HomeStreet, Inc.
Form 10-Q
August 08, 2014

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

FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF
THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended: June 30, 2014
Commission file number: 001-35424

HOMESTREET, INC.
(Exact name of registrant as specified in its charter)

Washington	91-0186600
(State or other jurisdiction of incorporation)	(IRS Employer Identification No.)

601 Union Street, Suite 2000
Seattle, Washington 98101
(Address of principal executive offices)
(Zip Code)
(206) 623-3050
(Registrant's telephone number, including area code)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x No o

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

Large Accelerated Filer	o	Accelerated Filer	x
Non-accelerated Filer	o	Smaller Reporting Company	o

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

The number of outstanding shares of the registrant's common stock as of July 31, 2014 was 14,852,971.

PART I – FINANCIAL INFORMATION

ITEM 1 FINANCIAL STATEMENTS

Unless we state otherwise or the content otherwise requires, references in this Form 10-Q to “HomeStreet,” “we,” “our,” “us” or the “Company” refer collectively to HomeStreet, Inc., a Washington corporation, HomeStreet Bank (“Bank”), HomeStreet Capital Corporation and other direct and indirect subsidiaries of HomeStreet, Inc.

PART I – FINANCIAL INFORMATION
ITEM 1. FINANCIAL STATEMENTS

HOMESTREET, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION
(Unaudited)

(in thousands, except share data)	June 30, 2014	December 31, 2013
ASSETS		
Cash and cash equivalents (including interest-bearing instruments of $57,392 and $9,436)	$74,991	$ 33,908
Investment securities (includes $436,971 and $481,683 carried at fair value)	454,966	498,816
Loans held for sale (includes $536,658 and $279,385 carried at fair value)	549,440	279,941
Loans held for investment (net of allowance for loan losses of $21,926 and $23,908)	1,812,895	1,871,813
Mortgage servicing rights (includes $108,869 and $153,128 carried at fair value)	117,991	162,463
Other real estate owned	11,083	12,911
Federal Home Loan Bank stock, at cost	34,618	35,288
Premises and equipment, net	43,896	36,612
Goodwill	11,945	12,063
Other assets	123,851	122,239
Total assets	$3,235,676	$ 3,066,054
LIABILITIES AND SHAREHOLDERS’ EQUITY		
Liabilities:		
Deposits	$2,417,712	$ 2,210,821
Federal Home Loan Bank advances	384,090	446,590
Securities sold under agreements to repurchase	14,681	—
Accounts payable and other liabilities	69,087	77,906
Long-term debt	61,857	64,811
Total liabilities	2,947,427	2,800,128
Shareholders’ equity:		
Preferred stock, no par value, authorized 10,000 shares, issued and outstanding, 0 shares and 0 shares	—	—
Common stock, no par value, authorized 160,000,000, issued and outstanding, 14,849,692 shares and 14,799,991 shares	511	511
Additional paid-in capital	95,923	94,474
Retained earnings	192,972	182,935
Accumulated other comprehensive income	(1,157)	(11,994)
Total shareholders' equity	288,249	265,926
Total liabilities and shareholders' equity	$3,235,676	$ 3,066,054

See accompanying notes to interim consolidated financial statements (unaudited).

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HOMESTREET, INC. AND SUBSIDIARIES
INTERIM CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
(in thousands, except share data)	2014	2013	2014	2013
Interest income:				
Loans	$23,419	$17,446	$46,102	$35,495
Investment securities	2,664	2,998	5,634	5,657
Other	142	24	299	54
	26,225	20,468	52,035	41,206
Interest expense:				
Deposits	2,356	2,367	4,716	5,856
Federal Home Loan Bank advances	444	387	857	680
Securities sold under agreements to repurchase	1	11	1	11
Long-term debt	265	283	580	1,999
Other	12	5	22	10
	3,078	3,053	6,176	8,556
Net interest income	23,147	17,415	45,859	32,650
Provision (reversal of provision) for credit losses	—	400	(1,500)	2,400
Net interest income after provision for credit losses	23,147	17,015	47,359	30,250
Noninterest income:				
Net gain on mortgage loan origination and sale activities	41,794	52,424	67,304	106,379
Mortgage servicing income	10,184	2,183	18,129	5,255
Income from WMS Series LLC	246	993	53	1,613
Gain (loss) on debt extinguishment	11	—	(575)	—
Depositor and other retail banking fees	917	761	1,732	1,482
Insurance agency commissions	232	190	636	370
(Loss) gain on sale of investment securities available for sale (includes unrealized gain (loss) reclassified from accumulated other comprehensive income of $(20) and $238 for the three months ended June 30, 2014 and 2013, and $693 and $190 for the six months ended June 30, 2014 and 2013, respectively)	(20)	238	693	190
Other	286	767	385	1,210
	53,650	57,556	88,357	116,499
Noninterest expense:				
Salaries and related costs	40,606	38,579	76,077	73,641
General and administrative	11,145	10,270	21,267	21,200
Legal	542	599	941	1,210
Consulting	603	763	1,554	1,459
Federal Deposit Insurance Corporation assessments	572	143	1,192	710
Occupancy	4,675	3,381	9,107	6,183
Information services	4,862	3,574	9,377	6,570
Net cost of operation and sale of other real estate owned	(34)	(597)	(453)	1,538
	62,971	56,712	119,062	112,511
Income before income taxes	13,826	17,859	16,654	34,238
Income tax expense (includes reclassification adjustments of $(7) and $83 for the three months ended	4,464	5,791	4,991	11,230

June 30, 2014 and 2013, and $243 and $66 for the six months ended June 30, 2014 and 2013, respectively)				
NET INCOME	$9,362	$12,068	$11,663	$23,008
Basic income per share	$0.63	$0.84	$0.79	$1.60
Diluted income per share	$0.63	$0.82	$0.78	$1.56
Basic weighted average number of shares outstanding	14,800,853	14,376,580	14,792,638	14,368,135
Diluted weighted average number of shares outstanding	14,954,998	14,785,481	14,956,079	14,794,805

See accompanying notes to interim consolidated financial statements (unaudited).

