other securities management adjusted the third party providers modeling to be more reflective of the characteristics of the Company’s remaining TRUP CDOs. Further, during the year ended December 31, 2014, two of our TRUP CDOs, which had previously incurred significant fair value write downs, were repaid in full, resulting in equally significant fair value gains on those securities in 2014. The net result of the fair value analysis of these Level 3 measurements was a fair value gain of $4.9 million for the year-ended December 31, 2014, primarily a result of repayment of the two securities noted above, compared to a $255,000 fair value loss in the year ended December 31, 2013 and a $3.3 million gain in the year ended December 31, 2012. The small loss in the year ending December 31, 2013, was primarily the result of a modest adjustment to the discount rate which more than offset the impact of the passage of time on the years to maturity in the discounted present value calculation used to estimate the fair value of these securities. In management's opinion the small valuation change was consistent with general market stability for credit spreads supported by other market observations. The more significant gain in the year ended December 31, 2012, was primarily caused by a reduction in the spread between the benchmark credit equivalent indices used to establish an appropriate discount rate and a similar maturity point on the interest rate swap curve, which resulted in a more substantial adjustment to the discount rate.

At December 31, 2014, Banner also directly owned approximately $19 million in amortized cost of single issuer TPS securities for which no market data or independent valuation source is available. Similar to the TRUP CDOs above, there were too few, if any, issuances of new TPS securities or sales of existing TPS securities to provide Level 1 or even Level 2 fair value measurements for these

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securities. Management, therefore, utilized a discounted cash-flow model to calculate the present value of each security's expected future cash flows to determine their respective fair values. Management took into consideration the limited market data that was available regarding similar securities and assessed the performance of the three individual issuers of TPS securities owned by the Company. At December 31, 2014, the Company again sought input from independent third parties to help it establish an appropriate set of parameters to identify a reasonable range of discount rates for use in its fair value model. Management concluded that market yields have been reasonably stable in recent periods but that the indicated spreads and implied yields for non-investment grade securities as well as the yields associated with individual issuers in the third party analyst reports suggested that a 500 basis point spread over the three-month LIBOR index, 25 basis points less than the spread as used a year earlier, was a reasonable basis for determining an appropriate discount rate to estimate the fair value of these securities. These factors were then incorporated into the model at December 31, 2014, where a discount rate equal to three-month LIBOR plus 500 basis points was used to calculate the respective fair values of these securities The result of this Level 3 fair value measurement was a fair value gain of $35,000 in the year ended December 31, 2014, compared to a gain of $74,000 in the year ended December 31, 2013 and a gain of $578,000 in the year ended December 31, 2012. The much larger valuation change in 2012 was the result of decreasing the spreads to 525 basis points from a range of 600–800 used in 2011. The Company has and will continue to assess the appropriate fair value hierarchy for determination of these fair values on a quarterly basis.

For trading securities other than TRUP CDOs and single-issuer TPS securities and for securities—available-for-sale we used matrix pricing models from investment reporting and valuation services. Management considers this to be a Level 2 input method.

- Fair valuations for FHLB advances are estimated using fair market values provided by the lender, the FHLB of Seattle. The FHLB of Seattle prices advances by discounting the future contractual cash flows for individual advances using its current cost of funds curve to provide the discount rate. Management considers this to be a Level 2 input method.

- The fair valuations of junior subordinated debentures (TPS-related debt that the Company has issued) were also valued using discounted cash flows. These debentures carry interest rates that reset quarterly, using the three-month LIBOR index plus spreads of 1.38% to 3.35%. While the quarterly reset of the index on this debt would seemingly keep its fair value reasonably close to book values, the disparity in the fixed spreads above the index and the inability to determine realistic current market spreads, due to lack of new issuances and trades, resulted in having to rely more heavily on assumptions about what spread would be appropriate if market transactions were to take place. In periods prior to the third quarter of 2008, the discount rate used was based on recent issuances or quotes from brokers on the date of valuation for comparable bank holding companies and was considered to be a Level 2 input method. However, as noted above in the discussion of TPS and TRUP CDOs, due to the unprecedented disruption of certain financial markets, management concluded that there were insufficient transactions or other indicators to continue to reflect these measurements as Level 2 inputs. Due to this reliance on assumptions and not on directly observable transactions, management believes fair value for these instruments should follow a Level 3 input methodology. Since the discount rate used in the fair value modeling is the most sensitive unobservable estimate in the calculation, the Company again utilized input from the same independent third party noted above to help it establish an appropriate set of parameters to identify a reasonable range of discount rates for use in its fair value model. In valuing the debentures at June 30, 2012, these changes in credit quality were the primary factor contributing to a reduction in the discount rate from 800 basis points to 550 basis points. In further valuing the debentures at September 30, 2012, management evaluated the general market tightening of credit spreads as noted above and reduced the discount rate to the period-ending three-month LIBOR plus 525 basis points. This spread of 525 basis points to LIBOR was used to establish discount rates and fair value estimates at December 31, 2012 and 2013. As noted above in the discussion about single-issuer TPS securities, since market spreads have been reasonably stable in recent periods; however, we further reduced the spread to 500 basis points at December 31, 2014, resulting in a fair value loss on these instruments

of $4.1 million for the year ended December 31, 2014, compared to a $865,000 loss in the year ended December 31, 2013 and a $23.1 million loss in the year ended December 31, 2012. The fair value adjustment in the current year was primarily the result of the passage of time on the years to maturity in the discounted present value calculation used to estimate the fair value.

- Derivative instruments include interest rate commitments related to one- to four family loans and residential mortgage backed securities and interest rate swaps. The fair value of interest rate lock commitments and forward sales commitments are estimated using quoted or published market prices for similar instruments, adjusted for factors such as pull-through rate assumptions based on historical trends, where appropriate. The fair value of interest rate swaps is determined by using current market quotes on similar instruments provided by active broker/dealers in the swap market. Management considers these to be Level 2 input methods. The changes in the fair value of all these derivative instruments are primarily attributable to changes in the level of market interest rates. The Company has elected to record the fair value of these derivative instruments on a net basis.

