UMPQUA HOLDINGS CORP
Form 10-Q
November 06, 2007

Table of Contents

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
FORM 10-Q

þ **Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 for the quarterly period ended: September 30, 2007**

o **Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 for the transition period from __________ to __________.**

Commission File Number: 000-25597
Umpqua Holdings Corporation
(Exact Name of Registrant as Specified in Its Charter)

OREGON	**93-1261319**
(State or Other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification Number)

One SW Columbia Street, Suite 1200
Portland, Oregon 97258
(Address of Principal Executive Offices)(Zip Code)
(503) 727-4100
(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.

þ Yes o No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act. (Check one):

þ Large accelerated filer o Accelerated filer o Non-accelerated filer

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

o Yes þ No

Indicate the number of shares outstanding for each of the issuer s classes of common stock, as of the latest practical date:

Common stock, no par value: 59,941,599 shares outstanding as of October 31, 2007

UMPQUA HOLDINGS CORPORATION
FORM 10-Q
Table of Contents

PART I. FINANCIAL INFORMATION
Item 1. Financial Statements (unaudited)

UMPQUA HOLDINGS CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS
(UNAUDITED)

(in thousands, except shares)

	September 30, 2007	December 31, 2006
ASSETS		
Cash and due from banks	$ 148,434	$ 169,769
Temporary investments	46,787	165,879
Total cash and cash equivalents	195,221	335,648
Investment securities		
Trading	4,144	4,204
Available for sale, at fair value	911,883	715,187
Held to maturity, at amortized cost	7,116	8,762
Loans held for sale	19,964	16,053
Loans and leases	6,079,435	5,361,862
Allowance for loan and lease losses	(88,278)	(60,090)
Net loans and leases	5,991,157	5,301,772
Restricted equity securities	15,297	15,255
Premises and equipment, net	107,189	101,830
Goodwill and other intangible assets, net	767,210	679,493
Mortgage servicing rights, net	9,474	9,952
Other assets	197,156	156,080
Total assets	$ 8,225,811	$ 7,344,236
LIABILITIES AND SHAREHOLDERS EQUITY		
Deposits		
Noninterest bearing	$ 1,294,334	$ 1,222,107
Interest bearing	5,223,883	4,618,187
Total deposits	6,518,217	5,840,294
Securities sold under agreements to repurchase	52,883	47,985
Federal funds purchased	20,000	
Term debt	75,010	9,513
Junior subordinated debentures, at fair value	131,984	
Junior subordinated debentures, at amortized cost	104,947	203,688
Other liabilities	89,580	86,545
Total liabilities	6,992,621	6,188,025

COMMITMENTS AND CONTINGENCIES (NOTE 5)

SHAREHOLDERS EQUITY				
Preferred stock, no par value, 2,000,000 shares authorized; none issued and outstanding				
Common stock, no par value, 100,000,000 shares authorized; issued and outstanding: 59,864,335 in 2007 and 58,080,171 in 2006		987,543		930,867
Retained earnings		253,487		234,783
Accumulated other comprehensive loss		(7,840)		(9,439)
Total shareholders equity		1,233,190		1,156,211
Total liabilities and shareholders equity	$	8,225,811	$	7,344,236

See notes to condensed consolidated financial statements

3

Table of Contents

UMPQUA HOLDINGS CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF INCOME
(UNAUDITED)

(in thousands, except per share amounts)

	Three months ended September 30,		Nine months ended September 30,	
	2007	**2006**	**2007**	**2006**
INTEREST INCOME				
Interest and fees on loans	$ 116,111	$ 106,320	$ 331,889	$ 265,444
Interest and dividends on investment securities				
Taxable	9,137	6,797	25,376	20,201
Exempt from federal income tax	1,588	1,142	4,151	2,740
Dividends	96	105	249	205
Interest on temporary investments	929	374	2,439	837
Total interest income	127,861	114,738	364,104	289,427
INTEREST EXPENSE				
Interest on deposits	48,138	34,121	133,750	81,112
Interest on securities sold under agreements to repurchase and federal funds purchased	530	2,155	1,757	6,346
Interest on term debt	874	692	1,767	2,775
Interest on junior subordinated debentures	4,444	3,971	12,329	10,359
Total interest expense	53,986	40,939	149,603	100,592
Net interest income	73,875	73,799	214,501	188,835
PROVISION FOR LOAN AND LEASE LOSSES	20,420	2,352	23,916	2,427
Net interest income after provision for loan and lease losses	53,455	71,447	190,585	186,408
NON-INTEREST INCOME				
Service charges on deposit accounts	8,448	7,606	23,648	19,540
Brokerage commissions and fees	2,498	2,506	7,594	7,408
Mortgage banking revenue, net	1,366	1,445	5,772	5,792
Net loss on sale of investment securities	(13)		(10)	(1)
Other income	6,244	1,919	11,434	6,745
Total non-interest income	18,543	13,476	48,438	39,484
NON-INTEREST EXPENSE				
Salaries and employee benefits	28,005	26,387	85,172	71,525
Net occupancy and equipment	9,166	8,540	26,774	22,907
Communications	1,807	1,744	5,293	4,689
Marketing	1,982	1,780	4,405	4,596

