

National Bank Holdings Corp
Form 10-Q
November 07, 2018

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended September 30, 2018

OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from _____ to _____

Commission File Number: 001-35654

NATIONAL BANK HOLDINGS CORPORATION

(Exact name of registrant as specified in its charter)

| | |
|---------------------------------|---------------------|
| Delaware | 27-0563799 |
| (State or other jurisdiction of | (I.R.S. Employer |
| incorporation or organization) | Identification No.) |

7800 East Orchard, Suite 300, Greenwood Village, Colorado 80111

(Address of principal executive offices) (Zip Code)

Registrant's telephone, including area code: (720) 529-3336

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

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

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

| | |
|-------------------------|---------------------------|
| Large accelerated filer | Accelerated filer |
| Non-accelerated filer | Smaller reporting company |
| | Emerging growth company |

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

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

APPLICABLE ONLY TO CORPORATE ISSUERS:

Indicate the number of shares outstanding of each of the issuer’s classes of common stock, as of the latest practicable date.

As of November 5, 2018, the registrant had outstanding 30,768,683 shares of Class A voting common stock, each with \$0.01 par value per share, excluding 143,695 shares of restricted Class A common stock issued but not yet vested.

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CAUTIONARY NOTE REGARDING FORWARD-LOOKING STATEMENTS

This report contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995, notwithstanding that such statements are not specifically identified. Any statements about our expectations, beliefs, plans, predictions, forecasts, objectives, assumptions or future events or performance are not historical facts and may be forward-looking. These statements are often, but not always, made through the use of words or phrases such as “anticipate,” “believe,” “can,” “would,” “should,” “could,” “may,” “predict,” “seek,” “potential,” “will,” “estimate,” “tend,” “continue,” “ongoing,” “expect,” “intend” and similar words or phrases. These statements are only predictions and involve estimates, known and unknown risks, assumptions and uncertainties. We have based these statements largely on our current expectations and projections about future events and financial trends that we believe may affect our financial condition, liquidity, results of operations, business strategy and growth prospects.

Forward-looking statements involve certain important risks, uncertainties and other factors, any of which could cause actual results to differ materially from those in such statements and, therefore, you are cautioned not to place undue reliance on such statements. Factors that could cause actual results to differ from those discussed in the forward-looking statements include, but are not limited to:

our ability to execute our business strategy, as well as changes in our business strategy or development plans;

business and economic conditions generally and in the financial services industry;

economic, market, operational, liquidity, credit and interest rate risks associated with our business;

effects of any changes in trade, monetary and fiscal policies and laws, including the interest rate policies of the Federal Reserve Board;

changes imposed by regulatory agencies to increase our capital to a level greater than the current level required for well-capitalized financial institutions;

effects of inflation, as well as, interest rate, securities market and monetary supply fluctuations;

changes in the economy or supply-demand imbalances affecting local real estate values;

changes in consumer spending, borrowings and savings habits;

with respect to our mortgage business, our inability to negotiate our fees with Fannie Mae, Freddie Mac, Ginnie Mae or other investors for the purchase of our loans, our obligation to indemnify purchasers or to repurchase the related loans if they fail to meet certain criteria, higher rate of delinquencies and defaults as a result of the geographic concentration of our servicing portfolio, or the impact of interest rates on the value of our mortgage servicing rights;

our ability to identify potential candidates for, obtain regulatory approval for, and consummate, acquisitions or consolidations of financial institutions on attractive terms, or at all;

our ability to integrate acquisitions or consolidations and to achieve synergies, operating efficiencies and/or other expected benefits within expected time-frames, or at all, or within expected cost projections, and to preserve the goodwill of acquired financial institutions;

our ability to realize the anticipated benefits from enhancements or updates to our core operating systems from time to time without significant change in our client service or risk to our control environment;

our dependence on information technology and telecommunications systems of third party service providers and the risk of system failures, interruptions or breaches of security, including those that could result in disclosure or misuse of confidential or proprietary client or other information;

our ability to achieve organic loan and deposit growth and the composition of such growth;

changes in sources and uses of funds, including loans, deposits and borrowings;

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increased competition in the financial services industry, nationally, regionally or locally, resulting in, among other things, lower returns;

continued consolidation in the financial services industry;

our ability to maintain or increase market share and control expenses;

the effect of changes in accounting policies and practices, as may be adopted by the regulatory agencies, as well as the Public Company Accounting Oversight Board, the Financial Accounting Standards Board and other accounting standard setters;

the trading price of shares of the Company's stock;

the effects of tax legislation or challenges to our tax position;

our ability to realize deferred tax assets or the need for a valuation allowance, or the effects of changes in tax laws on our deferred tax assets;

costs and effects of changes in laws and regulations and of other legal and regulatory developments, including, but not limited to, changes in regulation that affect the fees that we charge, the resolution of legal proceedings or regulatory or other governmental inquiries, and the results of regulatory examinations, reviews or other inquiries; and changes in regulations that apply to us as a Colorado state-chartered bank;

technological changes;

the timely development and acceptance of new products and services and perceived overall value of these products and services by our clients;

changes in our management personnel and our continued ability to hire and retain qualified personnel;

ability to implement and/or improve operational management and other internal risk controls and processes and our reporting system and procedures;

regulatory limitations on dividends from our bank subsidiary;

changes in estimates of future loan reserve requirements based upon the periodic review thereof under relevant regulatory and accounting requirements;

widespread natural and other disasters, dislocations, political instability, acts of war or terrorist activities, cyberattacks or international hostilities through impacts on the economy and financial markets generally or on us or our counterparties specifically;

a cyber-security incident, data breach or a failure of a key information technology system;

impact of reputational risk on such matters as business generation and retention;

other risks and uncertainties listed from time to time in the Company's reports and documents filed with the Securities and Exchange Commission; and

our success at managing the risks involved in the foregoing items.

Any forward-looking statement speaks only as of the date on which it is made, and we undertake no obligation to update any forward-looking statement to reflect events or circumstances after the date on which the statement is made or to reflect the occurrence of unanticipated events or circumstances, except as required by applicable law.

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PART I: FINANCIAL INFORMATION

Item 1: FINANCIAL STATEMENTS

NATIONAL BANK HOLDINGS CORPORATION AND SUBSIDIARIES

Consolidated Statements of Financial Condition (Unaudited)

(In thousands, except share and per share data)

| | September 30, 2018 | December 31, 2017 |
|--|--------------------|-------------------|
| ASSETS | | |
| Cash and due from banks | \$ 110,959 | \$ 193,297 |
| Interest bearing bank deposits | 500 | 64,067 |
| Cash and cash equivalents | 111,459 | 257,364 |
| Investment securities available-for-sale (at fair value) | 796,549 | 855,345 |
| Investment securities held-to-maturity (fair value of \$242,370 and \$256,771 at September 30, 2018 and December 31, 2017, respectively) | 249,464 | 258,730 |
| Non-marketable securities | 16,975 | 15,030 |
| Loans | 3,905,311 | 3,178,947 |
| Allowance for loan losses | (33,813) | (31,264) |
| Loans, net | 3,871,498 | 3,147,683 |
| Loans held for sale | 80,506 | 4,629 |
| Other real estate owned | 35,135 | 10,491 |
| Premises and equipment, net | 110,824 | 93,708 |
| Goodwill | 115,027 | 59,630 |
| Intangible assets, net | 13,937 | 1,607 |
| Other assets | 183,730 | 139,248 |
| Total assets | \$ 5,585,104 | \$ 4,843,465 |
| LIABILITIES AND SHAREHOLDERS' EQUITY | | |
| Liabilities: | | |
| Deposits: | | |
| Non-interest bearing demand deposits | \$ 1,089,631 | \$ 902,439 |
| Interest bearing demand deposits | 675,213 | 474,607 |
| Savings and money market | 1,729,563 | 1,484,463 |
| Time deposits | 1,119,625 | 1,118,050 |
| Total deposits | 4,614,032 | 3,979,559 |
| Securities sold under agreements to repurchase | 55,695 | 130,463 |
| Federal Home Loan Bank advances | 144,540 | 129,115 |
| Other liabilities | 97,772 | 71,921 |
| Total liabilities | 4,912,039 | 4,311,058 |
| Shareholders' equity: | | |
| Common stock, par value \$0.01 per share: 400,000,000 shares authorized; 51,498,943 and 51,518,162 shares issued; 30,759,595 and | 515 | 515 |

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26,875,585 shares outstanding at September 30, 2018 and December 31, 2017, respectively

| | | |
|---|--------------|--------------|
| Additional paid-in capital | 1,013,314 | 970,668 |
| Retained earnings | 95,055 | 60,795 |
| Treasury stock of 20,583,334 and 24,479,020 shares at September 30, 2018 and December 31, 2017, respectively, at cost | (415,605) | (493,329) |
| Accumulated other comprehensive loss, net of tax | (20,214) | (6,242) |
| Total shareholders' equity | 673,065 | 532,407 |
| Total liabilities and shareholders' equity | \$ 5,585,104 | \$ 4,843,465 |

See accompanying notes to the consolidated interim financial statements.

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NATIONAL BANK HOLDINGS CORPORATION AND SUBSIDIARIES

Consolidated Statements of Operations (Unaudited)

(In thousands, except share and per share data)

| | For the three months ended September 30, | | For the nine months ended September 30, | |
|--|---|-----------|--|------------|
| | 2018 | 2017 | 2018 | 2017 |
| Interest and dividend income: | | | | |
| Interest and fees on loans | \$ 49,181 | \$ 36,064 | \$ 141,994 | \$ 102,238 |
| Interest and dividends on investment securities | 6,289 | 6,005 | 19,625 | 19,108 |
| Dividends on non-marketable securities | 268 | 234 | 761 | 619 |
| Interest on interest-bearing bank deposits | 171 | 276 | 1,231 | 687 |
| Total interest and dividend income | 55,909 | 42,579 | 163,611 | 122,652 |
| Interest expense: | | | | |
| Interest on deposits | 5,451 | 4,068 | 14,950 | 11,759 |
| Interest on borrowings | 686 | 613 | 1,856 | 1,380 |
| Total interest expense | 6,137 | 4,681 | 16,806 | 13,139 |
| Net interest income before provision for loan losses | 49,772 | 37,898 | 146,805 | 109,513 |
| Provision for loan losses | 807 | 3,880 | 2,721 | 9,700 |
| Net interest income after provision for loan losses | 48,965 | 34,018 | 144,084 | 99,813 |
| Non-interest income: | | | | |
| Service charges | 4,592 | 3,585 | 13,473 | 10,458 |
| Bank card fees | 3,686 | 3,076 | 10,720 | 9,014 |
| Mortgage banking income | 7,819 | 668 | 24,701 | 1,716 |
| Bank-owned life insurance income | 463 | 475 | 1,361 | 1,417 |
| Other non-interest income | 1,429 | 1,611 | 4,290 | 7,149 |
| OREO related income | 72 | 136 | 913 | 449 |
| Total non-interest income | 18,061 | 9,551 | 55,458 | 30,203 |
| Non-interest expense: | | | | |
| Salaries and benefits | 28,127 | 19,363 | 87,910 | 59,662 |
| Occupancy and equipment | 6,925 | 5,208 | 22,070 | 15,887 |
| Telecommunications and data processing | 2,186 | 1,702 | 8,653 | 4,841 |
| Marketing and business development | 1,128 | 683 | 3,589 | 1,878 |
| FDIC deposit insurance | 401 | 715 | 1,911 | 2,106 |
| Bank card expenses | 1,258 | 971 | 4,491 | 2,751 |
| Professional fees | 1,117 | 754 | 4,686 | 2,441 |
| Other non-interest expense | 2,564 | 2,700 | 9,515 | 7,839 |
| Problem asset workout | 665 | 1,636 | 2,221 | 3,389 |
| Gain on OREO sales, net | (450) | (497) | (386) | (2,254) |
| Core deposit intangible asset amortization | 511 | 1,370 | 1,817 | 4,110 |

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| | | | | |
|--|------------|------------|------------|------------|
| Total non-interest expense | 44,432 | 34,605 | 146,477 | 102,650 |
| Income before income taxes | 22,594 | 8,964 | 53,065 | 27,366 |
| Income tax expense | 4,354 | 1,733 | 8,849 | 2,668 |
| Net income | \$ 18,240 | \$ 7,231 | \$ 44,216 | \$ 24,698 |
| Income per share—basic | \$ 0.59 | \$ 0.27 | \$ 1.44 | \$ 0.92 |
| Income per share—diluted | \$ 0.58 | \$ 0.26 | \$ 1.41 | \$ 0.89 |
| Weighted average number of common shares outstanding: | | | | |
| Basic | 30,869,683 | 26,947,821 | 30,700,977 | 26,902,128 |
| Diluted | 31,540,716 | 27,628,734 | 31,388,786 | 27,636,675 |

See accompanying notes to the consolidated interim financial statements.

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NATIONAL BANK HOLDINGS CORPORATION AND SUBSIDIARIES

Consolidated Statements of Comprehensive Income (Unaudited)

(In thousands)

| | For the three months ended September 30, | | For the nine months ended September 30, | |
|--|--|----------|---|-----------|
| | 2018 | 2017 | 2018 | 2017 |
| Net income | \$ 18,240 | \$ 7,231 | \$ 44,216 | \$ 24,698 |
| Other comprehensive (loss) income, net of tax: | | | | |
| Securities available-for-sale: | | | | |
| Net unrealized (losses) gains arising during the period, net of tax benefit (expense) of \$786 and (\$121) for the three months ended September 30, 2018 and 2017, respectively; and net of tax benefit (expense) of \$3,776 and (\$913) for the nine months ended September 30, 2018 and 2017, respectively | (2,499) | 197 | (11,471) | 1,473 |
| Less: amortization of net unrealized holding gains to income, net of tax benefit of \$97 and \$207 for the three months ended September 30, 2018 and 2017, respectively; and net of tax benefit of \$270 and \$642 for the nine months ended September 30, 2018 and 2017, respectively | (308) | (336) | (1,022) | (1,046) |
| Other comprehensive (loss) income | (2,807) | (139) | (12,493) | 427 |
| Comprehensive income | \$ 15,433 | \$ 7,092 | \$ 31,723 | \$ 25,125 |

See accompanying notes to the consolidated interim financial statements.

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NATIONAL BANK HOLDINGS CORPORATION AND SUBSIDIARIES

Consolidated Statements of Changes in Shareholders' Equity (Unaudited)

Nine months ended September 30, 2018 and 2017

(In thousands, except share and per share data)

| | Common stock | Additional paid-in capital | Retained earnings | Treasury stock | Accumulated other comprehensive income (loss), net | Total |
|---|-----------------|----------------------------------|----------------------|-------------------|--|------------|
| Balance, December 31, 2016 | \$ 514 | \$ 984,087 | \$ 55,454 | \$ (502,104) | \$ (1,762) | \$ 536,189 |
| Net income | — | — | 24,698 | — | — | 24,698 |
| Stock-based compensation | — | 2,771 | — | — | — | 2,771 |
| Issuance of stock under purchase and equity compensation plans, including gain on reissuance of treasury stock of \$5,080, net | 1 | (12,898) | — | 5,850 | — | (7,047) |
| Cash dividends declared (\$0.25 per share) | — | — | (6,794) | — | — | (6,794) |
| Warrant exercise | — | (1,933) | — | 1,933 | — | — |
| Other comprehensive income | — | — | — | — | 427 | 427 |
| Balance, September 30, 2017 | \$ 515 | \$ 972,027 | \$ 73,358 | \$ (494,321) | \$ (1,335) | \$ 550,244 |
| Balance, December 31, 2017 | \$ 515 | \$ 970,668 | \$ 60,795 | \$ (493,329) | \$ (6,242) | \$ 532,407 |
| Net income | — | — | 44,216 | — | — | 44,216 |
| Stock-based compensation | — | 3,244 | — | — | — | 3,244 |
| Issuance of stock under purchase and equity compensation plans, including gain on reissuance of treasury stock of \$7,947, net | — | (2,841) | — | 9,754 | — | 6,913 |
| Reissuance of treasury stock of 3,398,477 shares for acquisition of Peoples, Inc. | — | 42,243 | — | 67,970 | — | 110,213 |

| | | | | | | |
|--|--------|--------------|-----------|--------------|-------------|------------|
| Cash dividends declared (\$0.37 per share) | — | — | (11,461) | — | — | (11,461) |
| Reclassification of certain tax effects from accumulated other comprehensive income(1) | — | — | 1,479 | — | (1,479) | — |
| Cumulative effect adjustment(2) | — | — | 26 | — | — | 26 |
| Other comprehensive loss | — | — | — | — | (12,493) | (12,493) |
| Balance, September 30, 2018 | \$ 515 | \$ 1,013,314 | \$ 95,055 | \$ (415,605) | \$ (20,214) | \$ 673,065 |

- (1) Related to the adoption of Accounting Standards Update No. 2018-02, Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income. Refer to note 2 – Recent Accounting Pronouncements of our consolidated financial statements for further details.
- (2) Related to the adoption of Accounting Standards Update No. 2017-12, Derivatives and Hedging: Targeted Improvements to Accounting for Hedging Activities. Refer to note 2 – Recent Accounting Pronouncements of our consolidated financial statements for further details.

See accompanying notes to the consolidated interim financial statements.

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NATIONAL BANK HOLDINGS CORPORATION AND SUBSIDIARIES

Consolidated Statements of Cash Flows (Unaudited)

(In thousands)

| | For the nine months ended September 30, | |
|---|--|-----------|
| | 2018 | 2017 |
| Cash flows from operating activities: | | |
| Net income | \$ 44,216 | \$ 24,698 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Provision for loan losses | 2,721 | 9,700 |
| Depreciation and amortization | 8,908 | 9,862 |
| Current income tax receivable | 2,021 | 570 |
| Deferred income taxes | 5,271 | 2,116 |
| Net excess tax benefit on stock-based compensation | (1,271) | (3,442) |
| Discount accretion, net of premium amortization on securities | 2,292 | 1,953 |
| Loan accretion | (18,192) | (18,936) |
| Gain on sale of mortgages, net | (22,109) | (1,716) |
| Origination of loans held for sale, net of repayments | (808,527) | (66,333) |
| Proceeds from sales of loans held for sale | 809,419 | 75,619 |
| Bank-owned life insurance income | (1,361) | (1,417) |
| Impairment on mortgage servicing rights | 68 | — |
| Originations of mortgage servicing rights | (25) | — |
| Gain on the sale of other real estate owned, net | (386) | (2,254) |
| Impairment on other real estate owned | 220 | 766 |
| (Loss) gain on sale of fixed assets | (2) | 33 |
| Gain from banking center divestitures | — | (2,886) |
| Stock-based compensation | 3,244 | 2,771 |
| Change in other assets | (19,712) | (2,299) |
| Change in other liabilities | 16,275 | 9,917 |
| Net cash provided by operating activities | 23,070 | 38,722 |
| Cash flows from investing activities: | | |
| Purchase of FHLB stock | (9,577) | (7,377) |
| Proceeds from redemption of FHLB stock | 12,411 | 6,789 |
| Proceeds from maturities of investment securities held-to-maturity | 48,340 | 55,083 |
| Proceeds from maturities of investment securities available-for-sale | 168,773 | 171,326 |
| Proceeds from sales of investment securities available-for-sale | 33,517 | — |
| Proceeds from sales of non-marketable securities | 67 | — |
| Purchase of investment securities held-to-maturity | (40,735) | — |
| Purchase of investment securities available-for-sale | (42,199) | (98,503) |
| Net increase in loans | (202,863) | (273,127) |
| Purchases of premises and equipment, net | (5,033) | (1,769) |
| Proceeds from sales of loans | 713 | 33,813 |
| Proceeds from sales of other real estate owned | 1,694 | 5,580 |
| Net cash activity from acquisition | 68,984 | — |
| Net cash provided by (used in) investing activities | 34,092 | (108,185) |

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| | | |
|---|-------------|------------|
| Cash flows from financing activities: | | |
| Net (decrease) increase in deposits | (95,438) | 80,579 |
| (Decrease) increase in repurchase agreements | (74,768) | 803 |
| Advances from FHLB | 573,994 | 263,129 |
| FHLB payoffs | (592,395) | (172,679) |
| Issuance of stock under purchase and equity compensation plans | (2,139) | (7,125) |
| Proceeds from exercise of stock options | 9,052 | 78 |
| Payment of dividends | (11,373) | (6,898) |
| Net cash (used in) provided by financing activities | (193,067) | 157,887 |
| (Decrease) increase in cash, cash equivalents and restricted cash | (135,905) | 88,424 |
| Cash, cash equivalents and restricted cash at beginning of the year | 257,364 | 152,736 |
| Cash, cash equivalents and restricted cash at end of period | \$ 121,459 | \$ 241,160 |
| Supplemental disclosure of cash flow information during the period: | | |
| Cash paid for interest | \$ 14,853 | \$ 11,437 |
| Net tax refunds | \$ 2,489 | \$ 33 |
| Supplemental schedule of non-cash investing activities: | | |
| Loans transferred to other real estate owned at fair value | \$ 24,919 | \$ 760 |
| (Decrease) increase in loans purchased but not settled | \$ (11,195) | \$ 6,554 |
| Loans transferred from loans held for sale to loans | \$ 1,038 | \$ 4,406 |
| Treasury stock reissued for acquisition | \$ 110,213 | \$ — |

See accompanying notes to the consolidated interim financial statements.

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NATIONAL BANK HOLDINGS CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

September 30, 2018

Note 1 Basis of Presentation

National Bank Holdings Corporation ("NBHC" or the "Company") is a bank holding company that was incorporated in the State of Delaware in 2009 with the intent to acquire and operate financial services franchises and other complementary businesses in targeted markets. The Company is headquartered immediately south of Denver, in Greenwood Village, Colorado, and its primary operations are conducted through its wholly owned subsidiary, NBH Bank (the "Bank"), a Colorado state-chartered bank and a member of the Federal Reserve System. The Company provides a variety of banking products to both commercial and consumer clients through a network of 104 banking centers located primarily in Colorado and the greater Kansas City region, and through online and mobile banking products and services. On January 1, 2018, the Company completed the acquisition of Peoples, Inc. refer to note 3 – Acquisition Activities for further details.

The accompanying interim unaudited consolidated financial statements serve to update the National Bank Holdings Corporation Annual Report on Form 10-K for the year ended December 31, 2017 and include the accounts of the Company and its wholly owned subsidiary, NBH Bank. The accompanying unaudited consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles ("GAAP") and where applicable, with general practices in the banking industry or guidelines prescribed by bank regulatory agencies. However, they may not include all information and notes necessary to constitute a complete set of financial statements under GAAP applicable to annual periods and accordingly should be read in conjunction with the financial information contained in the Company's most recent Form 10-K. The unaudited consolidated financial statements reflect all adjustments which are, in the opinion of management, necessary for a fair statement of the results presented. All such adjustments are of a normal recurring nature. All significant intercompany balances and transactions have been eliminated in consolidation. Certain reclassifications of prior years' amounts are made whenever necessary to conform to current period presentation. The results of operations for the interim period is not necessarily indicative of the results that may be expected for the full year or any other interim period. All amounts are in thousands, except share and per share data, or as otherwise noted.

GAAP requires management to make estimates that affect the reported amounts of assets, liabilities, revenues and expenses, and disclosures of contingent assets and liabilities. By their nature, estimates are based on judgment and available information. Management has made significant estimates in certain areas, such as the amount and timing of expected cash flows from assets, the valuation of other real estate owned ("OREO"), the fair value adjustments on assets acquired and liabilities assumed, the valuation of core deposit intangible assets, the valuation of investment securities for other-than-temporary impairment ("OTTI"), the valuation of stock-based compensation, the valuation of mortgage servicing rights, the fair values of financial instruments, the allowance for loan losses ("ALL") and contingent liabilities. Because of the inherent uncertainties associated with any estimation process and future changes in market and

economic conditions, it is possible that actual results could differ significantly from those estimates.

Beginning in the first quarter 2018, loans previously referred to as "non 310-30 loans" are referred to as "originated and acquired loans," which include originated loans as well as acquired loans not accounted for under ASC 310-30. No amounts were reclassified resulting from this change in terminology.

The Company's significant accounting policies followed in the preparation of the unaudited consolidated financial statements are disclosed in note 2 of the audited financial statements for the year ended December 31, 2017 and are contained in the Company's Annual Report on Form 10-K. There have not been any significant changes to the application of significant accounting policies since December 31, 2017, except for the following additions:

Mortgage Servicing— Mortgage servicing rights ("MSRs") associated with loans originated and sold, where servicing is retained, are initially capitalized at fair value and included in intangible assets, net on the consolidated statements of financial condition. For subsequent measurement purposes, the Company measures servicing assets based on the lower of cost or market using the amortization method. The values of these capitalized servicing rights are amortized as an offset to the loan servicing income earned in relation to the servicing revenue expected to be earned. The carrying values of these rights are reviewed quarterly for impairment based on the fair value of those assets. For purposes of impairment evaluation and measurement, management stratifies MSRs based on the predominant risk characteristics of the underlying loans, including loan type and loan term. If, by individual stratum, the carrying amount of these MSRs exceeds fair value, a valuation allowance is established and the impairment is recognized in mortgage banking income. If the fair value of impaired MSRs subsequently increases, management recognizes the increase in fair value in

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current period mortgage banking income and, through a reduction in the valuation allowance, adjusts the carrying value of the MSR to a level not in excess of amortized cost.