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The following tables present financial assets and liabilities measured at fair value on a recurring basis and the level within the fair value hierarchy of the fair value measurements for those assets and liabilities as of December 31, 2014 and 2013 (in thousands):

	December 31, 2014			
	Level 1	Level 2	Level 3	Total
Assets:				
Securities—available-for-sale				
U.S. Government and agency	$—	$29,770	$—	$29,770
Municipal bonds	—	50,028	—	50,028
Corporate bonds	—	5,018	—	5,018
Mortgage-backed securities	—	300,810	—	300,810
Asset-backed securities	—	25,395	—	25,395
	—	411,021	—	411,021
Securities—trading				
U.S. Government and agency	—	1,505	—	1,505
Municipal bonds	—	1,440	—	1,440
TPS and TRUP CDOs	—	—	19,118	19,118
Mortgage-backed securities	—	18,136	—	18,136
Equity securities and other	—	59	—	59
	—	21,140	19,118	40,258
Derivatives				
Interest rate lock commitments	—	—	317	317
Interest rate swaps	—	6,290	—	6,290
	$—	$438,451	$19,435	$457,886
Liabilities				
Advances from FHLB at fair value	$—	$32,250	$—	$32,250
Junior subordinated debentures net of unamortized deferred issuance costs at fair value	—	—	78,001	78,001
Derivatives				
Interest rate forward sales commitments	—	198	—	198
Interest rate swaps	—	6,290	—	6,290
	$—	$38,738	$78,001	$116,739

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	December 31, 2013			
	Level 1	Level 2	Level 3	Total
Assets:				
Securities—available-for-sale				
U.S. Government and agency	$—	$58,660	$—	$58,660
Municipal bonds	—	52,855	—	52,855
Corporate bonds	—	6,964	—	6,964
Mortgage-backed securities	—	326,610	—	326,610
Asset-backed securities	—	25,191	—	25,191
	—	470,280	—	470,280
Securities—trading				
U.S. Government and agency	—	1,481	—	1,481
Municipal bonds	—	5,023	—	5,023
TPS and TRUP CDOs	—	—	35,140	35,140
Mortgage-backed securities	—	20,760	—	20,760
Equity securities and other	—	68	—	68
	—	27,332	35,140	62,472
Derivatives				
Interest rate lock commitments	—	—	130	130
Interest rate swaps	—	4,946	—	4,946
	$—	$502,558	$35,270	$537,828
Liabilities				
Advances from FHLB at fair value	$—	$27,250	$—	$27,250
Junior subordinated debentures net of unamortized deferred issuance costs at fair value	—	—	73,928	73,928
Derivatives				
Interest rate forward sales commitments	—	43	—	43
Interest rate swaps	—	4,946	—	4,946
	$—	$32,239	$73,928	$106,167

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The following table provides a reconciliation of the assets and liabilities measured at fair value using significant unobservable inputs (Level 3) on a recurring basis during the year ended December 31, 2014 and 2013 (in thousands):

	Year Ended December 31, 2014 Level 3 Fair Value Inputs	
	TPS and TRUP CDOs	Borrowings—Junior Subordinated Debentures
Beginning balance at December 31, 2013	$35,140	$73,928
Total gains or losses recognized		
Assets gains (losses)	5,481	—
Liabilities (gains) losses	—	4,073
Purchases, issuances and settlements	—	—
Paydowns and maturities	(21,502)	—
Transfers in and/or out of Level 3	—	—
Ending balance at December 31, 2014	$19,119	$78,001

	Year Ended December 31, 2013 Level 3 Fair Value Inputs	
	TPS and TRUP CDOs	Borrowings—Junior Subordinated Debentures
Beginning balance at December 31, 2012	$35,741	$73,063
Total gains or losses recognized		
Assets gains (losses)	(181)	—
Liabilities (gains) losses	—	865
Purchases, issuances and settlements	—	—
Paydowns and maturities	(420)	—
Transfers in and/or out of Level 3	—	—
Ending balance at December 31, 2013	$35,140	$73,928

The Company has elected to continue to recognize the interest income and dividends from the securities reclassified to fair value as a component of interest income as was done in prior years when they were classified as available-for-sale. Interest expense related to the FHLB advances and junior subordinated debentures continues to be measured based on contractual interest rates and reported in interest expense. The change in fair value of these financial instruments has been recorded as a component of other operating income.

Items Measured at Fair Value on a Non-recurring Basis

Carrying values of certain impaired loans are periodically evaluated to determine if valuation adjustments, or partial write-downs, should be recorded. These non-recurring fair value adjustments are recorded when observable market prices or current appraised values of collateral indicate a shortfall in collateral value or discounted cash flows indicate a shortfall compared to current carrying values of the related loan. If the Company determines that the value of the impaired loan is less than the carrying value of the loan, the Company either establishes an impairment reserve as a specific component of the allowance for loan and lease losses (ALLL) or charges off the impaired amount. The remaining impaired loans are evaluated for reserve needs in homogenous pools within the Company’s ALLL methodology. As of December 31, 2014, the Company reviewed all of its adversely classified loans totaling $64 million and identified $46 million which were considered impaired. Of those $46 million in impaired loans, $34

million were individually evaluated to determine if valuation adjustments, or partial write-downs, should be recorded, or if specific impairment reserves should be established. The $34 million had original carrying values of $37 million which have been reduced by partial write-downs totaling $3 million. In addition to these write-downs, in order to bring the impaired loan balances to fair value, Banner also established $3 million in specific reserves on these impaired loans. Impaired loans that were collectively evaluated for reserve purposes within homogenous pools totaled $11 million and were found to require allowances totaling $126,000. The valuation inputs for impaired loans are considered to be Level 3 inputs.

The Company records REO (acquired through a lending relationship) at fair value on a non-recurring basis. All REO properties are recorded at the lower of the estimated fair value of the properties, less expected selling costs, or the carrying amount of the defaulted loans. 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. Banner considers any valuation inputs related to REO to be Level 3 inputs. The individual carrying values of these assets are reviewed for impairment at least annually and any additional impairment charges are expensed to operations. For the years ended

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December 31, 2014 and 2013, the Company recognized $37,000 and $785,000, respectively of impairment charges related to these types of assets.

Mortgage servicing rights are reported in other assets. Mortgage servicing rights are initially reported at fair value and are amortized in proportion to, and over the period of, the estimated future net servicing income of the underlying financial assets. Mortgage servicing rights are subsequently evaluated for impairment based upon the fair value of the rights compared to the amortized cost (remaining unamortized initial fair value). If the fair value is less than the amortized cost, a valuation allowance is created through an impairment charge to servicing fee income. However, if the fair value is greater than the amortized cost, the amount above the amortized cost is not recognized in the carrying value. In 2014, the Company did not record any impairment charges against mortgage servicing rights. In 2013, the Company reversed $1.3 million in previously recorded impairment charges against mortgage servicing rights.