Services	4,864	4,199	14,066	11,016
Supplies	984	925	2,572	2,276
Intangible amortization	1,767	1,195	4,400	2,533
Merger related expenses	263	2,451	3,200	4,358
Other expenses	4,055	3,465	10,968	9,009
Total non-interest expense	52,893	50,686	156,850	132,909
Income before income taxes	19,105	34,237	82,173	92,983
Provision for income taxes	5,928	11,381	28,421	33,069
Net income	$ 13,177	$ 22,856	$ 53,752	$ 59,914
Basic earnings per share	$ 0.22	$ 0.40	$ 0.90	$ 1.19
Diluted earnings per share	$ 0.22	$ 0.39	$ 0.89	$ 1.17

See notes to condensed consolidated financial statements

Table of Contents

UMPQUA HOLDINGS CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS EQUITY
(UNAUDITED)

(in thousands, except shares)

	Common Stock		Retained	Accumulated Other Comprehensive Income	
	Shares	Amount	Earnings	(Loss)	Total
BALANCE AT JANUARY 1, 2006	44,556,269	$ 564,579	$ 183,591	$ (9,909)	$ 738,261
Net income			84,447		84,447
Other comprehensive income, net of tax:					
Unrealized gains on securities arising during the year				470	470
Comprehensive income					$ 84,917
Stock-based compensation		1,932			1,932
Stock repurchased and retired	(6,142)	(179)			(179)
Issuances of common stock under stock plans and related tax benefit	784,715	10,814			10,814
Stock issued in connection with acquisition	12,745,329	353,721			353,721
Cash dividends ($0.60 per share)			(33,255)		(33,255)
Balance at December 31, 2006	58,080,171	$ 930,867	$ 234,783	$ (9,439)	$ 1,156,211
BALANCE AT JANUARY 1, 2007	58,080,171	$ 930,867	$ 234,783	$ (9,439)	$ 1,156,211
Adoption of fair value option junior subordinated debentures			(2,064)		(2,064)
Net income			53,752		53,752
Other comprehensive income, net of tax:					
Unrealized gains on securities arising during the period				1,599	1,599
Comprehensive income					$ 55,351
Stock-based compensation		2,596			2,596
Stock repurchased and retired	(4,048,387)	(96,075)			(96,075)
Issuances of common stock under stock plans and related tax benefit	668,978	8,043			8,043
	5,163,573	142,112			142,112

Stock issued in connection with acquisition					
Cash dividends ($0.55 per share)			(32,984)		(32,984)
Balance at September 30, 2007	59,864,335	$ 987,543	$ 253,487	$ (7,840)	$ 1,233,190

See notes to condensed consolidated financial statements

5

Table of Contents

UMPQUA HOLDINGS CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(UNAUDITED)

(in thousands)

	Three months ended September 30,		Nine months ended September 30,	
	2007	2006	2007	2006
Net income	$ 13,177	$ 22,856	$ 53,752	$ 59,914
Unrealized gains arising during the period on investment securities available for sale	12,425	16,008	2,665	1,617
Reclassification adjustment for losses realized in net income, (net of tax benefit of $5,000 and $4,000 for the three and nine months ended September 30, 2007, respectively)	8		6	1
Income tax expense related to unrealized gains/losses on investment securities, available for sale	(4,978)	(6,403)	(1,072)	(648)
Net unrealized gains on investment securities available for sale	7,455	9,605	1,599	970
Comprehensive income	$ 20,632	$ 32,461	$ 55,351	$ 60,884

See notes to condensed consolidated financial statements

6

Table of Contents

UMPQUA HOLDINGS CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(UNAUDITED)

(in thousands)

	Nine months ended September 30, 2007	2006
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	$ 53,752	$ 59,914
Adjustments to reconcile net income to net cash provided by operating activities:		
Restricted equity securities stock dividends	(180)	(205)
Amortization of investment premiums, net	152	907
Loss on sale of investment securities available-for-sale	10	1
Provision for loan and lease losses	23,916	2,427
Depreciation, amortization and accretion	9,295	8,503
Change in fair value of mortgage servicing rights	977	
Change in fair value of junior subordinated debentures	(4,531)	
Stock-based compensation	2,596	1,563
Net decrease (increase) in trading account assets	60	(36)
Origination of loans held for sale	(200,179)	(194,856)
Proceeds from sales of loans held for sale	196,521	186,873
Increase in mortgage servicing rights	(499)	(1,337)
Excess tax benefits from the exercise of stock options	(243)	(855)
Net (increase) decrease in other assets	(17,021)	23,665
Net decrease in other liabilities	(7,914)	(2,068)
Net cash provided by operating activities	56,712	84,496
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchases of investment securities available-for-sale	(219,303)	
Sales and maturities of investment securities available-for-sale	110,517	56,303
Maturities of investment securities held-to-maturity	1,628	2,237
Redemption of restricted equity securities	5,525	9,242
Net loan and lease originations	(300,243)	(457,625)
Proceeds from sales of loans	18,442	19,129
Proceeds from disposals of furniture and equipment	4,314	193
Purchases of premises and equipment	(6,997)	(8,196)
Sales of real estate owned		93
Cash acquired in merger, net of cash consideration paid	78,729	36,950
Net cash used by investing activities	(307,388)	(341,674)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Net increase in deposit liabilities	215,245	348,851
Net increase (decrease) in Federal funds purchased	20,000	(55,000)
Net increase in securities sold under agreements to repurchase	4,898	6,606