Reserve for Mortgage Loan Repurchase Losses—The Company sells mortgage loans to various third parties, including government-sponsored entities, under contractual provisions that include various representations and warranties that typically cover ownership of the loan, compliance with loan criteria set forth in the applicable agreement, validity of the lien securing the loan, absence of delinquent taxes or liens against the property securing the loan, and similar matters. The Company may be required to repurchase the mortgage loans with identified defects, indemnify the investor or insurer, or reimburse the investor for credit loss incurred on the loan (collectively “repurchase”) in the event of a material breach of such contractual representations or warranties. Risk associated with potential repurchases or other forms of settlement is managed through underwriting and quality assurance practices.

The Company establishes mortgage repurchase reserves related to various representations and warranties that reflect management’s estimate of losses based on a combination of factors. Such factors incorporate actual and historic loss history, delinquency trends in the portfolio and economic conditions. The Company establishes a reserve at the time loans are sold and quarterly updates the reserve estimate during the estimated loan life. The repurchase reserve is included in other liabilities on the consolidated statements of financial condition.

Note 2 Recent Accounting Pronouncements

Revenue from Contracts with Customers—In May 2014, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) 2014-09, Revenue from Contracts with Customers. This update supersedes revenue recognition requirements in ASC Topic 605, Revenue Recognition, including most industry-specific revenue recognition guidance in the FASB Accounting Standards Codification (“ASC”). The new guidance stipulates that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The guidance provides specific steps that entities should apply in order to achieve this principle. The amendments are effective for interim and annual periods beginning after December 15, 2017, with early application permitted for interim and annual periods beginning after December 15, 2016. ASU 2014-09 allows for either full retrospective or modified retrospective adoption.

The new guidance does not apply to revenue associated with financial assets and liabilities including loans, leases, securities, and derivatives that are accounted for under other GAAP. Accordingly, the majority of the Company’s revenues are not affected. The Company adopted ASU No. 2014-09 on January 1, 2018 utilizing the modified retrospective approach. Additionally, the Company has determined certain service charges, bank card fees and real estate sales are within the scope of the ASU, but has not identified changes to the timing or amount of revenue recognition. Accounting policies and procedures did not change materially as the principles of revenue recognition from the ASU are largely consistent with existing guidance and current practices applied by the Company. Refer to note 11 of our consolidated financial statements for required disclosures under the new standard.

Leases—In February 2016, the FASB issued ASU 2016-02, Leases. The guidance in ASU 2016-02 supersedes the lease recognition requirements in ASC Topic 840, Leases. The new standard establishes a right-of-use (“ROU”) model that requires a lessee to record a ROU asset and lease liability on the balance sheet for all leases with terms longer than 12 months. Leases will be classified as either finance or operating, with classification affecting the pattern of expense recognition in the income statements. The new standard is effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years, with early adoption permitted. ASU 2016-02 will be effective for the Company on January 1, 2019 and initially required transition using a modified retrospective approach for leases existing at, or entered into after, the beginning of the earliest comparative period presented in the financial statements. In July 2018, the Financial Accounting Standards Board issued ASU 2018-11 which, among other things, provides an additional transition method that allows entities to not apply the guidance in ASU 2016-02 in the comparative periods presented in the financial statements and instead recognize a cumulative-effect adjustment to the opening balance of retained earnings in the period of adoption. We expect to elect to apply certain practical expedients provided under ASU 2016-02 whereby we will not reassess (i) whether any expired or existing contracts are or contain leases, (ii) the lease classification for any expired or existing leases and (iii) initial direct costs for any existing leases. We also do not expect to apply the recognition requirements of ASU 2016-02 to any short-term leases (as defined by related accounting guidance). The Company has reviewed all existing lease agreements for which the amended guidance is to be applied, and it does not expect the adoption of the new standard to have a material impact on its results of operations or balance sheet as a result of the recognition of right-to-use assets and lease liabilities related to operating leases. The most significant effects of the adoption of this guidance will be additional financial statement disclosures.

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Financial Instruments - Credit Losses—In June 2016, the FASB issued ASU 2016-13, Measurement of Credit Losses on Financial Instruments. This update replaces the current incurred loss methodology for recognizing credit losses with a current expected credit loss model, which requires the measurement of all expected credit losses for financial assets held at the reporting date based on historical experience, current conditions, and reasonable and supportable forecasts. This amendment broadens the information that an entity must consider in developing its expected credit loss estimates. Additionally, the update amends the accounting for credit losses for available-for-sale debt securities and purchased financial assets with a more-than-insignificant amount of credit deterioration since origination. This update requires enhanced disclosures to help investors and other financial statement users better understand significant estimates and judgments used in estimating credit losses, as well as the credit quality and underwriting standards of a company's loan portfolio. The amendments in this update are effective for fiscal years beginning after December 15, 2019, including interim periods within those fiscal years. Early adoption in fiscal years beginning after December 15, 2018 is permitted. The amendment requires the use of the modified retrospective approach for adoption. The Company is in the process of evaluating the impact of the ASU's adoption on the Company's consolidated financial statements.

Derivatives and Hedging - Targeted Improvements to Accounting for Hedging Activities—In August 2017, the FASB issued ASU 2017-12, Derivatives and Hedging: Targeted Improvements to Accounting for Hedging Activities. The purpose of this updated guidance is to better align a company's financial reporting for hedging activities with the economic objectives of those activities. ASU 2017-12 is effective for public business entities for annual and interim periods in fiscal years beginning after December 15, 2018. Early adoption is permitted, including in an interim period. ASU 2017-12 requires a modified retrospective transition method in which the Company will recognize the cumulative effect of the change on the opening balance of each affected component of equity in the consolidated statements of financial condition as of the date of adoption. The Company adopted ASU 2017-12 during the first quarter of 2018 and recorded a cumulative effect adjustment of \$26 thousand within equity in the consolidated statements of financial condition.

Reclassification of Certain Tax Effects—In February 2018, the FASB issued ASU 2018-02, Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income. This update allows a reclassification from accumulated other comprehensive income (AOCI) to retained earnings for stranded tax effects resulting from the Tax Cuts and Jobs Act. The amendments eliminate the stranded tax effects that were created as a result of the reduction of historical U.S. federal corporate income tax rate to the newly enacted U.S. federal corporate income tax rate. The update is effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2018, with early adoption permitted, and is to be applied either in the period of adoption or retrospectively to each period in which the effect of the change in the U.S. federal corporate income tax rate in the Tax Cuts and Jobs Act is recognized. The Company early adopted ASU 2018-02 in the first quarter of 2018, resulting in a \$1.5 million reclassification from accumulated other comprehensive loss to retained earnings on the consolidated statements of financial condition and the consolidated statements of changes in shareholders' equity.

Other Pronouncements—The Company early adopted ASU 2018-15, Intangibles – Goodwill and Other – Internal-Use Software: Customer's Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement That is a Service Contract (Subtopic 350-40) on a prospective basis with no material impact on its financial statements. The Company also adopted ASU 2016-01, Financial Instruments - Recognition and Measurement of Financial Assets and Financial Liabilities (Topic 825), ASU 2016-18, Restricted Cash (a consensus of the FASB Emerging Issues Task

Force, ASU 2016-15, Statement of Cash Flows: Classification of Certain Cash Receipts and Cash Payments and ASU 2017-05 Other Income – Gains and Losses from the Derecognition of Nonfinancial Assets (Subtopic 610-20) with no material impact on its financial statements.

The Company reviewed ASU 2017-04, Intangibles - Goodwill and Other (Topic 350): Simplifying the Test for Goodwill Impairment and ASU 2018-07, Compensation – Stock Compensation (Topic 718): Improvements to Nonemployee Share-Based Payment Accounting and does not expect the adoption of these pronouncements to have a material impact on its financial statements.

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Note 3 Acquisition Activities

On January 1, 2018, the Company completed its acquisition of Peoples, Inc. (“Peoples”), the bank holding company of Colorado-based Peoples National Bank and Kansas-based Peoples Bank. Immediately following the completion of the acquisition, Peoples National Bank and Peoples Bank merged into NBH Bank. Pursuant to the merger agreement executed in June 2017, the Company paid \$36.2 million of cash consideration and 3,398,477 shares of the Company’s Class A common stock in exchange for all of the outstanding common stock of Peoples. Included in the cash consideration is \$10.0 million of restricted cash placed in escrow for certain potential liabilities for which the Company is indemnified pursuant to the merger agreement. The restricted cash is included in other assets in the Company’s consolidated statements of financial condition at September 30, 2018. The transaction has a value of \$146.4 million in the aggregate, based on the Company’s closing price of \$32.43 on the acquisition date. Acquisition-related costs of \$0.0 million and \$8.0 million were included in the Company’s consolidated statements of operations for the three and nine months ended September 30, 2018. The financial results of Peoples are included in the financial results of the Company subsequent to the acquisition date.

The Company determined that this acquisition constitutes a business combination as defined in ASC Topic 805, Business Combinations. Accordingly, as of the date of the acquisition, the Company recorded the assets acquired and liabilities assumed at fair value. The Company determined fair values in accordance with the guidance provided in ASC Topic 820, Fair Value Measurements and Disclosures. Fair value is established by discounting the expected future cash flows with a market discount rate for like maturities and risk instruments. The estimation of expected future cash flows, market conditions and other future events and actual results could differ materially. The determination of the fair values of fixed assets, loans, OREO, core deposit intangible, mortgage servicing rights and mortgage repurchase reserve involves a high degree of judgment and complexity. The Company has made the determination of fair values using the best information available at the time; however, purchase accounting is not complete and the assumptions used are subject to change and, if changed, could have a material effect on the Company's financial position and results of operations.

The table below summarizes the net assets acquired (at fair value) and consideration transferred in connection with the Peoples acquisition:

| | |
|--|------------|
| Assets: | |
| Cash and due from banks | \$ 105,173 |
| Investment securities available-for-sale | 118,512 |
| Non-marketable securities | 4,796 |
| Loans | 542,707 |
| Loans held for sale | 54,260 |
| Other real estate owned | 1,253 |
| Premises and equipment | 18,584 |
| Core deposit intangible asset | 10,477 |
| Mortgage servicing rights | 4,301 |

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| | |
|---|------------|
| Other assets | 15,361 |
| Total assets acquired | \$ 875,424 |
| Liabilities: | |
| Total deposits | 729,911 |
| FHLB borrowings | 33,825 |
| Other liabilities | 20,683 |
| Total liabilities assumed | \$ 784,419 |
| Identifiable net assets acquired | \$ 91,005 |
| Consideration: | |
| NBHC common stock paid at January 1, 2018, closing price of \$32.43 | \$ 110,213 |
| Cash | 36,189 |
| Total | \$ 146,402 |
| Estimated goodwill created | \$ 55,397 |

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In connection with the Peoples acquisition, the Company recorded \$55.4 million of goodwill, a \$10.5 million core deposit intangible asset, a \$4.3 million mortgage servicing rights intangible asset and a \$4.0 million mortgage repurchase reserve, included in other liabilities. The core deposit intangible will be amortized straight-line over ten years and the mortgage servicing rights intangible is amortized in proportion to and over the period of the estimated net servicing income. The Federal Home Loan Bank (“FHLB”) borrowings of \$33.8 million were paid off during the first quarter of 2018.

The fair value of the acquired assets and liabilities noted in the table may change during the provisional period, which may last up to twelve months subsequent to the acquisition date. The Company may obtain additional information to refine the valuation of the acquired assets and liabilities and adjust the recorded fair value. Adjustments recorded to the acquired assets and liabilities will be applied prospectively in accordance with ASU 2015-16.

At the date of acquisition, the gross contractual amounts receivable, inclusive of all principal and interest, was \$713.6 million. The Company’s best estimate of the contractual principal cash flows for loans not expected to be collected was \$6.1 million.

The following pro forma information combines the historical results of Peoples and the Company. In accordance with the merger agreement, the Peoples national mortgage business was wound down prior to acquisition. Accordingly, the pro forma information excludes the results of the Peoples national mortgage business for prior periods presented. The pro forma financial information does not include the potential impacts of possible business model changes, current market conditions, revenue enhancements, expense efficiencies, or other factors. If the Peoples acquisition had been completed on January 1, 2017, pro forma total revenue for the Company would have been approximately \$67.8 million and \$69.0 million for the three months ended September 30, 2018 and 2017, respectively. Pro forma net income for the Company would have been approximately \$18.2 million and \$10.4 million for the three months ended September 30, 2018 and 2017, respectively. Pro forma basic and dilutive earnings per share for the Company would have been \$0.59 and \$0.58 for the three months ended September 30, 2018, respectively, and \$0.34 and \$0.34 for the three months ended September 30, 2017, respectively.

If the Peoples acquisition had been completed on January 1, 2017, pro forma total revenue for the Company would have been approximately \$202.3 million and \$201.0 million for the nine months ended September 30, 2018 and 2017, respectively. Pro forma net income for the Company would have been approximately \$50.5 million and \$32.0 million for the nine months ended September 30, 2018 and 2017, respectively. Pro forma basic and dilutive earnings per share for the Company would have been \$1.65 and \$1.61 for the nine months ended September 30, 2018, respectively, and \$1.06 and \$1.03 for the nine months ended September 30, 2017, respectively.

For the three and nine months ended September 30, 2018, the pro forma information reflects adjustments made to exclude acquisition-related expenses of the Company of \$0.0 million and \$8.0 million, respectively. For the three months ended September 30, 2017, the pro-forma information reflects adjustments made to exclude acquisition-related expenses of the Company of \$0.4 million and include estimated amortization and accretion of

purchase discounts and premiums of \$0.2 million in addition to estimated amortization of acquired identifiable intangibles of \$0.3 million. For the nine months ended September 30, 2017, the pro-forma information reflects adjustments made to exclude acquisition-related expenses of the Company of \$0.7 million and include estimated amortization and accretion of purchase discounts and premiums of \$0.7 million in addition to estimated amortization of acquired identifiable intangibles of \$0.8 million. The pro forma information is theoretical in nature and not necessarily indicative of future consolidated results of operations of the Company or the consolidated results of operations which would have resulted had the Company acquired Peoples during the periods presented.

The Company has determined that it is impractical to report the amounts of revenue and earnings of legacy Peoples since the acquisition date due to the integration of operations shortly after the acquisition date. Accordingly, reliable and separate complete revenue and earnings information is no longer available. In addition, such amounts would require significant estimates related to the proper allocation of merger cost savings that cannot be objectively made.

Note 4 Investment Securities

The Company's investment securities portfolio is comprised of available-for-sale and held-to-maturity investment securities. These investment securities totaled \$1.0 billion at September 30, 2018 and included \$0.8 billion of available-for-sale securities and \$0.2 billion of held-to-maturity securities. At December 31, 2017, investment securities totaled \$1.1 billion and included \$0.8 billion of available-for-sale securities and \$0.3 billion of held-to-maturity securities.

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Available-for-sale

At September 30, 2018 and December 31, 2017, the Company held \$796.5 million and \$855.3 million of available-for-sale investment securities, respectively. Available-for-sale securities are summarized as follows as of the dates indicated:

| | September 30, 2018 | | | |
|--|--------------------|---------------------------|----------------------------|------------|
| | Amortized cost | Gross unrealized gains | Gross unrealized losses | Fair value |
| Mortgage-backed securities (“MBS”): | | | | |
| Residential mortgage pass-through securities issued or guaranteed by U.S. Government agencies or sponsored enterprises | \$ 158,227 | \$ 1,176 | \$ (3,090) | \$ 156,313 |
| Other residential MBS issued or guaranteed by U.S. Government agencies or sponsored enterprises | 667,864 | 8 | (28,834) | 639,038 |
| Municipal securities | 739 | — | (10) | 729 |
| Other securities | 469 | — | — | 469 |
| Total investment securities available-for-sale | \$ 827,299 | \$ 1,184 | \$ (31,934) | \$ 796,549 |

| | December 31, 2017 | | | |
|--|-------------------|---------------------------|----------------------------|------------|
| | Amortized cost | Gross unrealized gains | Gross unrealized losses | Fair value |
| Mortgage-backed securities: | | | | |
| Residential mortgage pass-through securities issued or guaranteed by U.S. Government agencies or sponsored enterprises | \$ 167,269 | \$ 2,371 | \$ (992) | \$ 168,648 |
| Other residential MBS issued or guaranteed by U.S. Government agencies or sponsored enterprises | 702,107 | 351 | (17,228) | 685,230 |
| Municipal securities | 1,054 | — | (6) | 1,048 |
| Other securities | 419 | — | — | 419 |
| Total investment securities available-for-sale | \$ 870,849 | \$ 2,722 | \$ (18,226) | \$ 855,345 |

At September 30, 2018 and December 31, 2017, mortgage-backed securities represented primarily all of the Company’s available-for-sale investment portfolio and all mortgage-backed securities were backed by government sponsored enterprises (“GSE”) collateral such as Federal Home Loan Mortgage Corporation (“FHLMC”) and Federal National Mortgage Association (“FNMA”), and the government sponsored agency Government National Mortgage Association (“GNMA”).

The tables below summarize the available-for-sale securities with unrealized losses as of the dates shown, along with the length of the impairment period:

| | September 30, 2018 | | 12 months or more | | Total Fair value | Unrealized losses |
|--|--------------------------------------|----------------------|-------------------|----------------------|------------------------|----------------------|
| | Less than 12 months Fair value | Unrealized losses | Fair value | Unrealized losses | | |
| Mortgage-backed securities: | | | | | | |
| Residential mortgage pass-through securities issued or guaranteed by U.S. Government agencies or sponsored enterprises | \$ 76,124 | \$ (1,947) | \$ 36,292 | \$ (1,142) | \$ 112,416 | \$ (3,089) |
| Other residential MBS issued or guaranteed by U.S. Government agencies or sponsored enterprises | 289,627 | (6,960) | 345,438 | (21,874) | 635,065 | (28,834) |
| Municipal securities | 510 | (10) | — | — | 510 | (10) |
| Total | \$ 366,260 | \$ (8,918) | \$ 381,730 | \$ (23,016) | \$ 747,990 | \$ (31,934) |

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| | December 31, 2017 | | | | Total Fair value | Unrealized losses |
|--|--------------------------------------|----------------------|------------------------------------|----------------------|------------------------|----------------------|
| | Less than 12 months Fair value | Unrealized losses | 12 months or more Fair value | Unrealized losses | | |
| Mortgage-backed securities: | | | | | | |
| Residential mortgage pass-through securities issued or guaranteed by U.S. Government agencies or sponsored enterprises | \$ 62,178 | \$ (408) | \$ 36,086 | \$ (584) | \$ 98,264 | \$ (992) |
| Other residential MBS issued or guaranteed by U.S. Government agencies or sponsored enterprises | 162,346 | (830) | 412,967 | (16,398) | 575,313 | (17,228) |
| Municipal securities | 514 | (6) | — | — | 514 | (6) |
| Total | \$ 225,038 | \$ (1,244) | \$ 449,053 | \$ (16,982) | \$ 674,091 | \$ (18,226) |

The unrealized losses in the Company's investment portfolio at September 30, 2018 were caused by changes in interest rates. The portfolio included 220 securities, having an aggregate fair value of \$748.0 million, which were in an unrealized loss position at September 30, 2018, compared to 87 securities, with an aggregate fair value of \$674.1 million at December 31, 2017.

Management evaluated all of the available for sale securities in an unrealized loss position at September 30, 2018 and December 31, 2017, and concluded no other-than-temporary impairment (“OTTI”) existed at September 30, 2018 or December 31, 2017. During the nine months ended September 30, 2018, the Company recorded a \$0.2 million recovery included in other non-interest expense related to one security with an aggregate fair value of \$0.3 million which had a previously incurred OTTI impairment of \$0.2 million during the nine months ended September 30, 2017. The unrealized losses on the remaining securities in an unrealized loss position were caused by changes in interest rates. The Company has no intention to sell these securities before recovery of their amortized cost and believes it will not be required to sell the securities before the recovery of their amortized cost.

Certain securities are pledged as collateral for public deposits, securities sold under agreements to repurchase, and to secure borrowing capacity at the Federal Reserve Bank and FHLB, if needed. The fair value of available-for-sale investment securities pledged as collateral totaled \$294.5 million and \$334.6 million at September 30, 2018 and at December 31, 2017, respectively.

Mortgage-backed securities do not have a single maturity date and actual maturities may differ from contractual maturities depending on the repayment characteristics and experience of the underlying financial instruments. The estimated weighted average life of the available-for-sale mortgage-backed securities portfolio was 3.5 years and 3.4

years at September 30, 2018 and December 31, 2017, respectively. This estimate is based on assumptions and actual results may differ. At September 30, 2018 and December 31, 2017, the duration of the total available-for-sale investment portfolio was 3.1 years and 3.1 years, respectively.

As of September 30, 2018, municipal securities with an amortized cost and fair value of \$0.2 million were due after one year through five years and municipal securities with an amortized cost and fair value of \$0.5 million were due after five years through ten years. Other securities of \$0.5 million as of September 30, 2018, have no stated contractual maturity date.

Held-to-maturity

At September 30, 2018 and December 31, 2017, the Company held \$249.5 million and \$258.7 million of held-to-maturity investment securities, respectively. Held-to-maturity investment securities are summarized as follows as of the dates indicated:

| | September 30, 2018 | | | |
|--|--------------------|------------------------------|-------------------------------|------------|
| | Amortized cost | Gross unrealized gains | Gross unrealized losses | Fair value |
| Mortgage-backed securities: | | | | |
| Residential mortgage pass-through securities issued or guaranteed by U.S. Government agencies or sponsored enterprises | \$ 166,955 | \$ — | \$ (4,247) | \$ 162,708 |
| Other residential MBS issued or guaranteed by U.S. Government agencies or sponsored enterprises | 82,509 | — | (2,847) | 79,662 |
| Total investment securities held-to-maturity | \$ 249,464 | \$ — | \$ (7,094) | \$ 242,370 |

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| | December 31, 2017 | | | Fair value |
|--|-------------------|------------------------|-------------------------|------------|
| | Amortized cost | Gross unrealized gains | Gross unrealized losses | |
| Mortgage-backed securities: | | | | |
| Residential mortgage pass-through securities issued or guaranteed by U.S. Government agencies or sponsored enterprises | \$ 204,352 | \$ 151 | \$ (455) | \$ 204,048 |
| Other residential MBS issued or guaranteed by U.S. Government agencies or sponsored enterprises | 54,378 | — | (1,655) | 52,723 |
| Total investment securities held-to-maturity | \$ 258,730 | \$ 151 | \$ (2,110) | \$ 256,771 |

The tables below summarize the held-to-maturity securities with unrealized losses as of the dates shown, along with the length of the impairment period:

| | September 30, 2018 | | | | Total Fair value | Unrealized losses |
|--|--------------------------------|-------------------|------------------------------|-------------------|------------------|-------------------|
| | Less than 12 months Fair value | Unrealized losses | 12 months or more Fair value | Unrealized losses | | |
| Mortgage-backed securities: | | | | | | |
| Residential mortgage pass-through securities issued or guaranteed by U.S. Government agencies or sponsored enterprises | \$ 148,167 | \$ (3,674) | \$ 14,541 | \$ (573) | \$ 162,708 | \$ (4,247) |
| Other residential MBS issued or guaranteed by U.S. Government agencies or sponsored enterprises | 41,705 | (686) | 37,957 | (2,161) | 79,662 | (2,847) |
| Total | \$ 189,872 | \$ (4,360) | \$ 52,498 | \$ (2,734) | \$ 242,370 | \$ (7,094) |

| | December 31, 2017 | | | | Total Fair value | Unrealized losses |
|---|--------------------------------|-------------------|------------------------------|-------------------|------------------|-------------------|
| | Less than 12 months Fair value | Unrealized losses | 12 months or more Fair value | Unrealized losses | | |
| Mortgage-backed securities: | | | | | | |
| Residential mortgage pass-through securities issued or guaranteed by U.S. | \$ 149,182 | \$ (220) | \$ 17,506 | \$ (235) | \$ 166,688 | \$ (455) |

| | | | | | | |
|---|------------|----------|-----------|------------|------------|------------|
| Government agencies or sponsored enterprises | | | | | | |
| Other residential MBS issued or guaranteed by U.S. Government agencies or sponsored enterprises | 6,460 | (65) | 46,264 | (1,590) | 52,724 | (1,655) |
| Total | \$ 155,642 | \$ (285) | \$ 63,770 | \$ (1,825) | \$ 219,412 | \$ (2,110) |

The held-to-maturity portfolio included 52 securities, having an aggregate fair value of \$242.4 million, which were in an unrealized loss position at September 30, 2018, compared to 36 securities, with a fair value of \$219.4 million, at December 31, 2017.

The unrealized losses in the Company's investments at September 30, 2018 and December 31, 2017 were caused by changes in interest rates. Management evaluated all of the held-to-maturity securities in an unrealized loss position and concluded that no OTTI existed at September 30, 2018 or December 31, 2017. The Company has no intention to sell these securities before the recovery of their amortized cost and believes it will not be required to sell the securities before the recovery of their amortized cost.

The carrying value of held-to-maturity investment securities pledged as collateral totaled \$166.9 million and \$142.0 million at September 30, 2018 and December 31, 2017, respectively.

Actual maturities of mortgage-backed securities may differ from scheduled maturities depending on the repayment characteristics and experience of the underlying financial instruments. The estimated weighted average expected life of the held-to-maturity mortgage-backed securities portfolio as of September 30, 2018 and December 31, 2017 was 3.0 years and 3.1 years, respectively. This estimate is based on assumptions and actual results may differ. The duration of the total held-to-maturity investment portfolio was 2.8 years and 2.8 years as of September 30, 2018 and December 31, 2017, respectively.

