

GLACIER BANCORP INC
Form 10-K
February 23, 2017

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

FORM 10-K

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the fiscal year ended December 31, 2016 or
 TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF
1934
For the transition period from _____ to _____
Commission file number 000-18911

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

| | |
|---|--------------------------------------|
| MONTANA | 81-0519541 |
| (State or other jurisdiction of incorporation or organization) | (IRS Employer Identification No.) |

49 Commons Loop, Kalispell, Montana 59901
(Address of principal executive offices) (Zip Code)
(406) 756-4200

(Registrant's telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act:

Common Stock, \$0.01 par value per share NASDAQ Global Select Market

(Title of each class) (Name of each exchange on which registered)

Securities registered pursuant to Section 12(g) of the Act: NONE

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes No

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 No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months. Yes No

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

Indicate by check mark whether the Registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company.

Large accelerated filer Accelerated filer
Non-accelerated filer (Do not check if a smaller reporting company) Smaller reporting company

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

The aggregate market value of the voting common equity held by non-affiliates of the Registrant at June 30, 2016 (the last business day of the most recent second quarter), was \$2,002,577,309 (based on the average bid and ask price as quoted on the NASDAQ Global Select Market at the close of business on that date).

The number of shares of Registrant's common stock outstanding on February 13, 2017 was 76,525,402. No preferred shares are issued or outstanding.

Document Incorporated by Reference

Portions of the 2017 Annual Meeting Proxy Statement dated on or about March 15, 2017 are incorporated by reference into Parts I and III of this Form 10-K.

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ABBREVIATIONS/ACRONYMS

| | |
|--|--|
| ALCO – Asset Liability Committee | GLBA – Gramm-Leach-Bliley Financial Services Modernization Act of 1999 |
| ALLL or allowance – allowance for loan and lease losses | HMDA – Home Mortgage Disclosure Act |
| ASC – Accounting Standards Codification TM | Interstate Act – Riegle-Neal Interstate Banking and Branching Efficiency Act of 1994 |
| ATM – automated teller machine | IRS – Internal Revenue Service |
| Bank – Glacier Bank | LIBOR – London Interbank Offered Rate |
| Basel III – third installment of the Basel Accords | LIHTC – Low-Income Housing Tax Credit |
| BHCA – Bank Holding Company Act of 1956, as amended | NII – net interest income |
| Board – Glacier Bancorp, Inc.’s Board of Directors | NMTC – New Markets Tax Credits |
| bp or bps – basis point(s) | NOW – negotiable order of withdrawal |
| BSA – Bank Secrecy Act | NRSRO – Nationally Recognized Statistical Rating Organizations |
| Cañon – Cañon Bank Corporation and its subsidiary, | OCI – other comprehensive income |
| Cañon National Bank | OREO – other real estate owned |
| CB – Montana Community Banks, Inc. and its subsidiary, | Patriot Act – Uniting and Strengthening America by Providing Appropriate |
| Community Bank, Inc. | Tools Required to Intercept and Obstruct Terrorism Act of 2001 |
| CCP – Core Consolidation Project | Proxy Statement – the 2017 Annual Meeting Proxy Statement |
| CDE – Certified Development Entity | Repurchase agreements – securities sold under agreements to repurchase |
| CDFI Fund – Community Development Financial Institutions Fund | S&P – Standard and Poor’s |
| CEO – Chief Executive Officer | SEC – United States Securities and Exchange Commission |
| CET1 – Tier 1 Common Equity | SERP – Supplemental Executive Retirement Plan |
| CFO – Chief Financial Officer | SOX Act – Sarbanes-Oxley Act of 2002 |
| CFPB – Consumer Financial Protection Bureau | TSB – Treasure State Bank |
| Company – Glacier Bancorp, Inc. | TDR – troubled debt restructuring |
| COSO – Committee of Sponsoring Organizations of the Treadway Commission | VIE – variable interest entity |
| CRA – Community Reinvestment Act of 1977 | |
| DDA – demand deposit account | |
| DIF – federal Deposit Insurance Fund | |
| DFAST – Dodd-Frank Act stress test | |
| Dodd-Frank Act – Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 | |
| EVE – economic value of equity | |
| Fannie Mae – Federal National Mortgage Association | |
| FASB – Financial Accounting Standards Board | |
| FDIC – Federal Deposit Insurance Corporation | |
| FHLB – Federal Home Loan Bank | |
| Final Rules – final rules implemented by the federal banking agencies that amended regulatory risk-based capital rules | |

Foothills – TFB Bancorp, Inc. and its subsidiary,

The Foothills Bank

FRB – Federal Reserve Bank

Freddie Mac – Federal Home Loan Mortgage

Corporation

GAAP – accounting principles generally accepted in the

United States of America

Ginnie Mae – Government National Mortgage

Association

PART I

Item 1. Business

Glacier Bancorp, Inc. (“Company”), headquartered in Kalispell, Montana, is a Montana corporation incorporated in 2004 as a successor corporation to the Delaware corporation originally incorporated in 1990. The Company is a publicly-traded company and its common stock trades on the NASDAQ Global Select Market under the symbol GBCI. The Company provides commercial banking services from 142 locations in Montana, Idaho, Wyoming, Colorado, Utah and Washington through its wholly-owned bank subsidiary, Glacier Bank (“Bank”). The Company offers a wide range of banking products and services, including transaction and savings deposits, real estate, commercial, agriculture, and consumer loans and mortgage origination services. The Company serves individuals, small to medium-sized businesses, community organizations and public entities. For information regarding the Company’s lending, investment and funding activities, see “Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operations.”

Subsidiaries

The Company includes the parent holding company and the Bank. The Bank consists of thirteen bank divisions, a treasury division and an information technology division. The Bank divisions include the following: Glacier Bank, Kalispell; First Security Bank of Missoula; Valley Bank of Helena; Big Sky Western Bank, Bozeman; Western Security Bank, Billings; and First Bank of Montana, Lewistown, all operating in Montana; as well as Mountain West Bank, Coeur d’Alene operating in Idaho, Utah and Washington; Citizens Community Bank, Pocatello, operating in Idaho; 1st Bank, Evanston, operating in Wyoming and Utah; First Bank of Wyoming, Powell and First State Bank, Wheatland, each operating in Wyoming; North Cascades Bank, Chelan, operating in Washington; and Bank of the San Juans, Durango, operating in Colorado. The treasury division includes the Bank’s investment portfolio and wholesale borrowings and the information technology division includes the Bank’s internal data processing and information technology expenses. The Bank divisions operate under separate names, management teams and advisory directors. The Company considers the Bank to be its sole operating segment.

The Bank has subsidiary interests in variable interest entities (“VIE”) for which the Bank has both the power to direct the VIE’s significant activities and the obligation to absorb losses or right to receive benefits of the VIE that could potentially be significant to the VIE. These subsidiary interests are included in the Company’s consolidated financial statements. The parent holding company also owns the following non-bank subsidiaries, each of which issued trust preferred securities as Tier 1 capital instruments: Glacier Capital Trust II, Glacier Capital Trust III, Glacier Capital Trust IV, Citizens (ID) Statutory Trust I, Bank of the San Juans Bancorporation Trust I, First Company Statutory Trust 2001, and First Company Statutory Trust 2003. The trust subsidiaries are not included in the Company’s consolidated financial statements.

As of December 31, 2016, the Company and its subsidiaries were not engaged in any operations in foreign countries.

Recent and Pending Acquisitions

The Company’s strategy is to profitably grow its business through internal growth and selective acquisitions. The Company continues to look for profitable expansion opportunities primarily in existing and new markets in the Rocky Mountain states. During the last five years, the Company has completed the following acquisitions:

- Treasure State Bank (“TSB”) on August 31, 2016;
- Cañon Bank Corporation and its subsidiary, Cañon National Bank, on October 31, 2015 (collectively, “Cañon”);
- Montana Community Banks, Inc. and its subsidiary, Community Bank, on February 28, 2015 (collectively, “CB”);
- FNBR Holding Corporation and its subsidiary, First National Bank of the Rockies, on August 31, 2014;
- North Cascades Bancshares, Inc. and its subsidiary, North Cascades National Bank, on July 31, 2013; and
- Wheatland Bankshares, Inc. and its subsidiary, First State Bank, on May 31, 2013.

On November 15, 2016, the Company announced the signing of a definitive agreement to acquire TFB Bancorp, Inc. and its wholly-owned subsidiary, The Foothills Bank, a community bank based in Yuma, Arizona (collectively, “Foothills”). Foothills provides banking services to individuals and businesses in Arizona, with banking offices located in Yuma, Prescott and Casa Grande, Arizona. As of December 31, 2016, Foothills had total assets of \$335 million, gross loans of \$280 million and total deposits of \$282 million. The acquisition, which has received Foothills’ shareholder approval, is subject to required regulatory approvals and other customary conditions of closing and is expected to be completed during the second quarter of 2017. Foothills will be merged into Glacier Bank and will operate as a separate bank division under its existing name, management team and advisory directors.

Market Area

The Company and the Bank have 142 locations, of which 9 are loan or administration offices, in 48 counties within 6 states including Montana, Idaho, Wyoming, Colorado, Utah, and Washington. The Company and the Bank have 60 locations in Montana, 28 locations in Idaho, 17 locations in Wyoming, 20 locations in Colorado, 4 locations in Utah and 13 locations in Washington.

The market area's economic base primarily focuses on tourism, construction, mining, energy, manufacturing, agriculture, service industry, and health care. The tourism industry is highly influenced by national parks, ski resorts, significant lakes and rural scenic areas.

Competition

Commercial banking is a highly competitive business and operates in a rapidly changing environment. There are a large number of depository institutions including savings and loans, commercial banks, and credit unions in the markets in which the Company has offices. Competition is also increasing for deposit and lending services from internet-based competitors. Non-depository financial service institutions, primarily in the securities, insurance and retail industries, have also become competitors for retail savings, investment funds and lending activities. In addition to offering competitive interest rates, the principal methods used by the Bank to attract deposits include the offering of a variety of services including on-line banking, mobile banking and convenient office locations and business hours. The primary factors in competing for loans are interest rates and rate adjustment provisions, loan maturities, loan fees, and the quality of service to borrowers and brokers.

Based on the Federal Deposit Insurance Corporation ("FDIC") summary of deposits survey as of June 30, 2016, the Bank has approximately 24 percent of the total FDIC insured deposits in the 13 counties that it services in Montana. In Idaho, the Bank has approximately 7 percent of the deposits in the 9 counties that it services. In Wyoming, the Bank has 26 percent of the deposits in the 8 counties it services. In Colorado, the Bank has 5 percent of the deposits in the 9 counties it services. In Utah, the Bank has 11 percent of the deposits in the 3 counties it services. In Washington, the Bank has 4 percent of the deposits in the 6 counties it services.

Employees

As of December 31, 2016, the Company and the Bank employed 2,291 persons, 2,099 of whom were employed full time and none of whom were represented by a collective bargaining group. The Company and the Bank provide their qualifying employees with a comprehensive benefit program, including health, dental and vision insurance, life and accident insurance, long-term disability coverage, vacation and sick leave, 401(k) plan, profit sharing plan, stock-based compensation plan, deferred compensation plans, and a supplemental executive retirement plan. The Company considers its employee relations to be excellent. See Note 13 in the Consolidated Financial Statements in "Item 8. Financial Statements and Supplementary Data" for detailed information regarding employee benefit plans and eligibility requirements.

Board of Directors and Committees

The Company's Board of Directors ("Board") has the ultimate authority and responsibility for overseeing risk management at the Company. Some aspects of risk oversight are fulfilled at the Board level, and the Board delegates other aspects of its risk oversight function to its committees. The Board has established, among others, an Audit Committee, a Compensation Committee, a Nominating/Corporate Governance Committee, a Compliance Committee, and a Risk Oversight Committee. Additional information regarding Board committees is set forth under the heading "Meetings and Committees of the Board of Directors - Committee Membership" in the Company's 2017 Annual Meeting Proxy Statement and is incorporated herein by reference.

Website Access

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Copies of the Company's Annual Report on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934 are available free of charge through the Company's website (www.glacierbancorp.com) as soon as reasonably practicable after the Company has filed the material with, or furnished it to, the United States Securities and Exchange Commission ("SEC"). Copies can also be obtained by accessing the SEC's website (www.sec.gov).

Supervision and Regulation

The following discussion provides an overview of certain elements of the extensive regulatory framework applicable to the Company and the Bank. This regulatory framework is primarily designed for the protection of depositors, the federal Deposit Insurance Fund (“DIF”) and the banking system as a whole, rather than specifically for the protection of shareholders.

To the extent this section describes statutory and regulatory provisions, it does not purport to be complete and is qualified by reference to those provisions. These statutes and regulations, as well as related policies, continue to be subject to change by Congress, state legislatures and federal and state regulators. Changes in statutes, regulations or regulatory policies applicable to the Company, including the interpretation or implementation thereof cannot be predicted and could have a material effect on the Company’s business or operations. Numerous changes to the statutes, regulations or regulatory policies applicable to the Company have been made or proposed in recent years. Continued efforts to monitor and comply with new regulatory requirements add to the complexity and cost of the Company’s business.

The Company is subject to regulation and supervision by the Federal Reserve and regulation by the State of Montana as a Montana corporation. The Company is also subject to the disclosure and regulatory requirements of the Securities Act of 1933, as amended, and the Securities Exchange Act of 1934, as amended, both as administered by the SEC. The Bank is subject to regulation and supervision by the Montana Department of Administration's Banking and Financial Institutions Division, the FDIC, and, with respect to branches of the Bank outside of Montana, applicable state regulators.

Federal Bank Holding Company Regulation

General. The Company is a bank holding company as defined in the Bank Holding Company Act of 1956, as amended (“BHCA”), due to its ownership of and control over the Bank. As a bank holding company, the Company is subject to regulation, supervision and examination by the Federal Reserve. In general, the BHCA limits the business of bank holding companies to owning or controlling banks and engaging in other activities closely related to banking. The Company must also file reports with and provide additional information to the Federal Reserve.

Holding Company Bank Ownership. The BHCA requires every bank holding company to obtain the prior approval of the Federal Reserve before: 1) acquiring, directly or indirectly, ownership or control of any voting shares of another bank or bank holding company if, after such acquisition, it would own or control more than 5 percent of such shares; 2) acquiring all or substantially all of the assets of another bank or bank holding company; or 3) merging or consolidating with another bank holding company.

Holding Company Control of Non-banks. With some exceptions, the BHCA prohibits a bank holding company from acquiring or retaining direct or indirect ownership or control of more than 5 percent of the voting shares of any company that is not a bank or bank holding company, or from engaging directly or indirectly in activities other than those of banking, managing or controlling banks or providing services for its subsidiaries. The principal exceptions to these prohibitions involve certain non-bank activities that, by federal statute, agency regulation or order, have been identified as activities closely related to the business of banking or of managing or controlling banks.

Transactions with Affiliates. Bank subsidiaries of a bank holding company are subject to restrictions imposed by the Federal Reserve Act on extensions of credit to the holding company or its subsidiaries, on investments in securities, and on the use of securities as collateral for loans to any borrower. The Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (“Dodd-Frank Act”) further extended the definition of an “affiliate” and treats credit exposure arising from derivative transactions, securities lending and borrowing transactions as a covered transaction under the regulations. It also expands the scope of covered transactions required to be collateralized, requires collateral to be maintained at all times for covered transactions required to be collateralized, and places limits on

acceptable collateral. These regulations and restrictions may limit the Company's ability to obtain funds from the Bank for its cash needs, including funds for payment of dividends, interest and operational expenses.

Tying Arrangements. The Company is prohibited from engaging in certain tie-in arrangements in connection with any extension of credit, sale or lease of property or furnishing of services. For example, with certain exceptions, neither the Company nor the Bank may condition an extension of credit to a customer on either 1) a requirement that the customer obtain additional services provided by the Company or the Bank or 2) an agreement by the customer to refrain from obtaining other services from a competitor.

Support of Bank Subsidiaries. Under Federal Reserve policy and the Dodd-Frank Act, the Company is expected to act as a source of financial and managerial strength to the Bank. This means that the Company is required to commit, as necessary, capital and resources to support the Bank, including at times when the Company may not be in a financial position to provide such resources, and it may not be in the Company's or the Company's shareholders' best interests to do so. Any capital loans a bank holding company makes to its bank subsidiaries are subordinate to deposits and to certain other indebtedness of the bank subsidiaries.

State Law Restrictions. As a Montana corporation, the Company is subject to certain limitations and restrictions under applicable Montana corporate law. For example, state law restrictions in Montana include limitations and restrictions relating to indemnification of directors, distributions to shareholders, transactions involving directors, officers or interested shareholders, maintenance of books, records and minutes, and observance of certain corporate formalities.