Term debt borrowings		600,000
Proceeds from the issuance of junior subordinated debentures	60,000	
Repayment of junior subordinated debentures	(36,084)	
Repayment of term debt	(33,637)	(605,087)
Dividends paid on common stock	(32,055)	(17,664)
Excess tax benefits from the exercise of stock options	243	855
Proceeds from stock options exercised	7,714	8,936
Retirement of common stock	(96,075)	(39)
Net cash provided by financing activities	110,249	287,458
Net (decrease) increase in cash and cash equivalents	(140,427)	30,280
Cash and cash equivalents, beginning of period	335,648	161,754
Cash and cash equivalents, end of period	$ 195,221	$ 192,034
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:		
Cash paid during the period for:		
Interest	$ 148,143	$ 95,172
Income taxes	$ 37,931	$ 38,808

See notes to condensed consolidated financial statements

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

Note 1 Summary of Significant Accounting Policies

The accounting and financial reporting policies of Umpqua Holdings Corporation (referred to in this report as we , our or the Company) conform to accounting principles generally accepted in the United States of America. The accompanying interim consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries, Umpqua Bank (Bank), and Strand, Atkinson, Williams & York, Inc. (Strand). All material inter-company balances and transactions have been eliminated. The consolidated financial statements have not been audited. A more detailed description of our accounting policies is included in the 2006 Annual Report filed on Form 10-K. There have been no significant changes to these policies, except due to adoption of Statement of Financial Accounting Standards (SFAS) No. 156, *Accounting for Servicing of Financial Assets an amendment of FASB Statement No. 140, Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities*, SFAS No. 157, *Fair Value Measurements*, SFAS No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities,* and FASB Interpretation No. (FIN) 48, *Accounting for Uncertainty in Income Taxes*, (FIN 48). The changes to accounting policies under these standards are described in detail in Notes 3, 4, 7 and 10. These interim condensed consolidated financial statements should be read in conjunction with the financial statements and related notes contained in the 2006 Annual Report filed on Form 10-K.

In management s opinion, all accounting adjustments necessary to accurately reflect the financial position and results of operations on the accompanying financial statements have been made. These adjustments include normal and recurring accruals considered necessary for a fair and accurate presentation. The results for interim periods are not necessarily indicative of results for the full year or any other interim period. Certain reclassifications of prior period amounts have been made to conform to current classifications.

Note 2 Business Combinations

On April 26, 2007, the Company acquired all of the outstanding common stock of North Bay Bancorp (North Bay) and its principal operating subsidiary, The Vintage Bank, along with its Solano Bank division. The results of North Bay s operations have been included in the consolidated financial statements since that date. This acquisition added North Bay s network of 10 Northern California branches, including locations in the Napa area and in the communities of St. Helena, American Canyon, Vacaville, Benicia, Vallejo and Fairfield, to our network of Northern California, Oregon and Washington locations. This merger was consistent with the Company s community banking expansion strategy and provided further opportunity to enter growth markets in Northern California.

The aggregate purchase price was $143.4 million and included 5.2 million common shares valued at $135.2 million, options to purchase 542,000 shares of common stock valued at $6.9 million and $1.1 million of direct merger costs. North Bay shareholders received 1.228 shares of the Company s common stock for each share of North Bay common stock (exchange ratio of 1.228:1). The value of the common shares issued was $26.18 per share based on the average closing market price of the Company s common stock for the fifteen trading days before the last five trading days before the merger. Outstanding North Bay stock options were converted (using the exchange ratio of 1.228:1) at a weighted average fair value of $12.78 per option.

The following table summarizes the purchase price allocation, including the estimated fair value of the assets acquired and liabilities assumed at the date of acquisition. Additional adjustments to the purchase price allocation may be required, specifically related to other assets, taxes and compensation adjustments.

Table of Contents

(in thousands)

		April 26, 2007
Assets Acquired:		
Cash and equivalents	$	78,729
Investment securities		85,589
Loans, net		437,863
Premises and equipment, net		12,940
Intangible assets		14,210
Goodwill		78,794
Other assets		19,481
Total assets acquired	$	727,606
Liabilities Assumed:		
Deposits	$	462,624
Term debt		99,227
Junior subordinated debentures		10,342
Other liabilities		13,301
Total liabilities assumed		585,494
Net Assets Acquired	$	142,112

The intangible assets represent the value ascribed to the long-term deposit relationships and merchant services portfolio income stream acquired. These intangible assets are being amortized on an accelerated basis over a weighted average estimated useful life of ten to fifteen years. The intangible assets are estimated not to have a significant residual value. Goodwill represents the excess of the total purchase price paid for North Bay over the fair values of the assets acquired, net of the fair values of liabilities assumed. Goodwill has been assigned to our Community Banking segment. Goodwill is not amortized, but is evaluated for possible impairment at least annually and more frequently if events and circumstances indicate that the asset might be impaired. No impairment losses were recognized in connection with intangible or goodwill assets during the period from acquisition to September 30, 2007. At September 30, 2007, goodwill recorded in connection with the North Bay acquisition was $77.2 million. The $1.6 million decrease from April 26, 2007 is primarily due to the recognition of a tax benefit upon exercise of fully vested acquired options.