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Note 5 Loans

The loan portfolio is comprised of loans originated by the Company and loans that were acquired in connection with the Company's acquisitions. Beginning in the first quarter 2018, loans previously referred to as "non 310-30 loans" are referred to as "originated and acquired loans," which include originated loans as well as acquired loans not accounted for under ASC 310-30. No amounts were reclassified resulting from this change in terminology.

The tables below show the loan portfolio composition including carrying value by segment of originated and acquired loans and loans accounted for under ASC Topic 310-30, Receivables—Loans and Debt Securities Acquired with Deteriorated Credit Quality, as of the dates shown. The carrying value of originated and acquired loans is net of discounts, fees, costs and fair value marks of \$11.4 million and \$4.3 million as of September 30, 2018 and December 31, 2017, respectively.

| | September 30, 2018 | | | |
|---|--|------------------------|--------------|------------|
| | Originated and acquired loans | ASC 310-30 loans | Total loans | % of total |
| Commercial | \$ 2,419,833 | \$ 22,258 | \$ 2,442,091 | 62.5% |
| Commercial real estate non-owner occupied | 569,401 | 41,842 | 611,243 | 15.7% |
| Residential real estate | 814,506 | 10,721 | 825,227 | 21.1% |
| Consumer | 26,650 | 100 | 26,750 | 0.7% |
| Total | \$ 3,830,390 | \$ 74,921 | \$ 3,905,311 | 100.0% |

| | December 31, 2017 | | | |
|---|--|------------------------|--------------|------------|
| | Originated and acquired loans | ASC 310-30 loans | Total loans | % of total |
| Commercial | \$ 1,845,130 | \$ 29,475 | \$ 1,874,605 | 59.0% |
| Commercial real estate non-owner occupied | 485,141 | 77,908 | 563,049 | 17.7% |
| Residential real estate | 703,478 | 12,759 | 716,237 | 22.5% |
| Consumer | 24,575 | 481 | 25,056 | 0.8% |
| Total | \$ 3,058,324 | \$ 120,623 | \$ 3,178,947 | 100.0% |

Delinquency for originated and acquired loans is shown in the following tables at September 30, 2018 and December 31, 2017:

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| | September 30, 2018 | | | | | Total originated and acquired loans | Loans > 90 days past due and Non-still accruing | |
|--|---------------------|---------------------|-------------------------------|----------------|--------------|-------------------------------------|---|-----------|
| | 30-59 days past due | 60-89 days past due | Greater than 90 days past due | Total past due | Current | | due and Non-still accruing | accrual |
| Originated and acquired loans: | | | | | | | | |
| Commercial: | | | | | | | | |
| Commercial and industrial | \$ 4,003 | \$ 2,050 | \$ 4,983 | \$ 11,036 | \$ 1,743,570 | \$ 1,754,606 | \$ 148 | \$ 5,951 |
| Owner occupied commercial real estate | — | 302 | 2,759 | 3,061 | 405,640 | 408,701 | — | 7,027 |
| Agriculture | — | 150 | 706 | 856 | 213,050 | 213,906 | — | 773 |
| Energy | — | — | 848 | 848 | 41,772 | 42,620 | — | 848 |
| Total commercial | 4,003 | 2,502 | 9,296 | 15,801 | 2,404,032 | 2,419,833 | 148 | 14,599 |
| Commercial real estate non-owner occupied: | | | | | | | | |
| Construction | — | 127 | 1,081 | 1,208 | 91,718 | 92,926 | — | 1,081 |
| Acquisition/development | — | — | 17 | 17 | 22,322 | 22,339 | — | 130 |
| Multifamily | — | — | — | — | 76,090 | 76,090 | — | — |
| Non-owner occupied | — | — | 132 | 132 | 377,914 | 378,046 | 132 | 581 |
| Total commercial real estate | — | 127 | 1,230 | 1,357 | 568,044 | 569,401 | 132 | 1,792 |
| Residential real estate: | | | | | | | | |
| Senior lien | 1,184 | 1,197 | 1,833 | 4,214 | 713,616 | 717,830 | 280 | 7,181 |
| Junior lien | 582 | 66 | 105 | 753 | 95,923 | 96,676 | — | 841 |
| Total residential real estate | 1,766 | 1,263 | 1,938 | 4,967 | 809,539 | 814,506 | 280 | 8,022 |
| Consumer | 198 | 1 | 11 | 210 | 26,440 | 26,650 | — | 45 |
| Total originated and acquired loans | \$ 5,967 | \$ 3,893 | \$ 12,475 | \$ 22,335 | \$ 3,808,055 | \$ 3,830,390 | \$ 560 | \$ 24,458 |

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| | December 31, 2017 | | | | Current | Total originated and acquired loans | Loans > 90 days past due and Non-still accruing | |
|---|---------------------|---------------------|-------------------------------|----------------|--------------|-------------------------------------|---|-----------|
| | 30-59 days past due | 60-89 days past due | Greater than 90 days past due | Total past due | | | due | accruing |
| Originated and acquired loans: | | | | | | | | |
| Commercial: | | | | | | | | |
| Commercial and industrial Owner occupied commercial real estate | \$ 554 | \$ 117 | \$ 1,389 | \$ 2,060 | \$ 1,373,962 | \$ 1,376,022 | \$ 150 | \$ 7,767 |
| Agriculture | 696 | — | 1,983 | 2,679 | 270,074 | 272,753 | — | 3,478 |
| Energy | 585 | — | 701 | 1,286 | 137,609 | 138,895 | — | 2,003 |
| Total commercial | — | — | 1,645 | 1,645 | 55,815 | 57,460 | — | 1,645 |
| Commercial real estate non-owner occupied: | 1,835 | 117 | 5,718 | 7,670 | 1,837,460 | 1,845,130 | 150 | 14,893 |
| Construction | — | — | 179 | 179 | 107,502 | 107,681 | — | 179 |
| Acquisition/development Multifamily | 1,097 | — | — | 1,097 | 13,318 | 14,415 | — | — |
| Non-owner occupied | — | — | — | — | 26,947 | 26,947 | — | — |
| Total commercial real estate | 56 | — | 574 | 630 | 335,468 | 336,098 | — | 605 |
| Residential real estate: | 1,153 | — | 753 | 1,906 | 483,235 | 485,141 | — | 784 |
| Senior lien | 1,167 | 885 | 1,396 | 3,448 | 643,034 | 646,482 | — | 4,724 |
| Junior lien | 233 | 91 | 41 | 365 | 56,631 | 56,996 | — | 459 |
| Total residential real estate | 1,400 | 976 | 1,437 | 3,813 | 699,665 | 703,478 | — | 5,183 |
| Consumer | 157 | 6 | 5 | 168 | 24,407 | 24,575 | — | 140 |
| Total originated and acquired loans | \$ 4,545 | \$ 1,099 | \$ 7,913 | \$ 13,557 | \$ 3,044,767 | \$ 3,058,324 | \$ 150 | \$ 21,000 |

Loans are considered past due or delinquent when the contractual principal or interest due in accordance with the terms of the loan agreement remains unpaid after the due date of the scheduled payment. Pooled loans accounted for under ASC 310-30 that are 90 days or more past due and still accruing are generally considered to be performing and therefore are not included in the tables above. Non-accrual loans include non-accrual loans and troubled debt restructurings on non-accrual status. Non-accrual originated and acquired loans totaled \$24.5 million at September 30, 2018, increasing \$3.5 million, or 16.5% from December 31, 2017.

The Company's internal risk rating system uses a series of grades that reflect its assessment of the credit quality of loans based on an analysis of the borrower's financial condition, liquidity and ability to meet contractual debt service

requirements. Loans that are perceived to have acceptable risk are categorized as “Pass” loans. “Special mention” loans represent loans that have potential credit weaknesses that deserve close attention. Special mention loans include borrowers that have potential weaknesses or unwarranted risks that, unless corrected, may threaten the borrower's ability to meet debt service requirements. However, these borrowers are still believed to have the ability to respond to and resolve the financial issues that threaten their financial situation. Loans classified as “Substandard” have a well-defined credit weakness and are inadequately protected by the current paying capacity of the obligor or of the collateral pledged, if any. Although these loans are identified as potential problem loans, they may never become non-performing. Substandard loans have a distinct possibility of loss if the deficiencies are not corrected. “Doubtful” loans are loans that management believes the collection of payments in accordance with the terms of the loan agreement are highly questionable and improbable. Doubtful loans are deemed impaired and put on non-accrual status.

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Credit exposure for all loans as determined by the Company's internal risk rating system was as follows as of September 30, 2018 and December 31, 2017, respectively:

| | September 30, 2018 | | | | |
|---|--------------------|--------------------|-------------|----------|--------------|
| | Pass | Special mention | Substandard | Doubtful | Total |
| Originated and acquired loans: | | | | | |
| Commercial: | | | | | |
| Commercial and industrial | \$ 1,719,659 | \$ 9,052 | \$ 24,583 | \$ 1,312 | \$ 1,754,606 |
| Owner occupied commercial real estate | 369,711 | 27,267 | 11,639 | 84 | 408,701 |
| Agriculture | 210,243 | 2,765 | 865 | 33 | 213,906 |
| Energy | 41,772 | — | 848 | — | 42,620 |
| Total commercial | 2,341,385 | 39,084 | 37,935 | 1,429 | 2,419,833 |
| Commercial real estate non-owner occupied: | | | | | |
| Construction | 90,907 | 811 | 1,208 | — | 92,926 |
| Acquisition/development | 22,209 | — | 130 | — | 22,339 |
| Multifamily | 76,090 | — | — | — | 76,090 |
| Non-owner occupied | 356,102 | 20,322 | 1,622 | — | 378,046 |
| Total commercial real estate | 545,308 | 21,133 | 2,960 | — | 569,401 |
| Residential real estate: | | | | | |
| Senior lien | 706,386 | 3,604 | 7,840 | — | 717,830 |
| Junior lien | 95,258 | 414 | 1,004 | — | 96,676 |
| Total residential real estate | 801,644 | 4,018 | 8,844 | — | 814,506 |
| Consumer | 26,604 | 1 | 45 | — | 26,650 |
| Total originated and acquired loans | \$ 3,714,941 | \$ 64,236 | \$ 49,784 | \$ 1,429 | \$ 3,830,390 |
| Loans accounted for under ASC 310-30: | | | | | |
| Commercial | \$ 18,182 | \$ 1,055 | \$ 3,021 | \$ — | \$ 22,258 |
| Commercial real estate non-owner occupied | 40,669 | 254 | 919 | — | 41,842 |
| Residential real estate | 8,284 | 932 | 1,501 | — | 10,717 |
| Consumer | — | — | 104 | — | 104 |
| Total loans accounted for under ASC 310-30 | \$ 67,135 | \$ 2,241 | \$ 5,545 | \$ — | \$ 74,921 |
| Total loans | \$ 3,782,076 | \$ 66,477 | \$ 55,329 | \$ 1,429 | \$ 3,905,311 |

December 31, 2017

| | Pass | Special mention | Substandard | Doubtful | Total |
|--|------|--------------------|-------------|----------|-------|
|--|------|--------------------|-------------|----------|-------|

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Originated and acquired loans:

Commercial:

| | | | | | |
|---------------------------------------|--------------|-----------|-----------|----------|--------------|
| Commercial and industrial | \$ 1,349,116 | \$ 10,829 | \$ 14,824 | \$ 1,253 | \$ 1,376,022 |
| Owner occupied commercial real estate | 250,224 | 17,030 | 5,424 | 75 | 272,753 |
| Agriculture | 118,068 | 18,824 | 1,870 | 133 | 138,895 |
| Energy | 55,814 | — | 1,646 | — | 57,460 |
| Total commercial | 1,773,222 | 46,683 | 23,764 | 1,461 | 1,845,130 |

Commercial real estate non-owner occupied:

| | | | | | |
|------------------------------|---------|-------|-------|---|---------|
| Construction | 107,502 | — | 179 | — | 107,681 |
| Acquisition/development | 14,415 | — | — | — | 14,415 |
| Multifamily | 24,817 | — | 2,130 | — | 26,947 |
| Non-owner occupied | 333,225 | 1,396 | 1,477 | — | 336,098 |
| Total commercial real estate | 479,959 | 1,396 | 3,786 | — | 485,141 |

Residential real estate:

| | | | | | |
|-------------------------------|---------|----|-------|---|---------|
| Senior lien | 641,294 | 91 | 5,097 | — | 646,482 |
| Junior lien | 56,172 | — | 824 | — | 56,996 |
| Total residential real estate | 697,466 | 91 | 5,921 | — | 703,478 |

| | | | | | |
|-------------------------------------|--------------|-----------|-----------|----------|--------------|
| Consumer | 24,432 | 1 | 142 | — | 24,575 |
| Total originated and acquired loans | \$ 2,975,079 | \$ 48,171 | \$ 33,613 | \$ 1,461 | \$ 3,058,324 |

Loans accounted for under ASC

310-30:

| | | | | | |
|------------|-----------|----------|----------|------|-----------|
| Commercial | \$ 23,954 | \$ 1,070 | \$ 4,451 | \$ — | \$ 29,475 |
|------------|-----------|----------|----------|------|-----------|

Commercial real estate non-owner occupied

| | | | | | |
|---|--------|-------|--------|---|--------|
| Commercial real estate non-owner occupied | 50,537 | 883 | 26,488 | — | 77,908 |
| Residential real estate | 10,072 | 1,055 | 1,632 | — | 12,759 |

| | | | | | |
|----------|-----|---|-----|---|-----|
| Consumer | 327 | 9 | 145 | — | 481 |
|----------|-----|---|-----|---|-----|

Total loans accounted for under ASC

| | | | | | |
|--------|-----------|----------|-----------|------|------------|
| 310-30 | \$ 84,890 | \$ 3,017 | \$ 32,716 | \$ — | \$ 120,623 |
|--------|-----------|----------|-----------|------|------------|

| | | | | | |
|-------------|--------------|-----------|-----------|----------|--------------|
| Total loans | \$ 3,059,969 | \$ 51,188 | \$ 66,329 | \$ 1,461 | \$ 3,178,947 |
|-------------|--------------|-----------|-----------|----------|--------------|

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Impaired Loans

Loans are considered to be impaired when it is probable that the Company will not be able to collect all amounts due in accordance with the contractual terms of the loan agreement. Impaired loans are comprised of originated and acquired loans on non-accrual status, loans in bankruptcy, and troubled debt restructurings (“TDRs”) described below. If a specific allowance is warranted based on the borrower’s overall financial condition, the specific allowance is calculated based on discounted cash flows using the loan’s initial contractual effective interest rate or the fair value of the collateral less selling costs for collateral dependent loans.

At September 30, 2018 and December 31, 2017, the Company’s recorded investment in impaired loans were \$34.6 million and \$30.9 million, respectively, of which \$7.8 million and \$8.5 million, respectively, were accruing TDRs. Impaired loans at September 30, 2018 were primarily comprised of eight relationships totaling \$15.1 million. Impaired loans had a collective related allowance for loan losses allocated to them of \$1.5 million and \$1.5 million at September 30, 2018 and December 31, 2017, respectively.

Additional information regarding impaired loans at September 30, 2018 and December 31, 2017 is set forth in the table below:

| | September 30, 2018 | | | December 31, 2017 | | |
|--|--------------------------|---------------------|-------------------------------------|--------------------------|---------------------|-------------------------------------|
| | Unpaid principal balance | Recorded investment | Allowance for loan losses allocated | Unpaid principal balance | Recorded investment | Allowance for loan losses allocated |
| With no related allowance recorded: | | | | | | |
| Commercial: | | | | | | |
| Commercial and industrial | \$ 6,214 | \$ 4,684 | \$ — | \$ 6,481 | \$ 5,055 | \$ — |
| Owner occupied commercial real estate | 7,709 | 7,229 | — | 4,186 | 3,934 | — |
| Agriculture | 1,508 | 1,260 | — | 1,502 | 1,245 | — |
| Energy | 7,072 | 2,356 | — | 8,661 | 3,861 | — |
| Total commercial | 22,503 | 15,529 | — | 20,830 | 14,095 | — |
| Commercial real estate non-owner occupied: | | | | | | |
| Construction | 1,308 | 1,081 | — | 215 | 179 | — |
| Acquisition/development | 380 | 130 | — | — | — | — |
| Multifamily | — | — | — | 29 | 29 | — |
| Non-owner occupied | 642 | 554 | — | 901 | 853 | — |
| Total commercial real estate | 2,330 | 1,765 | — | 1,145 | 1,061 | — |
| Residential real estate: | | | | | | |
| Senior lien | 3,339 | 3,041 | — | 333 | 309 | — |

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| | | | | | | |
|---|-----------|-----------|----------|-----------|-----------|----------|
| Junior lien | 381 | 314 | — | — | — | — |
| Total residential real estate | 3,720 | 3,355 | — | 333 | 309 | — |
| Consumer | 49 | 45 | — | — | — | — |
| Total impaired loans with no related allowance recorded | \$ 28,602 | \$ 20,694 | \$ — | \$ 22,308 | \$ 15,465 | \$ — |
| With a related allowance recorded: | | | | | | |
| Commercial: | | | | | | |
| Commercial and industrial | \$ 7,630 | \$ 5,009 | \$ 1,323 | \$ 7,919 | \$ 5,339 | \$ 1,329 |
| Owner occupied commercial real estate | 1,382 | 1,197 | 89 | 873 | 713 | 4 |
| Agriculture | 888 | 851 | 34 | 2,122 | 2,083 | 133 |
| Energy | — | — | — | — | — | — |
| Total commercial | 9,900 | 7,057 | 1,446 | 10,914 | 8,135 | 1,466 |
| Commercial real estate non-owner occupied: | | | | | | |
| Construction | — | — | — | — | — | — |
| Acquisition/development | — | — | — | — | — | — |
| Multifamily | — | — | — | — | — | — |
| Non-owner occupied | 327 | 268 | 2 | 207 | 200 | 1 |
| Total commercial real estate | 327 | 268 | 2 | 207 | 200 | 1 |
| Residential real estate: | | | | | | |
| Senior lien | 6,173 | 5,309 | 28 | 6,481 | 5,753 | 24 |
| Junior lien | 1,366 | 1,250 | 8 | 1,295 | 1,179 | 8 |
| Total residential real estate | 7,539 | 6,559 | 36 | 7,776 | 6,932 | 32 |
| Consumer | — | — | — | 146 | 141 | 1 |
| Total impaired loans with a related allowance recorded | \$ 17,766 | \$ 13,884 | \$ 1,484 | \$ 19,043 | \$ 15,408 | \$ 1,500 |
| Total impaired loans | \$ 46,368 | \$ 34,578 | \$ 1,484 | \$ 41,351 | \$ 30,873 | \$ 1,500 |

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The table below shows additional information regarding the average recorded investment and interest income recognized on impaired loans for the periods presented:

| | For the three months ended | | | |
|---|-----------------------------|----------------------------|-----------------------------|----------------------------|
| | September 30, 2018 | | September 30, 2017 | |
| | Average recorded investment | Interest income recognized | Average recorded investment | Interest income recognized |
| With no related allowance recorded: | | | | |
| Commercial: | | | | |
| Commercial and industrial | \$ 4,518 | \$ 68 | \$ 4,272 | \$ 40 |
| Owner occupied commercial real estate | 7,278 | 17 | 2,069 | 19 |
| Agriculture | 1,259 | — | 1,349 | — |
| Energy | 2,044 | 15 | 7,960 | 116 |
| Total commercial | 15,099 | 100 | 15,650 | 175 |
| Commercial real estate non-owner occupied: | | | | |
| Construction | 1,081 | — | — | — |
| Acquisition/development | 590 | — | — | — |
| Multifamily | — | — | — | — |
| Non-owner occupied | 559 | — | 871 | 5 |
| Total commercial real estate | 2,230 | — | 871 | 5 |
| Residential real estate: | | | | |
| Senior lien | 3,062 | — | 574 | — |
| Junior lien | 316 | 1 | — | — |
| Total residential real estate | 3,378 | 1 | 574 | — |
| Consumer | 12 | — | — | — |
| Total impaired loans with no related allowance recorded | \$ 20,719 | \$ 101 | \$ 17,095 | \$ 180 |
| With a related allowance recorded: | | | | |
| Commercial: | | | | |
| Commercial and industrial | \$ 5,015 | \$ — | \$ 3,692 | \$ — |
| Owner occupied commercial real estate | 1,205 | 5 | 2,456 | 5 |
| Agriculture | 853 | 1 | 896 | 1 |
| Energy | — | — | — | — |
| Total commercial | 7,073 | 6 | 7,044 | 6 |
| Commercial real estate non-owner occupied: | | | | |
| Construction | — | — | 190 | — |
| Acquisition/development | — | — | — | — |
| Multifamily | — | — | 30 | — |
| Non-owner occupied | 277 | 4 | 209 | 2 |
| Total commercial real estate | 277 | 4 | 429 | 2 |
| Residential real estate: | | | | |
| Senior lien | 5,351 | 17 | 6,334 | 20 |
| Junior lien | 1,250 | 16 | 1,409 | 12 |
| Total residential real estate | 6,601 | 33 | 7,743 | 32 |
| Consumer | 35 | — | 206 | — |
| Total impaired loans with a related allowance recorded | \$ 13,986 | \$ 44 | \$ 15,422 | \$ 40 |

| | | | | |
|----------------------|-----------|--------|-----------|--------|
| Total impaired loans | \$ 34,705 | \$ 145 | \$ 32,517 | \$ 220 |
|----------------------|-----------|--------|-----------|--------|

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| | For the nine months ended | | | |
|---|-----------------------------|----------------------------|-----------------------------|----------------------------|
| | September 30, 2018 | | September 30, 2017 | |
| | Average recorded investment | Interest income recognized | Average recorded investment | Interest income recognized |
| With no related allowance recorded: | | | | |
| Commercial: | | | | |
| Commercial and industrial | \$ 5,206 | \$ 241 | \$ 5,802 | \$ 113 |
| Owner occupied commercial real estate | 7,415 | 52 | 2,116 | 60 |
| Agriculture | 1,259 | 6 | 1,470 | — |
| Energy | 2,080 | 52 | 9,035 | 116 |
| Total Commercial | 15,960 | 351 | 18,423 | 289 |
| Commercial real estate non-owner occupied: | | | | |
| Construction | 1,081 | — | — | — |
| Acquisition/development | 768 | — | — | — |
| Multifamily | — | — | — | — |
| Non-owner occupied | 580 | — | 886 | 17 |
| Total commercial real estate | 2,429 | — | 886 | 17 |
| Residential real estate: | | | | |
| Senior lien | 3,118 | — | 585 | — |
| Junior lien | 323 | 1 | — | — |
| Total residential real estate | 3,441 | 1 | 585 | — |
| Consumer | 13 | — | — | — |
| Total impaired loans with no related allowance recorded | \$ 21,843 | \$ 352 | \$ 19,894 | \$ 306 |
| With a related allowance recorded: | | | | |
| Commercial: | | | | |
| Commercial and industrial | \$ 5,175 | \$ — | \$ 4,363 | \$ — |
| Owner occupied commercial real estate | 1,234 | 14 | 2,479 | 15 |
| Agriculture | 866 | 4 | 907 | 4 |
| Energy | — | — | — | — |
| Total Commercial | 7,275 | 18 | 7,749 | 19 |
| Commercial real estate non-owner occupied: | | | | |
| Construction | — | — | 190 | — |
| Acquisition/development | — | — | — | — |
| Multifamily | — | — | 31 | 1 |
| Non-owner occupied | 297 | 14 | 216 | 7 |
| Total commercial real estate | 297 | 14 | 437 | 8 |
| Residential real estate: | | | | |
| Senior lien | 5,503 | 43 | 6,494 | 60 |
| Junior lien | 1,273 | 35 | 1,444 | 36 |
| Total residential real estate | 6,776 | 78 | 7,938 | 96 |
| Consumer | 38 | — | 218 | — |
| Total impaired loans with a related allowance recorded | \$ 14,386 | \$ 109 | \$ 16,342 | \$ 123 |
| Total impaired loans | \$ 36,229 | \$ 461 | \$ 36,236 | \$ 429 |

Interest income recognized on impaired loans noted in the tables above primarily represents interest earned on accruing TDRs. Interest income recognized on impaired loans during the three months ended September 30, 2018 and 2017 was \$0.1 million and \$0.2 million, respectively. Interest income recognized on impaired loans during the nine months ended September 30, 2018 and 2017 was \$0.5 million and \$0.4 million, respectively.

Troubled debt restructurings

The Company's policy is to review each prospective credit to determine the appropriateness and the adequacy of security or collateral prior to making a loan. In the event of borrower default the Company seeks recovery in compliance with lending laws, the respective loan agreements and credit monitoring and remediation procedures that may include restructuring a loan to provide a concession by the Company to the borrower from their original terms due to borrower financial difficulties in order to facilitate repayment. Additionally, if a borrower's repayment obligation has been discharged by a court, and that debt has not been reaffirmed by the borrower, regardless of past due status, the loan is considered to be a TDR.