Federal and State Regulation of the Bank

General. Deposits in the Bank, a Montana state-chartered bank with branches in Montana, Colorado, Idaho, Utah, Washington and Wyoming, are insured by the FDIC. The Bank is subject to primary supervision, periodic examination and regulation of the FDIC and the Montana Department of Administration's Banking and Financial Institutions Division as the Bank's primary regulators. These agencies have the authority to prohibit the Bank from engaging in what they believe constitute unsafe or unsound banking practices. The federal laws that apply to the Bank regulate, among other things, the scope of its business, its investments, its reserves against deposits, the timing of the availability of deposited funds, and the nature, amount of, and collateral for loans. Federal laws also regulate community reinvestment and insider credit transactions and impose safety and soundness standards. In addition to federal law and the laws of the State of Montana described above, with respect to the Bank's branches in Colorado, Idaho, Utah, Washington, and Wyoming, the Bank is also subject to various laws and regulations governing its activities in those states.

Consumer Protection. Although the Bank is not supervised directly by the Consumer Financial Protection Bureau ("CFPB"), its consumer banking activities are subject to regulation by the CFPB. The Bank is subject to a variety of federal and state consumer protection laws and regulations that govern its relationship with consumers including laws and regulations that impose certain disclosure requirements and regulate the manner in which the Bank takes deposits, make and collect loans, and provide other services. In recent years, examination and enforcement by state and federal banking agencies for non-compliance with consumer protection laws and their implementing regulations have increased and become more intense. Failure to comply with these laws and regulations may subject the Bank to various penalties, including but not limited to, enforcement actions, injunctions, fines, civil monetary penalties, criminal penalties, punitive damages, and the loss of certain contractual rights. The Bank has established a comprehensive compliance system to ensure consumer protection.

Community Reinvestment. The Community Reinvestment Act of 1977 ("CRA") requires that, in connection with examinations of financial institutions within their jurisdiction, federal bank regulators must evaluate the record of financial institutions in meeting the credit needs of its local communities, including low and moderate-income neighborhoods, consistent with the safe and sound operation of those banks. A bank's community reinvestment record is also considered by the applicable banking agencies in evaluating mergers, acquisitions, and applications to open a branch or facility. In some cases, a bank's failure to comply with the CRA and CRA protests filed by interested parties during applicable comment periods can result in the denial or delay of such applications. The Bank received a "satisfactory" rating in its most recent CRA examination.

Insider Credit Transactions. Banks are also subject to certain restrictions on extensions of credit to executive officers, directors, principal shareholders, and their related interests. Extensions of credit 1) must be made on substantially the same terms, including interest rates and collateral, and follow credit underwriting procedures that are at least as

stringent, as those prevailing at the time for comparable transactions with persons not related to the lending bank; and 2) must not involve more than the normal risk of repayment or present other unfavorable features. Banks are also subject to certain lending limits and restrictions on overdrafts to insiders. A violation of these restrictions may result in the assessment of substantial civil monetary penalties, regulatory enforcement actions, and other regulatory sanctions. The Dodd-Frank Act and federal regulations place additional restrictions on loans to insiders, and generally prohibits loans to senior officers other than for certain specified purposes.

Regulation of Management. Federal law 1) sets forth circumstances under which officers or directors of a bank may be removed by the institution's federal supervisory agency; 2) places restraints on lending by a bank to its executive officers, directors, principal shareholders, and their related interests; and 3) generally prohibits management personnel of a bank from serving as directors or in other management positions of another financial institution whose assets exceed a specified amount or which has an office within a specified geographic area.

Safety and Soundness Standards. Certain non-capital safety and soundness standards are also imposed upon banks. These standards cover, among other things, internal controls, information systems and internal audit systems, loan documentation, credit underwriting, interest rate exposure, asset growth, compensation, fees and benefits, such other operational and managerial standards as the agency determines to be appropriate, and standards for asset quality, earnings and stock valuation. Each insured depository institution must implement a comprehensive written information security program that includes administrative, technical, and physical safeguards appropriate to the institution's size and complexity and the nature and scope of its activities. The information security program must be designed to ensure the security and confidentiality of customer information, protect against unauthorized access to or use of such information and ensure the proper disposal of customer and consumer information. An institution that fails to meet these standards may be required to submit a compliance plan, or submit to regulatory sanctions, including restrictions on growth. The Bank has established comprehensive policies and risk management procedures to ensure the safety and soundness of the Bank.

Interstate Banking and Branching

The Riegle-Neal Interstate Banking and Branching Efficiency Act of 1994 ("Interstate Act") together with the Dodd-Frank Act, relaxed prior interstate branching restrictions under federal law by permitting, subject to regulatory approval, state and federally chartered commercial banks to establish branches in states where the laws permit banks chartered in such states to establish branches. The Interstate Act requires regulators to consult with community organizations before permitting an interstate institution to close a branch in a low-income area. Federal bank regulations prohibit banks from using their interstate branches primarily for deposit production and federal bank regulatory agencies have implemented a loan-to-deposit ratio screen to ensure compliance with this prohibition.

Dividends

A principal source of the Company's cash is from dividends received from the Bank, which are subject to government regulation and limitation on the Bank's ability to pay dividends. Regulatory authorities may prohibit banks and bank holding companies from paying dividends in a manner that would constitute an unsafe or unsound banking practice. In addition, a bank may not pay cash dividends if that payment could reduce the amount of its capital below that necessary to meet minimum applicable regulatory capital requirements. The Bank is subject to Montana state law and cannot declare a dividend greater than the previous two years' net earnings without providing notice to the state regulators. Additionally, current guidance from the Federal Reserve provides, among other things, that dividends per share on the Company's common stock generally should not exceed earnings per share, measured over the previous four fiscal quarters. The third installment of the Basel Accords ("Basel III") introduces additional limitations on a bank's ability to issue dividends by requiring banks to maintain a common equity conservation buffer of at least an additional 2.5 percent of risk-weighted assets over the minimum required capital ratio to avoid restrictions on dividends, redemptions and executive bonus payments. The Federal Reserve has issued a policy statement on the payment of cash dividends by bank holding companies which expresses the view that although no specific regulations restrict dividend payments by bank holding companies other than state corporate laws, a bank holding company should not pay cash dividends unless the company's earnings for the past year are sufficient to cover both the cash dividends and a prospective rate of earnings retention that is consistent with the bank holding company's capital needs, asset quality and overall financial condition.

Capital Adequacy

Regulatory Capital Guidelines. Federal bank regulatory agencies use capital adequacy guidelines in the examination and regulation of bank holding companies and banks. These guidelines are "risk-based," meaning that they are designed to make capital requirements more sensitive to differences in risk profiles among banks and bank holding companies. On July 2, 2013, the federal banking agencies approved the final rules ("Final Rules") implementing the Basel Committee's December 2010 final capital framework (commonly known as Basel III). The Final Rules substantially amended the regulatory risk-based capital rules applicable to the Company and the Bank. The phase-in period for the Final Rules became effective on January 1, 2015, with full compliance with the Final Rules phased in by January 1,

2019.

Generally speaking, effective January 1, 2015, the Final Rules do the following:

• created “Tier 1 Common Equity” (commonly referred to as “CET1”), which is a new measure of regulatory capital closer to pure tangible common equity than the previous Tier 1 definition;

• established a required minimum risk-based capital ratio for Tier 1 Common Equity at 4.5 percent and added a 2.5 percent capital conservation buffer;

• increased the required Tier 1 risk-based capital ratio to 6.0 percent and the required Total risk-based capital ratio to 8.0 percent;

• increased the required leverage ratio to 4 percent;
and

allowed for permanent grandfathering of non-qualifying instruments, such as trust preferred securities, issued prior to May 19, 2010 for depository institution holding companies with less than \$15 billion in total assets as of year end 2009, subject to a limit of 25 percent of Tier 1 capital.

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Among other things, the Final Rules require a new capital conservation buffer designed to absorb losses during periods of economic stress.

The Bank is required to meet this new capital conservation buffer requirement by 2019 in order to avoid constraints on capital distributions, such as dividends and equity repurchases, and certain bonus compensation for executive officers. The Final Rules also change the risk-weights of certain assets for purposes of the risk-based capital ratios and phases out certain instruments as qualifying capital. The Final Rules contain revisions to the prompt corrective action framework, which is designed to place restrictions on insured depository institutions, including the Bank, if their capital levels begin to show signs of weakness. Under the prompt corrective action requirements, which are designed to complement the capital conservation buffer, insured depository institutions will be required to meet the following increased capital level requirements in order to qualify as “well capitalized”: 1) a Tier 1 Common Equity capital ratio of at least 6.5%; 2) a Tier 1 capital ratio of at least 8%; 3) a total capital ratio of at least 10%; 4) a Tier 1 leverage ratio of at least 5%; and 5) not be subject to any order or written directive requiring a specific capital level. The FDIC’s rules (as amended by the Final Rules) also contain other capital classification categories, such as “adequately capitalized,” “undercapitalized,” “significantly undercapitalized,” and “critically undercapitalized,” which are based on an institution’s specific capital ratios. An institution may be downgraded to a capital category that is lower than indicated by its capital ratios if it is determined to be in an unsafe or unsound condition, or if it receives an unsatisfactory examination rating with respect to certain matters.

The application of the Final Rules may result in lower returns on invested capital, require the raising of additional capital or require regulatory action if the Bank were unable to comply with such requirements. In addition, management may be required to modify its business strategy due to the changes to the asset risk-weights for risk-based capital calculations and the requirement to meet the capital conservation buffers. The imposition of liquidity requirements in connection with Basel III could also cause the Bank to increase its holdings of liquid assets, change its business strategy, and make other changes to the terms of its funding. Management believes that, as of December 31, 2016, the Company would meet all capital adequacy requirements under the Basel III capital rules on a fully phased-in basis as if all such requirements were currently in effect.

Regulatory Oversight and Examination

Inspections. The Federal Reserve conducts periodic inspections of bank holding companies. The supervisory objectives of the inspection program are to ascertain whether the financial strength of a bank holding company is maintained on an ongoing basis and to determine the effects or consequences of transactions between a bank holding company or its non-banking subsidiaries and its bank subsidiaries. For bank holding companies under \$10 billion in assets, the inspection type and frequency varies depending on asset size, complexity of the organization, and the bank holding company’s rating at its last inspection.

Examinations. Banks are subject to periodic examinations by their primary regulators. Bank examinations have evolved from reliance on transaction testing in assessing a bank’s condition to a risk-focused approach. These examinations are extensive and cover the entire breadth of operations of a bank. Generally, safety and soundness examinations occur on an 18-month cycle for banks under \$500 million in total assets that are well capitalized and without regulatory issues, and 12-months otherwise. Examinations alternate between the federal and state bank regulatory agency or may occur on a combined schedule. The frequency of consumer compliance and CRA examinations is linked to the size of the institution and its compliance and CRA ratings at its most recent examinations. However, the examination authority of the Federal Reserve and the FDIC allows them to examine supervised banks as frequently as deemed necessary based on the condition of the bank or as a result of certain triggering events.

Commercial Real Estate Ratios. On December 18, 2015, the federal banking regulators issued guidance reminding financial institutions to re-examine existing regulations regarding concentrations in commercial real estate lending. The

purpose of the guidance is to guide banks in developing risk management practices and capital levels commensurate with the level and nature of real estate concentrations. The banking regulators are directed to examine each bank's exposure to commercial real estate loans that are dependent on cash flow from the real estate held as collateral and to focus their supervisory resources on institutions that may have significant commercial real estate loan concentration risk. The guidance provides that the strength of an institution's lending and risk management practices with respect to such concentrations will be taken into account in evaluating capital adequacy and does not specifically limit a bank's commercial real estate lending to a specified concentration level.

Corporate Governance and Accounting

Sarbanes-Oxley Act of 2002. The Sarbanes-Oxley Act of 2002 ("SOX Act") addresses, among other things, corporate governance, auditing and accounting, enhanced and timely disclosure of corporate information, and penalties for non-compliance. Generally, the SOX Act 1) requires chief executive officers and chief financial officers to certify to the accuracy of periodic reports filed with the SEC; 2) imposes specific and enhanced corporate disclosure requirements; 3) accelerates the time frame for reporting of insider transactions and periodic disclosures by public companies; 4) requires companies to adopt and disclose information about corporate governance practices, including whether or not they have adopted a code of ethics for senior financial officers and whether the audit committee includes at least one "audit committee financial expert"; and 5) requires the SEC, based on certain enumerated factors, to regularly and systematically review corporate filings.

As a publicly reporting company, the Company is subject to the requirements of the SOX Act and related rules and regulations issued by the SEC and NASDAQ. After enactment, the Company updated its policies and procedures to comply with the SOX Act's requirements and has found that such compliance, including compliance with Section 404 relating to the Company's internal control over financial reporting, has resulted in significant additional expense for the Company. The Company will continue to incur additional expense in its ongoing compliance with these requirements.

Anti-Money Laundering and Anti-Terrorism

The Bank Secrecy Act and the Patriot Act. The Bank Secrecy Act ("BSA") requires all financial institutions to (among other requirements) establish a risk-based system of internal controls reasonably designed to prevent money laundering and the financing of terrorism. The BSA sets forth various recordkeeping and reporting requirements (such as reporting suspicious activities that might signal criminal activity), including due diligence and "know your customer" documentation requirements.

The Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act of 2001 ("Patriot Act"), intended to combat terrorism, was renewed with certain amendments in 2006. The Patriot Act, in relevant part, 1) prohibits banks from providing correspondent accounts directly to foreign shell banks; 2) imposes due diligence requirements on banks opening or holding accounts for foreign financial institutions or wealthy foreign individuals; 3) requires financial institutions to establish an anti-money-laundering compliance program; and 4) eliminates civil liability for persons who file suspicious activity reports. The Patriot Act also includes provisions providing the government with power to investigate terrorism, including expanded government access to bank account records. Bank regulators are directed to consider a holding company's and bank's effectiveness in combating money laundering when reviewing and ruling on applications under the BHCA and the Bank Merger Act. The Company and the Bank have established comprehensive compliance programs designed to comply with the BSA and Patriot Act requirements.

Financial Services Modernization

Gramm-Leach-Bliley Act of 1999. The Gramm-Leach-Bliley Financial Services Modernization Act of 1999 ("GLBA") brought about significant changes to the laws affecting banks and bank holding companies. Generally, the GLBA 1) repeals historical restrictions on preventing banks from affiliating with securities firms; 2) provides a uniform framework for the activities of banks, savings institutions and their holding companies; 3) broadens the activities that may be conducted by national banks and banking subsidiaries of bank holding companies; 4) provides an enhanced framework for protecting the privacy of consumer information and requires notification to consumers of bank privacy policies; and 5) addresses a variety of other legal and regulatory issues affecting both day-to-day operations and long-term activities of financial institutions. The Bank is subject to FDIC regulations implementing the privacy protection provisions of the GLBA. These regulations require banks to disclose their privacy policy, including informing consumers of their information sharing practices and informing consumers of their rights to opt out of certain practices.

Deposit Insurance

FDIC Insured Deposits. The Bank's deposits are insured under the Federal Deposit Insurance Act, up to the maximum applicable limits and are subject to deposit insurance assessments by the FDIC designed to tie what banks pay for deposit insurance to the risks they pose. The Dodd-Frank Act redefined the assessment base used for calculating FDIC deposit insurance assessments by requiring the FDIC to determine deposit insurance assessments based on assets instead of deposits. Assessments are now based on the average consolidated total assets less average tangible equity capital of a financial institution. In addition, the Dodd-Frank Act raised the minimum designated reserve ratio (the FDIC is required to set the reserve ratio each year) of the DIF from 1.15 percent to 1.35 percent; requires that the DIF reserve ratio meet 1.35 percent by 2020; and eliminates the requirement that the FDIC pay dividends to insured depository institutions when the reserve ratio exceeds certain thresholds. In October 2015, the FDIC stated that it would offset the effect of the increase in the minimum reserve ratio on insured depository institutions with total

consolidated assets of less than \$10 billion by imposing a surcharge on insured depository institutions with total consolidated assets of \$10 billion or more. No institution may pay a dividend if it is in default on its federal deposit insurance assessment. The FDIC may also prohibit any insured institution from engaging in any activity determined by regulation or order to pose a serious risk to the DIF.

Safety and Soundness. The FDIC may terminate the deposit insurance of any insured depository institution if it determines after a hearing that the institution has engaged or is engaging in unsafe or unsound practices, is in an unsafe or unsound condition to continue operations, or has violated any applicable law, regulation, order or any condition imposed by an agreement with the FDIC. Management is not aware of any existing circumstances which would result in termination of the deposit insurance of the Bank.

Insurance of Deposit Accounts. The Dodd-Frank Act permanently increased FDIC deposit insurance from \$100,000 to \$250,000 per depositor. The FDIC insurance coverage limit applies per depositor, per insured depository institution for each account ownership category.

The Dodd-Frank Act

On July 21, 2010, the Dodd-Frank Act was signed into law. The Dodd-Frank Act significantly changed the bank regulatory structure and is affecting the lending, deposit, investment, trading and operating activities of financial institutions and the bank holding companies, including the Company and the Bank. Some of the provisions of the Dodd-Frank Act that may impact the Company's business are summarized below. In light of the new Administration in Washington D.C., there is talk of providing some relief from certain provisions of the Dodd-Frank Act. For example, the President signed two directives on February 3, 2017 ordering a review of financial industry regulations, including the Dodd-Frank Act, to ensure that existing laws align with the Administration's goals. At this time, it is too early to predict the likelihood, timing, and scope of any such amendment(s).