The following tables present financial assets and liabilities measured at fair value on a non-recurring basis and the level within the fair value hierarchy at December 31, 2014 and 2013 (in thousands):

	At or For the Year Ended December 31, 2014				
	Level 1	Level 2	Level 3	Total	Net Losses Recognized During the Period
Impaired loans	$—	$—	$4,725	$4,725	$(512)
REO	—	—	3,352	3,352	(453)

	At or For the Year Ended December 31, 2013				
	Level 1	Level 2	Level 3	Total	Net Losses Recognized During the Period
Impaired loans	$—	$—	$10,627	$10,627	$(4,890)
REO	—	—	4,044	4,044	(853)

Assets and Liabilities Measured at Fair Value Using Significant Unobservable Inputs (Level 3)

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

			December 31	
Financial Instruments	Valuation Technique	Unobservable Inputs	2014 Weighted Average Rate	2013 Weighted Average Rate
TPS securities	Discounted cash flows	Discount rate	5.26 %	5.50 %
TRUP CDOs	Discounted cash flows	Discount rate	3.96	3.85
Junior subordinated debentures	Discounted cash flows	Discount rate	5.26	5.50
Impaired loans	Discounted cash flows	Discount rate	Various	Various
		Market values	n/a	n/a

REO	Collateral Valuations Appraisals	Market values	n/a	n/a

TPS and TRUP CDOs: Management believes that the credit risk-adjusted spread used to develop the discount rate utilized in the fair value measurement of TPS and TRUP CDOs is indicative of the risk premium a willing market participant would require under current market conditions for instruments with similar contractual rates and terms and conditions and issuers with similar credit risk profiles and with similar expected probability of default. Management attributes the change in fair value of these instruments, compared to their par value, primarily to perceived general market adjustments to the risk premiums for these types of assets subsequent to their issuance.

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Junior subordinated debentures: Similar to the TPS and TRUP CDOs discussed above, management believes that the credit risk-adjusted spread utilized in the fair value measurement of the junior subordinated debentures is indicative of the risk premium a willing market participant would require under current market conditions for an issuer with Banner's credit risk profile. Management attributes the change in fair value of the junior subordinated debentures, compared to their par value, primarily to perceived general market adjustments to the risk premiums for these types of liabilities subsequent to their issuance. Future contractions in the risk adjusted spread relative to the spread currently utilized to measure the Company's junior subordinated debentures at fair value as of December 31, 2014, or the passage of time, will result in negative fair value adjustments. At December 31, 2014, the discount rate utilized was based on a credit spread of 500 basis points and three month LIBOR of 26 basis points.

Impaired 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 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. If this practical expedient is used, the impaired loans are considered to be held at fair value. 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.

REO: Fair value adjustments on REO are based on updated real estate appraisals, less selling costs,which are based on current market conditions.

MSRs: Management believes that the discount rate utilized in the fair valuation of our MSRs is indicative of a reasonable yield expectation in an orderly transaction between willing market participants at the measurement date. Generally, any significant increases in the prepayment rate and discount rate utilized in the fair value measurement of the mortgage servicing rights will result in negative fair value adjustments and a decrease in the fair value measurement. Alternatively, a decrease in the prepayment rate and discount rate will result in a positive fair value adjustment and increase in the fair value measurement. An increase in the weighted average life assumptions will result in a decrease in the prepayment rate and a decrease in the weighted average life will result in an increase of the prepayment rate.

Fair Values of Financial Instruments

The following table presents estimated fair values of the Company's financial instruments as of December 31, 2014 and 2013, whether or not recognized or recorded in the consolidated Statements of Financial Condition. The estimated fair value amounts have been determined by the Company using available market information and appropriate valuation methodologies. However, considerable judgment is necessary to interpret market data in the development of the estimates of fair value. Accordingly, the estimates presented herein are not necessarily indicative of the amounts the Company could realize in a current market exchange. The use of different market assumptions and/or estimation methodologies may have a material effect on the estimated fair value amounts. The carrying value and estimated fair value of financial instruments at December 31, 2014 and 2013 are as follows (in thousands):

	December 31, 2014		December 31, 2013	
	Carrying Value	Estimated Fair Value	Carrying Value	Estimated Fair Value
Assets:				
Cash and due from banks	$126,072	$126,072	$137,349	$137,349
Securities—trading	40,258	40,258	62,472	62,472
Securities—available-for-sale	411,021	411,021	470,280	470,280
Securities—held-to-maturity	131,258	137,608	102,513	103,610
Loans receivable held for sale	2,786	2,807	2,734	2,751
Loans receivable	3,831,034	3,722,179	3,415,711	3,297,936
FHLB stock	27,036	27,036	35,390	35,390
BOLI	63,759	63,759	61,945	61,945
Mortgage servicing rights	9,030	12,987	8,086	11,529
Derivatives:				
Interest rate swaps	6,290	6,290	4,946	4,946
Interest rate lock commitments	317	317	130	130
Liabilities:				
Demand, interest-bearing checking and money market	2,227,292	1,998,649	1,946,467	1,697,095
Regular savings	901,142	784,006	798,764	695,863
Certificates of deposit	770,516	764,549	872,695	867,904
Advances from FHLB at fair value	32,250	32,250	27,250	27,250
Junior subordinated debentures at fair value	78,001	78,001	73,928	73,928
Other borrowings	77,185	77,185	83,056	83,056
Derivatives:				
Interest rate swaps	6,290	6,290	4,946	4,946
Interest rate forward sales commitments	198	198	43	43

Fair value estimates, methods and assumptions and the level within the fair value hierarchy of the fair value measurements are set forth below for the Company's financial and off-balance sheet instruments:

Cash and Due from Banks: The carrying amount of these items is a reasonable estimate of their fair value. These fair values are considered Level 1 measures.

Securities: The estimated fair values of investment securities and mortgaged-backed securities are priced using current active market quotes, if available, which are considered Level 1 measurements. For most of the portfolio, matrix pricing based on the securities' relationship to other benchmark quoted prices is used to establish the fair value. These measurements are considered Level 2. Due to continued credit concerns in the capital markets and inactivity in the trust preferred markets that have limited the observability of market spreads for some of the

Company's TPS and TRUP CDO securities (see earlier discussion above in determining the securities' fair market value), management has classified these securities as a Level 3 fair value measure.

Loans Receivable Held for Sale: Carrying values are based on the lower of estimated fair values or book values. Fair values are estimated based on secondary market pricing for similar loans. This is considered a Level 2 fair value measure.