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During the nine months ended September 30, 2018, the Company restructured nine loans with a recorded investment of \$0.8 million at September 30, 2018 to facilitate repayment. All of the loan modifications were a reduction of the principal payment, a reduction in interest rate, or an extension of term. Loan modifications to loans accounted for under ASC 310-30 are not considered TDRs. The tables below provide additional information related to accruing TDRs at September 30, 2018 and December 31, 2017:

| | September 30, 2018 | | | Unfunded |
|---|--------------------|--------------|-----------|--------------|
| | Recorded | Average | Unpaid | commitments |
| | investment | year-to-date | principal | to fund TDRs |
| | recorded | recorded | balance | |
| Commercial | \$ 6,387 | \$ 6,477 | \$ 7,172 | \$ 3,343 |
| Commercial real estate non-owner occupied | 242 | 268 | 293 | — |
| Residential real estate | 1,141 | 1,177 | 1,148 | 12 |
| Consumer | — | — | — | — |
| Total | \$ 7,770 | \$ 7,922 | \$ 8,613 | \$ 3,355 |

| | December 31, 2017 | | | Unfunded |
|---|-------------------|--------------|-----------|--------------|
| | Recorded | Average | Unpaid | commitments |
| | investment | year-to-date | principal | to fund TDRs |
| | recorded | recorded | balance | |
| Commercial | \$ 6,595 | \$ 7,308 | \$ 7,171 | \$ 2,041 |
| Commercial real estate non-owner occupied | 455 | 489 | 500 | — |
| Residential real estate | 1,409 | 1,461 | 1,420 | 2 |
| Consumer | 1 | 3 | 1 | — |
| Total | \$ 8,460 | \$ 9,261 | \$ 9,092 | \$ 2,043 |

The following table summarizes the Company's carrying value of non-accrual TDRs as of September 30, 2018 and December 31, 2017:

| | September 30, 2018 | December 31, 2017 |
|---|--------------------|-------------------|
| Commercial | \$ 2,088 | \$ 5,808 |
| Commercial real estate non-owner occupied | — | — |
| Residential real estate | 1,684 | 1,336 |
| Consumer | — | 111 |
| Total non-accruing TDRs | \$ 3,772 | \$ 7,255 |

At September 30, 2018 and December 31, 2017, the Company had \$7.8 million and \$8.5 million, respectively, of accruing TDRs that had been restructured from the original terms in order to facilitate repayment.

Accrual of interest is resumed on loans that were previously on non-accrual only after the loan has performed sufficiently. The Company had two TDRs that were modified within the past twelve months and had defaulted on its restructured terms during the three months ended September 30, 2018 totaling \$0.2 million, and three TDRs that were modified within the past twelve months and had defaulted on their restructured terms during the nine months ended September 30, 2018 totaling \$0.4 million. For purposes of this disclosure, the Company considers "default" to mean 90 days or more past due on principal or interest. Non-accruing TDRs decreased \$3.5 million from December 31, 2017 due to one commercial loan relationship placed on accrual during the period and paydowns. The allowance for loan losses related to troubled debt restructurings on non-accrual status is determined by individual evaluation, including collateral adequacy, using the same process as loans on non-accrual status which are not classified as TDRs.

During the three and nine months ended September 30, 2017, the Company had one and four TDRs that had been modified within the past 12 months that defaulted on their restructured terms, respectively.

Loans accounted for under ASC 310-30

Loan pools accounted for under ASC Topic 310-30 are periodically re-measured to determine expected future cash flows. In determining the expected cash flows, the timing of cash flows and prepayment assumptions for smaller homogeneous loans are based on statistical models that take into account factors such as the loan interest rate, credit profile of the borrowers, the years in which the loans were originated, and whether the loans are fixed or variable rate loans. Prepayments may be assumed on loans if circumstances

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specific to that loan warrant a prepayment assumption. The re-measurement of loans accounted for under ASC 310-30 resulted in the following changes in the carrying amount of accretable yield during the nine months ended September 30, 2018 and 2017:

| | September 30, 2018 | September 30, 2017 |
|---|--------------------|--------------------|
| Accretable yield beginning balance | \$ 46,568 | \$ 60,476 |
| Reclassification from non-accretable difference | 10,070 | 9,697 |
| Reclassification to non-accretable difference | (1,929) | (907) |
| Accretion | (15,009) | (17,718) |
| Accretable yield ending balance | \$ 39,700 | \$ 51,548 |

Below is the composition of the net book value for loans accounted for under ASC 310-30 at September 30, 2018 and December 31, 2017:

| | September 30, 2018 | December 31, 2017 |
|--------------------------------------|--------------------|-------------------|
| Contractual cash flows | \$ 429,181 | \$ 489,892 |
| Non-accretable difference | (314,560) | (322,701) |
| Accretable yield | (39,700) | (46,568) |
| Loans accounted for under ASC 310-30 | \$ 74,921 | \$ 120,623 |

Note 6 Allowance for Loan Losses

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The tables below detail the Company's allowance for loan losses and recorded investment in loans as of and for the three and nine months ended September 30, 2018 and 2017:

| | Three months ended September 30, 2018 | | | | Total |
|---|---------------------------------------|--|----------------------------|----------|-----------|
| | Commercial | Non-owner occupied commercial real estate | Residential real estate | Consumer | |
| Beginning balance | \$ 23,582 | \$ 4,561 | \$ 3,781 | \$ 306 | \$ 32,230 |
| Originated and acquired beginning balance | 23,400 | 4,542 | 3,781 | 306 | 32,029 |
| Charge-offs | — | — | (13) | (381) | (394) |
| Recoveries | 1,097 | — | 2 | 71 | 1,170 |
| Provision | 606 | (78) | (49) | 322 | 801 |
| Originated and acquired ending balance | 25,103 | 4,464 | 3,721 | 318 | 33,606 |
| ASC 310-30 beginning balance | 182 | 19 | — | — | 201 |
| Charge-offs | — | — | — | — | — |
| Recoveries | — | — | — | — | — |
| Provision (recoupment) | 9 | (3) | — | — | 6 |
| ASC 310-30 ending balance | 191 | 16 | — | — | 207 |
| Ending balance | \$ 25,294 | \$ 4,480 | \$ 3,721 | \$ 318 | \$ 33,813 |

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| | Three months ended September 30, 2017 | | | | |
|---|---------------------------------------|--|----------------------------|----------|-----------|
| | Commercial | Non-owner occupied commercial real estate | Residential real estate | Consumer | Total |
| Beginning balance | \$ 24,656 | \$ 5,934 | \$ 4,067 | \$ 302 | \$ 34,959 |
| Originated and acquired beginning balance | 24,656 | 5,800 | 4,067 | 294 | 34,817 |
| Charge-offs | (8,618) | — | (16) | (209) | (8,843) |
| Recoveries | 11 | — | 14 | 26 | 51 |
| Provision | 4,063 | (280) | 77 | 162 | 4,022 |
| Originated and acquired ending balance | 20,112 | 5,520 | 4,142 | 273 | 30,047 |
| ASC 310-30 beginning balance | — | 134 | — | 8 | 142 |
| Charge-offs | — | — | — | — | — |
| Recoveries | — | — | — | — | — |
| (Recoupment) | — | (134) | — | (8) | (142) |
| ASC 310-30 ending balance | — | — | — | — | — |
| Ending balance | \$ 20,112 | \$ 5,520 | \$ 4,142 | \$ 273 | \$ 30,047 |

| | Nine months ended September 30, 2018 | | | | |
|---|--------------------------------------|--|----------------------------|----------|-----------|
| | Commercial | Non-owner occupied commercial real estate | Residential real estate | Consumer | Total |
| Beginning balance | \$ 21,385 | \$ 5,609 | \$ 3,965 | \$ 305 | \$ 31,264 |
| Originated and acquired beginning balance | 21,340 | 5,583 | 3,965 | 305 | 31,193 |
| Charge-offs | (437) | (11) | (103) | (894) | (1,445) |
| Recoveries | 1,152 | — | 8 | 174 | 1,334 |
| Provision | 3,048 | (1,108) | (149) | 733 | 2,524 |
| Originated and acquired ending balance | 25,103 | 4,464 | 3,721 | 318 | 33,606 |
| ASC 310-30 beginning balance | 45 | 26 | — | — | 71 |
| Charge-offs | (61) | — | — | — | (61) |
| Recoveries | — | — | — | — | — |
| Provision (recoupment) | 207 | (10) | — | — | 197 |
| ASC 310-30 ending balance | 191 | 16 | — | — | 207 |
| Ending balance | \$ 25,294 | \$ 4,480 | \$ 3,721 | \$ 318 | \$ 33,813 |
| Ending allowance balance attributable to: | | | | | |
| Originated and acquired loans individually evaluated for impairment | \$ 1,446 | \$ 2 | \$ 36 | \$ — | \$ 1,484 |
| | 23,657 | 4,462 | 3,685 | 318 | 32,122 |

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| | | | | | |
|--|--------------|------------|------------|-----------|--------------|
| Originated and acquired loans collectively evaluated for impairment ASC 310-30 loans | 191 | 16 | — | — | 207 |
| Total ending allowance balance | \$ 25,294 | \$ 4,480 | \$ 3,721 | \$ 318 | \$ 33,813 |
| Loans: | | | | | |
| Originated and acquired loans individually evaluated for impairment | \$ 22,585 | \$ 2,034 | \$ 4,319 | \$ 5,640 | \$ 34,578 |
| Originated and acquired loans collectively evaluated for impairment ASC 310-30 loans | 2,397,248 | 567,367 | 810,187 | 21,010 | 3,795,812 |
| ASC 310-30 loans | 22,258 | 41,842 | 10,721 | 100 | 74,921 |
| Total loans | \$ 2,442,091 | \$ 611,243 | \$ 825,227 | \$ 26,750 | \$ 3,905,311 |

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| | Nine months ended September 30, 2017 | | | | |
|---|--------------------------------------|--|----------------------------|-----------|--------------|
| | Commercial | Non-owner occupied commercial real estate | Residential real estate | Consumer | Total |
| Beginning balance | \$ 18,821 | \$ 5,642 | \$ 4,387 | \$ 324 | \$ 29,174 |
| Originated and acquired beginning balance | 18,821 | 5,422 | 4,387 | 319 | 28,949 |
| Charge-offs | (8,638) | — | (26) | (510) | (9,174) |
| Recoveries | 52 | 20 | 127 | 148 | 347 |
| Provision (recoupment) | 9,877 | 78 | (346) | 316 | 9,925 |
| Originated and acquired ending balance | 20,112 | 5,520 | 4,142 | 273 | 30,047 |
| ASC 310-30 beginning balance | — | 220 | — | 5 | 225 |
| Charge-offs | — | — | — | — | — |
| Recoveries | — | — | — | — | — |
| Recoupment | — | (220) | — | (5) | (225) |
| ASC 310-30 ending balance | — | — | — | — | — |
| Ending balance | \$ 20,112 | \$ 5,520 | \$ 4,142 | \$ 273 | \$ 30,047 |
| Ending allowance balance attributable to: | | | | | |
| Originated and acquired loans individually evaluated for impairment | \$ 914 | \$ 2 | \$ 195 | \$ 1 | \$ 1,112 |
| Originated and acquired loans collectively evaluated for impairment | 19,198 | 5,518 | 3,947 | 272 | 28,935 |
| ASC 310-30 loans | — | — | — | — | — |
| Total ending allowance balance | \$ 20,112 | \$ 5,520 | \$ 4,142 | \$ 273 | \$ 30,047 |
| Loans: | | | | | |
| Originated and acquired loans individually evaluated for impairment | \$ 18,714 | \$ 1,291 | \$ 8,252 | \$ 202 | \$ 28,459 |
| Originated and acquired loans collectively evaluated for impairment | 1,757,294 | 480,565 | 702,702 | 25,927 | 2,966,488 |
| ASC 310-30 loans | 31,875 | 79,798 | 13,420 | 503 | 125,596 |
| Total loans | \$ 1,807,883 | \$ 561,654 | \$ 724,374 | \$ 26,632 | \$ 3,120,543 |

In evaluating the loan portfolio for an appropriate ALL level, non-impaired originated and acquired loans were grouped into segments based on broad characteristics such as primary use and underlying collateral. Within the segments, the portfolio was further disaggregated into classes of loans with similar attributes and risk characteristics for purposes of applying loss ratios and determining applicable subjective adjustments to the ALL. The application of subjective adjustments was based upon qualitative risk factors, including economic trends and conditions, industry conditions, asset quality, loss trends, lending management, portfolio growth and loan review/internal audit results.

Net (recoveries) charge-offs on originated and acquired loans during the three and nine months ended September 30, 2018 were \$(0.8) million and \$0.1 million, respectively. Management's evaluation of credit quality resulted in a provision for originated and acquired loan losses of \$0.8 million and \$2.5 million during the three and nine months ended September 30, 2018, respectively. One large recovery of \$1.1 million resulted in lower provision.

During the nine months ended September 30, 2018, the Company re-estimated the expected cash flows of the loan pools accounted for under ASC 310-30. The re-measurement resulted in a provision of \$6 thousand and \$197 thousand for the three and nine months ended September 30, 2018, respectively, driven by provision in the commercial segment.

Net charge-offs on originated and acquired loans during the three and nine months ended September 30, 2017 were \$8.8 million and \$8.8 million, respectively. Management's evaluation of credit quality resulted in a provision for loan losses on the originated and acquired loans of \$4.0 million and \$9.9 million during the three and nine months ended September 30, 2017, respectively.

During the nine months ended September 30, 2017, the Company re-estimated the expected cash flows of the loan pools accounted for under ASC 310-30. The re-measurement resulted in a net recoupment of \$142 thousand and \$225 thousand for the three and nine months ended September 30, 2017, respectively.

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Note 7 Other Real Estate Owned

A summary of the activity in the OREO balances during the nine months ended September 30, 2018 and 2017 is as follows:

| | For the nine months ended September 30, | |
|--|--|-----------|
| | 2018 | 2017 |
| Beginning balance | \$ 10,491 | \$ 15,662 |
| Acquired through acquisition | 1,253 | — |
| Transfers from loan portfolio, at fair value | 24,919 | 760 |
| Impairments | (220) | (766) |
| Sales | (1,308) | (3,326) |
| Ending balance | \$ 35,135 | \$ 12,330 |

The Company transferred one large acquired 310-30 problem loan to OREO totaling \$24.1 million during the second quarter of 2018 as part of its asset resolution process. OREO net gains of \$0.4 million and net gains of \$2.3 million were included in the consolidated statement of operations for the nine months ended September 30, 2018 and 2017, respectively.

Note 8 Goodwill and Intangible Assets

In connection with all of our acquisitions, the Company recorded goodwill of \$115.0 million, core deposit intangible assets of \$48.8 million and mortgage servicing rights of \$4.3 million. In connection with the acquisition of Peoples completed in the first quarter of 2018, the Company recorded goodwill of \$55.4 million, core deposit intangibles assets of \$10.5 million and mortgage servicing rights of \$4.3 million. The goodwill is measured as the excess of the fair value of consideration paid over the fair value of net assets acquired. No goodwill impairment was recorded during the three or nine months ended September 30, 2018 or the year ended December 31, 2017.

Mortgage servicing rights represent rights to service loans originated by the Company and sold to government sponsored enterprises including FHLMC, FNMA, GNMA and FHLB. Mortgage loans serviced for others were \$404.5 million at September 30, 2018 and \$0.0 million at December 31, 2017.

The gross carrying amount of the core deposit intangible and the associated accumulated amortization at September 30, 2018 and December 31, 2017, are presented as follows:

| | September 30, 2018 | | Net | December 31, 2017 | | Net |
|-------------------------|-----------------------|--------------------------|-----------------|-----------------------|--------------------------|-----------------|
| | Gross carrying amount | Accumulated amortization | carrying amount | Gross carrying amount | Accumulated amortization | carrying amount |
| Core deposit intangible | \$ 48,834 | \$ 38,567 | \$ 10,267 | \$ 38,357 | \$ 36,750 | \$ 1,607 |

Below are the changes in the mortgage servicing rights for the period presented:

| | For the nine months ended September 30, 2018 |
|---|--|
| Beginning balance | \$ — |
| Acquired through acquisition | 4,301 |
| Originations | 25 |
| Impairment | (68) |
| Amortization | (588) |
| Ending balance | \$ 3,670 |
| Fair value of mortgage servicing rights | \$ 4,351 |

The fair value of mortgage servicing rights was determined based upon a discounted cash flow analysis. The cash flow analysis included assumptions for discount rates and prepayment speeds. Discount rates ranged from 9.5% to 10.5% and the constant prepayment speed ranged from 9.9% to 13.3% for the September 30, 2018 valuation.

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Mortgage servicing rights are evaluated for impairment and recognized to the extent fair value is less than the carrying amount. The Company evaluates impairment by type (FHLMC, FNMA, GNMA and FHLB) and interest rate. There was \$0.1 million in impairment at September 30, 2018 included in mortgage banking income on the consolidated statements of operations.

The Company is amortizing the core deposit intangibles from acquisitions on a straight line basis over 7-10 years from the date of the respective acquisitions, which represents the expected useful life of the assets. The Company recognized core deposit intangible amortization expense of \$0.5 million and \$1.8 million during the three and nine months ended September 30, 2018, respectively, and \$1.4 million and \$4.1 million during the three and nine months ended September 30, 2017, respectively. The Company is amortizing the mortgage servicing rights in proportion to and over the period of the estimated net servicing income of the underlying loans. The Company recognized mortgage servicing rights amortization expense of \$0.2 million and \$0.6 million during the three and nine months ended September 30, 2018.

The following table shows the estimated future amortization expense for the nine month periods ending below:

| Periods ending September 30, | Amount |
|------------------------------|----------|
| 2019 | \$ 1,473 |
| 2020 | 1,379 |
| 2021 | 1,301 |
| 2022 | 1,193 |
| 2023 | 1,078 |

Note 9 Borrowings

The Company enters into repurchase agreements to facilitate the needs of its clients. As of September 30, 2018 and December 31, 2017, the Company sold securities under agreements to repurchase totaling \$55.7 million and \$130.5 million, respectively, and none were for periods longer than one day. The Company pledged mortgage-backed securities with a fair value of approximately \$61.6 million and \$136.1 million as of September 30, 2018 and December 31, 2017, respectively, for these agreements. The Company monitors collateral levels on a continuous basis and may be required to provide additional collateral based on the fair value of the underlying securities. As of September 30, 2018 and December 31, 2017, the Company had \$4.2 million and \$5.7 million of excess collateral pledged for repurchase agreements, respectively.

As a member of the FHLB, the Bank has access to a line of credit and term financing from the FHLB with total available credit of \$1.0 billion at September 30, 2018. At September 30, 2018 and December 31, 2017 the Bank had \$67.2 million and \$0.0 million in line of credit advances from the FHLB, respectively, that mature within a day. At September 30, 2018 and December 31, 2017, the Bank had \$77.3 million and \$129.1 million in term advances from the FHLB, respectively. The term advances have fixed interest rates of 1.55% - 2.33%, with maturity dates of 2018 - 2020. The Bank had investment securities and loans pledged as collateral for FHLB advances. Investment securities pledged were \$27.4 million at September 30, 2018 and \$28.1 million at December 31, 2017. Loans pledged were \$1.6 million at September 30, 2018 and \$1.2 million at December 31, 2017. Interest expense related to FHLB advances totaled \$0.6 million and \$1.7 million for the three and nine months ended September 30, 2018, respectively, and \$0.6 million and \$1.3 million for the three and nine months ended September 30, 2017, respectively.

Note 10 Regulatory Capital

As a bank holding company, the Company is subject to regulatory capital adequacy requirements implemented by the Federal Reserve. The federal banking agencies have risk-based capital adequacy regulations intended to provide a measure of capital adequacy that reflects the degree of risk associated with a banking organization's operations. Under these regulations, assets are assigned to one of several risk categories, and nominal dollar amounts of assets and credit equivalent amounts of off-balance-sheet items are multiplied by a risk adjustment percentage for the category.

The Basel III rules, effective January 1, 2015, changed the components of regulatory capital, changed the way in which risk ratings are assigned to various categories of bank assets and defined a new Tier 1 common risk-based ratio. In addition, a capital conservative buffer requirement, designed to strengthen an institution's financial resilience during economic cycles through the restriction of capital distributions and other payments, became effective in 2017, with full phase-in beginning January 1, 2019. When fully phased-in, the capital conservation buffer adds a 2.5% capital requirement above existing regulatory minimum ratios.

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Under the Basel III requirements, at September 30, 2018 and December 31, 2017, the Company and the Bank met all capital requirements and the Bank had regulatory capital ratios in excess of the levels established for well-capitalized institutions, as detailed in the tables below.

| | September 30, 2018 | | | | | |
|--|--------------------|------------|---|------------|---|------------|
| | Actual | | Required to be well capitalized under prompt corrective action provisions | | Required to be considered adequately capitalized(1) | |
| | Ratio | Amount | Ratio | Amount | Ratio | Amount |
| Tier 1 leverage ratio: | | | | | | |
| Consolidated | 10.3% | \$ 564,445 | N/A | N/A | 4.0% | \$ 219,024 |
| NBH Bank | 9.1% | 496,365 | 5.0% | \$ 273,271 | 4.0% | 218,617 |
| Common equity tier 1 risk-based capital: | | | | | | |
| Consolidated | 12.9% | \$ 564,445 | N/A | N/A | 7.0% | \$ 383,292 |
| NBH Bank | 11.4% | 496,365 | 6.5% | \$ 355,252 | 7.0% | 382,580 |
| Tier 1 risk-based capital ratio: | | | | | | |
| Consolidated | 12.9% | \$ 564,445 | N/A | N/A | 8.5% | \$ 373,495 |
| NBH Bank | 11.4% | 496,365 | 8.0% | \$ 349,880 | 8.5% | 371,748 |
| Total risk-based capital ratio: | | | | | | |
| Consolidated | 13.8% | \$ 602,787 | N/A | N/A | 10.5% | \$ 461,376 |
| NBH Bank | 12.2% | 534,707 | 10.0% | \$ 437,350 | 10.5% | 459,218 |

| | December 31, 2017 | | | | | |
|--|-------------------|------------|---|------------|---|------------|
| | Actual | | Required to be well capitalized under prompt corrective action provisions | | Required to be considered adequately capitalized(1) | |
| | Ratio | Amount | Ratio | Amount | Ratio | Amount |
| Tier 1 leverage ratio: | | | | | | |
| Consolidated | 9.8% | \$ 470,877 | N/A | N/A | 4.0% | \$ 191,559 |
| NBH Bank | 8.1% | 382,918 | 5.0% | \$ 237,772 | 4.0% | 190,217 |
| Common equity tier 1 risk-based capital: | | | | | | |
| Consolidated | 12.9% | \$ 470,877 | N/A | N/A | 7.0% | \$ 335,228 |
| NBH Bank | 10.6% | 382,918 | 6.5% | \$ 309,103 | 7.0% | 332,881 |
| Tier 1 risk-based capital ratio: | | | | | | |
| Consolidated | 12.9% | \$ 470,877 | N/A | N/A | 8.5% | \$ 309,400 |
| NBH Bank | 10.6% | 382,918 | 8.0% | \$ 289,022 | 8.5% | 307,086 |
| Total risk-based capital ratio: | | | | | | |
| Consolidated | 13.8% | \$ 502,917 | N/A | N/A | 10.5% | \$ 382,200 |
| NBH Bank | 11.5% | 414,958 | 10.0% | \$ 361,277 | 10.5% | 379,341 |

(1) As of the fully phased-in date of January 1, 2019, including the capital conservation buffer.

Note 11 Revenue from Contracts with Clients

On January 1, 2018, the Company adopted ASU No. 2014-09 “Revenue from Contracts with Customers” (Topic 606) and all subsequent ASUs that modified Topic 606. As stated in Note 2, Recent Accounting Pronouncements, the implementation of the new standard did not have a material impact on the measurement or recognition of revenue; as such, a cumulative effect adjustment to opening retained earnings was not deemed necessary. Results for reporting periods beginning after January 1, 2018 are presented under Topic 606, while prior period amounts were not adjusted and continue to be reported in accordance with our historic accounting under Topic 605.

Topic 606 does not apply to revenue associated with financial instruments, including revenue from loans and securities. In addition, certain noninterest income streams such as fees associated with mortgage servicing rights, financial guarantees, and derivatives are also not in scope of the new guidance. Topic 606 is applicable to noninterest revenue streams such as deposit related fees, interchange fees, and merchant income. However, the recognition of these revenue streams did not change significantly upon adoption of Topic 606. Substantially all of the Company’s revenue is generated from contracts with customers. Noninterest revenue streams in-scope of Topic 606 are discussed below.

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Service Charges and other fees

Service charge fees are primarily comprised of monthly service fees, check orders, and other deposit account related fees. Other fees include revenue from processing wire transfers, bill pay service, cashier's checks, and other services. The Company's performance obligation for account analysis fees and monthly service fees is generally satisfied, and the related revenue recognized, over the period in which the service is provided. Check orders and other deposit account related fees are largely transactional based, and therefore, the Company's performance obligation is satisfied, and related revenue recognized, at a point in time. Payment for service charges on deposit accounts is primarily received immediately or in the following month through a direct charge to clients' accounts.

Bank card fees

Bank card fees are primarily comprised of debit card income, ATM fees, merchant services income, and other fees. Debit card income is primarily comprised of interchange fees earned whenever the Company's debit cards are processed through card payment networks such as Visa. ATM fees are primarily generated when a Company cardholder uses a non-Company ATM or a non-Company cardholder uses a Company ATM. Merchant services income mainly represents fees charged to merchants to process their debit card transactions. The Company's performance obligation for bank card fees are largely satisfied, and related revenue recognized, when the services are rendered or upon completion. Payment is typically received immediately or in the following month.

Loss (gain) on OREO Sales, net

Loss (gain) on OREO Sales, net is recognized when the Company meets its performance obligation to transfer title to the buyer. The gain or loss is measured as the excess of the proceeds received compared to the OREO carrying value. Sales proceeds are received in cash at the time of transfer.