The following table presents unaudited pro forma results of operations for the nine months ended September 30, 2007, and three and nine months ended September 30, 2006 as if the acquisition of North Bay had occurred on January 1, 2006. Any cost savings realized as a result of the North Bay merger are not reflected in the pro forma consolidated condensed statements of income. The pro forma results have been prepared for comparative purposes only and are not necessarily indicative of the results that would have been obtained had the acquisition actually occurred on January 1, 2006:

Table of Contents

Pro Forma Financial Information Unaudited
(in thousands, except per share data)

	Nine Months Ended September 30, 2007			
	Umpqua	North Bay (a)	Pro Forma Adjustments	Pro Forma Combined
Net interest income	$214,501	$8,732	$ 462(b)	$223,695
Provision for loan and lease losses	23,916			23,916
Non-interest income	48,438	1,434		49,872
Non-interest expense	156,850	6,985	(2,932)(c)	160,903
Income before income taxes	82,173	3,181	3,394	88,748
Provision for income taxes	28,421	1,054	1,358(d)	30,833
Net income	$ 53,752	$2,127	$ 2,036	$ 57,915
Earnings per share:				
Basic	$ 0.90			$ 0.93
Diluted	$ 0.89			$ 0.92
Average shares outstanding:				
Basic	59,790	1,772	404(e)	61,966
Diluted	60,450	1,839	419(e)	62,708

(a) North Bay amounts represent results from January 1, 2007 to acquisition date of April 26, 2007.

(b) Consists of additional net accretion of fair value adjustments related to the North Bay acquisition.

(c) Consists of merger related expenses of $3.2 million at Umpqua, adjusted for amortization of intangible assets and premises purchase accounting adjustment related to the North Bay acquisition.

(d) Income tax effect of pro forma adjustments at 40%.

(e) Additional shares issued at an exchange ratio of 1.228:1.

(in thousands, except per share data)

	Three Months Ended September 30, 2006			
	Umpqua	**North Bay**	**Pro Forma Adjustments**	**Pro Forma Combined**
Net interest income	$73,799	$6,956	$ 2(a)	$80,757
Provision for loan and lease losses	2,352			2,352
Non-interest income	13,476	1,239		14,715
Non-interest expense	50,686	5,388	600(b)	56,674
Income before income taxes	34,237	2,807	(598)	36,446
Provision for income taxes	11,381	931	(239) (c)	12,073
Net income	$22,856	$1,876	$ (359)	$24,373
Earnings per share:				
Basic	$ 0.40			$ 0.39
Diluted	$ 0.39			$ 0.38
Average shares outstanding:				
Basic	57,802	4,134	943(d)	62,879
Diluted	58,452	4,296	979(d)	63,727

(a) Consists of net accretion of fair value adjustments related to the North Bay acquisition.

(b) Consists of amortization of intangible assets and premises purchase accounting adjustment related to the North Bay acquisition.

(c) Income tax effect of pro forma adjustments at 40%.

(d) Additional shares issued at an exchange ratio of 1.228:1.

Table of Contents

(in thousands, except per share data)

	Nine Months Ended September 30, 2006			
	Umpqua	**North Bay**	**Pro Forma Adjustments**	**Pro Forma Combined**
Net interest income	$188,835	$21,651	$ (235)(a)	$210,251
Provision for loan and lease losses	2,427	200		2,627
Non-interest income	39,484	3,479		42,963
Non-interest expense	132,909	16,943	1,917(b)	151,769
Income before income taxes	92,983	7,987	(2,152)	98,818
Provision for income taxes	33,069	2,745	(861)(c)	34,953
Net income	$ 59,914	$ 5,242	$(1,291)	$ 63,865
Earnings per share:				
Basic	$ 1.19			$ 1.15
Diluted	$ 1.17			$ 1.13
Average shares outstanding:				
Basic	50,378	4,123	940(d)	55,441
Diluted	51,010	4,284	977(d)	56,271

(a) Consists of net accretion of fair value adjustments related to the North Bay acquisition.

(b) Consists of amortization of intangible assets and premises purchase accounting adjustment related to the North Bay acquisition.

(c) Income tax effect of pro forma adjustments at 40%.

(d) Additional shares issued at an exchange ratio of 1.228:1.

The following table summarizes activity in the Company s accrued restructuring charges, recorded in other liabilities, related to the North Bay acquisition from acquisition date of April 26, 2007 to September 30, 2007:

Accrued Restructuring Charges
(in thousands)

Beginning balance	$ 2,796
Utilization:	
Cash payments	(1,267)
Ending Balance	$ 1,529

The Company expects additional merger-related expenses incurred in connection with the North Bay acquisition to be insignificant.