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HOMESTREET, INC. AND SUBSIDIARIES
INTERIM CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)
(Unaudited)

(in thousands)	Three Months Ended June 30, 2014	Three Months Ended June 30, 2013	Six Months Ended June 30, 2014	Six Months Ended June 30, 2013
Net income	$9,362	$12,068	$11,663	$23,008
Other comprehensive income (loss), net of tax:				
Unrealized gain (loss) on investment securities available for sale:				
Unrealized holding gain (loss) arising during the period, net of tax expense (benefit) of $2,537 and $(7,737) for the three months ended June 30, 2014 and 2013, and $6,078 and $(9,483) for the six months ended June 30, 2014 and 2013, respectively	4,713	(14,367)	11,288	(17,610)
Reclassification adjustment for net gains included in net income, net of tax expense (benefit) of $(7) and $83 for the three months ended June 30, 2014 and 2013, and $243 and $66 for the six months ended June 30, 2014 and 2013, respectively	12	(155)	(451)	(124)
Other comprehensive income (loss)	4,725	(14,522)	10,837	(17,734)
Comprehensive income (loss)	$14,087	$(2,454)	$22,500	$5,274

See accompanying notes to interim consolidated financial statements (unaudited).

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HOMESTREET, INC. AND SUBSIDIARIES
INTERIM CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY
(Unaudited)

(in thousands, except share data)	Number of shares	Common stock	Additional paid-in capital	Retained earnings	Accumulated other comprehensive income (loss)	Total
Balance, January 1, 2013	14,382,638	$511	$90,189	$163,872	$ 9,190	$263,762
Net income	—	—	—	23,008	—	23,008
Dividends declared ($0.11 per share)	—	—	—	(1,580)	—	(1,580)
Share-based compensation expense	—	—	783	—	—	783
Common stock issued	24,038	—	82	—	—	82
Other comprehensive loss	—	—	—	—	(17,734)	(17,734)
Balance, June 30, 2013	14,406,676	$511	$91,054	$185,300	$ (8,544)	$268,321
Balance, January 1, 2014	14,799,991	$511	$94,474	$182,935	$ (11,994)	$265,926
Net income	—	—	—	11,663	—	11,663
Dividends declared ($0.11 per share)	—	—	—	(1,626)	—	(1,626)
Share-based compensation expense	—	—	1,199	—	—	1,199
Common stock issued	49,701	—	250	—	—	250
Other comprehensive income	—	—	—	—	10,837	10,837
Balance, June 30, 2014	14,849,692	$511	$95,923	$192,972	$ (1,157)	$288,249

See accompanying notes to interim consolidated financial statements (unaudited).

HOMESTREET, INC. AND SUBSIDIARIES
INTERIM CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

(in thousands)	Six Months Ended June 30, 2014		2013	
CASH FLOWS FROM OPERATING ACTIVITIES:				
Net income	$11,663		$23,008	
Adjustments to reconcile net income to net cash provided by (used in) operating activities:				
Depreciation, amortization and accretion	7,152		6,645	
(Reversal of) provision for credit losses	(1,500	)	2,400	
(Reversal of) provision for losses on other real estate owned	(19	)	339	
Fair value adjustment of loans held for sale	(12,660	)	32,661	
Origination of mortgage servicing rights	(20,365	)	(36,168	)
Change in fair value of mortgage servicing rights	20,736		(6,628	)
Net gain on sale of investment securities	(693	)	(190	)
Net fair value adjustment and gain on sale of other real estate owned	(712	)	(618	)
Loss on early retirement of long-term debt	575		—	
Net deferred income tax (benefit) expense	(15,623	)	10,883	
Share-based compensation expense	683		624	
Origination of loans held for sale	(1,512,392	)	(2,899,308	)
Proceeds from sale of loans originated as held for sale	1,282,100		3,016,255	
Cash used by changes in operating assets and liabilities:				
Increase in other assets	3,267		(33,328	)
Increase (decrease) in accounts payable and other liabilities	1,546		(1,457	)
Net cash (used in) provided by operating activities	(236,242	)	115,118	
CASH FLOWS FROM INVESTING ACTIVITIES:				
Purchase of investment securities	(30,780	)	(221,106	)
Proceeds from sale of investment securities	65,846		50,594	
Principal repayments and maturities of investment securities	24,455		18,079	
Proceeds from sale of other real estate owned	4,832		14,697	
Proceeds from sale of loans originated as held for investment	266,823		—	
Proceeds from sale of mortgage servicing rights	39,004		—	
Mortgage servicing rights purchased from others	(5	)	(10	)
Capital expenditures related to other real estate owned	—		(22	)
Origination of loans held for investment and principal repayments, net	(236,854	)	(113,428	)
Purchase of property and equipment	(11,348	)	(5,151	)
Net cash provided by (used in) investing activities	121,973		(256,347	)