The following table presents non-interest income, segregated by revenue streams in-scope and out-of-scope of Topic 606, and non-interest expense in-scope of Topic 606 for the three and nine months ended September 30, 2018 and 2017.

| For the three months ended September 30, 2018 | | For the nine months ended September 30, 2017 | |
|--|--|---|--|
| | | | |

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Non-interest income

In-scope of Topic 606:

| | | | | |
|---|-----------|----------|-----------|-----------|
| Service Charges and other fees | \$ 5,145 | \$ 3,961 | \$ 15,328 | \$ 14,551 |
| Bank card fees | 3,686 | 3,076 | 10,720 | 9,014 |
| Gain on banking center divestiture | — | — | — | 2,942 |
| Non-interest income (in-scope of Topic 606) | 8,831 | 7,037 | 26,048 | 26,507 |
| Non-interest income (out-of-scope of Topic 606) | 9,230 | 2,514 | 29,410 | 3,696 |
| Total non-interest income | \$ 18,061 | \$ 9,551 | \$ 55,458 | \$ 30,203 |

Non-interest expense

In-scope of Topic 606:

| | | | | |
|-------------------------------------|----------|----------|-----------|-----------|
| Loss (gain) on OREO sales, net | (450) | (497) | 64 | (2,254) |
| Total revenue in-scope of Topic 606 | \$ 8,381 | \$ 6,540 | \$ 26,112 | \$ 24,253 |

Contract Balances

A contract asset balance occurs when an entity performs a service for a client before the client pays consideration (resulting in a contract receivable) or before payment is due (resulting in a contract asset). A contract liability balance is an entity's obligation to transfer a service to a client for which the entity has already received payment (or payment is due) from the client. The Company's noninterest revenue streams are largely based on transactional activity or standard month-end revenue accruals. Consideration is often received immediately or shortly after the Company satisfies its performance obligation and revenue is recognized. The Company does not typically enter into long-term revenue contracts with clients, and therefore, does not experience significant contract balances. As of September 30, 2018 and December 31, 2017, the Company did not have any contract balances.

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Contract Acquisition Costs

In connection with the adoption of Topic 606, an entity is required to capitalize, and subsequently amortize into expense, certain incremental costs of obtaining a contract with a client if these costs are expected to be recovered. The incremental costs of obtaining a contract are those costs that an entity incurs to obtain a contract with a client that it would not have incurred if the contract had not been obtained (for example, sales commission). The Company utilizes the practical expedient which allows entities to immediately expense contract acquisition costs when the asset that would have resulted from capitalizing these costs would have been amortized in one year or less. Upon adoption of Topic 606, the Company did not capitalize any contract acquisition cost.

Note 12 Stock-based Compensation and Benefits

The Company provides stock-based compensation in accordance with shareholder-approved plans. During the second quarter of 2014, shareholders approved the 2014 Omnibus Incentive Plan (the "2014 Plan"). The 2014 Plan replaces the NBH Holdings Corp. 2009 Equity Incentive Plan (the "Prior Plan"), pursuant to which the Company granted equity awards prior to the approval of the 2014 Plan. Pursuant to the 2014 Plan, the Compensation Committee of the Board of Directors has the authority to grant, from time to time, awards of stock options, stock appreciation rights, restricted stock, restricted stock units, performance units, other stock-based awards, or any combination thereof to eligible persons.

Stock options

The Company issued stock options during the nine months ended September 30, 2018 and 2017, which are primarily time-vesting with 1/3 vesting on each of the first, second and third anniversary of the date of grant or date of hire.

The expense associated with the awarded stock options was measured at fair value using a Black-Scholes option-pricing model. The outstanding option awards vest or have vested on a graded basis over 1-4 years of continuous service and have 7-10 year contractual terms.

The following table summarizes stock option activity for the nine months ended September 30, 2018:

Weighted

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| | Options | Weighted average exercise price | average remaining contractual term in years | Aggregate intrinsic value |
|---|-----------|--|---|---------------------------------|
| Outstanding at December 31, 2017 | 1,598,318 | \$ 20.62 | 4.07 | \$ 19,017 |
| Granted | 154,854 | 32.94 | | |
| Exercised | (472,700) | 19.88 | | |
| Forfeited | (18,395) | 28.76 | | |
| Outstanding at September 30, 2018 | 1,262,077 | \$ 22.29 | 4.16 | \$ 19,389 |
| Options exercisable at September 30, 2018 | 1,007,163 | 20.17 | 2.98 | 17,610 |
| Options vested and expected to vest | 1,234,860 | 22.07 | 4.05 | 19,243 |

Stock option expense is a component of salaries and benefits in the consolidated statements of operations and totaled \$0.2 million and \$0.1 million for the three months ended September 30, 2018 and 2017, respectively, and \$0.6 million and \$0.5 million for the nine months ended September 30, 2018 and 2017, respectively. At September 30, 2018, there was \$0.9 million of total unrecognized compensation cost related to non-vested stock options granted under the plans. The cost is expected to be recognized over a weighted average period of 2.3 years.

Restricted stock awards

The Company issued time based restricted stock awards during the nine months ended September 30, 2018 and 2017. The restricted stock awards vest over a range of a 1 - 3 year period. Restricted stock with time-based vesting was valued at the fair value of the shares on the date of grant as they are assumed to be held beyond the vesting period.

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No market-based stock awards were granted during the nine months ended September 30, 2018 or September 30, 2017. During the nine months ended September 30, 2016, the Company granted market-based stock awards of 26,594 shares in accordance with the 2014 Plan. These shares have a five-year performance period and vest upon the later of the Company's stock price achieving an established price goal during the performance period and the third anniversary of the date of grant. The \$11.28 per share fair value of these awards was determined using a Monte Carlo Simulation at grant date. The market-based performance condition has been met for these awards and the total unrecognized compensation cost related to non-vested market-based stock awards totaled \$0.1 million, and is expected to be recognized over a weighted average period of approximately 0.4 years.

Performance stock units

During the nine months ended September 30, 2018 and 2017, the Company granted 77,125 and 49,758 performance stock units in accordance with the 2014 Plan, respectively. These performance stock units granted represent initial target awards and do not reflect potential increases or decreases resulting from the final performance results, which are to be determined at the end of the three-year performance period (vesting date). The actual number of shares to be awarded at the end of the performance period will range from 0% - 150% of the initial target awards. 60% of the award is based on the Company's cumulative earnings per share ("EPS target") during the performance period, and 40% of the award is based on the Company's cumulative total shareholder return ("TSR target"), or TSR, during the performance period. On the vesting date, the Company's TSR will be compared to the respective TSRs of the companies comprising the KBW Regional Index at the grant date to determine the shares awarded. The fair value of the EPS target portion of the award was determined based on the closing stock price of the Company's common stock on the grant date. The fair value of the TSR target portion of the award was determined using a Monte Carlo Simulation at the grant date. The weighted-average grant date fair value per unit for awards granted during the nine months ended September 30, 2018 of the EPS target portion and the TSR target portion was \$32.65 and \$27.51, respectively.

The following table summarizes restricted stock and performance stock unit activity during the nine months ended September 30, 2018:

Weighted

Weighted

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| | Restricted stock shares | average grant- date fair value | Performance stock units | average grant- date fair value |
|--------------------------------|----------------------------|-----------------------------------|----------------------------|-----------------------------------|
| Unvested at December 31, 2017 | 163,557 | \$ 22.60 | 125,082 | \$ 23.90 |
| Granted | 88,671 | 33.64 | 77,125 | 30.38 |
| Vested | (82,456) | 22.76 | — | — |
| Forfeited | (13,758) | 29.24 | (9,884) | 26.11 |
| Unvested at September 30, 2018 | 156,014 | \$ 28.21 | 192,323 | \$ 26.39 |

As of September 30, 2018, the total unrecognized compensation cost related to the non-vested restricted stock awards and performance stock units totaled \$2.5 million and \$3.6 million, respectively, and is expected to be recognized over a weighted average period of approximately 2.2 years and 2.0 years, respectively. Expense related to non-vested restricted stock awards totaled \$0.6 million and \$0.6 million during the three months ended September 30, 2018 and 2017, respectively, and \$1.6 million and \$1.7 million during the nine months ended September 30, 2018 and 2017, respectively. Expense related to non-vested performance stock units totaled \$0.4 million and \$0.2 million during the three months ended September 30, 2018 and 2017, respectively, and \$1.1 million and \$0.6 million during the nine months ended September 30, 2018 and 2017, respectively. Expense related to non-vested restricted stock awards and units is a component of salaries and benefits in the Company's consolidated statements of operations.

Employee Stock Purchase Plan

The 2014 Employee Stock Purchase Plan ("ESPP") is intended to be a qualified plan within the meaning of Section 423 of the Internal Revenue Code of 1986 and allows eligible employees to purchase shares of common stock through payroll deductions up to a limit of \$25,000 per calendar year and 2,000 shares per offering period. The price an employee pays for shares is 90.0% of the fair market value of Company common stock on the last day of the offering period. The offering periods are the six-month periods commencing on March 1 and June 1 of each year and ending on August 31 and February 28 (or February 29 in the case of a leap year) of each year. There are no vesting or other restrictions on the stock purchased by employees under the ESPP. Under the ESPP, the total number of shares of common stock reserved for issuance totaled 400,000 shares, of which 342,644 was available for issuance at September 30, 2018.

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Under the ESPP, employees purchased 12,515 shares during the nine months ended September 30, 2018, respectively, and 11,178 shares during the nine months ended September 30, 2017, respectively.

Note 13 Warrants

During the first quarter of 2017, 250,750 warrants were exercised in a non-cash transaction, representing the remaining outstanding warrants. The warrants were granted to certain lead shareholders of the Company at the time of the Company's initial capital raise (2009-2010), all with an exercise price of \$20.00 per share. Refer to the consolidated statements of changes in shareholders' equity for additional detail.

Note 14 Common Stock

The Company had 30,759,595 and 26,875,585 shares of Class A common stock outstanding at September 30, 2018 and December 31, 2017, respectively. Additionally, the Company had 156,014 and 163,557 shares outstanding at September 30, 2018 and December 31, 2017, respectively, of restricted Class A common stock issued but not yet vested under the 2014 Plan and the Prior Plan that are not included in shares outstanding until such time that they are vested; however, these shares do have voting and certain dividend rights during the vesting period.

On August 5, 2016, the Board of Directors authorized a new share repurchase program for up to \$50.0 million in either the open market or through privately negotiated transactions. The remaining authorization under this program as of September 30, 2018 was \$12.6 million.

Note 15 Earnings Per Share

The Company calculates earnings per share under the two-class method, as certain non-vested share awards contain non-forfeitable rights to dividends. As such, these awards are considered securities that participate in the earnings of the Company. Non-vested shares are discussed further in note 12.

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The Company had 30,759,595 and 26,802,964 shares of Class A common stock outstanding as of September 30, 2018 and 2017, respectively, exclusive of issued non-vested restricted shares. Certain stock options and non-vested restricted shares are potentially dilutive securities, but are not included in the calculation of diluted earnings per share because to do so would have been anti-dilutive for the three and nine months ended September 30, 2018 and 2017.

The following table illustrates the computation of basic and diluted earnings per share for the three and nine months ended September 30, 2018 and 2017:

| | For the three months ended | | For the nine months ended | |
|---|----------------------------|--------------------|---------------------------|--------------------|
| | September 30, 2018 | September 30, 2017 | September 30, 2018 | September 30, 2017 |
| Net income | \$ 18,240 | \$ 7,231 | \$ 44,216 | \$ 24,698 |
| Less: income allocated to participating securities | (18) | (14) | (49) | (43) |
| Income allocated to common shareholders | \$ 18,222 | \$ 7,217 | \$ 44,167 | \$ 24,655 |
| Weighted average shares outstanding for basic earnings per common share | 30,869,683 | 26,947,821 | 30,700,977 | 26,902,128 |
| Dilutive effect of equity awards | 671,033 | 680,913 | 687,809 | 723,304 |
| Dilutive effect of warrants | — | — | — | 11,243 |
| Weighted average shares outstanding for diluted earnings per common share | 31,540,716 | 27,628,734 | 31,388,786 | 27,636,675 |
| Basic earnings per share | \$ 0.59 | \$ 0.27 | \$ 1.44 | \$ 0.92 |
| Diluted earnings per share | \$ 0.58 | \$ 0.26 | \$ 1.41 | \$ 0.89 |

The Company had 1,262,077 and 1,661,140 outstanding stock options to purchase common stock at weighted average exercise prices of \$22.29 and \$20.62 per share at September 30, 2018 and 2017, respectively, which have time-vesting criteria, and as such, any dilution is derived only for the time frame in which the vesting criteria had been met and where the inclusion of those stock options is dilutive. Additionally, 250,750 warrants were exercised in a non-cash transaction during the first quarter of 2017, representing the remaining outstanding warrants to purchase shares of the Company's common stock. The warrants had an exercise price of \$20.00. The Company had 348,337 and 372,252 unvested restricted shares and units issued as of September 30, 2018 and 2017, respectively,

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which have performance, market and/or time-vesting criteria, and as such, any dilution is derived only for the time frame in which the vesting criteria had been met and where the inclusion of those restricted shares and units is dilutive.

Note 16 Income Taxes

The effective income tax rate for the three and nine months ended September 30, 2018 was 19.3% and 16.7%, respectively, compared to 19.3% and 9.8% for the three and nine months ended September 30, 2017, calculated based on a full year forecast method. The tax expense recorded for the three and nine months ended September 30, 2018 was lowered by a \$0.1 million and \$1.3 million discrete tax benefit from stock compensation activity during the respective periods. Without the discrete benefits, the three and nine months ended September 30, 2018 effective tax rate was 19.8% and 19.1%, respectively. The tax expense recorded for the three and nine months ended September 30, 2017 was lowered by a \$0.1 million and \$3.4 million tax benefit from stock compensation activity. Without the discrete benefits, the three and nine months ended September 30, 2017 effective tax rate was 19.9% and 22.3%, respectively. The quarterly tax rate differs from the federal statutory rate primarily due to tax benefits from stock compensation activity, interest income from tax-exempt lending, bank-owned life insurance income, and the relationship of these items to pre-tax income. See management's discussion and analysis for further information.

Note 17 Derivatives

Risk management objective of using derivatives

The Company is exposed to certain risks arising from both its business operations and economic conditions. The Company has established policies that neither carrying value nor fair value at risk should exceed established guidelines. The Company has designed strategies to confine these risks within the established limits and identify appropriate trade-offs in the financial structure of its balance sheet. These strategies include the use of derivative financial instruments to help achieve the desired balance sheet repricing structure while meeting the desired objectives of its clients. Currently, the Company employs certain interest rate swaps that are designated as fair value hedges as well as economic hedges. The Company manages a matched book with respect to its derivative instruments in order to minimize its net risk exposure resulting from such transactions.

Fair values of derivative instruments on the balance sheet

The table below presents the fair value of the Company's derivative financial instruments as well as their classification on the consolidated statements of financial condition as of September 30, 2018 and December 31, 2017.

Information about the valuation methods used to measure fair value is provided in note 19.

| | Balance Sheet location | Asset derivatives fair value | | Balance Sheet location | Liability derivatives fair value | |
|---|------------------------|------------------------------|-------------------|------------------------|----------------------------------|-------------------|
| | | September 30, 2018 | December 31, 2017 | | September 30, 2018 | December 31, 2017 |
| Derivatives designated as hedging instruments: | | | | | | |
| Interest rate products | Other assets | \$ 31,180 | \$ 10,489 | Other liabilities | \$ — | \$ 1,167 |
| Total derivatives designated as hedging instruments | | \$ 31,180 | \$ 10,489 | | \$ — | \$ 1,167 |
| Derivatives not designated as hedging instruments: | | | | | | |
| Interest rate products | Other assets | \$ 4,676 | \$ 2,483 | Other liabilities | \$ 4,659 | \$ 2,584 |
| Interest rate lock commitments | Other assets | 893 | 128 | Other liabilities | 150 | — |
| Forward contracts | Other assets | 357 | 5 | Other liabilities | 29 | 7 |
| Total derivatives not designated as hedging instruments | | \$ 5,926 | \$ 2,616 | | \$ 4,838 | \$ 2,591 |

Fair value hedges

Interest rate swaps designated as fair value hedges involve the receipt of variable-rate amounts from a counterparty in exchange for the Company making fixed-rate payments over the life of the agreements without the exchange of the underlying notional amount. As of September 30, 2018, the Company had interest rate swaps with a notional amount of \$472.7 million, which were designated as fair value hedges of interest rate risk. These interest rate swaps were associated with \$505.9 million of the Company's fixed-rate loans, before a \$(30.6) million fair value hedge adjustment in the carrying amount, included in loans receivable on the statements of financial

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condition. As of December 31, 2017, the Company had interest rate swaps with a notional amount of \$417.7 million that were designated as fair value hedges.

For derivatives designated and that qualify as fair value hedges, the gain or loss on the derivative as well as the offsetting loss or gain on the hedged item attributable to the hedged risk are recognized in earnings. The Company includes the gain or loss on the hedged items in the same line item as the offsetting loss or gain on the related derivatives.

Non-designated hedges

Derivatives not designated as hedges are not speculative and consist of interest rate swaps with commercial banking clients that facilitate their respective risk management strategies. Interest rate swaps are simultaneously hedged by offsetting interest rate swaps that the Company executes with a third party, such that the Company minimizes its net risk exposure resulting from such transactions. As the interest rate swaps associated with this program do not meet the strict hedge accounting requirements, changes in the fair value of both the client swaps and the offsetting swaps are recognized directly in earnings. As of September 30, 2018, the Company had matched interest rate swap transactions with an aggregate notional amount of \$188.5 million related to this program. As of December 31, 2017, the Company had matched interest rate swap transactions with an aggregate notional amount of \$202.2 million related to this program.

As part of its mortgage banking activities, the Company enters into interest rate lock commitments, which are commitments to originate loans where the interest rate on the loan is determined prior to funding and the clients have locked into that interest rate. The Company then locks in the loan and interest rate with an investor and commits to deliver the loan if settlement occurs ("best efforts") or commits to deliver the locked loan in a binding ("mandatory") delivery program with an investor. Fair value changes of certain loans under interest rate lock commitments are hedged with forward sales contracts of MBS. Forward sales contracts of MBS are recorded at fair value with changes in fair value recorded in non-interest income. Interest rate lock commitments and commitments to deliver loans to investors are considered derivatives. The market value of interest rate lock commitments and best efforts contracts are not readily ascertainable with precision because they are not actively traded in stand-alone markets. The Company determines the fair value of interest rate lock commitments and delivery contracts by measuring the fair value of the underlying asset, which is impacted by current interest rates, taking into consideration the probability that the interest rate lock commitments will close or will be funded.

Certain additional risks arise from these forward delivery contracts in that the counterparties to the contracts may not be able to meet the terms of the contracts. The Company does not expect any counterparty to any MBS contract to fail to meet its obligation. Additional risks inherent in mandatory delivery programs include the risk that, if the Company fails to deliver the loans subject to interest rate risk lock commitments, it will still be obligated to "pair off" MBS to the counterparty. Should this be required, the Company could incur significant costs in acquiring replacement loans and such costs could have an adverse effect on the consolidated financial statements.

The fair value of the mortgage banking derivative is recorded as a freestanding asset or liability with the change in value being recognized in current earnings during the period of change.

The Company had interest rate lock commitments with a notional value of \$84.0 million and forward contracts with a notional value of \$128.0 million at September 30, 2018. At December 31, 2017, the Company had interest rate lock commitments with a notional value of \$8.0 million and forward contracts with a notional value of \$9.0 million.

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Effect of derivative instruments on the consolidated statements of operations

The tables below present the effect of the Company's derivative financial instruments on the consolidated statements of operations for the three and nine months ended September 30, 2018 and 2017:

| | Location of gain (loss) | Amount of gain (loss) recognized in income on derivatives | | | |
|--|--|--|----------|--|------------|
| | | For the three months ended September 30, | | For the nine months ended September 30, | |
| Derivatives in fair value hedging relationships | recognized in income on derivatives | 2018 | 2017 | 2018 | 2017 |
| Interest rate products | Interest and fees on loans | \$ 4,516 | \$ — | \$ 21,856 | \$ — |
| Interest rate products | Other non-interest income | — | (128) | — | (2,233) |
| Total | | \$ 4,516 | \$ (128) | \$ 21,856 | \$ (2,233) |

| | Location of gain (loss) | Amount of (loss) recognized in income on hedged items | | | |
|------------------------|---|--|----------|--|----------|
| | | For the three months ended September 30, | | For the nine months ended September 30, | |
| Hedged items | recognized in income on hedged items | 2018 | 2017 | 2018 | 2017 |
| Interest rate products | Interest and fees on loans | \$ (4,719) | \$ — | \$ (21,983) | \$ — |
| Interest rate products | Other non-interest income | — | (283) | — | 1,437 |
| Total | | \$ (4,719) | \$ (283) | \$ (21,983) | \$ 1,437 |

| | Location of gain (loss) | Amount of gain (loss) recognized in income on derivatives | | | |
|--|--|--|---------|--|----------|
| | | For the three months ended September 30, | | For the nine months ended September 30, | |
| Derivatives not designated as hedging instruments | recognized in income on derivatives | 2018 | 2017 | 2018 | 2017 |
| Interest rate products | Other non-interest expense | \$ 5 | \$ (75) | \$ (120) | \$ (155) |
| Interest rate lock commitments | Mortgage banking income | (811) | 35 | (952) | 36 |
| Forward contracts | Mortgage banking income | (425) | 57 | 988 | (73) |
| Total | | \$ (1,231) | \$ 17 | \$ (84) | \$ (192) |

Credit-risk-related contingent features

The Company has agreements with its derivative counterparties that contain a provision where if the Company defaults on any of its indebtedness for reasons other than an error or omission of an administrative or operational nature, including default where repayment of the indebtedness has not been accelerated by the lender, then the Company could also be declared in default on its derivative obligations.

The Company also has agreements with certain of its derivative counterparties that contain a provision where if the Company fails to maintain its status as a well/adequately capitalized institution, then the counterparty has the right to terminate the derivative positions and the Company would be required to settle its obligations under the agreements.

As of September 30, 2018, the termination value of derivatives in a net liability position related to these agreements was \$4.7 million, which includes accrued interest but excludes any adjustment for nonperformance risk. The Company has minimum collateral posting thresholds with certain of its derivative counterparties and, as of September 30, 2018, the Company had met these thresholds. If the Company had breached any of these provisions at September 30, 2018, it could have been required to settle its obligations under the agreements at the termination value.

Note 18 Commitments and Contingencies

In the normal course of business, the Company enters into various off-balance sheet commitments to help meet the financing needs of clients. These financial instruments include commitments to extend credit, commercial and consumer lines of credit and standby letters of credit. The same credit policies are applied to these commitments as the loans on the consolidated statements of financial condition; however, these commitments involve varying degrees of credit risk in excess of the amount recognized in the consolidated statements of financial condition. At September 30, 2018 and December 31, 2017, the Company had loan commitments totaling \$765.4 million and \$680.8 million, respectively, and standby letters of credit that totaled \$8.5 million and \$7.2 million, respectively. The total amounts of unused commitments do not necessarily represent future credit exposure or cash requirements, as commitments often expire without being drawn upon. However, the contractual amount of these commitments, offset by any additional collateral pledged, represents the Company's potential credit loss exposure.

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Total unfunded commitments at September 30, 2018 and December 31, 2017 were as follows:

| | September 30, 2018 | December 31, 2017 |
|--|--------------------|-------------------|
| Commitments to fund loans | \$ 203,029 | \$ 181,904 |
| Unfunded commitments under lines of credit | 562,359 | 498,857 |
| Commercial and standby letters of credit | 8,499 | 7,185 |
| Total unfunded commitments | \$ 773,887 | \$ 687,946 |

Commitments to fund loans—Commitments to fund loans are legally binding agreements to lend to clients in accordance with predetermined contractual provisions providing there have been no violations of any conditions specified in the contract. These commitments are generally at variable interest rates and are for specific periods or contain termination clauses and may require the payment of a fee. The total amounts of unused commitments are not necessarily representative of future credit exposure or cash requirements, as commitments often expire without being drawn upon.

Unfunded commitments under lines of credit—In the ordinary course of business, the Company extends revolving credit to its clients. These arrangements may require the payment of a fee.

Commercial and standby letters of credit—As a provider of financial services, the Company routinely issues commercial and standby letters of credit, which may be financial standby letters of credit or performance standby letters of credit. These are various forms of “back-up” commitments to guarantee the performance of a client to a third party. While these arrangements represent a potential cash outlay for the Company, the majority of these letters of credit will expire without being drawn upon. Letters of credit are subject to the same underwriting and credit approval process as traditional loans, and as such, many of them have various forms of collateral securing the commitment, which may include real estate, personal property, receivables or marketable securities.

Contingencies

Mortgage loans sold to investors may be subject to repurchase or indemnification in the event of specific default by the borrower or subsequent discovery that underwriting standards were not met. The Company established a reserve liability for expected losses related to these representations and warranties based upon management’s evaluation of actual and historic loss history, delinquency trends in the portfolio and economic conditions. The Company recorded a repurchase reserve of \$3.9 million at September 30, 2018, which is included in other liabilities on the consolidated statements of financial condition.

In the ordinary course of business, the Company and the Bank may be subject to litigation. Based upon the available information and advice from the Company's legal counsel, management does not believe that any potential, threatened or pending litigation to which it is a party will have a material adverse effect on the Company's liquidity, financial condition or results of operations.