On June 2, 2006, the Company acquired all of the outstanding common stock of Western Sierra Bancorp (Western Sierra) of Cameron Park, California, and its principal operating subsidiaries, Western Sierra Bank, Central California Bank, Lake Community Bank and Auburn Community Bank. The results of Western Sierra s operations have been included in the consolidated financial statements since that date. This acquisition added Western Sierra s complete network of 31 Northern California branches, including locations in the Sacramento, Auburn, Lakeport and Sonora areas, to our network of California, Oregon and Washington locations. This merger was consistent with the Company s community banking expansion strategy and provided further opportunity to enter growth markets in Northern California.

The aggregate purchase price was $353.7 million and included 12.7 million common shares valued at $343.0 million, and 723,000 stock options valued at $10.7 million. Western Sierra shareholders received 1.61 shares of the Company s common stock for each share of Western Sierra common stock (exchange ratio of 1.61:1). The value of the common shares issued was determined as $26.91 per share based on the average closing market price of the Company s common stock for the two trading days before and after the last trading day before public announcement of the merger. Outstanding Western Sierra stock options were converted (using the exchange ratio of 1.61:1) at a weighted average fair value of $14.80 per option.

The following table summarizes the purchase price allocation, including the estimated fair value of the assets acquired and liabilities assumed at the date of acquisition. Additional adjustments to the purchase price allocation may be required, specifically related to taxes.

Table of Contents

(in thousands)

		June 2, 2006
Assets Acquired:		
Cash and equivalents	$	36,978
Investment securities		76,229
Loans, net		1,009,860
Premises and equipment, net		10,109
Core deposit intangible asset		27,624
Goodwill		247,799
Other assets		83,519
Total assets acquired	$	1,492,118
Liabilities Assumed:		
Deposits	$	1,016,053
Term debt		59,030
Junior subordinated debentures		38,746
Other liabilities		24,540
Total liabilities assumed		1,138,369
Net Assets Acquired	$	353,749

The core deposit intangible asset represents the value ascribed to the long-term deposit relationships acquired. This intangible asset is being amortized on a straight-line basis over a weighted average estimated useful life of ten years. The core deposit intangible asset is estimated not to have a significant residual value. Goodwill represents the excess of the total purchase price paid for Western Sierra over the fair values of the assets acquired, net of the fair values of liabilities assumed. Goodwill has been assigned to our Community Banking segment. Goodwill is not amortized, but is evaluated for possible impairment at least annually and more frequently if events and circumstances indicate that the asset might be impaired. No impairment losses were recognized in connection with core deposit intangible or goodwill assets during the period from acquisition to September 30, 2007. At September 30, 2007, goodwill recorded in connection with the Western Sierra acquisition was $247.9 million.

The following table presents unaudited pro forma results of operations for the nine months ended September 30, 2006 as if the acquisition of Western Sierra had occurred on January 1, 2006. Any cost savings realized as a result of the Western Sierra merger are not reflected in the pro forma consolidated condensed statements of income. The pro forma results have been prepared for comparative purposes only and are not necessarily indicative of the results that would have been obtained had the acquisition actually occurred on January 1, 2006:

Table of Contents

Pro Forma Financial Information Unaudited
(in thousands, except per share data)

	Nine Months Ended September 30, 2006			
	Umpqua	Western Sierra (a)	Pro Forma Adjustments	Pro Forma Combined
Net interest income	$ 188,835	$ 25,834	$ (99)(b)	$ 214,570
Provision for loan and lease losses	2,427	350		2,777
Non-interest income	39,484	5,040		44,524
Non-interest expense	132,909	18,168	(3,270)(c)	147,807
Income before income taxes	92,983	12,356	3,171	108,510
Provision for income taxes	33,069	4,898	1,268(d)	39,235
Net income	$ 59,914	$ 7,458	$ 1,903	$ 69,275
Earnings per share:				
Basic	$ 1.19			$ 1.21
Diluted	$ 1.17			$ 1.19
Average shares outstanding:				
Basic	50,378	4,401	2,685(e)	57,464
Diluted	51,010	4,517	2,755(e)	58,282

(a) Western Sierra amounts represent results from January 1, 2006 to acquisition date of June 2, 2006.

(b) Consists of additional net accretion of fair value adjustments related to the Western Sierra acquisition.

(c) Consists of merger related expenses of $4.4 million, partially offset by additional core deposit intangible amortization of $1.1 million.

(d) Income tax effect of pro forma adjustments at 40%.

(e) Additional shares issued at an exchange ratio of 1.61:1.

The following table summarizes activity in the Company s accrued restructuring charges related to the Western Sierra acquisition which are recorded in other liabilities:

Accrued Restructuring Charges
(in thousands)

	Nine months ended September 30, 2007
Beginning balance	$ 4,369
Additions:	
Severance, retention and other compensation	217
Premises	1,093
Utilization:	
Cash payments	(2,416)
Ending Balance	$ 3,263

These accrued restructuring charges will be utilized by May 2012. No additional merger-related expenses are expected in connection with the Western Sierra or any other acquisition prior to Western Sierra.

Note 3 Mortgage Servicing Rights

SFAS No. 156, issued in March 2006, requires all separately recognized servicing assets and liabilities to be initially measured at fair value. In addition, entities are permitted to choose to either subsequently measure servicing rights at fair value and report changes in fair value in earnings, or amortize servicing rights in proportion to and over the period of the estimated net servicing income or loss and assess the rights for impairment. Beginning with the fiscal year in which an entity adopts SFAS No. 156, it may elect to subsequently measure a class of servicing assets and liabilities at fair value. The effect of remeasuring an existing class of servicing assets and liabilities at fair value is to be reported as a cumulative-effect adjustment to retained earnings as of the beginning of the period of adoption. For the Company, this standard became effective on January 1, 2007.