(in thousands)	Six Months Ended June 30, 2014	2013
CASH FLOWS FROM FINANCING ACTIVITIES:		
Increase (decrease) in deposits, net	$206,891	$(13,711)
Proceeds from Federal Home Loan Bank advances	2,492,300	3,264,946
Repayment of Federal Home Loan Bank advances	(2,554,800)	(3,114,546)
Proceeds from securities sold under agreements to repurchase	14,681	159,790
Repayment of securities sold under agreements to repurchase	—	(159,790)
Proceeds from Federal Home Loan Bank stock repurchase	670	659
Repayment of long-term debt	(3,530)	—
Dividends paid	(1,626)	—
Proceeds from stock issuance, net	250	82
Excess tax benefits related to the exercise of stock options	516	159
Net cash provided by financing activities	155,352	137,589
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	41,083	(3,640)
CASH AND CASH EQUIVALENTS:		
Beginning of year	33,908	25,285
End of period	$74,991	$21,645
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:		
Cash paid during the period for:		
Interest	$7,159	$21,524
Federal and state income taxes (paid), net of refunds	7,610	6,714
Non-cash activities:		
Loans held for investment foreclosed and transferred to other real estate owned	2,922	6,225
Loans transferred from held for investment to held for sale	310,455	—
Loans transferred from held for sale to held for investment	17,095	—
Ginnie Mae loans recognized with the right to repurchase, net	$833	$2,127

See accompanying notes to interim consolidated financial statements (unaudited).

HomeStreet, Inc. and Subsidiaries
Notes to Interim Consolidated Financial Statements (Unaudited)

NOTE 1–SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:

HomeStreet, Inc. and its wholly owned subsidiaries (the "Company") is a diversified financial services company serving customers primarily in the Pacific Northwest, California and Hawaii. The Company is principally engaged in real estate lending, including mortgage banking activities, and commercial and consumer banking. The consolidated financial statements include the accounts of HomeStreet, Inc. and its wholly owned subsidiaries, HomeStreet Capital Corporation and HomeStreet Bank (the "Bank"), and the Bank's subsidiaries, HomeStreet/WMS, Inc., HomeStreet Reinsurance, Ltd., Continental Escrow Company, Union Street Holdings LLC and Lacey Gateway LLC. HomeStreet Bank was formed in 1986 and is a state-chartered savings bank.

The Company's accounting and financial reporting policies conform to accounting principles generally accepted in the United States of America (U.S. GAAP). Inter-company balances and transactions have been eliminated in consolidation. In preparing the consolidated financial statements, the Company is required to make estimates and assumptions that affect the reported amounts of assets and liabilities as of the date of the financial statements and revenues and expenses during the reporting periods and related disclosures. Although these estimates contemplate current conditions and how they are expected to change in the future, it is reasonably possible that actual conditions could be worse than anticipated in those estimates, which could materially affect the Company's results of operations and financial condition. Management has made significant estimates in several areas, and actual results could differ materially from those estimates. Certain amounts in the financial statements from prior periods have been reclassified to conform to the current financial statement presentation.

The information furnished in these unaudited interim financial statements reflects all adjustments that are, in the opinion of management, necessary for a fair statement of the results for the periods presented. These adjustments are of a normal recurring nature, unless otherwise disclosed in this Form 10-Q. The results of operations in the interim financial statements do not necessarily indicate the results that may be expected for the full year. The interim financial information should be read in conjunction with our Annual Report on Form 10-K for the year ended December 31, 2013, filed with the Securities and Exchange Commission ("2013 Annual Report on Form 10-K").

Purchase Accounting Adjustments

On December 6, 2013, the Company acquired two retail deposit branches and some related assets from AmericanWest Bank, a Washington state-chartered bank. On November 1, 2013, the Company completed its acquisition of Fortune Bank and YNB Financial Services Corp. ("YNB"), the parent of Yakima National Bank. The assets acquired and liabilities assumed in the acquisitions were accounted for under the acquisition method of accounting. The assets and liabilities, both tangible and intangible, were recorded at their estimated fair values as of the acquisition date. During the second quarter of 2014, the Company completed a more detailed fair value analysis of premises and equipment assumed in the acquisition of YNB and has determined that adjustments to the acquisition-date fair value are required. The Company also determined that adjustments were required to the provisional estimates for core deposit intangibles that were assumed in all three acquisitions. As a result of these adjustments, core deposit intangibles increased by $1.1 million, premises and equipment decreased by $740 thousand, and deferred tax liabilities increased by $280 thousand, resulting in a net decrease to goodwill of $118 thousand. These immaterial measurement period adjustments and corrections of accounting errors were made in the current period as they were not material to the current or prior periods.

Recent Accounting Developments

In January 2014, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") 2014-01, Investments - Equity Method and Joint Ventures (Topic 323): Accounting for Investments in Qualified Affordable Housing Projects. The ASU applies to all reporting entities that invest in qualified affordable housing projects through limited liability entities that are flow through entities for tax purposes. The amendments in this ASU eliminate the effective yield election and permit reporting entities to make an accounting policy election to account for their investments in qualified affordable housing projects using the proportional amortization method if certain conditions are met. Under the proportional amortization method, an entity amortizes the initial cost of the investment in proportion to the tax credits and other tax benefits received and recognizes the net investment performance in the income statement as a component of income tax expense (benefit). Those not electing the proportional amortization method would account for the investment using the equity method or cost method. The amendments in this ASU should be applied retrospectively to all periods presented and are effective for public business entities for annual periods and interim reporting periods within those annual periods, beginning after December 15, 2014, although early adoption is permitted. The Company elected to adopt this new accounting guidance as of January 1, 2014. It is being adopted prospectively, as the retrospective adjustments were not material. The Company's income tax expense for the six months ended June 30, 2014 includes discrete tax benefit items of $406 thousand related to the recognition of the cumulative effect for prior years of adoption of this new accounting guidance.