Note 19 Fair Value Measurements

The Company uses fair value measurements to record fair value adjustments to certain assets and liabilities and to disclose the fair value of its financial instruments. Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. For disclosure purposes, the Company groups its financial and non-financial assets and liabilities into three different levels based on the nature of the instrument and the availability and reliability of the information that is used to determine fair value. The three levels are defined as follows:

- Level 1—Includes assets or liabilities in which the valuation methodologies are based on unadjusted quoted prices in active markets for identical assets or liabilities.
- Level 2—Includes assets or liabilities in which the inputs to the valuation methodologies are based on similar assets or liabilities in inactive markets, quoted prices for identical or similar assets or liabilities in inactive markets, and inputs other than quoted prices that are observable, such as interest rates, yield curves, volatilities, prepayment speeds, and other inputs obtained from observable market input.
- Level 3—Includes assets or liabilities in which the inputs to the valuation methodology are based on at least one significant assumption that is not observable in the marketplace. These valuations may rely on management's judgment and may include internally-developed model-based valuation techniques.

Level 1 inputs are considered to be the most transparent and reliable and level 3 inputs are considered to be the least transparent and reliable. The Company assumes the use of the principal market to conduct a transaction of each particular asset or liability being

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measured and then considers the assumptions that market participants would use when pricing the asset or liability. Whenever possible, the Company first looks for quoted prices for identical assets or liabilities in active markets (level 1 inputs) to value each asset or liability. However, when inputs from identical assets or liabilities on active markets are not available, the Company utilizes market observable data for similar assets and liabilities. The Company maximizes the use of observable inputs and limits the use of unobservable inputs to occasions when observable inputs are not available. The need to use unobservable inputs generally results from the lack of market liquidity of the actual financial instrument or of the underlying collateral. Although, in some instances, third party price indications may be available, limited trading activity can challenge the observability of these quotations.

Changes in the valuation inputs used for measuring the fair value of financial instruments may occur due to changes in current market conditions or other factors. Such changes may necessitate a transfer of the financial instruments to another level in the hierarchy based on the new inputs used. The Company recognizes these transfers at the end of the reporting period that the transfer occurs. During the nine months ended September 30, 2018 and 2017, there were no transfers of financial instruments between the hierarchy levels.

The following is a description of the valuation methodologies used for assets and liabilities measured at fair value, as well as the general classification of each instrument under the valuation hierarchy:

Fair Value of Financial Instruments Measured on a Recurring Basis

Investment securities available-for-sale—Investment securities available-for-sale are carried at fair value on a recurring basis. To the extent possible, observable quoted prices in an active market are used to determine fair value and, as such, these securities are classified as level 1. At September 30, 2018 and December 31, 2017, the Company did not hold any level 1 securities. When quoted market prices in active markets for identical assets or liabilities are not available, quoted prices of securities with similar characteristics, discounted cash flows or other pricing characteristics are used to estimate fair values and the securities are then classified as level 2.

Loans held for sale—The Company has elected to record loans originated and intended for sale in the secondary market at estimated fair value. The portfolio consists primarily of fixed rate residential mortgage loans that are sold within 45 days. The Company estimates fair value based on quoted market prices for similar loans in the secondary market and is classified as level 2.

Interest rate swap derivatives—The Company's derivative instruments are limited to interest rate swaps that may be accounted for as fair value hedges or non-designated hedges. The fair values of the swaps incorporate credit valuation adjustments in order to appropriately reflect nonperformance risk in the fair value measurements. The credit valuation adjustment is the dollar amount of the fair value adjustment related to credit risk and utilizes a probability weighted calculation to quantify the potential loss over the life of the trade. The credit valuation adjustments are calculated by

determining the total expected exposure of the derivatives (which incorporates both the current and potential future exposure) and then applying the respective counterparties' credit spreads to the exposure offset by marketable collateral posted, if any. Certain derivative transactions are executed with counterparties who are large financial institutions ("dealers"). International Swaps and Derivative Association Master Agreements ("ISDA") and Credit Support Annexes ("CSA") are employed for all contracts with dealers. These contracts contain bilateral collateral arrangements. The fair value inputs of these financial instruments are determined using discounted cash flow analysis through the use of third-party models whose significant inputs are readily observable market parameters, primarily yield curves, with appropriate adjustments for liquidity and credit risk, and are classified as level 2.

Mortgage banking derivatives—The Company relies on a third-party pricing service to value its mortgage banking derivative financial assets and liabilities, which the Company classifies as a level 3 valuation. The external valuation model to estimate the fair value of its interest rate lock commitments to originate residential mortgage loans held for sale includes grouping the interest rate lock commitments by interest rate and terms, applying an estimated pull-through rate based on historical experience, and then multiplying by quoted investor prices determined to be reasonably applicable to the loan commitment groups based on interest rate, terms, and rate lock expiration dates of the loan commitment groups. The Company also relies on an external valuation model to estimate the fair value of its forward commitments to sell residential mortgage loans (i.e., an estimate of what the Company would receive or pay to terminate the forward delivery contract based on market prices for similar financial instruments), which includes matching specific terms and maturities of the forward commitments against applicable investor pricing.

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The tables below present the financial instruments measured at fair value on a recurring basis as of September 30, 2018 and December 31, 2017 on the consolidated statements of financial condition utilizing the hierarchy structure described above:

| | September 30, 2018 | | | Total |
|--|--------------------|------------|----------|------------|
| | Level 1 | Level 2 | Level 3 | |
| Assets: | | | | |
| Investment securities available-for-sale: | | | | |
| Mortgage-backed securities: | | | | |
| Residential mortgage pass-through securities issued or guaranteed by U.S. Government agencies or sponsored enterprises | \$ — | \$ 156,314 | \$ — | \$ 156,314 |
| Other residential MBS issued or guaranteed by U.S. Government agencies or sponsored enterprises | — | 639,038 | — | 639,038 |
| Municipal securities | — | 510 | — | 510 |
| Loans held for sale | — | 80,506 | — | 80,506 |
| Interest rate swap derivatives | — | 35,856 | — | 35,856 |
| Mortgage banking derivatives | — | — | 1,250 | 1,250 |
| Total assets at fair value | \$ — | \$ 912,224 | \$ 1,250 | \$ 913,474 |
| Liabilities: | | | | |
| Interest rate swap derivatives | \$ — | \$ 4,659 | \$ — | \$ 4,659 |
| Mortgage banking derivatives | — | — | 179 | 179 |
| Total liabilities at fair value | \$ — | \$ 4,659 | \$ 179 | \$ 4,838 |

| | December 31, 2017 | | | Total |
|--|-------------------|------------|---------|------------|
| | Level 1 | Level 2 | Level 3 | |
| Assets: | | | | |
| Investment securities available-for-sale: | | | | |
| Mortgage-backed securities: | | | | |
| Residential mortgage pass-through securities issued or guaranteed by U.S. Government agencies or sponsored enterprises | \$ — | \$ 168,648 | \$ — | \$ 168,648 |
| Other residential MBS issued or guaranteed by U.S. Government agencies or sponsored enterprises | — | 685,230 | — | 685,230 |
| Municipal securities | — | 829 | — | 829 |
| Loans held for sale | — | 4,629 | — | 4,629 |
| Interest rate swap derivatives | — | 12,972 | — | 12,972 |
| Mortgage banking derivatives | — | — | 133 | 133 |
| Total assets at fair value | \$ — | \$ 872,308 | \$ 133 | \$ 872,441 |
| Liabilities: | | | | |
| Interest rate swap derivatives | \$ — | \$ 3,751 | \$ — | \$ 3,751 |
| Mortgage banking derivatives | — | — | 7 | 7 |
| Total liabilities at fair value | \$ — | \$ 3,751 | \$ 7 | \$ 3,758 |

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The table below details the changes in level 3 financial instruments during the nine months ended September 30, 2018:

| | Mortgage banking derivatives, net |
|--------------------------------|--------------------------------------|
| Balance at December 31, 2017 | \$ 126 |
| Gain included in earnings, net | 945 |
| Balance at September 30, 2018 | \$ 1,071 |

Fair Value of Financial Instruments Measured on a Non-recurring Basis

Certain assets may be recorded at fair value on a non-recurring basis as conditions warrant. These non-recurring fair value measurements typically result from the application of lower of cost or fair value accounting or a write-down occurring during the period.

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The Company records collateral dependent loans that are considered to be impaired at their estimated fair value. A loan is considered impaired when it is probable that the Company will be unable to collect all contractual amounts due in accordance with the terms of the loan agreement. Collateral dependent impaired loans are measured based on the fair value of the collateral. The Company relies on third-party appraisals and internal assessments, utilizing a discount rate in the range of 0% - 25%, in determining the estimated fair values of these loans. The inputs used to determine the fair values of loans are considered level 3 inputs in the fair value hierarchy. At September 30, 2018, the Company measured five originated and acquired loans at fair value on a non-recurring basis, with a carrying balance of \$5.2 million and specific reserve balance of \$1.4 million. At September 30, 2017, the Company measured seven originated and acquired loans at fair value on a non-recurring basis, with a carrying balance of \$8.3 million and specific reserve balance of \$1.1 million.

OREO is recorded at the fair value of the collateral less estimated selling costs. The estimated fair values of OREO are updated periodically and further write-downs may be taken to reflect a new basis. The Company recognized \$220 thousand and \$766 thousand of OREO impairments in its consolidated statements of operations during the nine months ended September 30, 2018 and 2017, respectively. The fair values of OREO properties are derived from third party price opinions or appraisals that generally use an income approach or a market value approach. If reasonable comparable appraisals are not available, then the Company may use internally developed models to determine fair values. The inputs used to determine the fair value of OREO properties are considered level 3 inputs in the fair value hierarchy.

Mortgage servicing rights represent the value associated with servicing residential real estate loans that have been sold to outside investors with servicing retained. The fair value for servicing assets is determined through discounted cash flow analysis and utilizes discount rates ranging from 9.5% to 10.5% at September 30, 2018 and prepayment speed assumption ranges of 8.6% to 11.8% at September 30, 2018 as inputs. Mortgage servicing rights are subject to impairment testing. The carrying values of these rights are reviewed quarterly for impairment based upon the calculation of fair value. For purposes of measuring impairment, the rights are stratified into certain risk characteristics including note type and note term. If the valuation model reflects a value less than the carrying value, mortgage servicing rights are adjusted to fair value through a valuation allowance. There was a \$0.1 million valuation allowance recorded at September 30, 2018. The inputs used to determine the fair values of mortgage servicing rights are considered level 3 inputs in the fair value hierarchy.

The Company may be required to record fair value adjustments on other available-for-sale and municipal securities valued at par on a non-recurring basis.

The table below provides information regarding the assets recorded at fair value on a non-recurring basis during the nine months ended September 30, 2018 and 2017:

September 30, 2018

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| | Total | Losses from fair value changes |
|---------------------------|-----------|--------------------------------------|
| Impaired loans | \$ 34,578 | \$ 1,482 |
| Other real estate owned | 35,135 | 220 |
| Mortgage servicing rights | 3,670 | 68 |
| Total | \$ 73,383 | \$ 1,770 |

| | September 30, 2017 | |
|-------------------------|--------------------|--------------------------------------|
| | Total | Losses from fair value changes |
| Impaired loans | \$ 28,459 | \$ 9,171 |
| Other real estate owned | 12,330 | 766 |
| Total | \$ 40,789 | \$ 9,937 |

The Company did not record any liabilities measured at fair value on a non-recurring basis during the nine months ended September 30, 2018.

Note 20 Fair Value of Financial Instruments

The fair value of a financial instrument is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction in the principal market at the measurement date under current market conditions. The fair value of the financial instruments listed below does not reflect a premium or discount that could result from offering all of the Company's holdings of financial instruments at one time, nor does it reflect the underlying value of the Company, as ASC Topic 825 excludes certain financial

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instruments and all non-financial instruments from its disclosure requirements. The estimated fair value amounts have been determined by the Company using available market information and appropriate valuation methodologies and are based on the exit price notion set forth by ASU 2016-01 effective January 1, 2018 and applied to this disclosure on a prospective basis. Considerable judgment is required to interpret market data in order to develop the estimates of fair value. Accordingly, the estimates presented herein are not necessarily indicative of the amounts the Company could realize in a current market exchange.

The fair value of financial instruments at September 30, 2018 and December 31, 2017 are set forth below:

| | Level in fair value measurement hierarchy | September 30, 2018 | | December 31, 2017 | |
|--|--|--------------------|-------------------------|--------------------|-------------------------|
| | | Carrying amount | Estimated fair value | Carrying amount | Estimated fair value |
| ASSETS | | | | | |
| Cash and cash equivalents | Level 1 | \$ 111,459 | \$ 111,459 | \$ 257,364 | \$ 257,364 |
| Mortgage-backed securities—residential mortgage pass-through securities issued or guaranteed by U.S. Government agencies or sponsored enterprises available-for-sale | Level 2 | 156,314 | 156,314 | 168,648 | 168,648 |
| Mortgage-backed securities—other residential mortgage-backed securities issued or guaranteed by U.S. Government agencies or sponsored enterprises available-for-sale | Level 2 | 639,038 | 639,038 | 685,230 | 685,230 |
| Municipal securities | Level 2 | 510 | 510 | 829 | 829 |
| Municipal securities | Level 3 | 219 | 219 | 219 | 219 |
| Other available-for-sale securities | Level 3 | 469 | 469 | 419 | 419 |
| Mortgage-backed securities—residential mortgage pass-through securities issued or guaranteed by U.S. Government agencies or sponsored enterprises held-to-maturity | Level 2 | 166,955 | 162,708 | 204,352 | 204,048 |
| Mortgage-backed securities—other residential mortgage-backed securities issued or guaranteed by U.S. | Level 2 | 82,509 | 79,662 | 54,378 | 52,723 |

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| | | | | | |
|---|---------|-----------|-----------|-----------|-----------|
| Government agencies or sponsored enterprises held-to-maturity | | | | | |
| Non-marketable securities | Level 2 | 16,975 | 16,975 | 15,030 | 15,030 |
| Loans receivable | Level 3 | 3,905,311 | 3,836,202 | 3,178,947 | 3,167,508 |
| Loans held for sale | Level 2 | 80,506 | 80,506 | 4,629 | 4,629 |
| Accrued interest receivable | Level 2 | 21,436 | 21,436 | 14,255 | 14,255 |
| Interest rate swap derivatives | Level 2 | 35,856 | 35,856 | 12,972 | 12,972 |
| Mortgage banking derivatives | Level 3 | 1,251 | 1,251 | 133 | 133 |
| LIABILITIES | | | | | |
| Deposit transaction accounts | Level 2 | 3,494,407 | 3,494,407 | 2,861,509 | 2,861,509 |
| Time deposits | Level 2 | 1,119,625 | 1,104,620 | 1,118,050 | 1,108,733 |
| Securities sold under agreements to repurchase | Level 2 | 55,695 | 55,695 | 130,463 | 130,463 |
| Federal Home Loan Bank advances | Level 2 | 144,540 | 144,780 | 129,115 | 130,300 |
| Accrued interest payable | Level 2 | 7,729 | 7,729 | 5,776 | 5,776 |
| Interest rate swap derivatives | Level 2 | 4,659 | 4,659 | 3,751 | 3,751 |
| Mortgage banking derivatives | Level 3 | 179 | 179 | 7 | 7 |

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Item 2: MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS.

The following management's discussion and analysis of our financial condition and results of operations should be read in conjunction with our consolidated financial statements and related notes as of and for the three and nine months ended September 30, 2018, and with our annual report on Form 10-K (file number 001-35654), which includes our audited consolidated financial statements and related notes as of and for the years ended December 31, 2017, 2016 and 2015. This discussion and analysis contains forward-looking statements that involve risks, uncertainties and assumptions that may cause actual results to differ materially from management's expectations. Factors that could cause such differences are discussed in the section entitled "Cautionary Note Regarding Forward-Looking Statements" located elsewhere in this quarterly report and in Item 1A "Risk Factors" in the annual report on Form 10-K, referenced above, and should be read herewith.

All amounts are in thousands, except share and per share data, or as otherwise noted.

Overview

Our focus is on building strong banking relationships with small to medium-sized businesses and consumers, while maintaining a low risk profile designed to generate reliable income streams and attractive returns. We have established a solid financial services franchise with a sizable presence for deposit gathering and building client relationships necessary for growth. We believe that our established presence in core markets that are outperforming national averages positions us well for growth opportunities. As of September 30, 2018, we had \$5.6 billion in assets, \$3.9 billion in loans, \$4.6 billion in deposits and \$0.7 billion in equity.

Operating Highlights

Beginning in the first quarter 2018, loans previously referred to as "non 310-30 loans" are referred to as "originated and acquired loans," which include originated loans and acquired loans not accounted for under ASC 310-30. No amounts were reclassified resulting from this change in terminology.

On January 1, 2018, the Company completed its acquisition of Peoples, Inc. ("Peoples"), the bank holding company of Colorado-based Peoples National Bank and Kansas-based Peoples Bank. At the close of the acquisition, the Company acquired 20 banking centers located in the highly-attractive and geographically-relevant markets of Colorado Springs in Colorado, Overland Park and Lawrence in Kansas, and Taos and Albuquerque in New Mexico, and an in-market mortgage origination business. The acquisition added approximately \$842 million in total assets, net of FHLB

payoffs, \$543 million in loans and \$730 million in deposits. The merger consideration totaled \$146.4 million and consisted of \$110.2 million in Company stock and \$36.2 million in cash. All operating systems were converted during the first and second quarters of 2018.

Increased profitability and returns

Net income was \$44.2 million, or \$1.41 per diluted share, for the nine months ended September 30, 2018 compared to net income of \$24.7 million, or \$0.89 per diluted share, for the same period in the prior year. Net income during the nine months ended September 30, 2018 included \$6.3 million, after-tax, of expenses related to the acquisition of Peoples. Adjusting for these expenses, net income would have been \$50.5 million, or \$1.61 per diluted share.

The return on average tangible assets was 1.11% for the nine months ended September 30, 2018 compared to 0.79% for the same period in the prior year. Adjusting for Peoples acquisition expenses, the return on average tangible assets was 1.27% for the nine months ended September 30, 2018.

The return on average tangible common equity was 11.36% for the nine months ended September 30, 2018 compared to 7.41% for the same period prior year. Adjusting for Peoples acquisition expenses, the return on average tangible common equity was 12.94% for the nine months ended September 30, 2018.

Strategic execution

Completed the acquisition of Peoples on January 1, 2018.

Grew originated and acquired loans outstanding to \$3.8 billion, an increase of \$772.1 million, or 33.8% annualized, since December 31, 2017, driven by Peoples acquired loans and originated loan growth of 15.8% annualized.

Maintained a conservatively structured loan portfolio represented by diverse industries and concentrations with most industry sector concentrations at 5% or less of total loans, and all concentration levels remain well below our self-imposed limits.

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Continued to build and deepen relationships with our clients, resulting in strong average deposit growth of \$722.5 million since December 31, 2017, due to the Peoples acquisition and demand, savings, and money market deposit (“transaction deposits”) growth during the period.

Maintained strong expense management as the Company begins to realize benefits from the completed system conversions of the Peoples acquisition during 2018.

Loan portfolio

Total loans ended the quarter at \$3.9 billion and increased \$726.4 million, or 22.8%, since December 31, 2017, driven by the Peoples acquisition and loan originations during the period.

Originated loans grew 16.8% annualized, since December 31, 2017, due to strong growth in commercial loans of 31.1% annualized, offset partially by expected payoffs of non-owner occupied commercial real estate.

Credit quality

Credit quality remained strong, as non-performing originated and acquired loans (comprised of non-accrual loans and non-accrual TDRs) were 0.64% of total originated and acquired loans at September 30, 2018, compared to 0.69% at December 31, 2017. Non-performing assets to total loans and OREO totaled 1.51% at September 30, 2018 compared to 0.99% at December 31, 2017. Excluding OREO transferred from 310-30 loans, non-performing assets to total loans and OREO totaled 0.76% at September 30, 2018.

Provision for loan losses on originated and acquired loans totaled \$2.5 million during the nine months ended September 30, 2018, compared to \$9.9 million during the same period prior year. The current period provision was recorded to support the increase in originated loans and a decrease resulting from one large recovery of \$1.1 million.

Client deposit funded balance sheet

Total deposits averaged \$4.6 billion during the nine months ended September 30, 2018, increasing \$757.3 million, or 19.5%, compared to the same period prior year. The increase was driven by \$730 million in total deposits added on January 1, 2018 from the Peoples acquisition, coupled with transaction deposit growth, partially offset by the sale of four banking centers in the second quarter of 2017.

Average transaction deposits totaled \$3.5 billion during the nine months ended September 30, 2018, increasing \$765.8 million, or 28.1%, from the same period prior year, due to organic growth and the Peoples acquisition. Time deposits averaged \$1.1 billion during the nine months ended September 30, 2018, decreasing \$8.5 million from the same period prior year. An increase from the Peoples acquisition was offset by a decrease from legacy accounts.

The mix of transaction deposits to total deposits improved to 75.7% from 71.9% at December 31, 2017, due to the Peoples acquisition and our continued focus on developing long-term banking relationships. Cost of deposits totaled 0.43% during the nine months ended September 30, 2018, increasing 0.02% from the same period prior year.

Revenues

Fully taxable equivalent (FTE) net interest income totaled \$150.1 million during the nine months ended September 30, 2018 and increased \$36.4 million, or 32.0%, compared to the same period prior year. The FTE net interest margin widened 0.39% to 3.92% during the nine months ended September 30, 2018 as the yield on earning assets increased 0.41%, led by a 0.40% increase in the originated portfolio yields due to short-term rate increases, partially offset by an increase in the cost of deposits of 0.02%. Non-interest income totaled \$55.5 million during the nine months ended September 30, 2018, increasing \$25.3 million from the same period prior year, primarily due to the Peoples acquisition.

Expenses

Non-interest expense totaled \$146.5 million during the nine months ended September 30, 2018, representing an increase of \$43.8 million from same period prior year, driven by the Peoples acquisition. Included in the first nine months of 2018 were \$8.0 million of pre-tax acquisition costs.

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Income tax expense totaled \$8.8 million during the nine months ended September 30, 2018, compared to \$2.7 million during the same period prior year. The tax expense recorded for the nine months ended September 30, 2018 and 2017 were lowered by a \$1.3 million and \$3.4 million tax benefit from stock compensation activity, respectively. The September 30, 2018 and 2017 effective tax rate was 16.7% and 9.8%, respectively. Adjusting for the stock compensation activity, the September 30, 2018 and 2017 adjusted effective tax rate was 19.1% and 22.3%, respectively. The effective tax rate is lower compared to the prior year primarily due to the Tax Cuts and Jobs Act which, among other items, reduced the federal corporate tax rate to 21% effective January 1, 2018.

Strong capital position

Capital ratios are strong as our capital position remains in excess of federal bank regulatory thresholds. As of September 30, 2018, our consolidated tier 1 leverage ratio was 10.3% and our consolidated tier 1 risk-based capital and common equity tier 1 risk-based capital ratios were both 12.9%.

At September 30, 2018, common book value per share was \$21.88, while tangible common book value per share was \$18.04, or \$18.80 after consideration of the excess accretable yield value of \$0.76 per share.

Since early 2013, we have repurchased 26.6 million shares, or 50.9% of the outstanding shares, at an attractive weighted average price of \$20.03 per share.

Key Challenges

There are a number of significant challenges confronting us and our industry. In our short history, we primarily have acquired distressed financial institutions, and sought to rebuild them and implement operational efficiencies across the enterprise as a whole. We face continual challenges implementing our business strategy, including growing the assets, particularly loans, and deposits of our business amidst intense competition, raising interest rates from an extended low interest rate environment, adhering to changes in the regulatory environment and identifying and consummating disciplined merger and acquisition opportunities in a very competitive environment.

General economic conditions remained stable during the first nine months of 2018. Residential real estate values remain strong in our markets and nationally, with many markets, including Denver, hitting new post-crisis highs. Commercial real estate property fundamentals also remain strong, with stable occupancy and increasing lease rates, along with cyclically low capitalization rates leading to increasing valuations. A significant portion of our loan portfolio is secured by real estate and any deterioration in real estate values or credit quality or elevated levels of non-performing assets would ultimately have a negative impact on the quality of our loan portfolio.

The agriculture industry is in the fourth year of depressed commodity prices. Our agriculture portfolio is only 5.1% of total loans and is well-diversified across crop and livestock types. We have maintained relationships with agriculture clients that generally possess low leverage and, correspondingly, low bank debt to assets, minimizing any potential credit losses in the future.

Our originated and acquired loans outstanding portfolio at September 30, 2018 totaled \$3.8 billion, representing an increase of \$772.0 million, or 33.8% annualized compared to December 31, 2017, due to an increase of \$400.2 million in loans acquired from the Peoples acquisition and an increase of \$371.8 million in loan originations, partially offset by originated loan paydowns and payoffs during the nine months ended September 30, 2018. Our 310-30 loans have produced higher yields than our originated and acquired loans, due to accretion of fair value adjustments. During the nine months ended September 30, 2018, our weighted average rate on new loan fundings at the time of origination was 4.8% (fully taxable equivalent), compared to the nine months ended September 30, 2017 weighted average yield of our originated loan portfolio of 4.4% (fully taxable equivalent). Fully taxable equivalent net interest income reached an inflection point in the second quarter of 2017 and continued during the third quarter of 2018 as the yields and volumes of originated and acquired loans outpaced the decrease in higher yielding 310-30 loan balances. The inflection point was driven by both the strong new loan originations as well as the short-term market rate increases in 2017 and 2018. Future growth in our interest income will ultimately be dependent on our ability to continue to generate sufficient volumes of high-quality originated loans.