Loans Receivable: Fair values are estimated first by stratifying the portfolios of loans with similar financial characteristics. Loans are segregated by type such as multifamily real estate, residential mortgage, nonresidential mortgage, commercial/agricultural, consumer and other. Each loan category is further segmented into fixed- and adjustable-rate interest terms and by performing and non-performing categories. A preliminary estimate of fair value is then calculated based on discounted cash flows using as a discount rate the current rate offered on similar products, plus an adjustment for liquidity to reflect the non-homogeneous nature of the loans. The preliminary estimate is then further reduced by the amount of the allowance for loan losses to arrive at a final estimate of fair value. Fair value for significant non-performing loans is based on recent

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appraisals or estimated cash flows discounted using rates commensurate with risk associated with the estimated cash flows. Assumptions regarding credit risk, cash flows and discount rates are judgmentally determined using available market information and specific borrower information. Management considers this to be a Level 2 measurement.

FHLB Stock: The fair value is based upon the redemption value of the stock which equates to its carrying value. This fair value is considered a Level 3 measure.

Bank-Owned Life Insurance: The fair value of BOLI policies owned are based on the various insurance contracts' cash surrender value. This fair value is considered a Level 1 measure.

Mortgage Servicing Rights: Fair values are estimated based on current pricing for sales of servicing for new loans adjusted up or down based on the serviced loan's interest rate versus current new loan rates. Management considers this to be a Level 3 measure.

Deposit Liabilities: The fair value of deposits with no stated maturity, such as savings and checking accounts, is estimated by applying decay rate assumptions to segregated portfolios of similar deposit types to generate cash flows which are then discounted using short-term market interest rates. The market value of certificates of deposit is based upon the discounted value of contractual cash flows. The discount rate is determined using the rates currently offered on comparable instruments. Fair value estimates for deposits are considered Level 3 measures.

FHLB Advances and Other Borrowings: Fair valuations for Banner’s FHLB advances are estimated using fair market values provided by the lender, the FHLB of Seattle. The FHLB of Seattle prices advances by discounting the future contractual cash flows for individual advances using its current cost of funds curve to provide the discount rate. This is considered to be a Level 2 input method. Other borrowings are priced using discounted cash flows to the date of maturity based on using current rates at which such borrowings can currently be obtained. This fair value is considered a Level 3 measure.

Junior Subordinated Debentures: Due to continued credit concerns in the capital markets and inactivity in the trust preferred markets that have limited the observability of market spreads (see earlier discussion above in determining the junior subordinated debentures’ fair market value), junior subordinated debentures have been classified as a Level 3 fair value measure. Management believes that the credit risk adjusted spread and resulting discount rate utilized is indicative of those that would be used by market participants.

Derivative Instruments: Derivatives include interest rate swap agreements, interest rate lock commitments to originate loans held for sale and forward sales contracts to sell loans and securities related to mortgage banking activities. Fair values for the interest rate swaps which generally change as a result of changes in the level of market interest rates , are estimated based on dealer quotes and secondary market sources. Management considers these to be Level 2 inputs. The fair value of the interest rate lock commitments and forward sales commitments are estimated using quoted or published market prices for similar instruments, adjusted for factors such as pull-through rate assumptions where appropriate. The pull-through rate assumptions are considered Level 3 valuation inputs and are significant to the interest rate lock commitment valuation; as such, the interest rate lock commitment derivatives are classified as Level 3.

Limitations: The fair value estimates presented herein are based on pertinent information available to management as of December 31, 2014 and 2013. Although management is not aware of any factors that would significantly affect the estimated fair value amounts, such amounts have not been comprehensively revalued for purposes of these financial statements since that date and, therefore, current estimates of fair value may differ significantly from the amounts presented herein.

Fair value estimates are based on existing on- and off-balance-sheet financial instruments without attempting to estimate the value of anticipated future business. The fair value has not been estimated for assets and liabilities that are not considered financial instruments. Significant assets and liabilities that are not financial instruments include the deferred tax assets/liabilities; land, buildings and equipment; costs in excess of net assets acquired; and real estate held for sale.

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Note 23: BANNER CORPORATION (PARENT COMPANY ONLY)

Summary financial information is as follows (in thousands):

Statements of Financial Condition	December 31	
	2014	2013
ASSETS		
Cash	$52,124	$45,998
Investment in trust equities	3,716	3,716
Investment in subsidiaries	611,468	575,023
Other assets	8,279	7,280
	$675,587	$632,017
LIABILITIES AND STOCKHOLDERS' EQUITY		
Miscellaneous liabilities	$2,446	$6,157
Deferred tax liability	11,516	12,960
Junior subordinated debentures at fair value	78,001	73,928
Stockholders' equity	583,624	538,972
	$675,587	$632,017

Statements of Operations	Years Ended December 31		
	2014	2013	2012
INTEREST INCOME:			
Interest-bearing deposits	$96	$82	$218
OTHER INCOME (EXPENSE):			
Dividend income from subsidiaries	26,027	24,725	61,329
Equity in undistributed income of subsidiaries	33,707	23,994	23,507
Other income	67	3,016	55
Net change in valuation of financial instruments carried at fair value	(4,073)	(865)	(23,075)
Interest on other borrowings	(2,914)	(2,968)	(3,395)
Other expenses	(2,519)	(2,794)	(2,375)
Net income before taxes	50,391	45,190	56,264
BENEFIT FROM INCOME TAXES	(3,774)	(1,365)	(8,618)
NET INCOME	54,165	46,555	64,882
PREFERRED STOCK DIVIDEND AND DISCOUNT ACCRETION			
Preferred stock dividend	—	—	4,938
Preferred stock discount accretion	—	—	3,298
Gain on repurchase of preferred stock	—	—	(2,471)
NET INCOME AVAILABLE TO COMMON SHAREHOLDERS	$54,165	$46,555	$59,117

Statements of Cash Flows	Years Ended December 31		
	2014	2013	2012
OPERATING ACTIVITIES:			
Net income	$54,165	$46,555	$64,882
Adjustments to reconcile net income to net cash provided by operating activities:			
Equity in undistributed earnings of subsidiaries	(33,707)	(23,994)	(23,507)
Increase (decrease) in deferred taxes	(1,444)	17	(13,030)
Net change in valuation of financial instruments carried at fair value	4,073	865	23,075
(Increase) decrease in other assets	(3,822)	(4,655)	(496)
Increase (decrease) in other liabilities	222	(1,921)	4,940
Net cash provided from operating activities	19,487	16,867	55,864
INVESTING ACTIVITIES:			
Funds transferred to deferred compensation trust	(26)	(27)	(332)
Net cash used by investing activities	(26)	(27)	(332)
FINANCING ACTIVITIES:			
Issuance of stock for stockholder reinvestment program	127	72	36,317
Redemption of senior preferred stock	—	—	(121,528)
Cash dividends paid	(13,462)	(7,798)	(6,470)
Net cash used by financing activities	(13,335)	(7,726)	(91,681)
NET INCREASE (DECREASE) IN CASH	6,126	9,114	(36,149)
CASH, BEGINNING OF PERIOD	45,998	36,884	73,033
CASH, END OF PERIOD	$52,124	$45,998	$36,884