In January 2014, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) 2014-04, Reclassification of Residential Real Estate Collateralized Consumer Mortgage Loans upon foreclosure. The ASU clarifies that an in substance repossession or foreclosure occurs, and a creditor is considered to have received physical possession of residential real estate property collateralizing a consumer mortgage loan, upon either (1) the creditor obtaining legal title to the residential real estate property upon completion of a foreclosure or (2) the borrower conveying all interest in the residential real estate property to the creditor to satisfy that loan through completion of a deed in lieu of foreclosure or through a similar legal agreement. Additionally, the amendments require interim and annual disclosure of both (1) the amount of foreclosed residential real estate property held by the creditor and (2) the recorded investment in consumer mortgage loans collateralized by residential real estate property that are in the process of foreclosure according to local requirements of the applicable jurisdiction. The amendments are effective for annual and interim reporting periods beginning on or after December 15, 2014 and can be applied with a modified retrospective transition method or prospectively. The adoption of ASU No. 2014-04 is not expected to have a material impact on the Company's consolidated financial statements.

In May 2014, the FASB issued ASU 2014-09, Revenue from Contracts with Customers (Topic 606). This ASU clarifies the principles for recognizing revenue from contracts with customers. The new accounting guidance, which does not apply to financial instruments, is effective on a retrospective basis beginning on January 1, 2017. The Company does not expect the new guidance to have a material impact on its consolidated statements of financial condition or results of operation.

In June 2014, the FASB issued ASU 2014-11, Transfers and Servicing (Topic 860): Repurchase-to Maturity Transactions, Repurchase Financings, and Disclosures. The ASU applies to all entities that enter into repurchase-to-maturity transactions or repurchase financings. The amendments in this ASU require that repurchase-to-maturity transactions be accounted for as secured borrowings consistent with the accounting for other repurchase agreements. In addition, the amendments require separate accounting for a transfer of a financial asset executed contemporaneously with a repurchase agreement with the same counterparty (a repurchase financing), which will result in secured borrowing accounting for the repurchase agreement. The amendments require an entity to disclose information about transfers accounted for as sales in transactions that are economically similar to repurchase agreements, in which the transferor retains substantially all of the exposure to the economic return on the transferred financial asset throughout the term of the transaction. In addition the amendments require disclosure of the types of collateral pledged in repurchase agreements, securities lending transactions, and repurchase-to-maturity transactions and the tenor of those transactions. The amendments in this ASU are effective for public business entities for the first interim or annual period beginning after December 15, 2014. Early adoption is not permitted. The application of this guidance may require enhanced disclosures of the Company's repurchase agreements, but will have no impact on the Company's consolidated statements of financial condition or results of operations.

NOTE 2–INVESTMENT SECURITIES:

The following table sets forth certain information regarding the amortized cost and fair values of our investment securities available for sale.

	At June 30, 2014			
(in thousands)	Amortized cost	Gross unrealized gains	Gross unrealized losses	Fair value
Mortgage-backed securities:				
Residential	$111,460	$365	$(1,559)	$110,266
Commercial	13,209	465	—	13,674
Municipal bonds	124,772	2,085	(1,044)	125,813
Collateralized mortgage obligations:				
Residential	57,614	210	(1,057)	56,767
Commercial	16,325	—	(304)	16,021
Corporate debt securities	74,987	55	(2,622)	72,420
U.S. Treasury securities	41,966	44	—	42,010
	$440,333	$3,224	$(6,586)	$436,971

	At December 31, 2013			
(in thousands)	Amortized cost	Gross unrealized gains	Gross unrealized losses	Fair value
Mortgage-backed securities:				
Residential	$137,602	$187	$(3,879)	$133,910
Commercial	13,391	45	(3)	13,433
Municipal bonds	136,937	185	(6,272)	130,850
Collateralized mortgage obligations:				
Residential	93,112	85	(2,870)	90,327
Commercial	17,333	—	(488)	16,845
Corporate debt securities	75,542	—	(6,676)	68,866
U.S. Treasury securities	27,478	1	(27)	27,452
	$501,395	$503	$(20,215)	$481,683

Mortgage-backed securities ("MBS") and collateralized mortgage obligations ("CMO") represent securities issued by government sponsored entities ("GSEs"). Each of the MBS and CMO securities in our investment portfolio are guaranteed by Fannie Mae, Ginnie Mae or Freddie Mac. Municipal bonds are comprised of general obligation bonds (i.e., backed by the general credit of the issuer) and revenue bonds (i.e., backed by revenues from the specific project being financed) issued by various municipal corporations. As of June 30, 2014 and December 31, 2013, all securities held, including municipal bonds and corporate debt securities, were rated investment grade based upon external ratings where available and, where not available, based upon internal ratings which correspond to ratings as defined by Standard and Poor’s Rating Services (“S&P”) or Moody’s Investors Services (“Moody’s”). As of June 30, 2014 and December 31, 2013, substantially all securities held had ratings available by external ratings agencies.

Investment securities available for sale that were in an unrealized loss position are presented in the following tables based on the length of time the individual securities have been in an unrealized loss position.

	At June 30, 2014					
	Less than 12 months		12 months or more		Total	
(in thousands)	Gross unrealized losses	Fair value	Gross unrealized losses	Fair value	Gross unrealized losses	Fair value
Mortgage-backed securities:						
Residential	$(19)	$3,679	$(1,540)	$79,229	$(1,559)	$82,908
Municipal bonds	(48)	14,541	(996)	44,986	(1,044)	59,527
Collateralized mortgage obligations:						
Residential	(108)	9,354	(949)	32,299	(1,057)	41,653
Commercial	—	—	(304)	16,021	(304)	16,021
Corporate debt securities	(285)	4,770	(2,337)	59,547	(2,622)	64,317
	$(460)	$32,344	$(6,126)	$232,082	$(6,586)	$264,426