Continued regulation, impending new liquidity and capital constraints, and a continual need to bolster cybersecurity are adding costs and uncertainty to all U.S. banks and could affect profitability. Also, nontraditional participants in the market may offer increased competition as non-bank payment businesses are expanding into traditional banking products. While certain external factors are out of our control and may provide obstacles to our business strategy, we are prepared to deal with these challenges. We seek to remain flexible, yet methodical and proactive, in our strategic decision making so that we can quickly respond to market changes and the inherent challenges and opportunities that accompany such changes.

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Performance Overview

In evaluating our consolidated statements of financial condition and results of operations financial statement line items, we evaluate and manage our performance based on key earnings indicators, balance sheet ratios, asset quality metrics and regulatory capital ratios, among others. The table below presents some of the primary performance indicators that we use to analyze our business on a regular basis for the periods indicated:

| | As of and for the three months ended | | | As of and for the nine months ended | |
|---|--------------------------------------|-------------------|--------------------|-------------------------------------|--------------------|
| | September 30, 2018 | December 31, 2017 | September 30, 2017 | September 30, 2018 | September 30, 2017 |
| Key Ratios(1) | | | | | |
| Return on average assets | 1.30% | (0.83)% | 0.61% | 1.06% | 0.71% |
| Return on average tangible assets(2) | 1.35% | (0.78)% | 0.69% | 1.11% | 0.79% |
| Return on average tangible assets, adjusted(2) | 1.35% | 0.88% | 0.71% | 1.27% | 0.80% |
| Return on average equity | 10.79% | (7.26)% | 5.21% | 9.02% | 6.06% |
| Return on average tangible common equity(2) | 13.39% | (7.41)% | 6.43% | 11.36% | 7.41% |
| Return on average tangible common equity, adjusted(2) | 13.39% | 8.41% | 6.62% | 12.94% | 7.53% |
| Loans to deposits ratio (end of period) | 84.64% | 79.88% | 79.07% | 84.64% | 79.07% |
| Non-interest bearing deposits to total deposits (end of period) | 23.62% | 22.68% | 23.08% | 23.62% | 23.08% |
| Net interest margin(4) | 3.87% | 3.26% | 3.46% | 3.83% | 3.40% |
| Net interest margin FTE(2)(4)(10) | 3.96% | 3.41% | 3.60% | 3.92% | 3.53% |
| Interest rate spread FTE(5)(10) | 3.78% | 3.24% | 3.45% | 3.76% | 3.39% |
| Yield on earning assets(3) | 4.35% | 3.70% | 3.89% | 4.27% | 3.81% |
| Yield on earning assets FTE(2)(3)(10) | 4.43% | 3.84% | 4.03% | 4.35% | 3.94% |
| Cost of interest bearing liabilities(3) | 0.65% | 0.60% | 0.58% | 0.59% | 0.54% |
| Cost of deposits | 0.47% | 0.44% | 0.42% | 0.43% | 0.41% |
| Non-interest income to total revenue FTE | 26.19% | 18.71% | 19.50% | 26.98% | 20.99% |
| Non-interest expense to average assets | 3.16% | 2.79% | 2.93% | 3.50% | 2.95% |
| | 3.16% | 2.58% | 2.89% | 3.31% | 2.93% |

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| | | | | | |
|--|---------|---------|---------|---------|---------|
| Non-interest expense to average assets, adjusted Efficiency ratio | | | | | |
| FTE(2)(6)(10) | 63.69% | 69.08% | 67.87% | 70.38% | 68.48% |
| Efficiency ratio FTE, adjusted for acquisition-related costs(2)(6)(10) | 63.69% | 64.15% | 67.07% | 66.51% | 68.00% |
| Originated and Acquired Loans Asset Quality Data(7)(8)(9) | | | | | |
| Non-performing loans to total originated and acquired loans | 0.64% | 0.69% | 0.64% | 0.64% | 0.64% |
| Allowance for loan losses to total originated and acquired loans | 0.88% | 1.02% | 1.01% | 0.88% | 1.01% |
| Allowance for loan losses to non-performing loans | 137.40% | 148.54% | 156.85% | 137.40% | 156.85% |
| Net (recoveries) charge-offs to average loans(1) | (0.08)% | 0.27% | 1.18% | 0.00% | 0.41% |
| Total Loans Asset Quality Data(7)(8)(9) | | | | | |
| Non-performing loans to total loans | 0.63% | 0.66% | 0.61% | 0.63% | 0.61% |
| Non-performing assets to total loans and OREO | 1.51% | 0.99% | 1.01% | 1.51% | 1.01% |
| Allowance for loan losses to total loans | 0.87% | 0.98% | 0.96% | 0.87% | 0.96% |
| Allowance for loan losses to non-performing loans | 138.25% | 148.88% | 156.85% | 138.25% | 156.85% |
| Net (recoveries) charge-offs to average loans(1) | (0.08)% | 0.26% | 1.13% | 0.01% | 0.39% |

- (1) Ratios are annualized.
- (2) Ratio represents non-GAAP financial measure. See non-GAAP reconciliation below.
- (3) Interest earning assets include assets that earn interest/accretion or dividends. Any market value adjustments on investment securities are excluded from interest earning assets. Interest bearing liabilities include liabilities that must be paid interest.
- (4) Net interest margin represents net interest income, including accretion income on interest earning assets, as a percentage of average interest earning assets.
- (5) Interest rate spread represents the difference between the weighted average yield on interest earning assets and the weighted average cost of interest bearing liabilities.
- (6) The efficiency ratio represents non-interest expense, less intangible asset amortization, as a percentage of net interest income on a FTE basis plus non-interest income.
- (7) Non-performing loans consist of non-accruing loans and restructured loans on non-accrual, but exclude any loans accounted for under ASC 310-30 in which the pool is still performing. These ratios may, therefore, not be comparable to similar ratios of our peers.
- (8) Non-performing assets include non-performing loans, other real estate owned and other repossessed assets.

- (9) Total loans are net of unearned discounts and fees.
- (10) Presented on a fully taxable equivalent basis using the statutory rate of 21%, 35% and 35% for the three months ended September 30, 2018, December 31, 2017 and September 30, 2017, respectively. The taxable equivalent adjustments included above are \$1,126, \$1,676 and \$1,518 for the three months ended September 30, 2018, December 31, 2017 and September 30, 2017, respectively. The taxable equivalent adjustments included above are \$3,288 and \$4,176 for the nine months ended September 20, 2018 and September 30, 2017, respectively.

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About Non-GAAP Financial Measures

Certain of the financial measures and ratios we present, including “tangible assets,” “return on average tangible assets,” “return on average tangible common equity,” “tangible common book value,” “tangible common book value per share,” “tangible common equity,” “tangible common equity to tangible assets,” “adjusted net income,” “adjusted earnings per share,” “adjusted non-interest expense to average assets,” “adjusted return on average tangible assets,” “adjusted return on average tangible common equity,” “adjusted efficiency ratio” and “fully taxable equivalent (“FTE”)” metrics are supplemental measures that are not required by, or are not presented in accordance with, U.S. generally accepted accounting principles. We refer to these financial measures and ratios as “non-GAAP financial measures.” We consider the use of select non-GAAP financial measures and ratios to be useful for financial and operational decision making and useful in evaluating period-to-period comparisons. We believe that these non-GAAP financial measures provide meaningful supplemental information regarding our performance by excluding certain expenditures or assets that we believe are not indicative of our primary business operating results or by presenting certain metrics on a FTE basis. We believe that management and investors benefit from referring to these non-GAAP financial measures in assessing our performance and when planning, forecasting, analyzing and comparing past, present and future periods.

These non-GAAP financial measures should not be considered a substitute for financial information presented in accordance with GAAP, and you should not rely on non-GAAP financial measures alone as measures of our performance. The non-GAAP financial measures we present may differ from non-GAAP financial measures used by our peers or other companies. We compensate for these limitations by providing the equivalent GAAP measures whenever we present the non-GAAP financial measures and by including a reconciliation of the impact of the components adjusted for in the non-GAAP financial measure so that both measures and the individual components may be considered when analyzing our performance.

A reconciliation of our GAAP financial measures to the comparable non-GAAP financial measures is as follows.

Tangible Common Book Value Ratios

| | September 30, 2018 | December 31, 2017 | September 30, 2017 |
|--|-----------------------|----------------------|-----------------------|
| Total shareholders' equity | \$ 673,065 | \$ 532,407 | \$ 550,244 |
| Less: goodwill and core deposit intangible assets, net | (125,294) | (61,237) | (62,470) |
| Add: deferred tax liability related to goodwill | 7,098 | 10,873 | 10,485 |
| Tangible common equity (non-GAAP) | \$ 554,869 | \$ 482,043 | \$ 498,259 |

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| | | | |
|---|--------------|--------------|--------------|
| Total assets | \$ 5,585,104 | \$ 4,843,465 | \$ 4,768,972 |
| Less: goodwill and core deposit intangible assets, net | (125,294) | (61,237) | (62,470) |
| Add: deferred tax liability related to goodwill | 7,098 | 10,873 | 10,485 |
| Tangible assets (non-GAAP) | \$ 5,466,908 | \$ 4,793,101 | \$ 4,716,987 |
| Tangible common equity to tangible assets calculations: | | | |
| Total shareholders' equity to total assets | 12.05% | 10.99% | 11.54% |
| Less: impact of goodwill and core deposit intangible assets, net | (1.90)% | (0.93)% | (0.98)% |
| Tangible common equity to tangible assets (non-GAAP) | 10.15% | 10.06% | 10.56% |
| Tangible common book value per share calculations: | | | |
| Tangible common equity (non-GAAP) | \$ 554,869 | \$ 482,043 | \$ 498,259 |
| Divided by: ending shares outstanding | 30,759,595 | 26,875,585 | 26,802,964 |
| Tangible common book value per share (non-GAAP) | \$ 18.04 | \$ 17.94 | \$ 18.59 |
| Tangible common book value per share, excluding accumulated other comprehensive income (AOCI) calculations: | | | |
| Tangible common equity (non-GAAP) | \$ 554,869 | \$ 482,043 | \$ 498,259 |
| Accumulated other comprehensive loss, net of tax | 20,214 | 6,242 | 1,335 |
| Tangible common book value, excluding AOCI, net of tax (non-GAAP) | 575,083 | 488,285 | 499,594 |
| Divided by: ending shares outstanding | 30,759,595 | 26,875,585 | 26,802,964 |
| Tangible common book value per share, excluding AOCI, net of tax (non-GAAP) | \$ 18.70 | \$ 18.17 | \$ 18.64 |

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Return on Average Tangible Assets and Return on Average Tangible Equity

| | As of and for the three months ended | | | As of and for the nine months ended | |
|---|--------------------------------------|-------------------|--------------------|-------------------------------------|--------------------|
| | September 30, 2018 | December 31, 2017 | September 30, 2017 | September 30, 2018 | September 30, 2017 |
| Net income (loss) | \$ 18,240 | \$ (10,119) | \$ 7,231 | \$ 44,216 | \$ 24,698 |
| Add: impact of core deposit intangible amortization expense, after tax | 388 | 752 | 836 | 1,381 | 2,507 |
| Net income (loss) adjusted for impact of core deposit intangible amortization expense, after tax | \$ 18,628 | \$ (9,367) | \$ 8,067 | \$ 45,597 | \$ 27,205 |
| Average assets | \$ 5,576,320 | \$ 4,845,738 | \$ 4,690,283 | \$ 5,603,179 | \$ 4,657,894 |
| Less: average goodwill and core deposit intangible asset, net of deferred tax liability related to goodwill | (118,435) | (50,945) | (52,665) | (119,040) | (54,024) |
| Average tangible assets (non-GAAP) | \$ 5,457,885 | \$ 4,794,793 | \$ 4,637,618 | \$ 5,484,139 | \$ 4,603,870 |
| Average shareholders' equity | \$ 670,515 | \$ 552,810 | \$ 550,758 | \$ 655,577 | \$ 544,662 |
| Less: average goodwill and core deposit intangible asset, net of deferred tax liability related to goodwill | (118,435) | (50,945) | (52,665) | (119,040) | (54,024) |
| Average tangible common equity (non-GAAP) | \$ 552,080 | \$ 501,865 | \$ 498,093 | \$ 536,537 | \$ 490,638 |
| Return on average assets | 1.30% | (0.83)% | 0.61% | 1.06% | 0.71% |
| Return on average tangible assets (non-GAAP) | 1.35% | (0.78)% | 0.69% | 1.11% | 0.79% |
| Return on average equity | 10.79% | (7.26)% | 5.21% | 9.02% | 6.06% |
| Return on average tangible common equity (non-GAAP) | 13.39% | (7.41)% | 6.43% | 11.36% | 7.41% |

Fully Taxable Equivalent Yield on Earning Assets and Net Interest Margin

| | As of and for the three months ended | As of and for the nine months ended |
|--|--------------------------------------|-------------------------------------|
|--|--------------------------------------|-------------------------------------|

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| | September 30, 2018 | December 31, 2017 | September 30, 2017 | September 30, 2018 | September 30, 2017 |
|---|-----------------------|----------------------|-----------------------|-----------------------|-----------------------|
| Interest income | \$ 55,909 | \$ 41,889 | \$ 42,579 | \$ 163,611 | \$ 122,652 |
| Add: impact of taxable equivalent adjustment | 1,126 | 1,676 | 1,518 | 3,288 | 4,176 |
| Interest income FTE (non-GAAP) | \$ 57,035 | \$ 43,565 | \$ 44,097 | \$ 166,899 | \$ 126,828 |
| Net interest income | \$ 49,772 | \$ 36,913 | \$ 37,898 | \$ 146,805 | \$ 109,513 |
| Add: impact of taxable equivalent adjustment | 1,126 | 1,676 | 1,518 | 3,288 | 4,176 |
| Net interest income FTE (non-GAAP) | \$ 50,898 | \$ 38,589 | \$ 39,416 | \$ 150,093 | \$ 113,689 |
| Average earning assets | \$ 5,104,137 | \$ 4,495,651 | \$ 4,344,374 | \$ 5,124,538 | \$ 4,305,354 |
| Yield on earning assets | 4.35% | 3.70% | 3.89% | 4.27% | 3.81% |
| Yield on earning assets FTE (non-GAAP) | 4.43% | 3.84% | 4.03% | 4.35% | 3.94% |
| Net interest margin | 3.87% | 3.26% | 3.46% | 3.83% | 3.40% |
| Net interest margin FTE (non-GAAP) | 3.96% | 3.41% | 3.60% | 3.92% | 3.53% |

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Adjusted Financial Results

| | As of and for the three months ended | | | As of and for the nine months ended | |
|--|--------------------------------------|------------------|--------------------|-------------------------------------|--------------------|
| | September 30, 2018 | October 31, 2018 | September 30, 2018 | September 30, 2018 | September 30, 2017 |
| Adjustments to net income (loss): | | | | | |
| Net income (loss) | \$ 18,240 | \$ (10,119) | \$ 7,231 | \$ 44,216 | \$ 24,698 |
| Adjustments (non-GAAP)(1) | — | 20,002 | 245 | 6,321 | 432 |
| Adjusted net income (non-GAAP) | \$ 18,240 | \$ 9,883 | \$ 7,476 | 50,537 | \$ 25,130 |
| Adjustments to earnings (loss) per share: | | | | | |
| Earnings (loss) per share | \$ 0.58 | \$ (0.37) | \$ 0.26 | \$ 1.41 | \$ 0.89 |
| Adjustments (non-GAAP)(1) | — | 0.73 | 0.01 | 0.20 | 0.02 |
| Adjusted earnings per share - diluted (non-GAAP)(1) | \$ 0.58 | \$ 0.36 | \$ 0.27 | \$ 1.61 | \$ 0.91 |
| Adjustments to return on average tangible assets: | | | | | |
| Adjusted net income (non-GAAP)(1) | \$ 18,240 | \$ 9,883 | \$ 7,476 | \$ 50,537 | \$ 25,130 |
| Add: impact of core deposit intangible amortization expense, after tax | 388 | 752 | 836 | 1,381 | 2,507 |
| Net income adjusted for impact of core deposit intangible amortization expense, after tax(1) | 18,628 | 10,635 | 8,312 | 51,918 | 27,637 |
| Average tangible assets (non-GAAP) | 5,457,885 | 4,794,793 | 4,637,618 | 5,484,139 | 4,603,870 |
| Adjusted return on average tangible assets (non-GAAP) | 1.35% | 0.88% | 0.71% | 1.27% | 0.80% |
| Adjustments to return on average tangible common equity: | | | | | |
| Net income adjusted for impact of core deposit intangible amortization expense, after tax(1) | \$ 18,628 | \$ 10,635 | \$ 8,312 | \$ 51,918 | \$ 27,637 |
| Average tangible common equity (non-GAAP) | 552,080 | 501,865 | 498,093 | 536,537 | 490,638 |
| Adjusted return on average tangible common equity | 13.39% | 8.41% | 6.62% | 12.94% | 7.53% |

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(non-GAAP)

Adjustments to non-interest expense:

| | | | | | |
|---|-----------|-----------|-----------|------------|------------|
| Non-interest expense | \$ 44,432 | \$ 34,028 | \$ 34,605 | \$ 146,477 | \$ 102,650 |
| Adjustments (non-GAAP)(1) | — | 2,492 | 392 | 7,957 | 690 |
| Adjusted non-interest expense (non-GAAP) | 44,432 | 31,536 | 34,213 | 138,520 | 101,960 |
| Non-interest expense to average assets, adjusted (non-GAAP) | 3.16% | 2.58% | 2.89% | 3.31% | 2.93% |

Adjustments to efficiency ratio

| | | | | | |
|--|--------|----------|--------|----------|--------|
| Efficiency ratio, FTE | 63.69% | 69.08% | 67.87% | 70.38% | 68.48% |
| Adjustments (non-GAAP)(1) | \$ — | \$ 2,492 | \$ 392 | \$ 7,957 | \$ 690 |
| Efficiency ratio FTE, adjusted for acquisition costs | 63.69% | 64.15% | 67.07% | 66.51% | 68.00% |

(1) Adjustments:

Non-interest expense adjustments:

| | | | | | |
|--------------------------------------|------|-----------|--------|----------|--------|
| Acquisition-related | \$ — | \$ 2,001 | \$ 392 | \$ 7,957 | 690 |
| Bonus accrual | — | 491 | — | — | — |
| Total pre-tax adjustments (non-GAAP) | — | 2,492 | 392 | 7,957 | 690 |
| Collective tax expense impact | — | (947) | (147) | (1,636) | (258) |
| Deferred tax asset re-measurement | — | 18,457 | — | — | — |
| Adjustments (non-GAAP) | \$ — | \$ 20,002 | \$ 245 | \$ 6,321 | \$ 432 |

Application of Critical Accounting Policies

We use accounting principles and methods that conform to GAAP and general banking practices. We are required to apply significant judgment and make material estimates in the preparation of our financial statements and with regard to various accounting, reporting and disclosure matters. Assumptions and estimates are required to apply these principles where actual measurement is not possible or practical. The most significant of these estimates relate to the accounting for acquired loans and the determination of the ALL. These critical accounting policies and estimates are summarized in the sections captioned “Application of Critical Accounting Policies” in Management's Discussion and Analysis in our 2017 Annual Report on Form 10-K, and are further analyzed with other significant accounting policies in note 2, “Summary of Significant Accounting Policies” in the notes to our consolidated financial statements for the year ended December 31, 2017.

Financial Condition

Total assets increased to \$5.6 billion at September 30, 2018 from \$4.8 billion at December 31, 2017. Total loans were \$3.9 billion at September 30, 2018 and grew \$726.4 million from December 31, 2017, driven by the Peoples acquisition and originated loan growth.

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Originated loans grew 16.8% annualized as strong growth in commercial loans of 31.1% annualized was partially offset by scheduled payoffs of non-owner occupied commercial real estate loans. The 310-30 loan portfolio declined \$45.7 million, or 37.9%, from December 31, 2017. Cash and cash equivalents totaled \$111.5 million and decreased \$145.9 million, or 56.7%, from December 31, 2017 due to cash held for the Peoples acquisition at December 31, 2017 and cash used to fund loan growth. The investment securities portfolio decreased \$68.1 million, or 6.1%, to \$1.0 billion at September 30, 2018, due paydowns within the portfolio. OREO increased \$24.6 million due to the transfer of one large acquired 310-30 problem loan to OREO as part of the asset resolution process. During the nine months ended September 30, 2018 transaction deposits increased \$632.9 million, or 22.1%, driven by the Peoples acquisition. Time deposits increased \$1.6 million, or 0.1%.

Investment Securities

Available-for-sale

Total investment securities available-for-sale were \$796.5 million at September 30, 2018 and \$855.3 million at December 31, 2017, a decrease of \$58.8 million due to paydowns within the portfolio. During the nine months ended September 30, 2018 and 2017, maturities and pay downs of available-for-sale securities totaled \$168.8 million and \$171.3 million, respectively. Purchases of available-for-sale securities during the nine months ended September 30, 2018 and 2017 totaled \$42.2 million and \$98.5 million, respectively.

Our available-for-sale investment securities portfolio is summarized as of the dates indicated:

| | September 30, 2018 | | | | December 31, 2017 | | | |
|--|-----------------------|-----------------------|----------------------|------------------------|-----------------------|-----------------------|----------------------|------------------------|
| | Amortized cost | Fair value | Percent of portfolio | Weighted average yield | Amortized cost | Fair value | Percent of portfolio | Weighted average yield |
| Mortgage-backed securities: | | | | | | | | |
| Residential mortgage pass-through securities issued or guaranteed by U.S. Government agencies or sponsored enterprises | \$ 158,227 667,864 | \$ 156,313 639,038 | 19.6% 80.2% | 2.53% 2.06% | \$ 167,269 702,107 | \$ 168,648 685,230 | 19.8% 80.1% | 2.39% 1.93% |

| | | | | | | | | |
|--|------------|------------|--------|-------|------------|------------|--------|-------|
| Other residential MBS issued or guaranteed by U.S. Government agencies or sponsored enterprises Municipal securities | 739 | 729 | 0.1% | 3.71% | 1,054 | 1,048 | 0.1% | 2.60% |
| Other securities | 469 | 469 | 0.1% | 0.00% | 419 | 419 | 0.0% | 0.00% |
| Total investment securities available-for-sale | \$ 827,299 | \$ 796,549 | 100.0% | 2.15% | \$ 870,849 | \$ 855,345 | 100.0% | 2.02% |

As of September 30, 2018 and December 31, 2017, generally the entire available-for-sale investment portfolio is backed by mortgages. The residential mortgage pass-through securities portfolio is comprised of both fixed rate and adjustable rate FHLMC, FNMA and GNMA securities. The other mortgage-backed securities are comprised of securities backed by FHLMC, FNMA and GNMA securities.

At September 30, 2018 and December 31, 2017, adjustable rate securities comprised 3.9% and 4.9%, respectively, of the available-for-sale MBS portfolio. The remainder of the portfolio was comprised of fixed rate amortizing securities with 10 to 30 year contractual maturities, with a weighted average coupon of 2.37% per annum and 2.18% per annum at September 30, 2018 and December 31, 2017, respectively.

The available-for-sale investment portfolio included \$31.9 million and \$18.2 million of gross unrealized losses at September 30, 2018 and December 31, 2017, respectively, which were partially offset by \$1.2 million and \$2.7 million of gross unrealized gains at September 30, 2018 and December 31, 2017, respectively. We believe any unrecognized losses are a result of prevailing interest rates, and as such, we do not believe that any of the securities with unrealized losses were other-than-temporarily-impaired.

Held-to-maturity

At September 30, 2018, we held \$249.5 million of held-to-maturity investment securities, compared to \$258.7 million at December 31, 2017, a decrease of \$9.3 million, or 3.6%. During the nine months ended September 30, 2018 and 2017, maturities and pay downs of held-to-maturity securities totaled \$48.3 million and \$55.1 million, respectively. Purchases of held-to-maturity securities during the

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nine months ended September 30, 2018 totaled \$40.7 million. There were no purchases of held-to-maturity securities during the nine months ended September 30, 2017.

Held-to-maturity investment securities are summarized as follows as of the date indicated:

| | September 30, 2018 | | | | December 31, 2017 | | | |
|--|--------------------|------------|----------------------|------------------------|-------------------|------------|----------------------|------------------------|
| | Amortized cost | Fair value | Percent of portfolio | Weighted average yield | Amortized cost | Fair value | Percent of portfolio | Weighted average yield |
| Mortgage-backed securities: | | | | | | | | |
| Residential mortgage pass-through securities issued or guaranteed by U.S. Government agencies or sponsored enterprises | \$ 166,955 | \$ 162,708 | 66.9% | 3.25% | \$ 204,352 | \$ 204,048 | 79.0% | 3.23% |
| Other residential MBS issued or guaranteed by U.S. Government agencies or sponsored enterprises | 82,509 | 79,662 | 33.1% | 2.30% | 54,378 | 52,723 | 21.0% | 1.66% |
| Total investment securities held-to-maturity | \$ 249,464 | \$ 242,370 | 100.0% | 2.93% | \$ 258,730 | \$ 256,771 | 100.0% | 2.90% |

The residential mortgage pass-through and other residential MBS held-to-maturity investment portfolios are comprised of fixed rate FHLMC, FNMA and GNMA securities.