Note 24: STOCK REPURCHASES

During 2012, the Company repurchased or redeemed all of its Series A Preferred Stock, realizing gains aggregating $2.5 million, which was partially offset by accelerated amortization of a portion of the initial discount recorded at the issuance of the Series A Preferred Stock. As a result, the accrual for the quarterly dividend was reduced by the retirement of the repurchased shares. As of December 31, 2012, all of the Series A Preferred Stock had been retired.

On March 26, 2014, the Company announced that its Board of Directors had authorized the repurchase of up to 978,826 shares of the Company's common stock, or 5% of the Company's outstanding shares. Under the plan, shares may be repurchased by the Company in open market purchases. The extent to which the Company repurchases its shares and timing of such repurchases will depend upon market conditions and other corporate considerations.

The Company did not repurchase any of its common stock during the years ended December 31, 2014, 2013 or 2012 except for shares surrendered by employees to satisfy tax withholding obligations upon the vesting of restricted stock grants and shares redeemed relating to the termination of the ESOP.

Note 25: CALCULATION OF EARNINGS PER COMMON SHARE

The following tables show the calculation of earnings (loss) per common share (in thousands, except per share data):

	Years Ended December 31		
	2014	2013	2012
Net income	$54,165	$46,555	$64,882
Preferred stock dividend accrual	—	—	(4,938)
Preferred stock discount accretion	—	—	(3,298)
Gain on repurchase of preferred stock	—	—	2,471
Net income available to common shareholders	$54,165	$46,555	$59,117
Weighted average number of common shares outstanding			
Basic	19,359	19,361	18,650
Diluted	19,403	19,397	18,723
Earnings per common share			
Basic	$2.80	$2.40	$3.17
Diluted	$2.79	$2.40	$3.16

At December 31, 2014, there were 195,106 issued but unvested restricted stock shares that were included in the computation of diluted earnings per share.

Options to purchase an additional 10,664 shares of common stock and a warrant to purchase up to 243,998 shares of common stock were not included in the computation of diluted earnings per share because their exercise price resulted in them being anti-dilutive.

Note 26: SELECTED QUARTERLY FINANCIAL DATA (UNAUDITED)

Results of operations on a quarterly basis for the years ended December 31, 2014, 2013 and 2012 were as follows (dollars in thousands except for per share data):

	Year Ended December 31, 2014			
	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
Interest income	$45,106	$46,540	$49,764	$49,251
Interest expense	2,767	2,732	2,700	2,590
Net interest income before provision for loan losses	42,339	43,808	47,064	46,661
Provision for loan losses	—	—	—	—
Net interest income	42,339	43,808	47,064	46,661
Other operating income	8,858	20,133	13,350	11,913
Other operating expenses	35,581	38,435	38,495	41,230
Income before provision for income taxes	15,616	25,506	21,919	17,344
Provision for income taxes	5,046	8,499	7,076	5,599
Net income	10,570	17,007	14,843	11,745
Preferred stock dividend	—	—	—	—
Preferred stock discount accretion	—	—	—	—
Gain on repurchase and retirement of preferred stock	—	—	—	—
Net income available to common shareholders	$10,570	$17,007	$14,843	$11,745
Basic earnings per share	$0.55	$0.88	$0.77	$0.61
Diluted earnings per share	0.54	0.88	0.76	0.60
Dividends declared	0.18	0.18	0.18	0.18

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	Year Ended December 31, 2013			
	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
Interest income	$44,508	$45,571	$45,037	$44,595
Interest expense	3,540	3,323	3,144	2,988
Net interest income before provision for loan losses	40,968	42,248	41,893	41,607
Provision for loan losses	—	—	—	—
Net interest income	40,968	42,248	41,893	41,607
Other operating income	9,997	10,623	10,142	12,580
Other operating expenses	34,099	35,457	34,490	36,929
Income before provision for income taxes	16,866	17,414	17,545	17,258
Provision for income taxes	5,284	5,661	5,880	5,704
Net income	11,582	11,753	11,665	11,554
Preferred stock dividend	—	—	—	—
Preferred stock discount accretion	—	—	—	—
Gain on repurchase and retirement of preferred stock	—	—	—	—
Net income available to common shareholders	$11,582	$11,753	$11,665	$11,554
Basic earnings per share	$0.60	$0.60	$0.60	$0.60
Diluted earnings per share	0.60	0.60	0.60	0.60
Dividends declared	0.12	0.12	0.15	0.15

	Year Ended December 31, 2012			
	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
Interest income	$47,198	$47,265	$47,174	$45,525
Interest expense	6,072	4,975	4,476	3,991
Net interest income before provision for loan losses	41,126	42,290	42,698	41,534
Provision for loan losses	5,000	4,000	3,000	1,000
Net interest income	36,126	38,290	39,698	40,534
Other operating income	10,971	(9,064)	11,684	13,311
Other operating expenses	37,913	35,666	33,355	34,519
Income (loss) before provision for income taxes	9,184	(6,440)	18,027	19,326
Provision (benefit) for income taxes	—	(31,830)	2,407	4,638
Net income	9,184	25,390	15,620	14,688
Preferred stock dividend	1,550	1,550	1,227	611
Preferred stock discount accretion	454	454	1,216	1,174
Gain on repurchase and retirement of preferred stock	—	—	(2,070)	(401)
Net income available to common shareholders	$7,180	$23,386	$15,247	$13,304
Basic earnings per share	$0.40	$1.27	$0.81	$0.69
Diluted earnings per share	0.40	1.27	0.80	0.69
Dividends declared	0.01	0.01	0.01	0.01

Note 27: FINANCIAL INSTRUMENTS WITH OFF-BALANCE-SHEET RISK

The Company has financial instruments with off-balance-sheet risk generated in the normal course of business to meet the financing needs of its customers. These financial instruments include commitments to extend credit, commitments related to standby letters of credit, commitments to originate loans, commitments to sell loans, and commitments to

buy or sell securities. These instruments involve, to varying degrees, elements of credit and interest rate risk similar to the risk involved in on-balance sheet items recognized in our Consolidated Statements of Financial Condition.