Corporate Governance. The Dodd-Frank Act requires publicly traded companies to provide their shareholders with 1) a non-binding shareholder vote on executive compensation; 2) a non-binding shareholder vote on the frequency of such vote; 3) disclosure of "golden parachute" arrangements in connection with specified change in control transactions; and 4) a non-binding shareholder vote on golden parachute arrangements in connection with these change in control transactions. Effective August 5, 2015, the SEC adopted a rule mandated by the Dodd-Frank Act that requires a public company to disclose the ratio of the compensation of its Chief Executive Officer ("CEO") to the median compensation of its employees. This rule is intended to provide shareholders with information that they can use to evaluate a CEO's compensation. Companies will be required to provide disclosure of their pay ratios for their first fiscal year beginning on or after January 1, 2017.

Prohibition Against Charter Conversions of Financial Institutions. The Dodd-Frank Act generally prohibits a depository institution from converting from a state to federal charter, or vice versa, while it is the subject to an enforcement action unless the depository institution seeks prior approval from its primary regulator and complies with specified procedures to ensure compliance with the enforcement action.

Repeal of Demand Deposit Interest Prohibition. The Dodd-Frank Act repeals the federal prohibitions on the payment of interest on demand deposits, thereby permitting depository institutions to pay interest on business transaction and other accounts.

Consumer Financial Protection Bureau. The Dodd-Frank Act established the CFPB and empowered it to exercise broad rulemaking, supervision and enforcement authority for a wide range of consumer protection laws. The Bank is subject to consumer protection regulations issued by the CFPB, but as a financial institution with assets of less than \$10 billion, the Bank is generally not subject to supervision and examination by the CFPB. The CFPB has issued and continues to issue numerous regulations under which the Company will continue to incur additional expense in its ongoing compliance with CFPB regulations. Significant recent CFPB developments that may affect the Bank's operations and compliance costs include:

The issuance of proposals to ban consumer finance companies from including arbitration clauses that block class action lawsuits in their consumer contracts. The proposals under consideration would require that companies that choose to use arbitration clauses for individual disputes submit to the CFPB the arbitration claims filed and awards issued. The current proposals would apply to credit cards, checking and deposit accounts, prepaid cards, money transfer services, certain auto loans and installment loans.

Positions taken by the CFPB on fair lending, including applying the disparate impact theory which could make it more difficult for lenders to charge different rates or apply different terms to loans to different customers.

The issuance of a final rule amending Regulation C, which implements the Home Mortgage Disclosure Act ("HMDA"), requiring most lenders to report expanded information in order for the CFPB to more effectively monitor fair lending concerns and other information shortcomings identified by the CFPB.

Positions taken by the CFPB regarding the Electronic Fund Transfer Act and Regulation E, which require companies to obtain consumer authorizations before automatically debiting a consumer's account for pre-authorized electronic funds transfers.

Actions taken to regulate and supervise credit bureaus and debt collections.

Proposed Legislation

New Legislation and Compliance Burdens. The economic and political environment of the past several years has led to a number of proposed legislative, governmental and regulatory initiatives that may significantly impact the banking industry, including tax reform. Other regulatory initiatives by federal and state banking agencies may also significantly impact the Bank's business. The Bank cannot predict whether these or any other proposals will be enacted or the ultimate impact of any such initiatives on its operations, competitive situation, financial conditions, or results of operations. While recent history has demonstrated that new legislation or changes to existing laws or regulations typically result in a greater compliance burden (and therefore increase the general costs of doing business), the new Administration has expressed an attempt to reduce regulatory burden.

Effects of Federal Government Monetary Policy

Government Policies. The Company's earnings and growth are affected not only by general economic conditions, but also by the fiscal and monetary policies of the federal government, particularly the Federal Reserve. The Federal Reserve implements national monetary policy for such purposes of promoting maximum employment, stable prices and moderate long-term interest rates. Through its open market operations in U.S. government securities, control of the discount rate applicable to borrowings from the Federal Reserve, establishment of reserve requirements against certain deposits, and control of the rate of interest applicable to excess reserve balances and reverse repurchase agreements, the Federal Reserve influences the availability and cost of money and credit, and ultimately, a range of economic variables including employment, output, and prices of goods and services. The nature and impact of future changes in monetary policies and their impact on the Company or the Bank cannot be predicted with certainty.

Heightened Requirements for Bank Holding Companies with \$10 Billion or More in Assets

\$10 Billion Threshold. Various federal banking laws and regulations impose heightened requirements on certain large banks and bank holding companies. In relevant part, certain rules and requirements (e.g., stress testing, risk committees, CFPB oversight, etc.) also apply to banks and bank holding companies with at least \$10 billion in total consolidated assets. Although the Company does not currently have \$10 billion or more in total consolidated assets, it is reasonable to assume that the Company's total assets may exceed \$10 billion in the foreseeable future, based on the Company's organic growth rates or if the Company engages in any future acquisitions.

Item 1A. Risk Factors

An investment in the Company's common stock involves certain risks. The following is a discussion of what the Company believes are the most significant risks and uncertainties that may affect the Company's business, financial condition and future results.

Economic conditions in the market areas the Bank serves may adversely impact its earnings and could increase the credit risk associated with its loan portfolio and the value of its investment portfolio.

Substantially all of the Bank's loans are to businesses and individuals in Montana, Idaho, Wyoming, Utah, Colorado and Washington, and a softening of the economies in these market areas could have a material adverse effect on its business, financial condition, results of operations and prospects. Although the Company has minimal exposure to the energy industry, a further decline in this sector could have an unfavorable effect on the Company's performance. Any future deterioration in economic conditions nationally or in the markets the Bank serves could result in the following consequences, any of which could have an adverse impact, which could be material, on the Company's business, financial condition, results of operations and prospects:

- loan delinquencies may increase;
- problem assets and foreclosures may increase;
- collateral for loans made may decline in value, in turn reducing customers' borrowing power, reducing the value of assets and collateral associated with existing loans;
- certain securities within the investment portfolio could become other-than-temporarily impaired, requiring a write-down through earnings to fair value, thereby reducing equity;
- low cost or non-interest bearing deposits may decrease; and
- demand for loan and other products and services may decrease.

National and global economic and geopolitical conditions could adversely affect the Company's future results of operations or market price of its stock.

The Company's business is impacted by factors such as economic, political and market conditions, broad trends in industry and finance, and changes in government monetary policies, all of which are beyond the Company's control. National and global economies are constantly in flux, as evidenced by recent market volatility resulting from, among

other things, a new presidential administration and new economic policies associated therewith, the uncertain future relationship of the United Kingdom with the European Union (e.g., Brexit), and the ever-changing landscape of the energy industry. Future economic conditions cannot be predicted, and any renewed deterioration in the economies of the nation as a whole or in the Company's markets could have an adverse effect, which could be material, on its business, financial condition, results of operations and prospects, and could cause the market price of the Company's stock to decline.

The Company will be subject to heightened regulatory requirements when the Company exceeds \$10 billion in assets. It is reasonable to assume, based on the Company's organic growth rates and if the Company engages in any future acquisitions, that the Company's total consolidated assets may exceed \$10 billion in the foreseeable future. The Dodd-Frank Act and its implementing regulations impose additional requirements on bank holding companies with \$10 billion or more in total assets, including compliance with specific sections of the Federal Reserve's prudential oversight requirements and annual stress testing requirements. The Durbin Amendment, which was passed as part of Dodd-Frank, instructed the Federal Reserve to establish rules limiting the amount of interchange fees that can be charged to merchants for debit card processing. The Federal Reserve's final rules contained several key pieces, including in relevant part an interchange fee cap, certain fraud prevention adjustments, and, most notably, an exemption from the interchange fee cap for small issuers. Issuers with less than \$10 billion in total assets (as of the end of the previous calendar year) are exempt from the Federal Reserve's interchange fee cap. However, if the Company's total assets exceed \$10 billion, the interchange fee cap of the Durbin Amendment will negatively affect the interchange income the Bank receives from electronic payment transactions. Banks with \$10 billion or more in total assets are also examined by the CFPB. As a fairly new agency with evolving regulations and practices, it is uncertain as to how the CFPB's various examinations may affect the Company's business.

The Company and the Bank operate in a highly regulated environment and changes or increases in, or supervisory enforcement of, banking or other laws and regulations or governmental fiscal or monetary policies could adversely affect the Company.

The Company and the Bank are subject to extensive regulation, supervision and examination by federal and state banking regulators. In addition, as a publicly-traded company, the Company is subject to regulation by the SEC. Any change in applicable regulations or federal, state or local legislation or in policies or interpretations or regulatory approaches to compliance and enforcement, income tax laws and accounting principles could have a substantial impact on the Company and its operations. Changes in laws and regulations may also increase expenses by imposing additional fees or taxes or restrictions on operations. Additional legislation and regulations that could significantly affect powers, authority and operations may be enacted or adopted in the future, which could have a material adverse effect on the Company's financial condition and results of operations. Failure to appropriately comply with any such laws, regulations or principles could result in sanctions by regulatory agencies or damage to the Company's reputation, all of which could adversely affect the Company's business, financial condition or results of operations.

A failure in or breach of the Bank's operational or security systems, or those of the Bank's third party service providers, including as a result of cyber attacks, could disrupt business, result in the disclosure or misuse of confidential or proprietary information, damage the Company's reputation, increase costs and cause losses.

The Bank's operations rely heavily on the secure processing, storage and transmission of confidential and other information on its computer systems and networks. Any failure, interruption or breach in security or operational integrity of these systems could result in failures or disruptions in the Bank's online banking system, customer relationship management, general ledger, deposit and loan servicing, financial reporting and other systems. The security and integrity of the Bank's systems could be threatened by a variety of interruptions or information security breaches, including those caused by computer hacking, cyber attacks, electronic fraudulent activity or attempted theft of financial assets. The Bank cannot assure that any such failures, interruption or security breaches will not occur, or if they do occur, that they will be adequately addressed. While the Bank has certain protective policies and procedures in place, the nature and sophistication of the threats continue to evolve. The Bank may be required to expend significant additional resources in the future to modify and enhance its protective measures.

Additionally, the Bank faces the risk of operational disruption, failure, termination or capacity constraints of any of the third parties that facilitate its business activities, including exchanges, clearing agents, clearing houses or other financial intermediaries. Such parties could also be the source of an attack on, or breach of, the Bank's operational systems.

Any failures, interruptions or security breaches in the Bank's information systems could damage its reputation, result in a loss of customer business, result in a violation of privacy or other laws, or expose the Company to civil litigation, regulatory fines or losses not covered by insurance.

Regulators have significant discretion and authority to prevent or remedy unsafe or unsound practices or violations of laws or regulations by financial institutions and bank holding companies in the performance of their supervisory and enforcement duties. Existing and proposed federal and state laws and regulations restrict, limit and govern all aspects of the Company's activities and may affect the ability to expand its business over time, may result in an increase in the Company's compliance costs, and may affect its ability to attract and retain qualified executive officers and employees. Recently, these powers have been utilized more frequently due to the challenging national, regional and local economic conditions. The exercise of regulatory authority may have a negative impact on the Company's financial condition and results of operations, including limiting the types of financial services and products the Company may offer or increasing the ability of non-banks to offer competing financial services and products. Additionally, the Company's business is affected significantly by the fiscal and monetary policies of the federal government and its agencies, including the Federal Reserve.

The Company cannot accurately predict the full effects of recent legislation or the various other governmental, regulatory, monetary and fiscal initiatives which have been and may be enacted on the financial markets and on the Company. The terms and costs of these activities, or the failure of these actions to help stabilize the financial markets, asset prices, market liquidity and a continuation or worsening of current financial market and economic conditions could materially and adversely affect the Company's business, financial condition, results of operations, and the trading price of the Company's common stock.

The allowance for loan and lease losses may not be adequate to cover actual loan losses, which could adversely affect earnings.

The Bank maintains an allowance for loan and lease losses ("ALLL" or "allowance") in an amount that it believes is adequate to provide for losses in the loan portfolio. While the Bank strives to carefully manage and monitor credit quality and to identify loans that may become non-performing, at any time there are loans included in the portfolio that will result in losses, but that have not been identified as non-performing or potential problem loans. With respect to real estate loans and property taken in satisfaction of such loans ("other real estate owned" or "OREO"), the Bank can be required to recognize significant declines in the value of the underlying real estate collateral or OREO quite suddenly as values are updated through appraisals and evaluations (new or updated) performed in the normal course of monitoring the credit quality of the loans. There are many factors that can cause the value of real estate to decline, including declines in the general real estate market, changes in methodology applied by appraisers, and/or using a different appraiser than was used for the prior appraisal or evaluation. The Bank's ability to recover on real estate loans by selling or disposing of the underlying real estate collateral is adversely impacted by declining values, which increases the likelihood the Bank will suffer losses on defaulted loans beyond the amounts provided for in the ALLL. This, in turn, could require material increases in the Bank's provision for loan losses and ALLL. By closely monitoring credit quality, the Bank attempts to identify deteriorating loans before they become non-performing assets and adjust the ALLL accordingly. However, because future events are uncertain, and if difficult economic conditions occur, there may be loans that deteriorate to a non-performing status in an accelerated time frame. As a result, future additions to the ALLL may be necessary beyond the levels commensurate with any loan growth. Because the loan portfolio contains a number of loans with relatively large balances, the deterioration of one or a few of these loans may cause a significant increase in non-performing loans, requiring an increase to the ALLL. Additionally, future significant additions to the ALLL may be required based on changes in the mix of loans comprising the portfolio, changes in the financial condition of borrowers, which may result from changes in economic conditions, or changes in the assumptions used in determining the ALLL. Additionally, federal and state banking regulators, as an integral part of their supervisory function, periodically review the Bank's loan portfolio and the adequacy of the ALLL. These regulatory authorities may require the Bank to recognize further loan loss provisions or charge-offs based upon their judgments, which may be different from the Bank's judgments. Any increase in the ALLL could have an adverse effect, which could be material, on the Company's financial condition and results of operations.

The Bank has a high concentration of loans secured by real estate, so any future deterioration in the real estate markets could require material increases in the ALLL and adversely affect the Company's financial condition and results of operations.

The Bank has a high degree of concentration in loans secured by real estate. Any future deterioration in the real estate markets could adversely impact borrowers' ability to repay loans secured by real estate and the value of real estate collateral, thereby increasing the credit risk associated with the loan portfolio. The Bank's ability to recover on these loans by selling or disposing of the underlying real estate collateral would be adversely impacted by any decline in real estate values, which increases the likelihood that the Bank will suffer losses on defaulted loans secured by real estate beyond the amounts provided for in the ALLL. This, in turn, could require material increases in the ALLL which would adversely affect the Company's financial condition and results of operations.

Non-performing assets could increase, which could adversely affect the Company's results of operations and financial condition.

The Bank may experience increases in non-performing assets in the future. Non-performing assets (which include OREO) adversely affect the Company's financial condition and results of operations in various ways. The Bank does not record interest income on non-accrual loans or OREO, thereby adversely affecting its earnings. When the Bank takes collateral in foreclosures and similar proceedings, it is required to mark the related asset to the then fair value of the collateral, less estimated cost to sell, which may result in a charge-off of the value of the asset and lead the Bank to increase the provision for loan losses. An increase in the level of non-performing assets also increases the Bank's risk profile and may impact the capital levels its regulators believe are appropriate in light of such risks. Further decreases in the value of these assets, or the underlying collateral, or in these borrowers' performance or financial condition, whether or not due to economic and market conditions beyond the Bank's control, could adversely affect the Company's business, results of operations and financial condition, perhaps materially. In addition to the carrying costs to maintain OREO, the resolution of non-performing assets increases the Bank's loan administration costs generally, and requires significant commitments of time from management and the Company's directors, which reduces the time they have to focus on profitably growing the Company's business.

The Bank's loan portfolio mix increases the exposure to credit risks tied to deteriorating conditions. The loan portfolio contains a high percentage of commercial, commercial real estate, real estate acquisition and development loans in relation to the total loans and total assets. These types of loans have historically been viewed as having more risk of default than residential real estate loans or certain other types of loans or investments. In fact, the FDIC has issued pronouncements alerting banks of its concern about banks with a heavy concentration of commercial real estate loans. These types of loans also typically are larger than residential real estate loans and other commercial loans. Because the Bank's loan portfolio contains a significant number of commercial and commercial real estate loans with relatively large balances, the deterioration of one or more of these loans may cause a significant increase in non-performing loans. An increase in non-performing loans could result in a loss of earnings from these loans, an increase in the provision for loan losses, or an increase in loan charge-offs, which could have a material adverse impact on results of operations and financial condition.

Competition in the Bank's market areas may limit future success.