	At December 31, 2013					
	Less than 12 months		12 months or more		Total	
(in thousands)	Gross unrealized losses	Fair value	Gross unrealized losses	Fair value	Gross unrealized losses	Fair value
Mortgage-backed securities:						
Residential	$(3,767)	$98,717	$(112)	$6,728	$(3,879)	$105,445
Commercial	(3)	7,661	—	—	(3)	7,661
Municipal bonds	(5,991)	106,985	(281)	3,490	(6,272)	110,475
Collateralized mortgage obligations:						
Residential	(2,120)	63,738	(750)	15,081	(2,870)	78,819
Commercial	(488)	16,845	—	—	(488)	16,845
Corporate debt securities	(6,676)	68,844	—	—	(6,676)	68,844
U.S. Treasury securities	(27)	25,452	—	—	(27)	25,452
	$(19,072)	$388,242	$(1,143)	$25,299	$(20,215)	$413,541

The Company has evaluated securities available for sale that are in an unrealized loss position and has determined that the decline in value is temporary and is related to the change in market interest rates since purchase. The decline in value is not related to any issuer- or industry-specific credit event. As of June 30, 2014 and December 31, 2013, the Company does not expect any credit losses on its debt securities. In addition, as of June 30, 2014 and December 31, 2013, the Company had not made a decision to sell any of its debt securities held, nor did the Company consider it more likely than not that it would be required to sell such securities before recovery of their amortized cost basis. The Company did not hold any marketable equity securities as of June 30, 2014 and December 31, 2013.

The following tables present the fair value of investment securities available for sale by contractual maturity along with the associated contractual yield for the periods indicated below. Contractual maturities for mortgage-backed securities and collateralized mortgage obligations as presented exclude the effect of expected prepayments. Expected maturities will differ from contractual maturities because borrowers may have the right to prepay obligations before the underlying mortgages mature. The weighted-average yield is computed using the contractual coupon of each security weighted based on the fair value of each security and does not include adjustments to a tax equivalent basis.

	At June 30, 2014									
	Within one year		After one year through five years		After five years through ten years		After ten years		Total	
(in thousands)	Fair Value	Weighted Average Yield	Fair Value	Weighted Average Yield	Fair Value	Weighted Average Yield	Fair Value	Weighted Average Yield	Fair Value	Weighted Average Yield
Mortgage-backed securities:										
Residential	$—	— %	$—	— %	$—	— %	$110,266	1.80 %	$110,266	1.80 %
Commercial	—	—	—	—	—	—	13,674	4.43	13,674	4.43
Municipal bonds	—	—	45	3.26	21,451	3.41	104,316	4.21	125,812	4.07
Collateralized mortgage obligations:										
Residential	—	—	—	—	—	—	56,767	2.09	56,767	2.09
Commercial	—	—	—	—	9,823	1.98	6,198	1.41	16,021	1.76
Corporate debt securities	—	—	—	—	41,206	3.35	31,214	3.77	72,420	3.53
U.S. Treasury securities	1,001	0.18	41,009	0.35	—	—	—	—	42,010	0.34
Total available for sale	$1,001	0.18 %	$41,054	0.35 %	$72,480	3.18 %	$322,435	2.92 %	$436,970	2.72 %

	At December 31, 2013									
	Within one year		After one year through five years		After five years through ten years		After ten years		Total	
(in thousands)	Fair Value	Weighted Average Yield	Fair Value	Weighted Average Yield	Fair Value	Weighted Average Yield	Fair Value	Weighted Average Yield	Fair Value	Weighted Average Yield
Mortgage-backed securities:										
Residential	$—	— %	$—	— %	$10,581	1.63 %	$123,329	1.82 %	$133,910	1.81 %
Commercial	—	—	—	—	—	—	13,433	4.51	13,433	4.51
Municipal bonds	—	—	—	—	19,598	3.51	111,252	4.29	130,850	4.17
Collateralized mortgage obligations:										
Residential	—	—	—	—	19,987	2.31	70,340	2.17	90,327	2.20
Commercial	—	—	—	—	5,270	1.90	11,575	1.42	16,845	1.57
	—	—	—	—	32,848	3.31	36,018	3.75	68,866	3.54

Corporate debt securities														
U.S. Treasury securities	1,001	0.18		26,451	0.30		—	—		—	—		27,452	0.29	
Total available for sale	$1,001	0.18	%	$26,451	0.30	%	$88,284	2.84	%	$365,947	2.92	%	$481,683	2.75	%

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Sales of investment securities available for sale were as follows.

	Three Months Ended June 30,		Six Months Ended June 30,	
(in thousands)	2014	2013	2014	2013
Proceeds	$11,541	$34,840	$65,846	$50,594
Gross gains	118	318	895	322
Gross losses	(137)	(80)	(201)	(132)

There were $49.4 million and $47.3 million in investment securities pledged to secure advances from the Federal Home Loan Bank of Seattle ("FHLB") at June 30, 2014 and December 31, 2013, respectively. At June 30, 2014 and December 31, 2013, there were $33.8 million and $37.7 million, respectively, of securities pledged to secure derivatives in a liability position. At June 30, 2014, there were $15.0 million of securities pledged under repurchase agreements and none at December 31, 2013.

Tax-exempt interest income on securities available for sale totaling $863 thousand and $1.4 million for the three months ended June 30, 2014 and 2013, respectively, and $1.8 million and $2.7 million for the six months ended June 30, 2014 and 2013, respectively, was recorded in the Company's consolidated statements of operations.

NOTE 3–LOANS AND CREDIT QUALITY:

For a detailed discussion of loans and credit quality, including accounting policies and the methodology used to estimate the allowance for credit losses, see Note 1, Summary of Significant Accounting Policies and Note 6, Loans and Credit Quality within our 2013 Annual Report on Form 10-K.

The Company's portfolio of loans held for investment is divided into two portfolio segments, consumer loans and commercial loans, which are the same segments used to determine the allowance for loan losses. Within each portfolio segment, the Company monitors and assesses credit risk based on the risk characteristics of each of the following loan classes: single family and home equity loans within the consumer loan portfolio segment and commercial real estate, multifamily, construction/land development and commercial business loans within the commercial loan portfolio segment.