Our exposure to credit loss in the event of nonperformance by the other party to the financial instrument from commitments to extend credit and standby letters of credit is represented by the contractual notional amount of those instruments. We use the same credit policies in making commitments and conditional obligations as for on-balance sheet instruments.

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Outstanding commitments for which no asset or liability for the notional amount has been recorded consisted of the following at the dates indicated (in thousands):

	Contract or Notional Amount	
	December 31, 2014	December 31, 2013
Commitments to extend credit	$1,166,165	$1,073,897
Standby letters of credit and financial guarantees	9,934	6,990
Commitments to originate loans	20,988	15,776
Derivatives also included in Note 28:		
Commitments to originate loans held for sale	29,851	21,434
Commitments to sell loans secured by one- to four-family residential properties	8,714	9,378
Commitments to sell securities related to mortgage banking activities	25,000	15,200

Commitments to extend credit are agreements to lend to a customer, as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Many of the commitments may expire without being drawn upon; therefore, the total commitment amounts do not necessarily represent future cash requirements. Each customer's creditworthiness is evaluated on a case-by-case basis. The amount of collateral obtained, if deemed necessary upon extension of credit, is based on management's credit evaluation of the customer. Collateral held varies, but may include accounts receivable, inventory, property, plant and equipment, and income producing commercial properties.

Standby letters of credit are conditional commitments issued to guarantee a customer's performance or payment to a third party. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to customers.

Interest rates on residential one- to four-family mortgage loan applications are typically rate locked (committed) to customers during the application stage for periods ranging from 30 to 60 days, the most typical period being 45 days. Traditionally, these loan applications with rate lock commitments had the pricing for the sale of these loans locked with various qualified investors under a best-efforts delivery program at or near the time the interest rate is locked with the customer. The Bank then attempts to deliver these loans before their rate locks expired. This arrangement generally required delivery of the loans prior to the expiration of the rate lock. Delays in funding the loans required a lock extension. The cost of a lock extension at times was borne by the customer and at times by the Bank. These lock extension costs have not had a material impact to our operations. In 2012, the Company also began entering into forward commitments at specific prices and settlement dates to deliver either: (1) residential mortgage loans for purchase by secondary market investors (i.e., Freddie Mac or Fannie Mae), or (2) mortgage-backed securities to broker/dealers. The purpose of these forward commitments is to offset the movement in interest rates between the execution of its residential mortgage rate lock commitments with borrowers and the sale of those loans to the secondary market investor. There were no counterparty default losses on forward contracts during 2014 or 2013. Market risk with respect to forward contracts arises principally from changes in the value of contractual positions due to changes in interest rates. The Company limits its exposure to market risk by monitoring differences between commitments to customers and forward contracts with market investors and securities broker/dealers. In the event the Company has forward delivery contract commitments in excess of available mortgage loans, the transaction is completed by either paying or receiving a fee to or from the investor or broker/dealer equal to the increase or decrease in the market value of the forward contract. Changes in the value of rate lock commitments are recorded as assets and liabilities as explained in Note 1: "Derivative Instruments."

NOTE 28: DERIVATIVES AND HEDGING

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. The Company obtains dealer quotations to value its derivative contracts.

The Company's predominant derivative and hedging activities involve interest rate swaps related to certain term loans and forward sales contracts associated with mortgage banking activities. Generally, these instruments help the Company 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 Designated in Hedge Relationships

The Company's 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. The Company has hedged exposure to changes in the fair value of certain fixed rate loans through the use of interest rate swaps. For a qualifying fair value hedge, changes in the value

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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.

In a program brought to Banner Bank through its merger with F&M Bank in 2007, customers received fixed interest rate commercial loans and the Bank subsequently hedged that fixed rate loan by entering into an interest rate swap with a dealer counterparty. The Bank receives fixed rate payments from the customers on the loans and makes similar fixed rate payments to the dealer counterparty on the swaps in exchange for variable rate payments based on the one-month LIBOR index. Some of these interest rate swaps are designated as fair value hedges. Through application of the “short cut method of accounting,” there is an assumption that the hedges are effective. The Bank discontinued originating interest rate swaps under this program in 2008.

As of December 31, 2014 and December 31, 2013, the notional values or contractual amounts and fair values of the Company's derivatives designated in hedge relationships were as follows (in thousands):

	Asset Derivatives				Liability Derivatives			
	December 31, 2014		December 31, 2013		December 31, 2014		December 31, 2013	
	Notional/ Contract Amount	Fair Value [1]	Notional/ Contract Amount	Fair Value [1]	Notional/ Contract Amount	Fair Value [2]	Notional/ Contract Amount	Fair Value [2]
Interest rate swaps	$7,089	$1,165	$7,420	$1,295	$7,089	$1,165	$7,420	$1,295

[1] Included in Loans Receivable on the Consolidated Statement of Financial Condition.
[2] Included in Other Liabilities on the Consolidated Statement of Financial Condition.

Derivatives Not Designated in Hedge Relationships

Interest Rate Swaps: Banner Bank, has been using an interest rate swap program for commercial loan customers, termed the Back-to-Back Program, since 2010. In the Back-to-Back Program, the Bank provides the client with a variable rate loan and enters into an interest rate swap in which the client receives a variable rate payment in exchange for a fixed rate payment. The Bank offsets its 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. There are also a few interest rate swaps from prior to 2009 that were not designated in hedge relationships that are included in these totals. 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 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 rate lock commitments with potential borrowers to originate loans that are intended to be sold and for closed loans that are awaiting sale and delivery into the secondary market.

Written loan commitments that relate to the origination of mortgage loans that will be held for resale are considered free-standing derivatives and do not qualify for hedge accounting. Written loan commitments generally have a term of up to 60 days before the closing of the loan. The loan commitment does not bind the potential borrower to enter into the loan, nor does it guarantee that the Company will approve the potential borrower for the loan. Therefore, when determining fair value, the Company makes estimates of expected “fallout” (loan commitments not expected to close), using models which consider cumulative historical fallout rates, current market interest rates and other factors.

Written loan commitments in which the borrower has locked in an interest rate results in market risk to the Company to the extent market interest rates change from the rate quoted to the borrower. The Company economically hedges the risk of changing interest rates associated with its interest rate lock commitments by entering into forward sales contracts.