Commercial banking is a highly competitive business and a consolidating industry. The Bank competes with other commercial banks, savings and loans, credit unions, finance, insurance and other non-depository companies operating in its market areas. The Bank is subject to substantial competition for loans and deposits from other financial institutions. Some of its competitors are not subject to the same degree of regulation and restriction as the Bank. Some of the Bank's competitors have greater financial resources than the Bank. If the Bank is unable to effectively compete in its market areas, the Bank's business, results of operations and prospects could be adversely affected.

Fluctuating interest rates can adversely affect profitability.

The Bank's profitability is dependent to a large extent upon net interest income, which is the difference (or "spread") between the interest earned on loans, investment securities and other interest earning assets and interest paid on deposits, borrowings, and other interest bearing liabilities. Because of the differences in maturities and repricing characteristics of interest earning assets and interest bearing liabilities, changes in interest rates do not produce equivalent changes in interest income earned on interest earning assets and interest paid on interest bearing liabilities. Accordingly, fluctuations in interest rates could adversely affect the Bank's interest rate spread, and, in turn, profitability. The Bank seeks to manage its interest rate risk within well established policies and guidelines. Generally, the Bank seeks an asset and liability structure that insulates net interest income from large deviations attributable to changes in market rates. However, the Bank's structures and practices to manage interest rate risk may not be effective in a highly volatile rate environment. Recently, the Federal Reserve increased the federal funds target range by 0.25 percent from 0.50 to 0.75 percent and has indicated further increases could continue depending on economic conditions.

The Company may not be able to continue to grow organically or through acquisitions.

Historically, the Company has expanded through a combination of organic growth and acquisitions. If market and regulatory conditions remain challenging, the Company may be unable to grow organically or successfully complete or integrate potential future acquisitions. The Company has historically used its strong stock currency to complete acquisitions. Downturns in the stock market and the Company's stock could have an impact on future acquisitions. Furthermore, there can be no assurance that the Company can successfully complete such transactions, since they are subject to regulatory review and approval.

Growth through future acquisitions could, in some circumstances, adversely affect profitability or other performance measures.

During 2016 and in prior years, the Company has been active in acquisitions and may in the future engage in selected acquisitions of additional financial institutions. There are risks associated with any such acquisitions that could adversely affect profitability and other performance measures. These risks include, among other things, incorrectly assessing the asset quality of a financial institution being acquired, discovering compliance or regulatory issues after the acquisition, encountering greater than anticipated cost and use of management time associated with integrating

acquired businesses into the Company's operations, and being unable to profitably deploy funds acquired in an acquisition. The Company may not be able to continue to grow through acquisitions, and if it does, there is a risk of negative impacts of such acquisitions on the Company's operating results and financial condition.

Acquisitions may also cause business disruptions that cause the Bank to lose customers or cause customers to remove their accounts from the Bank and move to competing financial institutions. Further, acquisitions may also disrupt the Bank's ongoing businesses or create inconsistencies in standards, controls, procedures, and policies that adversely affect relationships with employees, clients, customers, and depositors. The loss of key employees during acquisitions may also adversely affect the Company's business.

The Company anticipates that it might issue capital stock in connection with future acquisitions. Acquisitions and related issuances of stock may have a dilutive effect on earnings per share, book value per share, or the percentage ownership of current shareholders. In acquisitions involving the use of cash as consideration, there will be an impact on the Company's capital position.

The Company's business is heavily dependent on the services of the senior management team and proposed changes could have an impact on the Company.

The Company believes its success to date has been substantially dependent on the members of the executive management team, in particular Mick Blodnick, the Company's CEO. The unexpected loss of any of these persons could have an adverse effect on the Company's business and future growth prospects. Fortunately, the Company has a decentralized management style with separate Presidents for each of its bank divisions. Notwithstanding this, Mr. Blodnick has been instrumental in the Company's success. As previously announced, Mr. Blodnick retired as CEO at the end of 2016 but remains on the Board. The Company, following a national search, hired Randall Chesler in 2015 to be Mr. Blodnick's successor. Mr. Chesler has served as President of the Bank and a director of the Bank since August 1, 2015, he was elected to the Board of the Company at the Company's annual meeting in 2016, and he assumed the roles of President and CEO of the Company and CEO of the Bank effective January 1, 2017. The objective of this 17-month transition period was to facilitate a smooth succession of management at the President/CEO level.

A decline in the fair value of the Bank's investment portfolio could adversely affect earnings and capital. The fair value of the Bank's investment securities could decline as a result of factors including changes in market interest rates, tax reform, credit quality and credit ratings, lack of market liquidity and other economic conditions. An investment security is impaired if the fair value of the security is less than the carrying value. When a security is impaired, the Bank determines whether the impairment is temporary or other-than-temporary. If an impairment is determined to be other-than-temporary, an impairment loss is recognized by reducing the amortized cost only for the credit loss associated with the other-than-temporary loss with a corresponding charge to earnings for a like amount. Any such impairment charge would have an adverse effect, which could be material, on the Company's results of operations and financial condition, including its capital.

The size of the investment portfolio has stabilized over the past few years and represents 33 percent of total assets at December 31, 2016 and 36 percent of total assets at December 31, 2015. While the Bank believes that the terms of such investments have been kept relatively short, the Bank is subject to elevated interest rate risk exposure if rates were to increase sharply. Further, the change in the mix of the Bank's assets to more investment securities presents a different type of asset quality risk than the loan portfolio. At December 31, 2016, the investment portfolio consisted of 78 percent available-for-sale and 22 percent held-to-maturity designated investment securities. While the Company believes a relatively conservative management approach has been applied to the investment portfolio, there is always potential loss exposure under changing economic conditions.

Interest rate swaps expose the Bank to certain risks, and may not be effective in mitigating exposure to changes in interest rates.

The Bank has entered into interest rate swap agreements in order to manage a portion of the interest rate volatility risk. The Bank anticipates that it may enter into additional interest rate swaps. These swap agreements involve other risks, such as the risk that the counterparty may fail to honor its obligations under these arrangements, leaving the Bank vulnerable to interest rate movements. The Bank's current interest rate swap agreements include bilateral collateral agreements whereby the net fair value position is collateralized by the party in a net liability position. The bilateral collateral agreements reduce the Bank's counterparty risk exposure. There can be no assurance that these arrangements will be effective in reducing the Bank's exposure to changes in interest rates.

If goodwill recorded in connection with acquisitions becomes additionally impaired, it could have an adverse impact on earnings and capital.

Accounting standards require the Company to account for acquisitions using the acquisition method of accounting. Under acquisition accounting, if the purchase price of an acquired company exceeds the fair value of its net assets, the excess is carried on the acquirer's balance sheet as goodwill. In accordance with accounting principles generally accepted in the United States of America ("GAAP"), goodwill is not amortized but rather is evaluated for impairment on

an annual basis or more frequently if events or circumstances indicate that a potential impairment exists. The Company's goodwill was not considered impaired as of December 31, 2016 and 2015; however, there can be no assurance that future evaluations of goodwill will not result in findings of impairment and write-downs, which could be material. While a non-cash item, impairment of goodwill could have a material adverse effect on the Company's business, financial condition and results of operations. Furthermore, impairment of goodwill could subject the Company to regulatory limitations, including the ability to pay dividends on its common stock.

There can be no assurance the Company will be able to continue paying dividends on the common stock at recent levels.

The Company may not be able to continue paying quarterly dividends commensurate with recent levels given that the ability to pay dividends on the Company's common stock depends on a variety of factors. The payment of dividends is subject to government regulation in that regulatory authorities may prohibit banks and bank holding companies from paying dividends that would constitute an unsafe or unsound banking practice. This is heavily based on the Company's earnings and capital levels which currently are strong. Current guidance from the Federal Reserve provides, among other things, that dividends per share should not exceed earnings per share measured over the previous four fiscal quarters. The Bank is also subject to Montana state law and cannot declare a dividend greater than the previous two years' net earnings without providing notice to the state. As a result, future dividends will generally depend on the level of earnings at the Bank.

The FDIC has adopted a final rule to increase the federal Deposit Insurance Fund, including additional future premium increases and special assessments.

On March 15, 2016, the FDIC adopted a final rule to increase insurance premiums and has imposed special assessments to rebuild and maintain the federal deposit insurance fund, and any additional future premium increases or special assessments could have a material adverse effect on the Company's business, financial condition, and results of operations. Additional information regarding this matter is set forth under the heading "Supervision and Regulation" in "Item 1. Business."

The Dodd-Frank Act broadened the base for FDIC insurance assessments. In addition, the Dodd-Frank Act established 1.35 percent as the minimum Deposit Insurance Fund reserve ratio. The FDIC has determined that the fund reserve ratio should be 2.0 percent (which is beyond what is required by law) and has adopted a plan under which it will meet the statutory minimum fund reserve ratio of 1.35 percent by the statutory deadline of September 30, 2020. The Dodd-Frank Act made banks with \$10 billion or more in total assets responsible for the increase from 1.15 percent to 1.35 percent. As a result, the deposit insurance assessments to be paid by the Bank could increase.

The impact of Basel III is uncertain.

Basel III sets forth more robust global regulatory standards on capital adequacy, qualifying capital instruments, leverage ratios, market liquidity risk, and stress testing, which may be stricter than standards currently in place. The phase-in period for Basel III begins January 1, 2015 and ends on January 1, 2019. The implementation of these new standards could have an adverse impact on the Company's financial position and future earnings due to, among other things, the increased Tier 1 capital ratio requirements that will be implemented. Additional information regarding Basel III is set forth under the heading "Supervision and Regulation" in "Item 1. Business."

The Company has various anti-takeover measures that could impede a takeover.

The Company's articles of incorporation include certain provisions that could make more difficult the acquisition of the Company by means of a tender offer, a proxy contest, merger or otherwise. These provisions include a requirement that any "Business Combination" (as defined in the articles of incorporation) be approved by at least 80 percent of the voting power of the then outstanding shares, unless it is either approved by the Company's Board or certain price and procedural requirements are satisfied. In addition, the authorization of preferred stock, which is intended primarily as a financing tool and not as a defensive measure against takeovers, may potentially be used by management to make more difficult uninvited attempts to acquire control of the Company. These provisions may have the effect of lengthening the time required to acquire control of the Company through a tender offer, proxy contest or otherwise, and may deter any potentially unfriendly offers or other efforts to obtain control of the Company. This could deprive the Company's shareholders of opportunities to realize a premium for their common stock in the Company, even in circumstances where such action is favored by a majority of the Company's shareholders.

The Company's business is subject to the risks of earthquakes, tsunamis, floods, fires, and other natural catastrophes.

With Bank branches located in Montana, Idaho, Wyoming, Utah, Colorado and Washington, the Company's business could be affected by a major natural catastrophe, such as a fire, flood, earthquake, or other natural disaster. The occurrence of any of these natural disasters may result in a prolonged interruption of the Company's business, which could have a material adverse effect on the Company's financial condition and operations.

Item 1B. Unresolved Staff Comments

None

Item 2. Properties

The following schedule provides information on the Company's 142 properties as of December 31, 2016:

| (Dollars in thousands) | Properties | Properties | Net Book |
|------------------------|------------|------------|------------|
| | Leased | Owned | |
| Montana | 7 | 53 | \$82,116 |
| Idaho | 7 | 21 | 27,403 |
| Wyoming | 2 | 15 | 17,063 |
| Colorado | 2 | 18 | 16,401 |
| Utah | 1 | 3 | 2,213 |
| Washington | 3 | 10 | 6,050 |
| | 22 | 120 | \$ 151,246 |

The Company believes that all of its facilities are well maintained, generally adequate and suitable for the current operations of its business, as well as fully utilized. In the normal course of business, new locations and facility upgrades occur as needed.

For additional information regarding the Company's premises and equipment and lease obligations, see Note 4 to the Consolidated Financial Statements in "Item 8. Financial Statements and Supplementary Data."

Item 3. Legal Proceedings

The Company is involved in various claims, legal actions and complaints which arise in the ordinary course of business. In the Company's opinion, all such matters are adequately covered by insurance, are without merit or are of such kind, or involve such amounts, that unfavorable disposition would not have a material adverse effect on the financial condition or results of operations of the Company.

Item 4. Mine Safety Disclosures

Not Applicable

PART II

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

The Company's stock trades on the NASDAQ Global Select Market under the symbol: GBCI. As of December 31, 2016, there were approximately 1,607 shareholders of record for the Company's common stock. The market range of high and low closing prices for the Company's common stock for the periods indicated are shown below:

| | 2016 | | 2015 | |
|----------------|---------|-------|-------|-------|
| | High | Low | High | Low |
| First quarter | \$26.34 | 22.19 | 27.47 | 22.27 |
| Second quarter | 27.68 | 24.31 | 30.08 | 24.76 |
| Third quarter | 29.99 | 25.49 | 29.88 | 24.33 |
| Fourth quarter | 37.66 | 27.50 | 29.69 | 25.74 |

The following table summarizes the Company's dividends declared during the periods indicated:

| | Years ended | |
|----------------|--------------|------|
| | December 31, | |
| | 2016 | 2015 |
| First quarter | \$ 0.20 | 0.18 |
| Second quarter | 0.20 | 0.19 |
| Third quarter | 0.20 | 0.19 |
| Fourth quarter | 0.20 | 0.19 |
| Special | 0.30 | 0.30 |
| Total | \$ 1.10 | 1.05 |

Future cash dividends will depend on a variety of factors, including net income, capital, asset quality, general economic conditions and regulatory considerations. Information regarding the regulation considerations is set forth under the heading "Supervision and Regulation" in "Item 1. Business."

Issuer Stock Purchases

The Company made no stock repurchases during 2016.

Stock Performance Graphs

The following graphs compare the yearly cumulative total return of the Company's common stock over both a five-year and ten-year measurement period with the yearly cumulative total return on the stocks included in 1) the Russell 2000 Index; and 2) the SNL Bank Index comprised of banks and bank holding companies with total assets between \$5 billion and \$10 billion. Each of the cumulative total returns is computed assuming the reinvestment of dividends at the frequency with which dividends were paid during the applicable years.

Item 6. Selected Financial Data

The following financial data of the Company is derived from the Company's historical audited financial statements and related notes. The information set forth below should be read in conjunction with "Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations" and "Item 8. Financial Statements and Supplementary Data" contained elsewhere in this Annual Report on Form 10-K.

| (Dollars in thousands, except per share data) | December 31, | | | | | Compounded Annual Growth Rate | | | |
|---|--------------|-------------|-------------|-------------|-------------|-------------------------------|--------|--------|----|
| | 2016 | 2015 | 2014 | 2013 | 2012 | 1-Year | 5-Year | | |
| Selected Statements of Financial Condition Information | | | | | | | | | |
| Total assets | \$9,450,600 | \$9,089,232 | \$8,306,507 | \$7,884,350 | \$7,747,440 | 4.0 | % | 5.6 | % |
| Investment securities | 3,101,151 | 3,312,832 | 2,908,425 | 3,222,829 | 3,683,005 | (6.4) |)% | (0.2) |)% |
| Loans receivable, net | 5,554,891 | 4,948,984 | 4,358,342 | 3,932,487 | 3,266,571 | 12.2 | % | 10.8 | % |
| Allowance for loan and lease losses | (129,572) | (129,697) | (129,753) | (130,351) | (130,854) | (0.1) |)% | (1.2) |)% |
| Goodwill and intangibles | 159,400 | 155,193 | 140,606 | 139,218 | 112,274 | 2.7 | % | 6.9 | % |
| Deposits | 7,372,279 | 6,945,008 | 6,345,212 | 5,579,967 | 5,364,461 | 6.2 | % | 8.9 | % |
| Federal Home Loan Bank advances | 251,749 | 394,131 | 296,944 | 840,182 | 997,013 | (36.1) |)% | (25.1) |)% |
| Securities sold under agreements to repurchase and other borrowed funds | 478,090 | 430,016 | 404,418 | 321,781 | 299,540 | 11.2 | % | 12.2 | % |
| Stockholders' equity | 1,116,869 | 1,076,650 | 1,028,047 | 963,250 | 900,949 | 3.7 | % | 5.6 | % |
| Equity per share | 14.59 | 14.15 | 13.70 | 12.95 | 12.52 | 3.1 | % | 4.3 | % |
| Equity as a percentage of total assets | 11.82 | % 11.85 | % 12.38 | % 12.22 | % 11.63 | % (0.3) |)% | — | % |

| (Dollars in thousands, except per share data) | Years ended December 31, | | | | | Compounded Annual Growth Rate | | | |
|---|--------------------------|-----------|-----------|-----------|-----------|-------------------------------|--------|--------|----|
| | 2016 | 2015 | 2014 | 2013 | 2012 | 1-Year | 5-Year | | |
| Summary Statements of Operations | | | | | | | | | |
| Interest income | \$344,153 | \$319,681 | \$299,919 | \$263,576 | \$253,757 | 7.7 | % | 4.2 | % |
| Interest expense | 29,631 | 29,275 | 26,966 | 28,758 | 35,714 | 1.2 | % | (7.8) |)% |
| Net interest income | 314,522 | 290,406 | 272,953 | 234,818 | 218,043 | 8.3 | % | 5.9 | % |
| Provision for loan losses | 2,333 | 2,284 | 1,912 | 6,887 | 21,525 | 2.1 | % | (48.5) |)% |
| Non-interest income | 107,318 | 98,761 | 90,302 | 93,047 | 91,496 | 8.7 | % | 6.5 | % |
| Non-interest expense | 258,714 | 236,757 | 212,679 | 195,317 | 193,421 | 9.3 | % | 6.1 | % |
| Income before income taxes | 160,793 | 150,126 | 148,664 | 125,661 | 94,593 | 7.1 | % | 22.9 | % |
| Income tax expense | 39,662 | 33,999 | 35,909 | 30,017 | 19,077 | 16.7 | % | 40.4 | % |
| Net income | \$121,131 | \$116,127 | \$112,755 | \$95,644 | \$75,516 | 4.3 | % | 19.3 | % |
| Basic earnings per share | \$1.59 | \$1.54 | \$1.51 | \$1.31 | \$1.05 | 3.2 | % | 17.8 | % |
| Diluted earnings per share | \$1.59 | \$1.54 | \$1.51 | \$1.31 | \$1.05 | 3.2 | % | 17.8 | % |