Loans held for investment consist of the following:

(in thousands)	At June 30, 2014	At December 31, 2013
Consumer loans		
Single family	$749,204	$904,913
Home equity	136,181	135,650
	885,385	1,040,563
Commercial loans		
Commercial real estate	476,411	477,642
Multifamily	72,327	79,216
Construction/land development	219,282	130,465
Commercial business	185,177	171,054
	953,197	858,377

	1,838,582	1,898,940
Net deferred loan fees and discounts	(3,761)	(3,219)
	1,834,821	1,895,721
Allowance for loan losses	(21,926)	(23,908)
	$1,812,895	$1,871,813

Loans in the amount of $634.4 million and $800.5 million at June 30, 2014 and December 31, 2013, respectively, were pledged to secure borrowings from the FHLB as part of our liquidity management strategy. The FHLB does not have the right to sell or re-pledge these loans.

Concentrations of credit risk arise when a number of customers are engaged in similar business activities or activities in the same geographic region, or when they have similar economic features that would cause their ability to meet contractual obligations to be similarly affected by changes in economic conditions.

Loans held for investment are primarily secured by real estate located in the states of Washington, Oregon, California, Idaho and Hawaii. At June 30, 2014, we had concentrations representing 10% or more of the total portfolio by state and property type for the loan classes of single family, commercial real estate and construction/land development within the state of Washington, which represented 27.5%, 21.8% and 10.1% of the total portfolio, respectively. At December 31, 2013 we had concentrations representing 10% or more of the total portfolio by state and property type for the loan classes of single family and commercial real estate within the state of Washington, which represented 37.3% and 21.2% of the total portfolio, respectively. These loans were mostly located within the metropolitan area of Puget Sound, particularly within King County.

Credit Quality

Management considers the level of allowance for loan losses to be appropriate to cover credit losses inherent within the loans held for investment portfolio as of June 30, 2014. In addition to the allowance for loan losses, the Company maintains a separate allowance for losses related to unfunded loan commitments, and this amount is included in accounts payable and other liabilities on the consolidated statements of financial condition. Collectively, these allowances are referred to as the allowance for credit losses.

For further information on the policies that govern the determination of the allowance for loan losses levels, see Note 1, Summary of Significant Accounting Policies within our 2013 Annual Report on Form 10-K.

Activity in the allowance for credit losses was as follows.

	Three Months Ended June 30,		Six Months Ended June 30,	
(in thousands)	2014	2013	2014	2013
Allowance for credit losses (roll-forward):				
Beginning balance	$22,317	$28,594	$24,089	$27,751
Provision (reversal of provision) for credit losses	—	400	(1,500)	2,400
(Charge-offs), net of recoveries	(149)	(1,136)	(421)	(2,293)
Ending balance	$22,168	$27,858	$22,168	$27,858
Components:				
Allowance for loan losses	$21,926	$27,655	$21,926	$27,655
Allowance for unfunded commitments	242	203	242	203
Allowance for credit losses	$22,168	$27,858	$22,168	$27,858

Activity in the allowance for credit losses by loan portfolio and loan class was as follows.

	Three Months Ended June 30, 2014				
(in thousands)	Beginning balance	Charge-offs	Recoveries	(Reversal of) Provision	Ending balance
Consumer loans					
Single family	$9,406	$(172)	$25	$(148)	$9,111
Home equity	3,882	(136)	236	(465)	3,517
	13,288	(308)	261	(613)	12,628
Commercial loans					
Commercial real estate	4,309	(23)	100	(323)	4,063
Multifamily	965	—	—	(78)	887
Construction/land development	2,003	—	46	369	2,418
Commercial business	1,752	(288)	63	645	2,172
	9,029	(311)	209	613	9,540
Total allowance for credit losses	$22,317	$(619)	$470	$—	$22,168

	Three Months Ended June 30, 2013				
(in thousands)	Beginning balance	Charge-offs	Recoveries	(Reversal of) Provision	Ending balance
Consumer loans					
Single family	$14,478	$(1,141)	$171	$302	$13,810
Home equity	4,708	(299)	156	314	4,879
	19,186	(1,440)	327	616	18,689
Commercial loans					
Commercial real estate	5,958	(340)	—	105	5,723
Multifamily	635	—	—	55	690
Construction/land development	894	—	281	10	1,185
Commercial business	1,921	—	36	(386)	1,571
	9,408	(340)	317	(216)	9,169
Total allowance for credit losses	$28,594	$(1,780)	$644	$400	$27,858

	Six Months Ended June 30, 2014				
(in thousands)	Beginning balance	Charge-offs	Recoveries	(Reversal of) Provision	Ending balance
Consumer loans					
Single family	$11,990	$(283)	$41	$(2,637)	$9,111
Home equity	3,987	(559)	326	(237)	3,517
	15,977	(842)	367	(2,874)	12,628
Commercial loans					
Commercial real estate	4,012	(23)	156	(82)	4,063
Multifamily	942	—	—	(55)	887
Construction/land development	1,414	—	62	942	2,418
Commercial business	1,744	(288)	147	569	2,172
	8,112	(311)	365	1,374	9,540
Total allowance for credit losses	$24,089	$(1,153)	$732	$(1,500)	$22,168

	Six Months Ended June 30, 2013				
(in thousands)	Beginning balance	Charge-offs	Recoveries	(Reversal of) Provision	Ending balance
Consumer loans					
Single family	$13,388	$(1,862)	$246	$2,038	$13,810
Home equity	4,648	(1,138)	253	1,116	4,879
	18,036	(3,000)	499	3,154	18,689
Commercial loans					
Commercial real estate	5,312	(143)	—	554	5,723
Multifamily	622	—	—	68	690
Construction/land development	1,580	(148)	351	(598)	1,185
Commercial business	2,201	—	148	(778)	1,571
	9,715	(291)	499	(754)	9,169
Total allowance for credit losses	$27,751	$(3,291)	$998	$2,400	$27,858

The following table disaggregates our allowance for credit losses and recorded investment in loans by impairment methodology.