Mortgage loans which are held for sale are subject to changes in fair value due to fluctuations in interest rates from the loan's closing date through the date of sale of the loans into the secondary market. Typically, the fair value of these loans declines when interest rates increase and rises when interest rates decrease. To mitigate this risk, the Company enters into forward sales contracts on a significant portion of these loans to provide an economic hedge against those changes in fair value. Mortgage loans held for sale and the forward sales contracts are recorded at fair value with ineffective changes in value recorded in current earnings as loan sales and servicing income.

As of December 31, 2014 and December 31, 2013, the notional values or contractual amounts and fair values of the Company's derivatives not designated in hedge relationships were as follows (in thousands):

	Asset Derivatives				Liability Derivatives			
	December 31, 2014		December 31, 2013		December 31, 2014		December 31, 2013	
	Notional/ Contract Amount	Fair Value [1]	Notional/ Contract Amount	Fair Value [1]	Notional/ Contract Amount	Fair Value [2]	Notional/ Contract Amount	Fair Value [2]
Interest rate swaps	$134,512	$5,125	$135,122	$3,651	$134,512	$5,125	$135,122	$3,651
Mortgage loan commitments	29,311	317	14,107	57	—	—	7,326	43
Forward sales contracts	—	—	22,526	73	33,174	198	—	—
	$163,823	$5,442	$171,755	$3,781	$167,686	$5,323	$142,448	$3,694

(1) Included in Other Assets on the Consolidated Statements of Financial Condition, with the exception of those interest rate swaps from prior to 2009 that were not designated in hedge relationships (with a fair value of $558,000 at December 31, 2014 and $791,000 at December 31, 2013), which are included in Loans Receivable.

(2) Included in Other Liabilities on the Consolidated Statements of Financial Condition.

Gains (losses) recognized in income on non-designated hedging instruments for the years ended December 31, 2014 and 2013 were as follows (in thousands):

		For the Year Ended December 31	
	Location on Income Statement	2014	2013
Mortgage loan commitments	Mortgage banking operations	$221	$(174)
Forward sales contracts	Mortgage banking operations	(188)	310
		$33	$136

The Company is 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 management does 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, Banner Bank could be required to settle its obligations under certain of its 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 Banner Bank had breached any of these provisions at December 31, 2014 or December 31, 2013, it could have been required to settle its obligations under the agreements at the termination value. As of December 31, 2014 and 2013, the termination value of derivatives in a net liability position related to these agreements was $6.3 million and $2.7 million, respectively. The Company generally posts collateral against derivative liabilities in the form of government agency-issued bonds, mortgage-backed securities, or commercial mortgage-backed securities. Collateral posted against derivative liabilities was $11.1 million and $8.9 million as of December 31, 2014 and 2013, respectively.

Derivative assets and liabilities are recorded at fair value on the balance sheet and do not take into account the effects of master netting agreements. Master netting agreements allow the Company 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.

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The following table illustrates the potential effect of the Company's derivative master netting arrangements, by type of financial instrument, on the Company's Consolidated Statements of Financial Condition as of December 31, 2014 and December 31, 2013 (in thousands):

	December 31, 2014					
				Gross Amounts of Financial Instruments Not Offset in the Statement of Financial Condition		
	Gross Amounts Recognized	Amounts offset in the Statement of Financial Condition	Net Amounts in the Statement of Financial Condition	Netting Adjustment Per Applicable Master Netting Agreements	Fair Value of Financial Collateral in the Statement of Financial Condition	Net Amount
Derivative assets						
Interest rate swaps	$6,290	$—	$6,290	$(6)	$—	$6,284
	$6,290	$—	$6,290	$(6)	$—	$6,284
Derivative liabilities						
Interest rate swaps	$6,290	$—	$6,290	$(6)	$(6,279)	$5
	$6,290	$—	$6,290	$(6)	$(6,279)	$5

	December 31, 2013					
				Gross Amounts of Financial Instruments Not Offset in the Statement of Financial Condition		
	Gross Amounts Recognized	Amounts offset in the Statement of Financial Condition	Net Amounts in the Statement of Financial Condition	Netting Adjustment Per Applicable Master Netting Agreements	Fair Value of Financial Collateral in the Statement of Financial Condition	Net Amount
Derivative assets						
Interest rate swaps	$4,946	$—	$4,946	$(554)	$—	$4,392
	$4,946	$—	$4,946	$(554)	$—	$4,392
Derivative liabilities						
Interest rate swaps	$4,946	$—	$4,946	$(554)	$(2,657)	$1,735
	$4,946	$—	$4,946	$(554)	$(2,657)	$1,735

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BANNER CORPORATION

Exhibit	Index of Exhibits
2.1{a}	Agreement and Plan of Merger, dated as of November 5, 2014, by and among the Registrant, SKBHC Holdings LLC and Starbuck Bancshares, Inc. [incorporated herein by reference to Exhibit 2.1 to the Registrant's Current Report on Form 8-K filed on November 12, 2014 (File No. 000-26584)].
2.1{b}	Agreement and Plan of Merger dated as of August 7, 2014 by and between Banner Corporation and Siuslaw Financial Group, Inc. [incorporated herein by reference to Exhibit 2.1 to the Registrant's Current Report on Form 8-K filed on August 8, 2014 (File No. 000-26584)].
3{a}	Amended and Restated Articles of Incorporation of Registrant [incorporated by reference to the Registrant's Current Report on Form 8-K filed on April 28, 2010 (File No. 000-26584)], as amended on May 26, 2011 [incorporated by reference to the Current Report on Form 8-K filed on June 1, 2011 (File No. 000-26584)].
3{b}	Bylaws of Registrant [incorporated by reference to Exhibit 3.2 to the Current Report on Form 8-K filed on April 1, 2011 (File No. 000-26584)].
4{a}	Warrant to purchase shares of Company's common stock dated November 21, 2008 [incorporated by reference to the Registrant's Current Report on Form 8-K filed on November 24, 2008 (File No. 000-26584)]
10{a}	Executive Salary Continuation Agreement with Gary L. Sirmon [incorporated by reference to exhibits filed with the Annual Report on Form 10-K for the year ended March 31, 1996 (File No. 000-26584)].
10{b}	Amended and Restated Employment Agreement, with Mark J. Grescovich [incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed on June 4, 2013 (File No. 000-26584].
10{c}	1996 Stock Option Plan [incorporated by reference to Exhibit 99.1 to the Registration Statement on Form S-8 dated August 26, 1996 (File No. 333-10819)].
10{d}	Supplemental Retirement Plan as Amended with Jesse G. Foster [incorporated by reference to exhibits filed with the Annual Report on Form 10-K for the year ended March 31, 1997 (File No. 000-26584)].
10{e}	Supplemental Executive Retirement Program Agreement with D. Michael Jones [incorporated by reference to exhibits filed with the Annual Report on Form 10-K for the year ended December 31, 2003 (File No. 000-26584)].
10{f}	Form of Supplemental Executive Retirement Program Agreement with Gary Sirmon, Michael K. Larsen, Lloyd W. Baker, Cynthia D. Purcell and Richard B. Barton [incorporated by reference to exhibits filed with the Annual Report on Form 10-K for the year ended December 31, 2001 and the exhibits filed with the Form 8-K on May 6, 2008 (File No. 000-26584)].
10{g}	1998 Stock Option Plan [incorporated by reference to exhibits filed with the Registration Statement on Form S-8 dated February 2, 1999 (File No. 333-71625)].
10{h}	2001 Stock Option Plan [incorporated by reference to Exhibit 99.1 to the Registration Statement on Form S-8 dated August 8, 2001 (File No. 333-67168)].