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| | | | | | | | | | |
|---|--------|--------|--------|--------|--------|-----|---|------|---|
| Dividends declared per share ¹ | \$1.10 | \$1.05 | \$0.98 | \$0.60 | \$0.53 | 4.8 | % | 16.2 | % |
|---|--------|--------|--------|--------|--------|-----|---|------|---|

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| (Dollars in thousands) | At or for the Years ended December 31, | | | | | |
|---|--|-----------|-----------|-----------|-----------|---|
| | 2016 | 2015 | 2014 | 2013 | 2012 | |
| Selected Ratios and Other Data | | | | | | |
| Return on average assets | 1.32 | % 1.36 | % 1.42 | % 1.23 | % 1.01 | % |
| Return on average equity | 10.79 | % 10.84 | % 11.11 | % 10.22 | % 8.54 | % |
| Dividend payout ratio ¹ | 69.18 | % 68.18 | % 64.90 | % 45.80 | % 50.48 | % |
| Average equity to average asset ratio | 12.27 | % 12.52 | % 12.81 | % 11.99 | % 11.84 | % |
| Total capital (to risk-weighted assets) | 16.38 | % 17.17 | % 18.93 | % 18.97 | % 20.09 | % |
| Tier 1 capital (to risk-weighted assets) | 15.12 | % 15.91 | % 17.67 | % 17.70 | % 18.82 | % |
| Common Equity Tier 1 (to risk-weighted assets) | 13.42 | % 14.06 | % N/A | N/A | N/A | |
| Tier 1 capital (to average assets) | 11.90 | % 12.01 | % 12.45 | % 12.11 | % 11.31 | % |
| Net interest margin on average earning assets (tax-equivalent) | 4.02 | % 4.00 | % 3.98 | % 3.48 | % 3.37 | % |
| Efficiency ratio ² | 55.88 | % 55.40 | % 54.31 | % 54.51 | % 54.02 | % |
| Allowance for loan and lease losses as a percent of loans | 2.28 | % 2.55 | % 2.89 | % 3.21 | % 3.85 | % |
| Allowance for loan and lease losses as a percent of nonperforming loans | 257 | % 244 | % 209 | % 158 | % 133 | % |
| Non-performing assets as a percentage of subsidiary assets | 0.76 | % 0.88 | % 1.08 | % 1.39 | % 1.87 | % |
| Non-performing assets | \$71,385 | 80,079 | 89,900 | 109,420 | 143,527 | |
| Loans originated and acquired | \$3,474,000 | 3,000,830 | 2,404,299 | 2,477,804 | 2,237,977 | |
| Number of full time equivalent employees | 2,222 | 2,149 | 1,943 | 1,837 | 1,677 | |
| Number of locations | 142 | 144 | 129 | 118 | 108 | |

¹ Includes a special dividend declared of \$0.30 per share for 2016, 2015 and 2014.

² Non-interest expense before OREO expenses, core deposit intangibles amortization, goodwill impairment charges, and non-recurring expense items as a percentage of tax-equivalent net interest income and non-interest income, excluding gains or losses on sale of investments, OREO income, and non-recurring income items.

Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations

The following discussion is intended to provide a more comprehensive review of the Company's operating results and financial condition than can be obtained from reading the Consolidated Financial Statements alone. The discussion should be read in conjunction with the Consolidated Financial Statements and the notes thereto included in "Item 8. Financial Statements and Supplementary Data."

CAUTIONARY NOTE REGARDING FORWARD-LOOKING STATEMENTS

This Annual Report on Form 10-K may contain forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. These forward-looking statements include, but are not limited to, statements about the Company's plans, objectives, expectations and intentions that are not historical facts, and other statements identified by words such as "expects," "anticipates," "intends," "plans," "believes," "should," "projects," "seeks," "estimates", negative version of those words or other comparable words or phrases of a future or forward-looking nature. These forward-looking statements are based on current beliefs and expectations of management and are inherently subject to significant business, economic and competitive uncertainties and contingencies, many of which are beyond the Company's control. In addition, these forward-looking statements are subject to assumptions with respect to future business strategies and decisions that are subject to change. The following factors, among others, could cause actual results to differ materially from the anticipated results (express or implied) or other expectations in the forward-looking statements, including those set forth in this Annual Report on Form 10-K, or the documents incorporated by reference:

- the risks associated with lending and potential adverse changes of the credit quality of loans in the Company's portfolio;
- changes in trade, monetary and fiscal policies and laws, including interest rate policies of the Board of Governors of the Federal Reserve System or the Federal Reserve Board, which could adversely affect the Company's net interest income and profitability;
- changes in the cost and scope of insurance from the FDIC and other third parties;
- legislative or regulatory changes, including increased banking and consumer protection regulation that adversely affect the Company's business;
- inability to complete pending or prospective future acquisitions, limit certain sources of revenue, or increase cost of operations;
- costs or difficulties related to the completion and integration of acquisitions;
- the goodwill the Company has recorded in connection with acquisitions could become impaired, which may have an adverse impact on earnings and capital;
- reduced demand for banking products and services;
- the reputation of banks and the financial services industry could deteriorate, which could adversely affect the Company's ability to obtain (and maintain) customers;
- competition among financial institutions in the Company's markets may increase significantly;
- the risks presented by continued public stock market volatility, which could adversely affect the market price of the Company's common stock and the ability to raise additional capital or grow the Company through acquisitions;
- the projected business and profitability of an expansion or the opening of a new branch could be lower than expected;
- consolidation in the financial services industry in the Company's markets resulting in the creation of larger financial institutions who may have greater resources could change the competitive landscape;
- dependence on the CEO, the senior management team and the Presidents of Glacier Bank divisions;
- material failure, potential interruption or breach in security of the Company's systems and technological changes which could expose us to new risks (e.g., cybersecurity), fraud or system failures;
- natural disasters, including fires, floods, earthquakes, and other unexpected events;
- the Company's success in managing risks involved in the foregoing; and
- the effects of any reputational damage to the Company resulting from any of the foregoing.

Additional factors that could cause actual results to differ materially from those expressed in the forward-looking statements are discussed in “Item 1A. Risk Factors.” Please take into account that forward-looking statements speak only as of the date of this Annual Report on Form 10-K (or documents incorporated by reference, if applicable). Given the described uncertainties and risks, the Company cannot guarantee its future performance or results of operations and you should not place undue reliance on these forward-looking statements. The Company does not undertake any obligation to publicly correct, revise, or update any forward-looking statement if it later becomes aware that actual results are likely to differ materially from those expressed in such forward-looking statement, except as required under federal securities laws.

MANAGEMENT'S DISCUSSION AND ANALYSIS
OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS
YEAR ENDED DECEMBER 31, 2016 COMPARED TO DECEMBER 31, 2015

Highlights and Overview

During the current year, the Company completed a two year project to consolidate the Company's thirteen core bank division database systems into one core database system (Core Consolidation Project or "CCP"). The primary reasons for the project were to increase efficiencies and prepare the Company for the future, including reaching \$10 billion in asset size and complying with the Dodd-Frank Act stress tests ("DFAST"). The Bank divisions continue to operate as separate divisions with their own management teams, which has been a cornerstone of the Company's success. During 2015, the Company focused on the planning phase of the CCP project and during 2016 the Company converted the thirteen core bank division databases during various phases throughout the year. The employees of the Company worked diligently on the project which contributed to the success of the conversions while the minimally impacting the Company's customers. As a result of the successful completion of the project, the Company is well positioned to begin taking advantage of efficiencies and continue planning for DFAST in the coming years.

During the third quarter of 2016, the Company completed the acquisition of TSB, a bank based in Missoula, Montana. TSB became a part of the First Security Bank of Missoula bank division. During the fourth quarter of 2016, the Company also successfully completed the data processing system conversion for this acquisition. During the fourth quarter of 2016, the Company announced the acquisition of The Foothills Bank, a community bank based in Yuma, Arizona. Foothills provides banking services to individuals and businesses in Arizona, with four banking offices located in Yuma, Prescott, and Casa Grande Arizona. The branches of Foothills will become the Company's fourteenth Bank division. As of December 31, 2016, Foothills had total assets of \$335 million, gross loans of \$280 million and total deposits of \$282 million.

At year end, Mick Blodnick retired and effective January 1, 2017, Randy Chesler became the Company's President and Chief Executive Officer of the Company after a seventeen month succession period. Mr. Chesler brings to the Company more than 30 years of experience in the financial services industry, most recently as President of CIT Bank, the Salt Lake City-based banking subsidiary of CIT Group.

The Company experienced another strong year for organic loan growth, which allowed the Company to redeploy cash flows from investment securities to the loan portfolio. Deposit growth was another bright spot which funded the loan growth and allowed the Company to reduce borrowings. Excluding the acquisition, the loan portfolio increased \$554 million, or 11 percent, during the current year, with the primary increases in commercial real estate loans and commercial loans which increased \$331 million and \$235 million, respectively. Excluding the acquisition and wholesale deposits, the Company's non-interest bearing deposits increased \$111 million, or 6 percent, during the current year, while interest bearing deposits increased \$155 million, or 3 percent. Tangible stockholders' equity increased \$36 million, or \$0.40 per share, as a result of earnings retention and Company stock issued in connection with the current year acquisition, both of which offset the decrease in accumulated other comprehensive income and increases in goodwill and intangibles from the acquisition. The Company increased its total dividends declared from \$1.05 per share during 2015 to \$1.10 per share in 2016.

The Company continued to reduce its non-performing assets and ended the year at \$71.4 million which was a decrease of \$8.7 million or, 11 percent, from the prior year end. The provision for loan losses for the current year remained flat with prior year at \$2.3 million, while net charge offs were \$2.5 million in 2016 and \$2.3 million in 2015. Loan portfolio growth, composition, average loan size, credit quality considerations, and other environmental factors will continue to determine the provision for loan losses.

The Company had record earnings of \$121 million for 2016, which was an increase of \$5.0 million, or 4 percent, over the 2015 net income of \$116 million. Diluted earnings per share for 2016 was \$1.59, an increase of \$0.05, or 3 percent, from the prior year diluted earnings per share of \$1.54. The net income improvement for 2016 over 2015 was principally due to an increase in interest income from the commercial loan portfolio and an increase in non-interest income which outpaced the increase in non-interest expense.

Looking forward, the Company's future performance will depend on many factors including economic conditions in the markets the Company serves, interest rate changes, increasing competition for deposits and loans, loan quality and growth, the impact and successful integration of acquisitions, and regulatory burden.

Financial Highlights

| (Dollars in thousands, except per share data) | At or for the Years ended | | |
|---|---------------------------|-------------------|---|
| | December 31, 2016 | December 31, 2015 | |
| Operating results | | | |
| Net income | \$ 121,131 | 116,127 | |
| Basic earnings per share | \$ 1.59 | 1.54 | |
| Diluted earnings per share | \$ 1.59 | 1.54 | |
| Dividends declared per share | \$ 1.10 | 1.05 | |
| Market value per share | | | |
| Closing | \$36.23 | 26.53 | |
| High | \$37.66 | 30.08 | |
| Low | \$22.19 | 22.27 | |
| Selected ratios and other data | | | |
| Number of common stock shares outstanding | 76,525,402 | 76,086,288 | |
| Average outstanding shares - basic | 76,278,463 | 75,542,455 | |
| Average outstanding shares - diluted | 76,341,836 | 75,595,581 | |
| Return on average assets (annualized) | 1.32 | % 1.36 | % |
| Return on average equity (annualized) | 10.79 | % 10.84 | % |
| Efficiency ratio | 55.88 | % 55.40 | % |
| Dividend payout ratio | 69.18 | % 68.18 | % |
| Loan to deposit ratio | 78.10 | % 73.94 | % |
| Number of full time equivalent employees | 2,222 | 2,149 | |
| Number of locations | 142 | 144 | |
| Number of ATMs | 166 | 158 | |

Acquisitions

On August 31, 2016, the Company completed the acquisition of TSB, which resulted in goodwill of \$6.4 million. On October 31, 2015, the Company completed the acquisition of Cañon, which resulted in goodwill of \$9.8 million. On February 28, 2015, the Company completed the acquisition of CB, which resulted in goodwill of \$1.1 million. The Company's results of operations and financial condition include the acquisitions of TSB, Cañon and CB from the acquisition dates. For additional information regarding acquisitions, see Note 22 to the Consolidated Financial Statements in "Item 8. Financial Statements and Supplementary Data."

The following table provides information on the fair value of selected classifications of assets and liabilities acquired:

| (Dollars in thousands) | TSB | Cañon | CB |
|--|-----------------|------------------|-------------------|
| | August 31, 2016 | October 31, 2015 | February 28, 2015 |
| Total assets | \$ 76,165 | 270,121 | 175,774 |
| Investment securities | — | 68,486 | 42,350 |
| Loans receivable | 51,875 | 159,759 | 84,689 |
| Non-interest bearing deposits | 13,005 | 89,083 | 41,779 |
| Interest bearing deposits | 45,359 | 148,243 | 105,041 |
| Federal Home Loan Bank advances and securities sold under agreements to repurchase | 3,260 | — | 3,292 |

Financial Condition Analysis

Assets

The following table summarizes the Company's assets as of the dates indicated:

| (Dollars in thousands) | December 31, 2016 | December 31, 2015 | \$ Change | % Change |
|---|----------------------|----------------------|-------------|-------------|
| Cash and cash equivalents | \$ 152,541 | \$ 193,253 | \$(40,712) | (21)% |
| Investment securities, available-for-sale | 2,425,477 | 2,610,760 | (185,283) | (7)% |
| Investment securities, held-to-maturity | 675,674 | 702,072 | (26,398) | (4)% |
| Total investment securities | 3,101,151 | 3,312,832 | (211,681) | (6)% |
| Loans receivable | | | | |
| Residential real estate | 674,347 | 688,912 | (14,565) | (2)% |
| Commercial real estate | 2,990,141 | 2,633,953 | 356,188 | 14 % |
| Other commercial | 1,342,250 | 1,099,564 | 242,686 | 22 % |
| Home equity | 434,774 | 420,901 | 13,873 | 3 % |
| Other consumer | 242,951 | 235,351 | 7,600 | 3 % |
| Loans receivable | 5,684,463 | 5,078,681 | 605,782 | 12 % |
| Allowance for loan and lease losses | (129,572) | (129,697) | 125 | — % |
| Loans receivable, net | 5,554,891 | 4,948,984 | 605,907 | 12 % |
| Other assets | 642,017 | 634,163 | 7,854 | 1 % |
| Total assets | \$9,450,600 | \$9,089,232 | \$361,368 | 4 % |

Total investment securities decreased \$212 million, or 6 percent, from the prior year end. The Company continues to selectively purchase investments securities when the Company has excess liquidity, although, the overall trend is a reduction in the investment securities portfolio since the Company has successfully been able to redeploy the securities portfolio cash flow into the Company's higher yielding loan portfolio. Investment securities represented 33 percent of total assets at December 31, 2016 compared to 36 percent of total assets at December 31, 2015.

Excluding the acquisition of TSB, the loan portfolio increased \$554 million, or 11 percent, since December 31, 2015 with \$331 million and \$235 million of the increase coming from growth in commercial real estate and other commercial loans, respectively. This compares to the prior year organic growth of \$346 million, or 8 percent, with the primary growth in commercial loans as well. The Company was pleased by the organic growth over the past few years as many of the Company's market areas are demonstrating stronger economic conditions. The Company continues to originate loans under conservative underwriting standards and monitors the loan portfolio to maintain the risk profile within the Company's policy limits.