The Company determines its classes of servicing assets based on the asset type being serviced along with the methods used to manage the risk inherent in the servicing assets, which includes the market inputs used to value the servicing assets. The Company elected to measure its residential mortgage servicing assets at fair value subsequent to adoption. As the retrospective application of SFAS No.

Table of Contents

156 is not permitted, there was no change to prior period financial statements. Since there was no difference between the carrying amount and fair value of the mortgage servicing rights (MSR) on the date of adoption, there was also no cumulative effect adjustment to retained earnings.

Upon the change from the lower of cost or fair value accounting method to fair value accounting under SFAS No. 156, the calculation of amortization and the assessment of impairment were discontinued and the MSR valuation allowance was written off against the recorded value of the MSR. Those measurements have been replaced by fair value adjustments that encompass market-driven valuation changes and the runoff in value that occurs from the passage of time, which are each separately reported. Under the fair value method, the MSR, net, is carried in the balance sheet at fair value and the changes in fair value are reported in earnings under the caption mortgage banking revenue in the period in which the change occurs. Changes in the balance of the MSR were as follows:

(in thousands)

	Three months ended September 30,		Nine months ended September 30,	
	2007	**2006**	**2007**	**2006**
Balance, beginning of period[1]	$ 9,966	$ 11,550	$ 9,952	$ 10,890
Additions for new mortgage servicing rights capitalized	156	225	499	1,337
Changes in fair value:				
Due to changes in model inputs or assumptions[2]	(220)		675	
Other[3]	(428)		(1,652)	
Amortization of servicing rights		(292)		(933)
Impairment charge		(1,056)		(867)
Balance, end of period	$ 9,474	$ 10,427	$ 9,474	$ 10,427
Balance of loans serviced for others	$ 877,648	$ 978,723		
MSR as a percentage of serviced loans	1.08%	1.07%		

(1) Represents fair value as of June 30, 2007 and December 31, 2006 and amortized cost as of June 30, 2006 and December 31, 2005, which approximated fair value.

(2) Principally reflects changes in discount rates and prepayment speed assumptions, which are primarily affected by changes in interest rates.

(3)

Represents changes due to collection/realization of expected cash flows over time.

The amount of contractually specified servicing fees, late fees and ancillary fees earned, recorded in mortgage banking revenue on the consolidated statements of income, were $546,000 and $1.9 million, respectively, for the three and nine months ended September 30, 2007, as compared to $652,000 and $2.0 million for the same periods in 2006. Retained mortgage servicing rights are measured at fair values as of the date of sale. We use quoted market prices when available. Subsequent fair value measurements are determined using a discounted cash flow model. In order to determine the fair value of the MSR, the present value of expected future cash flows is estimated. Assumptions used include market discount rates, anticipated prepayment speeds, delinquency and foreclosure rates, and ancillary fee income. This model is periodically validated by an independent external model validation group. The model assumptions and the MSR fair value estimates are also compared to observable trades of similar portfolios as well as to MSR broker valuations and industry surveys. Key assumptions used in measuring the fair value of MSR as of September 30, 2007 were as follows:

Constant prepayment rate	12.17%
Discount rate	8.80%
Weighted average life (years)	5.8

The expected life of the loan can vary from management s estimates due to prepayments by borrowers, especially when rates fall. Prepayments in excess of management s estimates would negatively impact the recorded value of the mortgage servicing rights. The value of the mortgage servicing rights is also dependent upon the discount rate used in the model, which we base on current market rates. A significant increase in the discount rate would reduce the value of mortgage servicing rights.

Note 4 Junior Subordinated Debentures

As of September 30, 2007, the Company had 14 wholly-owned trusts (Trusts) that were formed to issue trust preferred securities and related common securities of the Trusts and are not consolidated. The Company formed a new Trust that issued trust preferred

Table of Contents

securities representing an obligation of $61.9 million, and redeemed existing trust preferred securities representing an obligation of $25.8 million in the third quarter. One Trust, representing an obligation of approximately $10.3 million (fair value of approximately $10.3 million as of the merger date), was assumed in connection with the North Bay merger and subsequently redeemed in June 2007. Four Trusts, representing aggregate total obligations of approximately $37.1 million (fair value of approximately $38.7 million as of the merger date), were assumed in connection with the Western Sierra merger. Five Trusts, representing aggregate total obligations of approximately $58.9 million (fair value of approximately $68.6 million as of the merger date), were assumed in connection with previous mergers.