10{i}	Form of Employment Contract entered into with Lloyd W. Baker, Cynthia D. Purcell, Richard B. Barton and Douglas M. Bennett [incorporated by reference to exhibits filed with the Form 8-K on June 25, 2014 (File No. 000-26584)].
10{j}	2004 Executive Officer and Director Stock Account Deferred Compensation Plan [incorporated by reference to exhibits filed with the Annual Report on Form 10-K for the year ended December 31, 2005 (File No. 000-26584)].
10{k}	2004 Executive Officer and Director Investment Account Deferred Compensation Plan [incorporated by reference to exhibits filed with the Annual Report on Form 10-K for the year ended December 31, 2005 (File No. 000-26584)].
10{l}	Long-Term Incentive Plan and Form of Repricing Agreement [incorporated by reference to the exhibits filed with the Form 8-K on May 6, 2008 (File No. 000-26584)].
10{m}	2005 Executive Officer and Director Stock Account Deferred Compensation Plan [incorporated by reference to exhibits filed with the Annual Report on Form 10-K for the year ended December 31, 2008 (File No. 000-26584)].
10{n}	Entry into an Indemnification Agreement with each of the Registrant's Directors [incorporated by reference to exhibits filed with the Form 8-K on January 29, 2010 (File No. 000-26584)].
10{o}	2012 Restricted Stock and Incentive Bonus Plan [incorporated by reference to Appendix B to the Registrant's Definitive Proxy Statement on Schedule 14A filed on March 19, 2013 (File No. 000-26584)].
10{p}	Form of Performance-Based Restricted Stock Award Agreement [incorporated by reference to Exhibit 10.1 included in the Registrant's Current Report on Form 8-K filed on June 4, 2013 (File No. 000-26584)].
10{q}	Form of Time-Based Restricted Stock Award Agreement [incorporated by reference to Exhibit 10.1 included in the Registrant's Current Report on Form 8-K filed on June 4, 2013 (File No. 000-26584)].
10{r}	2014 Omnibus Incentive Plan [incorporated by reference as Appendix C to the Registrant's Definitive Proxy Statement on Schedule 14A filed on March 24, 2014 (File No. 000-26584)].

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10{s}	Forms of Equity-Based Award Agreements: Incentive Stock Option Award Agreement, Non-Qualified Stock Option Award Agreement, Restricted Stock Award Agreement, Restricted Stock Unit Award Agreement, Stock Appreciation Right Award Agreement, and Performance Unit Award Agreement [incorporated by reference to Exhibits 10.2 - 10.7 included in the Registration Statement on Form S-8 dated May 9, 2014 (File No. 333-195835)].
10{t}	Employment agreement entered into with Johan Mehlum [incorporated by reference to Exhibit 10.1 included in the Registration Statement on Form S-4 dated October 8, 2014 (File No. 333-199211)].
10{u}	Employment agreement entered into with Lonnie Iholts [incorporated by reference to Exhibit 10.2 included in the Registration Statement on Form S-4 dated October 8, 2014 (File No. 333-199211)].
10{v}	Investor Letter Agreement dated as of November 5, 2014 by and between Banner Corporation, and Oaktree Principal Fund V (Delaware), L.P. and certain of its affiliates (incorporated herein by reference to Exhibit 2.1 to the Registrant's Current Report on Form 8-K filed on November 12, 2014 (File No. 000-26584)].
10{w}	Investor Letter Agreement dated as of November 5, 2014 by and between Banner Corporation, and Friedman Fleischer and Lowe Capital Partners III, L.P. and certain of its affiliates (incorporated herein by reference to Exhibit 2.1 to the Registrant's Current Report on Form 8-K filed on November 12, 2014 (File No. 000-26584)].
10{x}	Investor Letter Agreement dated as of November 5, 2014 by and between Banner Corporation, and GS Capital Partners VI Fund L.P. and certain of its affiliates (incorporated herein by reference to Exhibit 2.1 to the Registrant's Current Report on Form 8-K filed on November 12, 2014 (File No. 000-26584)]
14	Code of Ethics [incorporated by reference to exhibits filed with the Annual Report on Form 10-K for the year ended December 31, 2004 (File No. 000-26584)].
21	Subsidiaries of the Registrant.
23.1	Consent of Registered Independent Public Accounting Firm – Moss Adams LLP.
31.1	Certification of Chief Executive Officer pursuant to the Securities Exchange Act Rules 13a-14(a) and 15d-14(a) as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification of Chief Financial Officer pursuant to the Securities Exchange Act Rules 13a-14(a) and 15d-14(a) as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32	Certificate of Chief Executive Officer and Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101	The following materials from Banner Corporation’s Annual Report on Form 10-K for the year ended December 31, 2014, formatted in Extensible Business Reporting Language (XBRL): (a) Consolidated Balance Sheets; (b) Consolidated Statements of Operations; (c) Consolidated Statements of Comprehensive Income; (d) Consolidated Statements of Shareholders' Equity; (e) Consolidated Statements of Cash Flows; and (f) Notes to Consolidated Financial Statements. *

* Pursuant to Rule 406T of Regulation S-T, these interactive data files are deemed not filed or part of a registration statement or prospectus for purposes of Sections 11 or 12 of the Securities Act of 1933 or Section 18 of the Securities Exchange Act of 1934, as amended, and otherwise are not subject to liability under those sections.

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