Liabilities

The following table summarizes the liability balances as of the dates indicated, and the amount of change from December 31, 2015:

| (Dollars in thousands) | December 31, 2016 | December 31, 2015 | \$ Change | % Change |
|--|----------------------|----------------------|------------|-------------|
| Deposits | | | | |
| Non-interest bearing deposits | \$2,041,852 | \$1,918,310 | \$123,542 | 6 % |
| NOW and DDA accounts | 1,588,550 | 1,516,026 | 72,524 | 5 % |
| Savings accounts | 996,061 | 838,274 | 157,787 | 19 % |
| Money market deposit accounts | 1,464,415 | 1,382,028 | 82,387 | 6 % |
| Certificate accounts | 948,714 | 1,060,650 | (111,936) | (11)% |
| Core deposits, total | 7,039,592 | 6,715,288 | 324,304 | 5 % |
| Wholesale deposits | 332,687 | 229,720 | 102,967 | 45 % |
| Deposits, total | 7,372,279 | 6,945,008 | 427,271 | 6 % |
| Securities sold under agreements to repurchase | 473,650 | 423,414 | 50,236 | 12 % |
| Federal Home Loan Bank advances | 251,749 | 394,131 | (142,382) | (36)% |
| Other borrowed funds | 4,440 | 6,602 | (2,162) | (33)% |
| Subordinated debentures | 125,991 | 125,848 | 143 | — % |
| Other liabilities | 105,622 | 117,579 | (11,957) | (10)% |
| Total liabilities | \$8,333,731 | \$8,012,582 | \$321,149 | 4 % |

Excluding the TSB acquisition, non-interest bearing deposits increased \$111 million, or 6 percent, from December 31, 2015. Excluding the TSB acquisition, core interest bearing deposits increased \$155 million, or 3 percent, from December 31, 2015. Wholesale deposits (i.e., brokered deposits classified as NOW, DDA, money market deposit and certificate accounts) of \$333 million at December 31, 2016 increased \$103 million since December 31, 2015, the majority of the increase was driven by a need to obtain wholesale deposits necessary for an interest rate swap. In addition to increasing deposit balances, the Company was successful in originating and retaining new core deposit accounts during the current and prior year.

Securities sold under agreements to repurchase (“repurchase agreements”) of \$474 million at December 31, 2016 increased \$50.2 million, or 12 percent, from the prior year end. Repurchase agreements fluctuated as certain customers had significant deposit cash flows. Federal Home Loan Bank (“FHLB”) advances of \$252 million at December 31, 2016, decreased \$142 million, or 36 percent, as a result of long-term advances maturing and not being replaced due to the increase in core deposits which were sufficient to fund loan growth.

Stockholders' Equity

The following table summarizes the stockholders' equity balances as of the dates indicated and the amount of change from December 31, 2015:

| (Dollars in thousands, except per share data) | December 31, 2016 | December 31, 2015 | \$ Change | % Change |
|--|----------------------|----------------------|-----------|-------------|
| Common equity | \$1,124,251 | \$1,074,661 | \$49,590 | 5 % |
| Accumulated other comprehensive (loss) income | (7,382) | 1,989 | (9,371) | (471)% |
| Total stockholders' equity | 1,116,869 | 1,076,650 | 40,219 | 4 % |
| Goodwill and core deposit intangible, net | (159,400) | (155,193) | (4,207) | 3 % |
| Tangible stockholders' equity | \$957,469 | \$921,457 | \$36,012 | 4 % |
| Stockholders' equity to total assets | 11.82 % | 11.85 % | — | — % |
| Tangible stockholders' equity to total tangible assets | 10.31 % | 10.31 % | — | — % |
| Book value per common share | \$14.59 | \$14.15 | \$0.44 | 3 % |
| Tangible book value per common share | \$12.51 | \$12.11 | \$0.40 | 3 % |

Tangible stockholders' equity increased \$36.0 million, or 4 percent, from a year ago, the result of earnings retention and \$10.5 million of Company stock issued in connection with the TSB acquisition; such increases more than offset the increase in goodwill and other intangibles from the acquisition and the decrease in accumulated other comprehensive income. Tangible book value per common share increased \$0.40 per share from a year ago and was principally due to earnings retention.

Results of Operations

Income Summary

The following table summarizes revenue for the periods indicated, including the amount and percentage changes from December 31, 2015:

| (Dollars in thousands) | Years ended | | \$ Change | % Change | |
|--------------------------------------|-------------------|-------------------|-----------|----------|---|
| | December 31, 2016 | December 31, 2015 | | | |
| Net interest income | | | | | |
| Interest income | \$344,153 | \$319,681 | \$24,472 | 8 | % |
| Interest expense | 29,631 | 29,275 | 356 | 1 | % |
| Total net interest income | 314,522 | 290,406 | 24,116 | 8 | % |
| Non-interest income | | | | | |
| Service charges and other fees | 62,405 | 59,286 | 3,119 | 5 | % |
| Miscellaneous loan fees and charges | 4,613 | 4,276 | 337 | 8 | % |
| Gain on sale of loans | 33,606 | 26,389 | 7,217 | 27 | % |
| (Loss) gain on sale of investments | (1,463) | 19 | (1,482) | (7,800) | % |
| Other income | 8,157 | 8,791 | (634) | (7) | % |
| Total non-interest income | 107,318 | 98,761 | 8,557 | 9 | % |
| | \$421,840 | \$389,167 | \$32,673 | 8 | % |
| Net interest margin (tax-equivalent) | 4.02 | % 4.00 | | | % |

Net Interest Income

Net interest income for the the current year was \$315 million, an increase of \$24.1 million, or 8 percent, over the same period last year. Interest income for the the current year increased \$24.5 million, or 8 percent, from the prior year and was principally due to a \$24.0 million increase in income from commercial loans. Additional increases included a \$1.3 million in interest income from residential loans.

Interest expense of \$29.6 million for the current year increased \$356 thousand, or 1 percent, over the the same period in the prior year. Deposit interest expense for the current year increased \$2.3 million, or 14 percent, from the prior year and was driven by an increase in wholesale deposits and the additional interest expense for an interest rate swap with a notional amount of \$100 million that began accruing in December 2015. FHLB interest expense decreased \$2.6 million, or 30 percent, as the need for wholesale funding has decreased with strong deposit growth. The total funding cost (including non-interest bearing deposits) for 2016 was 37 basis points compared to 40 basis points for 2015.

The net interest margin as a percentage of earning assets, on a tax-equivalent basis, for 2016 was 4.02 percent, a 2 basis point increase from the net interest margin of 4.00 percent for 2015. The increase in the margin was primarily attributable to a shift in earning assets to higher yielding loans combined with a continued increase in low cost deposits.

Non-interest Income

Non-interest income of \$107.3 million for 2016 increased \$8.6 million, or 9 percent, over the same period last year. Service charges and other fees of \$62.4 million for 2016 increased \$3.1 million, or 5 percent, from the same period

last year as a result of an increased number of deposit accounts, both from organic growth and from recent acquisitions. The gain of \$33.6 million on the sale of loans for 2016 increased \$7.2 million, or 27 percent, from 2015 which was attributable to the stronger housing market and the low interest rate environment. Included in other income was operating revenue of \$127 thousand from OREO and gains of \$918 thousand from the sales of OREO, which totaled \$1.0 million for 2016 compared to \$1.1 million for the prior year.

Non-interest Expense

The following table summarizes non-interest expense for the periods indicated, including the amount and percentage changes from December 31, 2015:

| (Dollars in thousands) | Years ended | | \$ Change | % Change | |
|--------------------------------------|-------------------|-------------------|-----------|----------|---|
| | December 31, 2016 | December 31, 2015 | | | |
| Compensation and employee benefits | \$ 151,697 | \$ 134,409 | \$ 17,288 | 13 | % |
| Occupancy and equipment | 25,979 | 25,505 | 474 | 2 | % |
| Advertising and promotions | 8,433 | 8,661 | (228) | (3) | % |
| Data processing | 14,800 | 11,477 | 3,323 | 29 | % |
| Other real estate owned | 2,895 | 3,693 | (798) | (22) | % |
| Regulatory assessments and insurance | 4,780 | 5,283 | (503) | (10) | % |
| Core deposit intangible amortization | 2,970 | 2,964 | 6 | — | % |
| Other expenses | 47,160 | 44,765 | 2,395 | 5 | % |
| Total non-interest expense | \$ 258,714 | \$ 236,757 | \$ 21,957 | 9 | % |

Non-interest expense of \$259 million increased \$22.0 million, or 9 percent, over the prior year. Included in current year non-interest expense was \$4.3 million of CCP related expenses. Compensation and employee benefits for 2016 increased \$17.3 million, or 13 percent, from the same period due to the increased number of employees including from the acquired banks and annual salary increases. Occupancy and equipment expense of \$26.0 million for 2016 increased \$474 thousand, or 2 percent, over the prior year. Outsourced data processing expense increased \$3.3 million, or 29 percent, from the prior year primarily the result of additional costs from CCP. OREO expense of \$2.9 million in the current year decreased \$798 thousand, or 22 percent, from the the prior year. OREO expense for 2016 included \$761 thousand of operating expenses, \$1.8 million of fair value write-downs, and \$314 thousand of loss from the sales of OREO. Current year other expenses of \$47.2 million increased \$2.4 million, or 5 percent, from the prior year and was driven by increases from costs associated with CCP.

Efficiency Ratio

The efficiency ratio was 55.88 percent for 2016 compared to 55.40 percent for 2015. Although there were increases in both net interest income and non-interest income, such increases were outpaced by the increases in CCP expenses and compensation expenses which contributed to the higher efficiency ratio in 2016.

Provision for Loan Losses

The following table summarizes the provision for loan losses, net charge-offs and other select ratios for the previous eight quarters:

| (Dollars in thousands) | Provision for Loan Losses | Net Charge-Offs (Recoveries) | ALLL as a Percent of Loans | Accruing Loans 30-89 Days Past Due as a Percent of Loans | Non-Performing Assets to Total Sub-sidiary Assets |
|------------------------|---------------------------|------------------------------|----------------------------|--|---|
| Fourth quarter 2016 | \$ 1,139 | \$ 4,101 | 2.28 % | 0.45 % | 0.76 % |
| Third quarter 2016 | 626 | 478 | 2.37 % | 0.49 % | 0.84 % |
| Second quarter 2016 | — | (2,315) | 2.46 % | 0.44 % | 0.82 % |
| First quarter 2016 | 568 | 194 | 2.50 % | 0.46 % | 0.88 % |
| Fourth quarter 2015 | 411 | 1,482 | 2.55 % | 0.38 % | 0.88 % |
| Third quarter 2015 | 826 | 577 | 2.68 % | 0.37 % | 0.97 % |
| Second quarter 2015 | 282 | (381) | 2.71 % | 0.59 % | 0.98 % |
| First quarter 2015 | 765 | 662 | 2.77 % | 0.71 % | 1.07 % |

The provision for loan losses was \$2.3 million for 2016, an increase of \$49 thousand, or 2 percent, from the same period in the prior year. Net charge-offs during 2016 was \$2.5 million which was relatively flat compared to the net charge-offs of \$2.3 million for 2015, although the quarterly net charge-offs continue to experience a fair amount of volatility.

MANAGEMENT'S DISCUSSION AND ANALYSIS
OF THE RESULTS OF OPERATIONS
YEAR ENDED DECEMBER 31, 2015 COMPARED TO DECEMBER 31, 2014

Income Summary

The following table summarizes revenue for the periods indicated, including the amount and percentage changes from December 31, 2014:

| (Dollars in thousands) | Years ended | | | |
|--------------------------------------|-------------------|-------------------|-----------|----------|
| | December 31, 2015 | December 31, 2014 | \$ Change | % Change |
| Net interest income | | | | |
| Interest income | \$319,681 | \$299,919 | \$19,762 | 7 % |
| Interest expense | 29,275 | 26,966 | 2,309 | 9 % |
| Total net interest income | 290,406 | 272,953 | 17,453 | 6 % |
| Non-interest income | | | | |
| Service charges and other fees | 59,286 | 56,043 | 3,243 | 6 % |
| Miscellaneous loan fees and charges | 4,276 | 4,696 | (420) | (9)% |
| Gain on sale of loans | 26,389 | 19,797 | 6,592 | 33 % |
| Gain (loss) on sale of investments | 19 | (188) | 207 | (110)% |
| Other income | 8,791 | 9,954 | (1,163) | (12)% |
| Total non-interest income | 98,761 | 90,302 | 8,459 | 9 % |
| | \$389,167 | \$363,255 | \$25,912 | 7 % |
| Net interest margin (tax-equivalent) | 4.00 % | 3.98 % | | |

Net Interest Income

Interest income for 2015 increased \$19.8 million, or 7 percent, from the prior year and was principally due to an increase in interest income from commercial loans. Interest income of \$165 million from commercial loans increased \$19.3 million, or 13 percent, from the prior year and was primarily the result of an increased volume of commercial loans. Interest income of \$91.1 million on investment securities decreased \$2.0 million, or 2 percent, over the same period last year. On a tax-equivalent basis, interest income for 2015 of \$118.8 million on investment securities increased \$2.8 million, or 2 percent, over the prior year.

Interest expense for 2015 increased \$2.3 million, or 9 percent, from the prior year and was primarily due to the interest expense associated with the interest rate swaps undertaken to reduce the Company's sensitivity to rising interest rates. At December 31, 2015, the Company had interest rate swaps with total notional amounts of \$260 million, such interest rate swaps including two separate contracts with delayed start accrual periods that began in October 2014 and November 2015. The Company designated wholesale deposits as the cash flow hedge for its interest rate swaps and the related interest expense is included in wholesale deposits. Excluding the impact of the interest rate swaps, interest expense for 2015 decreased by \$1.7 million, or 7 percent, from the prior year. The total funding cost (including non-interest bearing deposits) for 2015 was 40 basis points compared to 39 basis points for the prior year.

The net interest margin as a percentage of earning assets, on a tax-equivalent basis, for 2015 was 4.00 percent, an increase of 2 basis points from the prior year net interest margin of 3.98 percent. The 2 basis points increase was attributable to a combination of items including a shift in earning assets to the higher yielding loan portfolio and an increased yield on the investment securities portfolio. In addition, the lower yield on core deposits offset the increased interest expense from the interest rate swaps. Excluding the effects of the interest rate swaps, the cost of funds for 2015 was 33 basis points compared to 38 basis points in the prior year.

Non-interest Income

Non-interest income of \$98.8 million for 2015 increased \$8.5 million, or 9 percent, over the same period in the prior year. Service charges and other fees of \$61.6 million for 2015 increased \$2.8 million, or 5 percent, from 2014 and was driven by the increased number of deposit accounts and higher usage of deposit services by customers. The gain of \$26.4 million on the sale of residential loans for 2015 increased \$6.6 million, or 33 percent, from the prior year which was attributable to an increase in mortgage refinancing and purchase activity. Other income of \$10.8 million for 2015 decreased \$1.2 million, or 10 percent, over the prior year due to a decrease in gain on sale of OREO and insurance proceeds recognized in the prior year fourth quarter from a bank-owned life insurance policy. Included in other income was operating revenue of \$123 thousand from OREO and gains of \$986 thousand from the sales of OREO, which totaled \$1.1 million for 2015, compared to \$2.3 million for the same period in the prior year.

Non-interest Expense

The following table summarizes non-interest expense for the periods indicated, including the amount and percentage changes from December 31, 2014:

| (Dollars in thousands) | Years ended | | \$ Change | % Change | |
|--------------------------------------|----------------------|----------------------|--------------|----------|---|
| | December 31, 2015 | December 31, 2014 | | | |
| Compensation and employee benefits | \$ 134,409 | \$ 118,571 | \$ 15,838 | 13 | % |
| Occupancy and equipment | 25,505 | 22,718 | 2,787 | 12 | % |
| Advertising and promotions | 8,661 | 7,912 | 749 | 9 | % |
| Data processing | 11,477 | 11,387 | 90 | 1 | % |
| Other real estate owned | 3,693 | 2,568 | 1,125 | 44 | % |
| Regulatory assessments and insurance | 5,283 | 5,064 | 219 | 4 | % |
| Core deposit intangible amortization | 2,964 | 2,811 | 153 | 5 | % |
| Other expenses | 44,765 | 41,648 | 3,117 | 7 | % |
| Total non-interest expense | \$ 236,757 | \$ 212,679 | \$ 24,078 | 11 | % |

Compensation and employee benefits expense for 2015 increased \$15.8 million, or 13 percent, from 2014 due to the increased number of employees, primarily from the acquired banks, additional benefit costs and annual salary increases. Occupancy and equipment expense increased \$2.8 million, or 12 percent, as a result of increased costs associated with acquisitions and equipment expense related to additional information technology infrastructure. OREO expense of \$3.7 million in 2015 increased \$1.1 million, or 44 percent, from the prior year. OREO expenses continued to fluctuate based on the level of activity in various quarters. OREO expense for 2015 included \$1.8 million of operating expenses, \$1.6 million of fair value write-downs, and \$349 thousand of loss from the sales of OREO. OREO expense for 2014 included \$1.4 million of operating expenses, \$691 thousand of fair value write-downs, and \$442 thousand of loss from the sales of OREO. Other expense of \$44.8 million for 2015 increased by \$3.1 million, or 7 percent, from the prior year primarily due to increases in conversion- and acquisition-related expenses.