Following is information about the Trusts as of September 30, 2007:

Junior Subordinated Debentures

(in thousands)

Trust Name	**Issue Date**	**Issued Amount**	**Carrying Value (1)**	**Rate (2)**	**Effective Rate (3)**	**Maturity Date**	**Redemption Date**
At Fair Value:							
Umpqua Statutory Trust II	October 2002	$ 20,619	$ 20,945	Floating (4)	8.23%	October 2032	October 2007
Umpqua Statutory Trust III	October 2002	30,928	31,376	Floating (5)	8.23%	November 2032	November 2007
Umpqua Statutory Trust IV	December 2003	10,310	10,479	Floating (6)	8.23%	January 2034	January 2009
Umpqua Statutory Trust V	December 2003	10,310	10,311	Floating (6)	8.23%	March 2034	March 2009
Umpqua Master Trust IA	August 2007	41,238	38,436	Floating (7)	8.23%	September 2037	September 2012
Umpqua Master Trust IB	September 2007	20,619	20,437	Floating (8)	8.23%	December 2037	December 2012
		134,024	131,984				
At Amortized Cost:							
HB Capital Trust I	March 2000	5,310	6,566	10.875%	7.94%	March 2030	March 2010
Humboldt Bancorp Statutory Trust I	February 2001	5,155	6,062	10.200%	8.03%	February 2031	February 2011
Humboldt Bancorp Statutory Trust II	December 2001	10,310	11,606	Floating (9)	7.75%	December 2031	December 2006
Humboldt Bancorp Staututory Trust III	September 2003	27,836	31,327	6.75%(10)	5.04%	September 2033	September 2008
CIB Capital Trust	November 2002	10,310	11,405	Floating (5)	7.76%	November 2032	November 2007
Western Sierra Statutory Trust I	July 2001	6,186	6,362	Floating (11)	6.85%	July 2031	July 2006
Western Sierra Statutory Trust II	December 2001	10,310	10,603	Floating (9)	7.15%	December 2031	December 2006
		10,310	10,508	Floating (12)	6.85%		

Western Sierra Statutory Trust III	September 2003					September 2033	September 2008
Western Sierra Statutory Trust IV	September 2003	10,310	10,508	Floating (12)	6.85%	September 2033	September 2008
		96,037	104,947				
	Total	$230,061	$236,931				

(1) Includes purchase accounting adjustments, net of accumulated amortization, for junior subordinated debentures assumed in connection with the Humboldt and Western Sierra mergers as well as fair value adjustment pursuant to the adoption of SFAS No. 159 related to trusts recorded at fair value.

(2) Contractual interest rate of junior subordinated debentures.

(3) Effective interest rate as of September 2007, including impact of purchase accounting amortization.

(4) Rate based on LIBOR plus

3.35%, adjusted quarterly.

(5) Rate based on LIBOR plus 3.45%, adjusted quarterly.

(6) Rate based on LIBOR plus 2.85%, adjusted quarterly.

(7) Rate based on LIBOR plus 1.35%, adjusted quarterly.

(8) Rate based on LIBOR plus 2.75%, adjusted quarterly.

(9) Rate based on LIBOR plus 3.60%, adjusted quarterly.

(10) Rate fixed for 5 years from issuance, then adjusted quarterly thereafter based on LIBOR plus 2.95%.

(11) Rate based on LIBOR plus 3.58%, adjusted quarterly.

(12) Rate based on LIBOR plus 2.90%, adjusted quarterly.

The $230.1 million of trust preferred securities issued to the Trusts as of September 30, 2007 ($203.7 million as of December 31, 2006) are reflected as junior subordinated debentures in the consolidated balance sheets. The common stock issued by the Trusts is recorded in other assets in the consolidated balance sheets, and totaled $6.9 million and $5.8 million at September 30, 2007 and December 31, 2006.

All of the debentures issued to the Trusts, less the common stock of the Trusts, qualified as Tier 1 capital as of September 30, 2007, under guidance issued by the Board of Governors of the Federal Reserve System (Federal Reserve Board). Effective April 11, 2005, the Federal Reserve Board adopted a rule that permits the inclusion of trust preferred securities in Tier 1 capital, but with stricter quantitative limits. Under the Federal Reserve Board rule, after a five-year transition period ending March 31, 2009, the aggregate amount of trust preferred securities and certain other restricted core capital elements is limited to 25% of Tier 1 capital, net of
goodwill. The amount of trust preferred securities and certain other elements in excess of the limit could be included in Tier 2 capital, subject to restrictions. At September 30, 2007, the Company s restricted core capital elements were 32% of total core capital, net of

goodwill. There can be no assurance that the Federal Reserve Board will not further limit the amount of trust preferred securities permitted to be included in Tier 1 capital for regulatory capital purposes.

Effective January 1, 2007, the Company adopted SFAS No. 159 and SFAS No. 157. See Note 10 for additional information on SFAS No. 157. SFAS No. 159 allows companies to measure at fair value most financial assets and liabilities that are currently required to be measured in a different manner, such as at amortized cost. Following the initial fair value measurement date, ongoing unrealized gains and losses on items for which fair value reporting has been elected are reported in earnings at each subsequent reporting date. Under SFAS No. 159, fair value reporting may be elected on an instrument-by-instrument basis, and thus companies may record identical financial assets and liabilities at fair value or by another measurement basis permitted under generally accepted accounting principles (GAAP).

Accounting for selected junior subordinated debentures at fair value enables us to more closely align our financial performance with the economic value of those liabilities. Additionally, we believe our adoption of the standard will have a positive impact on our ability to manage the market and interest rate risks associated with the junior subordinated debentures, and potentially benefit net interest income, net income and earnings per common share during the remainder of 2007, as well as future periods. The junior subordinated debentures measured at fair value and amortized cost have been presented as separate line items on the balance sheet. We use a discounted cash flow model to determine the fair value of the junior subordinated debentures using market discount rate assumptions.