	At June 30, 2014					
(in thousands)	Allowance: collectively evaluated for impairment	Allowance: individually evaluated for impairment	Total	Loans: collectively evaluated for impairment	Loans: individually evaluated for impairment	Total
Consumer loans						
Single family	$8,235	$876	$9,111	$678,418	$70,786	$749,204
Home equity	3,439	78	3,517	133,787	2,394	136,181
	11,674	954	12,628	812,205	73,180	885,385
Commercial loans						
Commercial real estate	3,851	212	4,063	445,130	31,281	476,411
Multifamily	485	402	887	69,202	3,125	72,327
Construction/land development	2,418	—	2,418	213,439	5,843	219,282
Commercial business	1,212	960	2,172	181,594	3,583	185,177
	7,966	1,574	9,540	909,365	43,832	953,197
Total	$19,640	$2,528	$22,168	$1,721,570	$117,012	$1,838,582

	At December 31, 2013					
(in thousands)	Allowance: collectively evaluated for impairment	Allowance: individually evaluated for impairment	Total	Loans: collectively evaluated for impairment	Loans: individually evaluated for impairment	Total
Consumer loans						
Single family	$10,632	$1,358	$11,990	$831,730	$73,183	$904,913
Home equity	3,903	84	3,987	133,006	2,644	135,650
	14,535	1,442	15,977	964,736	75,827	1,040,563
Commercial loans						
Commercial real estate	4,012	—	4,012	445,766	31,876	477,642
Multifamily	515	427	942	76,053	3,163	79,216
Construction/land development	1,414	—	1,414	124,317	6,148	130,465
Commercial business	1,042	702	1,744	168,199	2,855	171,054
	6,983	1,129	8,112	814,335	44,042	858,377
Total	$21,518	$2,571	$24,089	$1,779,071	$119,869	$1,898,940

Impaired Loans

The following tables present impaired loans by loan portfolio segment and loan class.

(in thousands)	At June 30, 2014 Recorded investment (1)	Unpaid principal balance (2)	Related allowance
With no related allowance recorded:			
Consumer loans			
Single family	$38,056	$40,366	$—
Home equity	1,991	2,068	—
	40,047	42,434	—
Commercial loans			
Commercial real estate	26,185	29,383	—
Multifamily	508	508	—
Construction/land development	5,843	14,974	—
Commercial business	1,033	1,911	—
	33,569	46,776	—
	$73,616	$89,210	$—
With an allowance recorded:			
Consumer loans			
Single family	$32,730	$32,826	$876
Home equity	403	402	78
	33,133	33,228	954
Commercial loans			
Commercial real estate	5,096	5,325	212
Multifamily	2,617	2,795	402
Construction/land development	—	—	—
Commercial business	2,550	2,824	960
	10,263	10,944	1,574
	$43,396	$44,172	$2,528
Total:			
Consumer loans			
Single family(3)	$70,786	$73,192	$876
Home equity	2,394	2,470	78
	73,180	75,662	954
Commercial loans			
Commercial real estate	31,281	34,708	212
Multifamily	3,125	3,303	402
Construction/land development	5,843	14,974	—
Commercial business	3,583	4,735	960
	43,832	57,720	1,574
Total impaired loans	$117,012	$133,382	$2,528

(1) Includes partial charge-offs and nonaccrual interest paid.

(2) Unpaid principal balance does not include partial charge-offs or nonaccrual interest paid. Related allowance is calculated on net book balances not unpaid principal balances.

(3) Includes $67.8 million in performing troubled debt restructurings ("TDRs").

(in thousands)	At December 31, 2013 Recorded investment (1)	Unpaid principal balance (2)	Related allowance
With no related allowance recorded:			
Consumer loans			
Single family	$39,341	$41,935	$—
Home equity	1,895	1,968	—
	41,236	43,903	—
Commercial loans			
Commercial real estate	31,876	45,921	—
Multifamily	508	508	—
Construction/land development	6,148	15,299	—
Commercial business	1,533	7,164	—
	40,065	68,892	—
	$81,301	$112,795	$—
With an allowance recorded:			
Consumer loans			
Single family	$33,842	$33,900	$1,358
Home equity	749	749	84
	34,591	34,649	1,442
Commercial loans			
Multifamily	2,655	2,832	427
Commercial business	1,322	1,478	702
	3,977	4,310	1,129
	$38,568	$38,959	$2,571
Total:			
Consumer loans			
Single family(3)	$73,183	$75,835	$1,358
Home equity	2,644	2,717	84
	75,827	78,552	1,442
Commercial loans			
Commercial real estate	31,876	45,921	—
Multifamily	3,163	3,340	427
Construction/land development	6,148	15,299	—
Commercial business	2,855	8,642	702
	44,042	73,202	1,129
Total impaired loans	$119,869	$151,754	$2,571

(1) Includes partial charge-offs and nonaccrual interest paid.
(2) Unpaid principal balance does not include partial charge-offs or nonaccrual interest paid. Related allowance is calculated on net book balances not unpaid principal balances.
(3) Includes $70.3 million in performing TDRs.

The following table provides the average recorded investment in impaired loans by portfolio segment and class.