Efficiency Ratio

The efficiency ratio was 55.40 percent for 2015 compared to 54.31 percent for 2014. The increase in the efficiency ratio resulted primarily from compensation expense from increased acquired bank employees and salary increases outpacing the increase in net interest income primarily from commercial loans and non-interest income principally from the increase in gain on sale of loans.

Provision for Loan Losses

The provision for loan losses was \$2.3 million for 2015, an increase of \$372 thousand, or 19 percent, from the same period in the prior year. Net charged-off loans during 2015 were \$2.3 million, a decrease of \$170 thousand from 2014.

ADDITIONAL MANAGEMENT'S DISCUSSION AND ANALYSIS

Investment Activity

Investment securities classified as available-for-sale are carried at estimated fair value and investment securities classified as held-to-maturity are carried at amortized cost. Unrealized gains or losses, net of tax, on available-for-sale securities are reflected as an adjustment to other comprehensive income. The Company's investment securities are summarized below:

| (Dollars in thousands) | December 31, 2016 | | December 31, 2015 | | December 31, 2014 | | December 31, 2013 | | December 31, 2012 | |
|---------------------------------------|-------------------|---------|-------------------|---------|-------------------|---------|-------------------|---------|-------------------|---------|
| | Carrying Amount | Percent |
| Available-for-sale | | | | | | | | | | |
| U.S. government and federal agency | \$39,407 | 1 % | \$47,451 | 1 % | \$44 | — % | \$— | — % | \$202 | — % |
| U.S. government sponsored enterprises | 19,570 | 1 % | 93,167 | 3 % | 21,945 | 1 % | 10,628 | — % | 17,480 | — % |
| State and local governments | 786,373 | 25 % | 885,019 | 27 % | 997,969 | 34 % | 1,385,078 | 43 % | 1,214,518 | 33 % |
| Corporate bonds | 471,951 | 15 % | 384,163 | 12 % | 314,854 | 11 % | 442,501 | 14 % | 288,795 | 8 % |
| Collateralized debt obligations | — | — % | — | — % | — | — % | — | — % | 1,708 | — % |
| Mortgage-backed securities | 1,108,176 | 36 % | 1,200,960 | 36 % | 1,052,616 | 36 % | 1,384,622 | 43 % | 2,160,302 | 59 % |
| Total available-for-sale | 2,425,477 | 78 % | 2,610,760 | 79 % | 2,387,428 | 82 % | 3,222,829 | 100 % | 3,683,005 | 100 % |
| Held-to-maturity | | | | | | | | | | |
| State and local governments | 675,674 | 22 % | 702,072 | 21 % | 520,997 | 18 % | — | — % | — | — % |
| Total held-to-maturity | 675,674 | 22 % | 702,072 | 21 % | 520,997 | 18 % | — | — % | — | — % |
| Total investment securities | \$3,101,151 | 100 % | \$3,312,832 | 100 % | \$2,908,425 | 100 % | \$3,222,829 | 100 % | \$3,683,005 | 100 % |

The Company's investment portfolio is primarily comprised of state and local government securities and mortgage-backed securities. State and local government securities are largely exempt from federal income tax and the Company's maximum federal statutory rate of 35 percent is used in calculating the tax-equivalent yields on the tax-exempt securities. Mortgage-backed securities are primarily short, weighted-average life U.S. agency guaranteed residential mortgage pass-through securities. To a lesser extent, mortgage-backed securities also consist of short, weighted-average life U.S. agency guaranteed residential collateralized mortgage obligations and U.S. agency guaranteed commercial mortgage-backed securities. Combined, the mortgage-backed securities provide the Company with ongoing liquidity as scheduled and pre-paid principal is received on the securities.

State and local government securities carry different risks that are not as prevalent in other security types. The Company evaluates the investment grade quality of its securities in accordance with regulatory guidance. Investment grade securities are those where the issuer has an adequate capacity to meet the financial commitments under the security for the projected life of the investment. An issuer has an adequate capacity to meet financial commitments if the risk of default by the obligor is low and the full and timely payment of principal and interest are expected. In

assessing credit risk, the Company may use credit ratings from Nationally Recognized Statistical Rating Organizations (“NRSRO” entities such as Standard and Poor’s [“S&P”] and Moody’s) as support for the evaluation; however, they are not solely relied upon. There have been no significant differences in the Company’s internal evaluation of the creditworthiness of any issuer when compared with the ratings assigned by the NRSROs.

The following table stratifies the state and local government securities by the associated NRSRO ratings. The highest issued rating was used to categorize the securities in the table for those securities where the NRSRO ratings were not at the same level.

| (Dollars in thousands) | December 31, 2016 | | December 31, 2015 | |
|--|-------------------|-----------|-------------------|-----------|
| | Amortized | Fair | Amortized | Fair |
| | Cost | Value | Cost | Value |
| S&P: AAA / Moody's: Aaa | \$345,527 | 346,301 | 366,961 | 374,470 |
| S&P: AA+, AA, AA- / Moody's: Aa1, Aa2, Aa3 | 879,271 | 894,652 | 936,947 | 971,717 |
| S&P: A+, A, A- / Moody's: A1, A2, A3 | 209,217 | 216,589 | 239,371 | 252,292 |
| S&P: BBB+, BBB, BBB- / Moody's: Baa1, Baa2, Baa3 | 2,270 | 2,352 | 2,858 | 3,017 |
| Not rated by either entity | 13,934 | 14,694 | 12,673 | 13,036 |
| Below investment grade | 850 | 874 | — | — |
| Total | \$1,451,069 | 1,475,462 | 1,558,810 | 1,614,532 |

State and local government securities largely consist of both taxable and tax-exempt general obligation and revenue bonds. The following table stratifies the state and local government securities by the associated security type.

| (Dollars in thousands) | December 31, 2016 | | December 31, 2015 | |
|--------------------------------|-------------------|-----------|-------------------|-----------|
| | Amortized | Fair | Amortized | Fair |
| | Cost | Value | Cost | Value |
| General obligation - unlimited | \$805,779 | 819,990 | 831,518 | 862,863 |
| General obligation - limited | 221,099 | 228,218 | 262,803 | 274,177 |
| Revenue | 389,506 | 391,615 | 423,171 | 434,610 |
| Certificate of participation | 23,590 | 24,603 | 28,245 | 29,634 |
| Other | 11,095 | 11,036 | 13,073 | 13,248 |
| Total | \$1,451,069 | 1,475,462 | 1,558,810 | 1,614,532 |

The following table outlines the five states in which the Company owns the highest concentrations of state and local government securities.

| (Dollars in thousands) | December 31, 2016 | | December 31, 2015 | |
|------------------------|-------------------|-----------|-------------------|-----------|
| | Amortized | Fair | Amortized | Fair |
| | Cost | Value | Cost | Value |
| Texas | \$193,652 | 196,641 | 211,023 | 218,051 |
| Washington | 188,778 | 193,035 | 179,173 | 187,949 |
| Michigan | 173,400 | 177,305 | 156,426 | 162,862 |
| Montana | 94,168 | 97,259 | 90,272 | 95,644 |
| California | 93,441 | 94,275 | 105,510 | 108,235 |
| All other states | 707,630 | 716,947 | 816,406 | 841,791 |
| Total | \$1,451,069 | 1,475,462 | 1,558,810 | 1,614,532 |

The following table presents the carrying amount and weighted-average yield of available-for-sale and held-to-maturity investment securities by contractual maturity at December 31, 2016. Weighted-average yields are based upon the amortized cost of securities and are calculated using the interest method which takes into consideration premium amortization, discount accretion and mortgage-backed securities' prepayment provisions. Weighted-average yields on tax-exempt investment securities exclude the federal income tax benefit.

| | One Year or Less | | After One through Five Years | | After Five through Ten Years | | After Ten Years | | Mortgage-Backed Securities | | Total |
|---------------------------------------|------------------|--------|------------------------------|--------|------------------------------|--------|-----------------|--------|----------------------------|--------|-------------|
| | Amount | Yield | Amount | Yield | Amount | Yield | Amount | Yield | Amount | Yield | Amount |
| (Dollars in thousands) | | | | | | | | | | | |
| Available-for-sale | | | | | | | | | | | |
| U.S. government and federal agency | \$— | — % | \$1,299 | 1.21 % | \$11,913 | 0.71 % | \$26,195 | 1.18 % | \$— | — % | \$39,407 |
| U.S. government sponsored enterprises | 430 | 2.23 % | 19,140 | 1.96 % | — | — % | — | — % | — | — % | 19,570 |
| State and local governments | 43,469 | 2.00 % | 52,011 | 2.15 % | 188,741 | 3.43 % | 502,152 | 4.22 % | — | — % | 786,373 |
| Corporate bonds | 105,751 | 2.00 % | 366,200 | 2.08 % | — | — % | — | — % | — | — % | 471,951 |
| Mortgage-backed securities | — | — % | — | — % | — | — % | — | — % | 1,108,176 | 1.90 % | 1,108,176 |
| Total available-for-sale | 149,650 | 2.00 % | 438,650 | 2.08 % | 200,654 | 3.26 % | 528,347 | 4.06 % | 1,108,176 | 1.90 % | 2,425,477 |
| Held-to-maturity | | | | | | | | | | | |
| State and local governments | — | — % | 594 | 1.84 % | 55,310 | 2.94 % | 619,770 | 4.08 % | — | — % | 675,674 |
| Total held-to-maturity | — | — % | 594 | 1.84 % | 55,310 | 2.94 % | 619,770 | 4.08 % | — | — % | 675,674 |
| Total investment securities | \$149,650 | 2.00 % | \$439,244 | 2.08 % | \$255,964 | 3.19 % | \$1,148,117 | 4.07 % | \$1,108,176 | 1.90 % | \$3,101,151 |

Interest income from investment securities consisted of the following:

| (Dollars in thousands) | Years ended | | |
|------------------------|-------------------|-------------------|-------------------|
| | December 31, 2016 | December 31, 2015 | December 31, 2014 |
| Taxable interest | \$40,366 | 40,200 | 45,920 |
| Tax-exempt interest | 50,026 | 50,886 | 47,132 |
| Total interest income | \$90,392 | 91,086 | 93,052 |

For additional information on investment securities, see Notes 1 and 2 to the Consolidated Financial Statements in "Item 8. Financial Statements and Supplementary Data."

Other-Than-Temporary Impairment on Securities Analysis

Non-marketable equity securities. Non-marketable equity securities largely consist of capital stock issued by the FHLB of Des Moines and are evaluated for impairment whenever events or circumstances suggest the carrying value may not be recoverable. Based on the Company's evaluation of its investments in non-marketable equity securities as of December 31, 2016, the Company determined that none of such securities had other-than-temporary impairment.

Debt securities. In evaluating debt securities for other-than-temporary impairment losses, management assesses whether the Company intends to sell the security or if it is more-likely-than-not that the Company will be required to sell the debt security. In so doing, management considers contractual constraints, liquidity, capital, asset/liability management and securities portfolio objectives. For debt securities with limited or inactive markets, the impact of macroeconomic conditions in the U.S. upon fair value estimates includes higher risk-adjusted discount rates and changes in credit ratings provided by NRSRO. In November 2016, S&P reaffirmed its AA+ rating of U.S. government long-term debt, and the outlook remains stable. In November 2016, Moody's reaffirmed its Aaa rating of U.S. government long-term debt and the outlook remains stable. In April 2016, Fitch reaffirmed its AAA rating of U.S. government long-term debt and the outlook remains stable. S&P, Moody's and Fitch have similar credit ratings and outlooks with respect to certain long-term debt instruments issued by Federal National Mortgage Association ("Fannie Mae"), Federal Home Loan Mortgage Corporation ("Freddie Mac") and other U.S. government agencies linked to the long-term U.S. debt.

The following table separates investment securities with an unrealized loss position at December 31, 2016 into two categories: investments purchased prior to 2016 and those purchased during 2016. Of those investments purchased prior to 2016, the fair market value and unrealized gain or loss at December 31, 2015 is also presented.

| (Dollars in thousands) | December 31, 2016 | | | December 31, 2015 | | |
|---|-------------------|-----------------|--|-------------------|-----------------|--|
| | Fair Value | Unrealized Loss | Unrealized Loss as a Percent of Fair Value | Fair Value | Unrealized Loss | Unrealized Loss as a Percent of Fair Value |
| Temporarily impaired securities purchased prior to 2016 | | | | | | |
| U.S. government and federal agency | \$32,957 | \$(162) | — % | \$39,773 | \$(401) | (1) % |
| U.S. government sponsored enterprises | 2,624 | (1) | — % | 2,604 | (14) | (1) % |
| State and local governments | 435,025 | (15,849) | (4) % | 448,065 | (6,089) | (1) % |
| Corporate bonds | 92,456 | (170) | — % | 94,255 | (840) | (1) % |
| Mortgage-backed securities | 604,361 | (7,052) | (1) % | 783,522 | (7,565) | (1) % |
| Total | \$1,167,423 | \$(23,234) | (2) % | \$1,368,219 | \$(14,909) | (1) % |
| Temporarily impaired securities purchased during 2016 | | | | | | |
| U.S. government sponsored enterprises | \$3,425 | \$(41) | (1) % | | | |
| State and local governments | 73,971 | (2,099) | (3) % | | | |
| Corporate bonds | 88,506 | (623) | (1) % | | | |
| Mortgage-backed securities | 203,705 | (4,273) | (2) % | | | |
| Total | \$369,607 | \$(7,036) | (2) % | | | |
| Temporarily impaired securities | | | | | | |
| U.S. government and federal agency | \$32,957 | \$(162) | — % | | | |
| U.S. government sponsored enterprises | 6,049 | (42) | (1) % | | | |
| State and local governments | 508,996 | (17,948) | (4) % | | | |
| Corporate bonds | 180,962 | (793) | — % | | | |
| Mortgage-backed securities | 808,066 | (11,325) | (1) % | | | |
| Total | \$1,537,030 | \$(30,270) | (2) % | | | |

With respect to severity, the following table provides the number of debt securities and amount of unrealized loss in the various ranges of unrealized loss as a percent of book value at December 31, 2016:

| (Dollars in thousands) | Number of Debt Securities | Unrealized Loss |
|------------------------|---------------------------|-----------------|
| 5.1% to 10.0% | 89 | \$(11,029) |
| 0.1% to 5.0% | 689 | (19,241) |
| Total | 778 | \$(30,270) |

With respect to the duration of the impaired debt securities, the Company identified 163 securities which have been continuously impaired for the twelve months ending December 31, 2016. The valuation history of such securities in the prior year(s) was also reviewed to determine the number of months in the prior year(s) in which the identified securities were in an unrealized loss position.

The following table provides details of the 163 debt securities which have been continuously impaired for the twelve months ended December 31, 2016, including the most notable loss for any one bond in each category.

| (Dollars in thousands) | Number of Debt Securities | Unrealized Loss for 12 Months Or More | Most Notable Loss |
|------------------------------------|---------------------------|---------------------------------------|-------------------|
| U.S. government and federal agency | 22 | \$(138) | \$(22) |
| State and local governments | 117 | (11,287) | (1,224) |
| Corporate bonds | 3 | (19) | (10) |
| Mortgage-backed securities | 21 | (668) | (214) |
| Total | 163 | \$(12,112) | |

Based on the Company's analysis of its impaired debt securities as of December 31, 2016, the Company determined that none of such securities had other-than-temporary impairment and the unrealized losses were primarily the result of interest rate changes and market spreads subsequent to acquisition. A substantial portion of the debt securities with unrealized losses at December 31, 2016 were issued by Fannie Mae, Freddie Mac, Government National Mortgage Association ("Ginnie Mae") and other agencies of the U.S. government or have credit ratings issued by one or more of the NRSRO entities in the four highest credit rating categories. All of the Company's impaired debt securities at December 31, 2016 have been determined by the Company to be investment grade.

Lending Activity

The Company focuses its lending activities primarily on the following types of loans: 1) first-mortgage, conventional loans secured by residential properties, particularly single-family; 2) commercial lending, including agriculture, that concentrates on targeted businesses; and 3) installment lending for consumer purposes (e.g., home equity, automobile, etc.). Supplemental information regarding the Company's loan portfolio and credit quality based on regulatory classification is provided in the section captioned "Loans by Regulatory Classification" included in "Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations." The regulatory classification of loans is based primarily on the type of collateral for the loans. Loan information included in "Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations" is based on the Company's loan segments and classes, which are based on the purpose of the loan, unless otherwise noted as a regulatory classification.