Umpqua selected the fair value measurement option for certain pre-existing junior subordinated debentures of $97.9 million (the Umpqua Statutory Trusts) as of the adoption date. The remaining junior subordinated debentures as of the adoption date were acquired through business combinations and were measured at fair value at the time of acquisition.

Retained earnings as of January 1, 2007 were reduced by $2.1 million, net of tax, as a result of the fair value election, as shown below:

(in thousands)

	Balance Sheet prior to Adoption	Net Gain/ (Loss) upon Adoption	Balance Sheet After Adoption
Other assets (1)	$ 1,934	$ (1,934)	$
Junior subordinated debentures	97,941	(2,491)	100,432
Other liabilities (2)	984	984	
Pretax cumulative effect of adoption of the fair value option		(3,441)	
Increase in deferred tax asset		1,377	
Cumulative effect of adoption of the fair value option (charged to retained earnings)		$ (2,064)	

(1) Consists of issuance costs related to junior subordinated debentures for which fair value option was elected.

(2) Consists of accrued interest related to junior subordinated debentures for which fair value option was elected.

The gains and losses described in the table above will not be recognized in earnings based upon application of SFAS No. 159. Regulatory capital will be reduced by the adjustment to retained earnings. However, the Company s capital exceeds the capital levels required to be classified as well-capitalized, and the reduction in retained earnings resulting from the adoption of SFAS No. 159 will have minimal effect on the Company s current regulatory capital ratios.

On July 19, 2007, the Company announced plans to issue $130 million of new trust preferred securities over the next four months and to use the proceeds to redeem $75 million of trust preferred securities related to three Trusts during the third and fourth quarters; to fund previously announced share repurchases; and, for other corporate purposes. Of the $61.9 million in new trust preferred securities issued in the third quarter, the Company used $25.8 million of the proceeds to redeem trust preferred securities issued by one Trust and the remainder to repurchase 1.65 million shares of common stock. On October 18, 2007, the Company announced that it intended to put on hold plans to issue additional trust preferred securities for at least another quarter until there is improvement in the credit markets. The Company selected the fair value measurement option for the trust preferred securities issued in the third quarter.

As a result of the fair value measurement election for the above financial instruments, we recorded gains of $4.1 million and $4.7 million for the three and nine months ended September 30, 2007 resulting from the change in fair value of the junior subordinated debentures recorded at fair value. These gains were recorded as other non-interest income. Interest expense on junior subordinated debentures is recorded on an accrual basis. The junior subordinated debentures recorded at fair value of $132.0 million had contractual unpaid principal amounts of $134.0 million outstanding as of September 30, 2007.

Table of Contents

Note 5 Commitments and Contingencies

Lease Commitments The Company leases 109 sites under non-cancelable operating leases. The leases contain various provisions for increases in rental rates, based either on changes in the published Consumer Price Index or a predetermined escalation schedule. Substantially all of the leases provide the Company with the option to extend the lease term one or more times upon expiration.

Rent expense for the three and nine months ended September 30, 2007 was $3.0 million and $8.9 million, respectively, compared to $2.7 million and $6.7 million in the comparable periods in 2006. Rent expense was offset by rent income for the three and nine months ended September 30, 2007 of $183,000 and $459,000, respectively, compared to $143,000 and $271,000 in the comparable periods in 2006.

Financial Instruments with Off-Balance-Sheet Risk The Company s financial statements do not reflect various commitments and contingent liabilities that arise in the normal course of the Bank s business and involve elements of credit, liquidity and interest rate risk. The following table presents a summary of the Bank s commitments and contingent liabilities:

(in thousands)

		As of September 30, 2007
Commitments to extend credit	$	1,498,690
Commitments to extend overdrafts	$	197,382
Commitments to originate loans held-for-sale	$	35,514
Forward sales commitments	$	22,000
Standby letters of credit	$	56,009

The Bank is a party to financial instruments with off-balance-sheet credit risk in the normal course of business to meet the financing needs of its customers. These financial instruments include commitments to extend credit, standby letters of credit and financial guarantees. Those instruments involve elements of credit and interest-rate risk similar to the amounts recognized in the consolidated balance sheets. The contract or notional amounts of those instruments reflect the extent of the Bank s involvement in particular classes of financial instruments.

The Bank s exposure to credit loss in the event of nonperformance by the other party to the financial instrument for commitments to extend credit and standby letters of credit, and financial guarantees written, is represented by the contractual notional amount of those instruments. The Bank uses the same credit policies in making commitments and conditional obligations as it does for on-balance-sheet instruments.

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any covenant or condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. While most standby letters of credit are not utilized, a significant portion of such utilization is on an immediate payment basis. The Bank evaluates each customer s creditworthiness on a case-by-case basis. The amount of collateral obtained, if it is deemed necessary by the Bank upon extension of credit, is based on management s credit evaluation of the counterparty. Collateral varies but may include cash, accounts receivable, inventory, premises and equipment and income-producing commercial properties.