	Three Months Ended June 30,		Six Months Ended June 30,	
(in thousands)	2014	2013	2014	2013
Consumer loans				
Single family	$70,977	$81,628	$71,713	$79,194
Home equity	2,466	3,550	2,525	3,607
	73,443	85,178	74,238	82,801
Commercial loans				
Commercial real estate	31,771	28,191	31,806	27,952
Multifamily	3,135	3,204	3,144	3,210
Construction/land development	5,875	9,115	5,966	10,378
Commercial business	3,200	1,921	3,085	2,054
	43,981	42,431	44,001	43,594
	$117,424	$127,609	$118,239	$126,395

Credit Quality Indicators

Management regularly reviews loans in the portfolio to assess credit quality indicators and to determine appropriate loan classification and grading in accordance with applicable bank regulations. The following tables present designated loan grades by loan portfolio segment and loan class.

	At June 30, 2014				
(in thousands)	Pass	Watch	Special mention	Substandard	Total
Consumer loans					
Single family	$719,493	$230	$ 15,346	$14,135	$749,204
Home equity	134,225	368	422	1,166	136,181
	853,718	598	15,768	15,301	885,385
Commercial loans					
Commercial real estate	380,101	71,009	18,403	6,898	476,411
Multifamily	67,671	1,531	3,125	—	72,327
Construction/land development	209,293	6,923	92	2,974	219,282
Commercial business	161,215	19,482	558	3,922	185,177
	818,280	98,945	22,178	13,794	953,197
	$1,671,998	$99,543	$ 37,946	$29,095	$1,838,582

(in thousands)	At December 31, 2013 Pass	Watch	Special mention	Substandard	Total
Consumer loans					
Single family	$817,877	$53,711	$12,746	$20,579	$904,913
Home equity	132,086	1,442	276	1,846	135,650
	949,963	55,153	13,022	22,425	1,040,563
Commercial loans					
Commercial real estate	368,817	63,579	37,758	7,488	477,642
Multifamily	74,509	1,544	3,163	—	79,216
Construction/land development	121,026	3,414	2,895	3,130	130,465
Commercial business	145,760	20,062	586	4,646	171,054
	710,112	88,599	44,402	15,264	858,377
	$1,660,075	$143,752	$57,424	$37,689	$1,898,940

The Company considers ‘adversely classified assets’ to include loans graded as Substandard, Doubtful, and Loss as well as other real estate owned ("OREO"). As of June 30, 2014 and December 31, 2013, none of the Company's loans were rated Doubtful or Loss. The total amount of adversely classified assets was $40.2 million and $50.6 million as of June 30, 2014 and December 31, 2013, respectively. For a detailed discussion on credit quality indicators used by management, see Note 6, Loans and Credit Quality within our 2013 Annual Report on Form 10-K.

Nonaccrual and Past Due Loans

Loans are placed on nonaccrual status when the full and timely collection of principal and interest is doubtful, generally when the loan becomes 90 days or more past due for principal or interest payment or if part of the principal balance has been charged off. Loans whose repayments are insured by the Federal Housing Authority ("FHA") or guaranteed by the Department of Veterans' Affairs ("VA") are generally maintained on accrual status even if 90 days or more past due.

The following table presents an aging analysis of past due loans by loan portfolio segment and loan class.

(in thousands)	At June 30, 2014 30-59 days past due	60-89 days past due	90 days or more past due	Total past due	Current	Total loans	90 days or more past due and accruing(1)
Consumer loans							
Single family	$10,967	$3,943	$39,020	$53,930	$695,274	$749,204	$32,032
Home equity	209	368	1,166	1,743	134,438	136,181	—
	11,176	4,311	40,186	55,673	829,712	885,385	32,032
Commercial loans							
Commercial real estate	—	—	9,871	9,871	466,540	476,411	—
Multifamily	—	—	—	—	72,327	72,327	—
Construction/land development	—	72	—	72	219,210	219,282	—
Commercial business	759	837	3,172	4,768	180,409	185,177	—
	759	909	13,043	14,711	938,486	953,197	—
	$11,935	$5,220	$53,229	$70,384	$1,768,198	$1,838,582	$32,032

(1) FHA-insured and VA-guaranteed single family loans that are 90 days or more past due are maintained on accrual status if they are determined to have little to no risk of loss.

(in thousands)	At 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	90 days or more past due and accruing[1]
Consumer loans							
Single family	$6,466	$4,901	$55,672	$67,039	$837,874	$904,913	$46,811
Home equity	375	75	1,846	2,296	133,354	135,650	—
	6,841	4,976	57,518	69,335	971,228	1,040,563	46,811
Commercial loans							
Commercial real estate	—	—	12,257	12,257	465,385	477,642	—
Multifamily	—	—	—	—	79,216	79,216	—
Construction/land development	—	—	—	—	130,465	130,465	—
Commercial business	—	—	2,743	2,743	168,311	171,054	—
	—	—	15,000	15,000	843,377	858,377	—
	$6,841	$4,976	$72,518	$84,335	$1,814,605	$1,898,940	$46,811

(1) FHA-insured and VA-guaranteed single family loans that are 90 days or more past due are maintained on accrual status if they are determined to have little to no risk of loss.

The following tables present performing and nonperforming loan balances by loan portfolio segment and loan class.

(in thousands)	At June 30, 2014 Accrual	Nonaccrual		Total
Consumer loans				
Single family	$742,216	$6,988		$749,204
Home equity	135,015	1,166		136,181
	877,231	8,154		885,385
Commercial loans				
Commercial real estate	466,540	9,871		476,411
Multifamily	72,327	—		72,327
Construction/land development	219,282	—		219,282
Commercial business	182,005	3,172		185,177
	940,154	13,043	(1)	953,197
	$1,817,385	$21,197		$1,838,582

(1) Includes $6.5 million of nonperforming loans at June 30, 2014 that are guaranteed by the Small Business Association ("SBA").

	At December 31, 2013		
(in thousands)	Accrual	Nonaccrual	Total
Consumer loans			
Single family	$896,052	$8,861	$904,913