The following table summarizes the Company's loan portfolio as of the dates indicated:

| (Dollars in thousands) | December 31, 2016 | | December 31, 2015 | | December 31, 2014 | | December 31, 2013 | | December 31, 2012 | |
|-------------------------------|-------------------|---------|-------------------|---------|-------------------|---------|-------------------|---------|-------------------|---------|
| | Amount | Percent |
| Residential real estate loans | \$674,347 | 12 % | \$688,912 | 14 % | \$611,463 | 14 % | \$577,589 | 15 % | \$516,467 | 16 % |
| Commercial loans | | | | | | | | | | |
| Real estate | 2,990,141 | 54 % | 2,633,953 | 53 % | 2,337,548 | 54 % | 2,049,247 | 52 % | 1,655,508 | 51 % |
| Other commercial | 1,342,250 | 24 % | 1,099,564 | 22 % | 925,900 | 21 % | 852,036 | 22 % | 623,397 | 19 % |
| Total | 4,332,391 | 78 % | 3,733,517 | 75 % | 3,263,448 | 75 % | 2,901,283 | 74 % | 2,278,905 | 70 % |
| Consumer and other | | | | | | | | | | |

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| | | | | | | | | | | |
|-------------------------------------|-------------|-------|-------------|-------|-------------|-------|-------------|-------|-------------|-------|
| loans | | | | | | | | | | |
| Home equity | 434,774 | 8 % | 420,901 | 9 % | 394,670 | 9 % | 366,465 | 9 % | 403,925 | 12 % |
| Other consumer | 242,951 | 4 % | 235,351 | 5 % | 218,514 | 5 % | 217,501 | 5 % | 198,128 | 6 % |
| Total | 677,725 | 12 % | 656,252 | 14 % | 613,184 | 14 % | 583,966 | 14 % | 602,053 | 18 % |
| Loans receivable | 5,684,463 | 102 % | 5,078,681 | 103 % | 4,488,095 | 103 % | 4,062,838 | 103 % | 3,397,425 | 104 % |
| Allowance for loan and lease losses | (129,572) | (2)% | (129,697) | (3)% | (129,753) | (3)% | (130,351) | (3)% | (130,854) | (4)% |
| Loans receivable, net | \$5,554,891 | 100 % | \$4,948,984 | 100 % | \$4,358,342 | 100 % | \$3,932,487 | 100 % | \$3,266,571 | 100 % |

The stated maturities or first repricing term (if applicable) for the loan portfolio at December 31, 2016 was as follows:

| (Dollars in thousands) | Residential Real Estate | Commercial | Consumer and Other | Total |
|-------------------------------------|----------------------------|------------|-----------------------|-----------|
| Variable rate maturing or repricing | | | | |
| In one year or less | \$ 230,469 | 1,142,540 | 312,502 | 1,685,511 |
| After one year through five years | 140,706 | 1,424,252 | 97,457 | 1,662,415 |
| Thereafter | 3,177 | 228,446 | 5,779 | 237,402 |
| Fixed rate maturing | | | | |
| In one year or less | 158,052 | 467,877 | 125,996 | 751,925 |
| After one year through five years | 131,297 | 679,500 | 133,015 | 943,812 |
| Thereafter | 10,646 | 389,776 | 2,976 | 403,398 |
| Total | \$ 674,347 | 4,332,391 | 677,725 | 5,684,463 |

Residential Real Estate Lending

The Company's lending activities consist of the origination of both construction and permanent loans on residential real estate. The Company actively solicits residential real estate loan applications from real estate brokers, contractors, existing customers, customer referrals, and on-line applications. The Company's lending policies generally limit the maximum loan-to-value ratio on residential mortgage loans to 80 percent of the lesser of the appraised value or purchase price. Policies allow for higher loan-to-values with appropriate risk mitigation such as documented compensating factors, credit enhancement, etc. For loans held for sale, the Company complies with the investor's loan-to-value guidelines. The Company also provides interim construction financing for single-family dwellings. These loans are supported by a term take-out commitment.

Consumer Land or Lot Loans

The Company originates land and lot acquisition loans to borrowers who intend to construct their primary residence on the respective land or lot. These loans are generally for a term of three to five years and are secured by the developed land or lot with the loan-to-value limited to the lesser of 75 percent of the appraised value or 75 percent of the cost.

Unimproved Land and Land Development Loans

Although the Company has originated very few unimproved land and land development loans since the economic downturn in 2008, the Company may originate such loans on properties intended for residential and commercial use where improved real estate market conditions have occurred. These loans are typically made for a term of 18 months to two years and are secured by the developed property with a loan-to-value not to exceed the lesser of 75 percent of cost or 65 percent of the appraised discounted bulk sale value upon completion of the improvements. The projects under development are inspected on a regular basis and advances are made on a percentage-of-completion basis. The loans are made to borrowers with real estate development experience and appropriate financial strength. Generally, the Company requires that a certain percentage of the development be pre-sold or that construction and term take-out commitments are in place prior to funding the loan. Loans made on unimproved land are generally made for a term of five to ten years with a loan-to-value not to exceed the lesser of 50 percent of appraised value or 50 percent of cost.

Residential Builder Guidance Lines

The Company provides Builder Guidance Lines that are comprised of pre-sold and spec-home construction and lot acquisition loans. The spec-home construction and lot acquisition loans are limited to a specific number and maximum amount. Generally, the individual loans will not exceed a one year maturity. The homes under construction are inspected on a regular basis and advances made on a percentage-of-completion basis.

Commercial Real Estate Loans

Loans are made to purchase, construct and finance commercial real estate properties. These loans are generally made to borrowers who own and will occupy the property and generally have a loan-to-value up to the lesser of 75 percent of the appraised value or 75 percent of the cost and require a minimum 1.2 times debt service coverage margin. Loans to finance investment or income properties are made but require additional equity and generally have a loan-to-value up to the lesser of 75 percent of appraised value or 75 percent of cost and require a higher debt service coverage margin commensurate with the specific property and projected income.

Construction Loans

During the construction loan term, all construction loan collateral properties are inspected at least monthly, or more frequently as needed, until completion. Draws on construction loans are predicated upon the results of the inspection and advanced based upon a percentage-of-completion basis versus original budget percentages. When construction loans become non-performing and the associated project is not complete, the Company on a case-by-case basis makes the decision to advance additional funds or to initiate collection/foreclosure proceedings. Such decision includes obtaining “as-is” and “at completion” appraisals for consideration of potential increases or decreases in the collateral’s value. The Company also considers the increased costs of monitoring progress to completion, and the related collection/holding period costs should collateral ownership be transferred to the Company.

Consumer Lending

The majority of consumer loans are secured by real estate, automobiles, or other assets. The Company intends to continue making such loans because of their short-term nature, generally between three months and five years. Moreover, interest rates on consumer loans are generally higher than on residential mortgage loans. The Company also originates second mortgage and home equity loans, especially to existing customers in instances where the first and second mortgage loans are less than 80 percent of the current appraised value of the property.

Home Equity Loans

The Company’s home equity loans of \$435 million and \$421 million as of December 31, 2016 and 2015, respectively, consist of 1-4 family junior lien mortgages and first and junior lien lines of credit secured by residential real estate. At December 31, 2016, the home equity loan portfolio consisted of 85 percent variable interest rate and 15 percent fixed interest rate loans. Approximately 54 percent of the home equity loans were in a first lien status with the remaining 46 percent in junior lien status. Approximately 12 percent of the home equity loans were closed-end amortizing loans and 88 percent were open-end, revolving home equity lines of credit. At December 31, 2015, the home equity loan portfolio consisted of 78 percent variable interest rate and 22 percent fixed interest rate loans. Approximately 53 percent of the home equity loans were in a first lien status with the remaining 47 percent in junior lien status. Approximately 15 percent of the home equity loans were closed-end amortizing loans and 85 percent were open-end, revolving home equity lines of credit.

Prior to 2014, home equity lines of credit were generally originated with maturity terms from 10 to 15 years. At origination, borrowers chose a variable interest rate or fixed interest rate for the full term of the line of credit, or a fixed interest rate for the first 3 or 5 years from the origination date which then converts to a variable interest rate for the remaining term of such home equity lines of credit. During the draw period, a borrower with a variable interest rate term had the option of converting to a fixed interest rate for all or a portion of the remaining term to maturity. Beginning in 2014, home equity lines of credit are originated with maturity terms of 15 years. At origination, borrowers can choose a variable interest rate that changes quarterly, or after the first 3, 5 or 10 years from the origination date.

The draw period for home equity lines of credit usually exists from origination to maturity. During the draw period, the Company has home equity lines of credit where the borrowers pay interest only and home equity lines of credit where borrowers pay principal and interest.

Credit Risk Management

The Company is committed to a conservative management of the credit risk within the loan portfolio, including the early recognition of problem loans. The Company’s credit risk management includes stringent credit policies, individual loan approval limits, limits on concentrations of credit, and committee approval of larger loan requests. Management practices also include regular internal and external credit examinations, identification and review of individual loans and leases experiencing deterioration of credit quality, procedures for the collection of non-performing assets, quarterly monitoring of the loan portfolio, semi-annual review of loans by industry, and

periodic stress testing of the loans secured by real estate. Federal and state regulatory safety and soundness examinations are conducted annually.

The Company's loan policy and credit administration practices establish standards and limits for all extensions of credit that are secured by interests in or liens on real estate, or made for the purpose of financing the construction of real property or other improvements. Ongoing monitoring and review of the loan portfolio is based on current information, including: the borrowers' and guarantors' creditworthiness, value of the real estate and other collateral, the project's performance against projections, and monthly inspections by Company employees or external parties until the real estate project is complete.

Monitoring of the junior lien and home equity lines of credit portfolios includes evaluating payment delinquency, collateral values, bankruptcy notices and foreclosure filings. Additionally, the Company places junior lien mortgages and junior lien home equity lines of credit on non-accrual status when there is evidence that the associated senior lien is 90 days past due or is in the process of foreclosure, regardless of the junior lien delinquency status.

Loan Approval Limits

Individual loan approval limits have been established for each lender based on the loan types and experience of the individual. Each bank division has an Officer Loan Committee consisting of senior lenders and members of senior management. Each of the Bank divisions' Officer Loan Committees has loan approval authority between \$250,000 and \$1,000,000. Each of the Bank divisions' Advisory Boards has loan approval authority up to \$2,000,000. Loans, or a combination of loans, including new and renewed, exceeding these limits and up to \$10,000,000 are subject to approval by the Company's Executive Loan Committee consisting of the Bank divisions' senior loan officers and the Company's Chief Credit Administrator. Loans, or a combination of loans, including new and renewed, greater than \$10,000,000 are subject to approval by the Bank's Board of Directors. Under banking laws, loans to one borrower and related entities are limited to a prescribed percentage of the unimpaired capital and surplus of the Bank.

Interest Reserves

Interest reserves are used to periodically advance loan funds to pay interest charges on the outstanding balance of the related loan. As with any extension of credit, the decision to establish a loan-funded interest reserve upon origination of construction loans, including residential construction and land, lot and other construction loans, is based on prudent underwriting, including the feasibility of the project, expected cash flow, creditworthiness of the borrower and guarantors, and the protection provided by the real estate and other underlying collateral. Interest reserves provide an effective means for addressing the cash flow characteristics of construction loans. In response to the downturn in the housing market and potential impact upon construction lending, the Company discourages the creation or continued use of interest reserves.

Interest reserves are advanced provided the related construction loan is performing as expected. Loans with interest reserves may be extended, renewed or restructured only when the related loan continues to perform as expected and meets the prudent underwriting standards identified above. Such renewals, extension or restructuring are not permitted in order to keep the related loan current.

In monitoring the performance and credit quality of a construction loan, the Company assesses the adequacy of any remaining interest reserve, and whether the use of an interest reserve remains appropriate in the presence of emerging weakness and associated risks in the construction loan.

The ongoing accrual and recognition of uncollected interest as income continues only when facts and circumstances continue to reasonably support the contractual payment of principal or interest. Loans are typically designated as non-accrual when the collection of the contractual principal or interest is unlikely and has remained unpaid for ninety days or more. For such loans, the accrual of interest and its capitalization into the loan balance will be discontinued.

The Company had \$111 million and \$65.2 million of loans with remaining interest reserves of \$1.2 million and \$1.5 million as of December 31, 2016 and 2015, respectively. The Company did not extend, renew or restructure any loans with interest reserves during 2016. During 2015, the Company extended, renewed or restructured 3 loans with interest reserves, such loans having an aggregate outstanding principal balance of \$2.2 million as of December 31, 2015. Such actions were based on prudent underwriting standards and not to keep the loans current. As of December 31, 2016, the Company had no construction loans with interest reserves that are currently non-performing or which are potential problem loans.

Loan Purchases and Sales

Fixed rate, long-term mortgage loans are generally sold in the secondary market. The Company is active in the secondary market, primarily through the origination of conventional, Rural Development, Federal Housing Administration and Department of Veterans Affairs residential mortgages. The sale of loans in the secondary mortgage market reduces the Company's risk of holding long-term, fixed rate loans during periods of rising interest rates. In connection with conventional loan sales, the Company typically sells the majority of mortgage loans originated with servicing released. The Company has also been very active in generating commercial Small Business Administration loans, and other commercial loans, with a portion of those loans sold to investors. The Company has not originated any type of subprime mortgages, either for the loan portfolio or for sale to investors. In addition, the Company has not purchased investment securities collateralized with subprime mortgages. The Company does not actively purchase loans from other financial institutions, and substantially all of the Company's loans receivable are with customers in the Company's geographic market areas.

Loan Origination and Other Fees

In addition to interest earned on loans, the Company receives fees for originating loans. Loan fees generally are a percentage of the principal amount of the loan and are charged to the borrower, and are normally deducted from the proceeds of the loan. Loan origination fees are generally 1.0 percent to 1.5 percent on residential mortgages and 0.5 percent to 1.5 percent on commercial loans. Consumer loans require a fixed fee amount as well as a minimum interest amount. The Company also receives other fees and charges relating to existing loans, which include charges and fees collected in connection with loan modifications.

Appraisal and Evaluation Process

The Company's loan policy and credit administration practices have adopted and implemented the applicable legal and regulatory requirements, which establishes criteria for obtaining appraisals or evaluations (new or updated), including transactions that are otherwise exempt from the appraisal requirements.

Each of the Bank divisions monitor conditions, including supply and demand factors, in the real estate markets served so they can react quickly to changing market conditions to mitigate potential losses from specific credit exposures within the loan portfolio. Evidence of the following real estate market conditions and trends is obtained from lending personnel and third party sources:

- demographic indicators, including employment and population trends;
- foreclosures, vacancy, construction and absorption rates;
- property sales prices, rental rates, and lease terms;
- current tax assessments;
- economic indicators, including trends within the lending areas; and
- valuation trends, including discount and capitalization rates.

Third party information sources include federal, state, and local governments and agencies thereof, private sector economic data vendors, real estate brokers, licensed agents, sales, rental and foreclosure data tracking services.

The time between ordering an appraisal or evaluation and receipt from third party vendors is typically two to six weeks for residential property depending on geographic market and four to six weeks for non-residential property. For real estate properties that are of highly specialized or limited use, significantly complex or large, additional time beyond the typical times may be required for new appraisals or evaluations (new or updated).

As part of the Company's credit administration and portfolio monitoring practices, the Company's regular internal and external credit examinations review a significant number of individual loan files. Appraisals and evaluations (new or updated) are reviewed to determine whether the timeliness, methods, assumptions, and findings are reasonable and in compliance with the Company's loan policy and credit administration practices. Such reviews include the adequacy of the steps taken by the Company to ensure that the individuals who perform appraisals and evaluations (new or updated) are appropriately qualified and are not subject to conflicts of interest. If there are any deficiencies noted in the reviews, they are reported to Bank management and prompt corrective action is taken.

Non-performing Assets

The following table summarizes information regarding non-performing assets at the dates indicated:

| (Dollars in thousands) | At or for the Years ended | | | | | |
|---|---------------------------|-------------------|-------------------|-------------------|-------------------|---|
| | December 31, 2016 | December 31, 2015 | December 31, 2014 | December 31, 2013 | December 31, 2012 | |
| Other real estate owned | \$20,954 | 26,815 | 27,804 | 26,860 | 45,115 | |
| Accruing loans 90 days or more past due | | | | | | |
| Residential real estate | 266 | — | 35 | 429 | 451 | |
| Commercial | 428 | 2,051 | 105 | 160 | 791 | |
| Consumer and other | 405 | 80 | 74 | 15 | 237 | |
| Total | 1,099 | 2,131 | 214 | 604 | 1,479 | |
| Non-accrual loans | | | | | | |
| Residential real estate | 4,528 | 8,073 | 6,798 | 10,702 | 14,237 | |
| Commercial | 39,033 | 36,510 | 48,138 | 61,577 | 68,887 | |
| Consumer and other | 5,771 | 6,550 | 6,946 | 9,677 | 13,809 | |
| Total | 49,332 | 51,133 | 61,882 | 81,956 | 96,933 | |
| Total non-performing assets ¹ | \$71,385 | 80,079 | 89,900 | 109,420 | 143,527 | |
| Non-performing assets as a percentage of subsidiary assets | 0.76 | % 0.88 | % 1.08 | % 1.39 | % 1.87 | % |
| Allowance for loan and lease losses as a percentage of non-performing loans | 257 | % 244 | % 209 | % 158 | % 133 | % |
| Accruing loans 30-89 days past due | \$25,617 | 19,413 | 25,904 | 32,116 | 27,097 | |
| Accruing troubled debt restructurings | \$52,077 | 63,590 | 69,129 | 81,110 | 100,151 | |
| Non-accrual troubled debt restructurings | \$21,693 | | | | | |