The fair value of the held-to-maturity investment portfolio was \$242.4 million and \$256.8 million, at September 30, 2018 and December 31, 2017, respectively, and included \$7.1 million of unrealized losses and \$2.0 million of net unrealized losses for the respective periods.

Loans Overview

At September 30, 2018, our loan portfolio was comprised of new loans that we have originated and loans that were acquired in connection with our six acquisitions to date. Beginning in the first quarter 2018, loans previously referred to as "non 310-30 loans" are referred to as "originated and acquired loans," which include originated loans and acquired loans not accounted for under ASC 310-30. No amounts were reclassified resulting from this change in terminology.

As discussed in note 5 to our consolidated financial statements, in accordance with applicable accounting guidance, all acquired loans are recorded at fair value at the date of acquisition, and an allowance for loan losses is not carried over with the loans but, rather, the fair value of the loans encompasses both credit quality and contractual interest rate considerations. Loans that exhibit signs of credit deterioration at the date of acquisition are accounted for in accordance with the provisions of ASC 310-30.

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The table below shows the loan portfolio composition at the respective dates:

| | September 30, 2018 | December 31, 2017 | September 30, 2018 vs. December 31, 2017 % Change |
|---|--------------------|-------------------|---|
| Originated: | | | |
| Commercial: | | | |
| Commercial and industrial | \$ 1,693,456 | \$ 1,375,028 | 23.2% |
| Owner-occupied commercial real estate | 313,711 | 264,357 | 18.7% |
| Agriculture | 207,990 | 135,397 | 53.6% |
| Energy | 42,620 | 57,460 | (25.8)% |
| Total commercial | 2,257,777 | 1,832,242 | 23.2% |
| Commercial real estate non-owner occupied | 407,786 | 464,121 | (12.1)% |
| Residential real estate | 635,360 | 633,578 | 0.3% |
| Consumer | 24,246 | 23,398 | 3.6% |
| Total originated | 3,325,169 | 2,953,339 | 12.6% |
| Acquired: | | | |
| Commercial: | | | |
| Commercial and industrial | 61,150 | 994 | 6,051.9% |
| Owner-occupied commercial real estate | 94,990 | 8,396 | 1,031.4% |
| Agriculture | 5,916 | 3,498 | 69.1% |
| Total commercial | 162,056 | 12,888 | 1,157.4% |
| Commercial real estate non-owner occupied | 161,615 | 21,020 | 668.9% |
| Residential real estate | 179,146 | 69,900 | 156.3% |
| Consumer | 2,404 | 1,177 | 104.2% |
| Total acquired | 505,221 | 104,985 | 381.2% |
| ASC 310-30 loans | 74,921 | 120,623 | (37.9)% |
| Total loans | \$ 3,905,311 | \$ 3,178,947 | 22.8% |

The table below shows the originated and acquired loans by loan segment at the respective dates:

| | September 30, 2018 | December 31, 2017 | September 30, 2018 vs. December 31, 2017 % Change |
|---|--------------------|-------------------|---|
| Commercial | \$ 2,419,833 | \$ 1,845,130 | 31.1% |
| Commercial real estate non-owner occupied | 569,401 | 485,141 | 17.4% |
| Residential real estate | 814,506 | 703,478 | 15.8% |
| Consumer | 26,650 | 24,575 | 8.4% |
| Total originated and acquired loans | \$ 3,830,390 | \$ 3,058,324 | 25.2% |

Our loan portfolio totaled \$3.9 billion at September 30, 2018, increasing \$726.4 million, or 22.8%, since December 31, 2017, driven by the Peoples acquisition and originations during the period. Originated loans grew 16.8% annualized as strong growth in commercial loans of 31.1% annualized was partially offset by scheduled payoffs of non-owner occupied commercial real estate loans. The acquired 310-30 loan portfolio declined \$45.7 million, or 37.9%, from December 31, 2017, largely due to the transfer of one large acquired 310-30 problem loan transferred to OREO during the nine months ended September 30, 2018 as part of the asset resolution process.

We have successfully generated new relationships with small to medium-sized businesses and consumers, experiencing particularly strong loan growth in our commercial and industrial portfolio, which at September 30, 2018, was comprised of diverse industry segments. These segments included government and municipal loans of \$460.9 million, finance and financial services, primarily lender finance loans of \$359.8 million, healthcare-related loans of \$190.5 million, manufacturing-related loans of \$123.4 million and a variety of smaller subcategories of commercial and industrial loans. Originated and acquired agriculture loans totaled \$213.9 million and were 35.5% of the Company's risk-based capital and 5.5% of total loans, and are well-diversified across crop and livestock types.

Originated and acquired non-owner occupied CRE loans were 98.7% of the Company's risk-based capital, or 15.5% of total loans, and no specific property type comprised more than 5.0% of total loans. The Company maintains very little exposure to retail properties, comprising less than 2.3% of total loans. Multi-family loans totaled \$76.1 million, or 1.9% of total loans as of September 30, 2018.

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New loan origination is a direct result of our ability to recruit and retain top banking talent, connect with clients in our markets and provide needed services at competitive rates. Loan originations totaled \$1.1 billion over the past twelve months, led by commercial loan originations of \$822.4 million. Originations are defined as closed end funded loans and revolving lines of credit advances, net of any current period paydowns. Management utilizes this more conservative definition of originations to better approximate the impact of originations on loans outstanding and ultimately net interest income.

The following table represents new loan originations during 2018 and 2017:

| | Third quarter 2018 | Second quarter 2018 | First quarter 2018 | Fourth quarter 2017 | Third quarter 2017 |
|--|--------------------------|---------------------------|-----------------------|---------------------------|--------------------------|
| Commercial: | | | | | |
| Commercial and industrial | \$ 123,440 | \$ 232,643 | \$ 123,984 | \$ 167,699 | \$ 73,917 |
| Owner occupied commercial real estate | 35,549 | 19,009 | 23,576 | 8,937 | 32,787 |
| Agriculture | 23,833 | 38,220 | 25,873 | 14,050 | 3,335 |
| Energy | 5,412 | (929) | (10,778) | (8,121) | (6,993) |
| Total commercial | 188,234 | 288,943 | 162,655 | 182,565 | 103,046 |
| Commercial real estate non-owner occupied | 42,300 | 28,316 | 20,694 | 21,323 | 46,654 |
| Residential real estate | 40,293 | 30,259 | 21,698 | 25,995 | 28,471 |
| Consumer | 3,797 | 3,588 | 3,238 | 1,815 | 3,122 |
| Total | \$ 274,624 | \$ 351,106 | \$ 208,285 | \$ 231,698 | \$ 181,293 |

Included in originations are net fundings under revolving lines of credit of \$34,070, \$151,888, \$59,236, \$65,686 and \$(12,804) as of the third quarter 2018, second quarter 2018, first quarter 2018, fourth quarter 2017 and third quarter 2017, respectively.

The tables below show the contractual maturities of our total loans for the dates indicated:

| | September 30, 2018 | | | Total |
|---------------------------------------|----------------------|-----------------------------------|----------------------|--------------|
| | Due within 1 year | Due after 1 but within 5 years | Due after 5 years | |
| Commercial: | | | | |
| Commercial and industrial | \$ 129,038 | \$ 744,708 | \$ 881,850 | \$ 1,755,596 |
| Owner occupied commercial real estate | 39,591 | 131,640 | 252,228 | 423,459 |

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| | | | | |
|---|------------|--------------|--------------|--------------|
| Agriculture | 37,402 | 152,144 | 30,870 | 220,416 |
| Energy | 12,512 | 30,108 | — | 42,620 |
| Total commercial | 218,543 | 1,058,600 | 1,164,948 | 2,442,091 |
| Commercial real estate non-owner occupied | 79,836 | 369,661 | 161,746 | 611,243 |
| Residential real estate | 26,249 | 62,378 | 736,600 | 825,227 |
| Consumer | 8,943 | 13,868 | 3,939 | 26,750 |
| Total loans | \$ 333,571 | \$ 1,504,507 | \$ 2,067,233 | \$ 3,905,311 |

| | December 31, 2017 | | | |
|---|----------------------|-----------------------------------|----------------------|--------------|
| | Due within 1 year | Due after 1 but within 5 years | Due after 5 years | Total |
| Commercial: | | | | |
| Commercial and industrial | \$ 83,314 | \$ 551,567 | \$ 745,746 | \$ 1,380,627 |
| Owner occupied commercial real estate | 18,044 | 115,421 | 156,306 | 289,771 |
| Agriculture | 14,513 | 102,390 | 29,845 | 146,748 |
| Energy | 25,970 | 31,489 | — | 57,459 |
| Total commercial | 141,841 | 800,867 | 931,897 | 1,874,605 |
| Commercial real estate non-owner occupied | 118,980 | 316,242 | 127,827 | 563,049 |
| Residential real estate | 6,820 | 38,824 | 670,593 | 716,237 |
| Consumer | 5,909 | 15,014 | 4,133 | 25,056 |
| Total loans | \$ 273,550 | \$ 1,170,947 | \$ 1,734,450 | \$ 3,178,947 |

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The stated interest rate (which excludes the effects of non-refundable loan origination and commitment fees, net of costs and the accretion of fair value marks) of originated and acquired loans with maturities over one year is as follows at the dates indicated:

| | September 30, 2018 | | | | | |
|---|--------------------|-----------------------|--------------|-----------------------|--------------|-----------------------|
| | Fixed | | Variable | | Total | |
| | Balance | Weighted average rate | Balance | Weighted average rate | Balance | Weighted average rate |
| Commercial and industrial(1) | \$ 844,233 | 3.69% | \$ 781,703 | 4.73% | \$ 1,625,936 | 4.19% |
| Owner occupied commercial real estate | 181,906 | 4.51% | 190,270 | 4.88% | 372,176 | 4.90% |
| Agriculture | 46,904 | 4.95% | 130,106 | 4.98% | 177,010 | 4.97% |
| Energy | 43 | 4.49% | 30,065 | 4.54% | 30,108 | 4.54% |
| Total commercial | 1,073,086 | 3.96% | 1,132,144 | 4.78% | 2,205,230 | 4.38% |
| Commercial real estate non-owner occupied | 200,831 | 4.56% | 294,313 | 4.87% | 495,144 | 4.74% |
| Residential real estate | 368,819 | 3.54% | 420,120 | 4.46% | 788,939 | 4.03% |
| Consumer | 14,666 | 5.15% | 3,041 | 5.18% | 17,707 | 5.15% |
| Total loans with > 1 year maturity | \$ 1,657,402 | 3.95% | \$ 1,849,618 | 4.72% | \$ 3,507,020 | 4.36% |
| | December 31, 2017 | | | | | |
| | Fixed | | Variable | | Total | |
| | Balance | Weighted average rate | Balance | Weighted average rate | Balance | Weighted average rate |
| Commercial and industrial(1) | \$ 696,224 | 3.34% | \$ 597,253 | 4.14% | \$ 1,293,477 | 3.71% |
| Owner occupied commercial real estate | 125,821 | 4.20% | 133,408 | 4.26% | 259,229 | 4.39% |
| Agriculture | 35,605 | 4.70% | 89,487 | 4.42% | 125,092 | 4.50% |
| Energy | 132 | 4.37% | 31,357 | 4.57% | 31,489 | 4.57% |
| Total commercial | 857,782 | 3.57% | 851,505 | 4.20% | 1,709,287 | 3.89% |
| Commercial real estate non-owner occupied | 161,846 | 4.42% | 237,772 | 4.46% | 399,618 | 4.44% |
| Residential real estate | 372,104 | 3.40% | 325,227 | 3.94% | 697,331 | 3.65% |

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| | | | | | | |
|---------------------------------------|--------------|-------|--------------|-------|--------------|-------|
| Consumer | 15,883 | 4.68% | 2,805 | 4.59% | 18,688 | 4.67% |
| Total loans with > 1 year maturity | \$ 1,407,615 | 3.64% | \$ 1,417,309 | 4.19% | \$ 2,824,924 | 3.91% |

- (1) Included in commercial fixed rate loans are loans totaling \$475,003 and \$417,660 that have been swapped to variable rates at current market pricing at September 30, 2018 and December 31, 2017, respectively. Included in the commercial segment are tax exempt loans totaling \$642,085 and \$617,889 with a weighted average rate of 3.23% and 3.15% at September 30, 2018 and December 31, 2017, respectively.

Accretable Yield

At September 30, 2018, the accretable yield balance was \$39.7 million compared to \$46.6 million at December 31, 2017. We re-measure the expected cash flows quarterly for all 24 remaining loan pools accounted for under ASC 310-30 utilizing the same cash flow methodology used at the time of acquisition. This re-measurement resulted in a net \$8.1 million and \$8.8 million reclassification from non-accretable difference to accretable yield during the nine months ended September 30, 2018 and 2017, respectively.

In addition to the accretable yield on loans accounted for under ASC 310-30, the fair value adjustments on loans outside the scope of ASC 310-30 are also accreted to interest income over the life of the loans. The Peoples acquisition added accretable fair value marks of \$9.8 million on originated and acquired loans. Total remaining accretable yield and fair value mark was as follows for the dates indicated:

| | September 30, 2018 | December 31, 2017 |
|---|--------------------|-------------------|
| Remaining accretable yield on loans accounted for under ASC 310-30 | \$ 39,700 | \$ 46,568 |
| Remaining accretable fair value mark on originated and acquired loans | 9,176 | 1,771 |
| Total remaining accretable yield and fair value mark | \$ 48,876 | \$ 48,339 |

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Asset Quality

Asset quality is fundamental to our success and remains a strong point, driven by our disciplined adherence to our self-imposed concentration limits across industry sector and real estate property type. Accordingly, for the origination of loans, we have established a credit policy that allows for responsive, yet controlled lending with credit approval requirements that are scaled to loan size. Within the scope of the credit policy, each prospective loan is reviewed in order to determine the appropriateness and the adequacy of the loan characteristics and the security or collateral prior to making a loan. We have established underwriting standards and loan origination procedures that require appropriate documentation, including financial data and credit reports. For loans secured by real property, we require property appraisals, title insurance or a title opinion, hazard insurance and flood insurance, in each case where appropriate.

Additionally, we have implemented procedures to timely identify loans that may become problematic in order to ensure the most beneficial resolution to the Company. Asset quality is monitored by our credit risk management department and evaluated based on quantitative and subjective factors such as the timeliness of contractual payments received. Additional factors that are considered, particularly with commercial loans over \$500,000, include the financial condition and liquidity of individual borrowers and guarantors, if any, and the value of our collateral. To facilitate the oversight of asset quality, loans are categorized based on the number of days past due and on an internal risk rating system, and both are discussed in more detail below.

In the event of borrower default, we may seek recovery in compliance with state lending laws, the respective loan agreements, and credit monitoring and remediation procedures that may include modifying or restructuring a loan from its original terms, for economic or legal reasons, to provide a concession to the borrower from their original terms due to borrower financial difficulties in order to facilitate repayment. Such restructured loans are considered TDRs in accordance with ASC 310-40, Troubled Debt Restructurings by Creditors. Under this guidance, modifications to loans that fall within the scope of ASC 310-30 are not considered troubled debt restructurings, regardless of otherwise meeting the definition of a troubled debt restructuring. Assets that have been foreclosed on or acquired through deed-in-lieu of foreclosure are classified as OREO until sold, and are carried at the lower of the related loan balance or the fair value of the collateral less estimated costs to sell, with any initial valuation adjustments charged to the ALL and any subsequent declines in carrying value charged to impairments on OREO.

Non-performing Assets

Non-performing assets consist of non-accrual loans, TDRs on non-accrual, OREO and other repossessed assets. Non-accrual loans and TDRs on non-accrual accounted for under ASC 310-30, as described below, may be excluded from our non-performing assets to the extent that the cash flows of the loan pools are still estimable. Interest income that would have been recorded had non-accrual loans performed in accordance with their original contract terms during the three and nine months ended September 30, 2018 was \$0.3 million and \$1.0 million, respectively, and \$0.5 million and \$1.0 million during the three and nine months ended September 30, 2017, respectively.

All loans accounted for under ASC 310-30 were classified as performing assets at September 30, 2018, as the future cash flows on the loan pools were considered estimable. While individual loans making up the pools may be accounted for on a cost recovery basis, the cash flows on the loan pools are considered estimable and, therefore, interest income, through accretion of the difference between the carrying value of the loans in the pool and the pool's expected future cash flows, is being recognized on all acquired loan pools accounted for under ASC 310-30.

On January 1, 2018, we completed the acquisition of Peoples, adding \$542.7 million in loans to our consolidated statements of financial condition. As a result, originated and acquired special mention loans increased by \$16.1 million from December 31, 2017 to September 30, 2018, with the additions from Peoples partially offset by upgrades within the agriculture sector. Originated and acquired substandard loans increased during the same period by \$16.2 million with the addition from Peoples partially offset by upgrades to pass within the multi-family sector, as well as paydowns of other substandard loans. Despite the increases in these categories from the acquisition of Peoples, the ratios of criticized loans and classified loans to total originated and acquired loans have trended positively since the acquisition. Additionally, the loans added for the Peoples acquisition included \$4.7 million of non-accrual loans and \$0.5 million of loans 90 days or more past due and still accruing interest as of January 1, 2018, which represented 0.9% and 0.1% of Peoples acquired loans as of that date, respectively.

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The following table sets forth the non-performing assets as of the dates presented:

| | September 30, 2018 | December 31, 2017 |
|---|--------------------|-------------------|
| Non-accrual loans: | | |
| Commercial: | | |
| Commercial and industrial | \$ 4,993 | \$ 3,747 |
| Owner occupied commercial real estate | 6,745 | 3,336 |
| Agriculture | 773 | 2,003 |
| Energy | — | — |
| Total commercial | 12,511 | 9,086 |
| Commercial real estate non-owner occupied | 1,792 | 784 |
| Residential real estate | 6,338 | 3,846 |
| Consumer | 45 | 29 |
| Total non-accrual loans, excluding restructured loans | 20,686 | 13,745 |
| Restructured loans on non-accrual: | | |
| Commercial: | | |
| Commercial and industrial | 958 | 4,020 |
| Owner occupied commercial real estate | 282 | 143 |
| Agriculture | — | — |
| Energy | 848 | 1,645 |
| Total commercial | 2,088 | 5,808 |
| Commercial real estate non-owner occupied | — | — |
| Residential real estate | 1,684 | 1,336 |
| Consumer | — | 111 |
| Total restructured loans on non-accrual | 3,772 | 7,255 |
| Total non-performing loans | 24,458 | 21,000 |
| OREO | 35,135 | 10,491 |
| Total non-performing assets | \$ 59,593 | \$ 31,491 |
| Loans 90 days or more past due and still accruing interest | \$ 560 | \$ 150 |
| Accruing restructured loans | \$ 7,770 | \$ 8,461 |
| ALL | \$ 33,813 | \$ 31,264 |
| Total non-performing loans to total loans | 0.63% | 0.66% |
| Loans 90 days or more past due and still accruing interest to total loans | 0.01% | 0.00% |
| Total non-performing assets to total loans and OREO | 1.51% | 0.99% |
| ALL to non-performing loans | 138.25% | 148.88% |

During the nine months ended September 30, 2018, total non-performing loans increased \$3.5 million, or 16.5%, from December 31, 2017 due to acquired Peoples loans, partially offset by one previously identified commercial and industrial loan placed back on accrual during the first quarter of 2018 as well as paydowns during the period. During the nine months ended September 30, 2018, accruing TDRs decreased \$0.7 million.

The Peoples acquisition added \$1.4 million of OREO at January 1, 2018. During the nine months ended September 30, 2018, the Company transferred one large acquired 310-30 problem loan totaling \$24.1 million from 310-30 loans

to OREO as part of the asset resolution process. During the nine months ended September 30, 2018, \$1.7 million of OREO was sold resulting in a net gain of \$0.4 million while OREO write-downs were \$0.2 million. Total non-performing assets to total loans and OREO was 1.51% and 0.99% at September 30, 2018 and December 31, 2017, respectively. Included in this ratio at September 30, 2018 are acquired non-performing loans and OREO of 0.45% compared to 0.46% at December 31, 2017. Excluding OREO transferred from 310-30 loans, total non-performing assets to total loans and OREO was 0.76% at September 30, 2018.

Past Due Loans

Past due status is monitored as an indicator of credit deterioration. Loans are considered past due or delinquent when the contractual principal or interest due in accordance with the terms of the loan agreement remains unpaid after the due date of the scheduled payment. Originated and acquired loans that are 90 days or more past due and are put on non-accrual status unless the loan is well secured and in the process of collection.

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The table below shows the past due status of originated and acquired loans, based on contractual terms of the loans as of September 30, 2018 and December 31, 2017:

| | September 30, 2018 | December 31, 2017 |
|---|--------------------|-------------------|
| Loans 30-89 days past due and still accruing interest | \$ 7,915 | \$ 3,681 |
| Loans 90 days past due and still accruing interest | 560 | 150 |
| Non-accrual loans | 24,458 | 21,000 |
| Total past due and non-accrual loans | \$ 32,933 | \$ 24,831 |
| Total 90 days past due and still accruing interest and non-accrual loans to total originated and acquired loans | 0.65% | 0.69% |
| Total non-accrual loans to total originated and acquired loans | 0.64% | 0.69% |

Loans 30-89 days past due and still accruing interest increased \$4.2 million from December 31, 2017 to September 30, 2018, and loans 90 days or more past due and still accruing interest increased \$0.4 million from December 31, 2017 to September 30, 2018, for a collective increase in total past due loans of \$4.6 million, primarily due to the Peoples acquisition. Non-accrual loans increased \$3.5 million at September 30, 2018 compared to December 31, 2017, further described within the Non-Performing Assets discussion of Management's Discussion and Analysis. There were no ASC 310-30 loan pools past due or on non-accrual at September 30, 2018.

Allowance for Loan Losses

The ALL represents the amount that we believe is necessary to absorb probable losses inherent in the loan portfolio at the balance sheet date and involves a high degree of judgment and complexity. Determination of the ALL is based on an evaluation of the collectability of loans, the realizable value of underlying collateral, economic conditions, historical net loan losses, the estimated loss emergence period, estimated default rates, any declines in cash flow assumptions from acquisition, loan structures, growth factors and other elements that warrant recognition and, to the extent applicable, prior loss experience. The ALL is critical to the portrayal and understanding of our financial condition, liquidity and results of operations. The determination and application of the ALL accounting policy involves judgments, estimates, and uncertainties that are subject to change. Changes in these assumptions, estimates or the conditions surrounding them may have a material impact on our financial condition, liquidity or results of operations.

In accordance with the applicable guidance for business combinations, acquired loans were recorded at their acquisition date fair values, which were based on expected future cash flows and included an estimate for future loan losses; therefore, no ALL was recorded as of the acquisition date. Any estimated losses on acquired loans that arise after the acquisition date are reflected in a charge to the provision for loan losses in the consolidated statements of operations.

310-30 ALL

Loans accounted for under the accounting guidance provided in ASC 310-30 have been grouped into pools based on the predominant risk characteristics of purpose and/or type of loan. The timing and receipt of expected principal, interest and any other cash flows of these loans are periodically remeasured and the expected future cash flows of the collective pools are compared to the carrying value of the pools. To the extent that the expected future cash flows of each pool is less than the book value of the pool, an allowance for loan losses will be established through a charge to the provision for loan losses. If the remeasured expected future cash flows are greater than the book value of the pools, then the improvement in the expected future cash flows is accreted into interest income over the remaining expected life of the loan pool. During the nine months ended September 30, 2018 and 2017, these re-measurements resulted in overall increases in expected cash flows in certain loan pools, which, absent previous valuation allowances within the same pool, are reflected in increased accretion as well as an increased amount of accretable yield and are recognized over the expected remaining lives of the underlying loans as an adjustment to yield.

During the three and nine months ended September 30, 2018, loans accounted for under ASC 310-30 had provision of \$6 thousand and \$197 thousand, respectively. During the three and nine months ended September 30, 2017, loans accounted for under ASC 310-30 had \$142 thousand and \$255 thousand of recoupment, respectively.

Originated and Acquired ALL

For all originated and acquired loans, the determination of the ALL follows a process to determine the appropriate level of ALL that is designed to account for changes in credit quality and other risk factors. This process provides an ALL consisting of a specific

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allowance component based on certain individually evaluated loans and a general allowance component based on estimates of reserves needed for all other loans, segmented based on similar risk characteristics.

Impaired loans less than \$250,000 are included in the general allowance population. Impaired loans over \$250,000 are subject to individual evaluation on a regular basis to determine the need, if any, to allocate a specific reserve to the impaired loan. Typically, these loans consist of commercial, commercial real estate and agriculture loans and exclude homogeneous loans such as residential real estate and consumer loans. Specific allowances are determined by collectively analyzing:

- the borrower's resources, ability, and willingness to repay in accordance with the terms of the loan agreement;
- the likelihood of receiving financial support from any guarantors;
- the adequacy and present value of future cash flows, less disposal costs, of any collateral;
- the impact current economic conditions may have on the borrower's financial condition and liquidity or the value of the collateral.

In evaluating the loan portfolio for an appropriate ALL level, unimpaired loans are grouped into segments based on broad characteristics such as primary use and underlying collateral. We have identified four primary loan segments that are further stratified into eleven loan classes to provide more granularity in analyzing loss history and to allow for more definitive qualitative adjustments based upon specific factors affecting each loan class. Following are the loan classes within each of the four primary loan segments:

| | | | |
|---------------------------------------|-----------------------------|-------------------------|----------------|
| Commercial | Non-owner occupied | | |
| Commercial and industrial | commercial real estate | Residential real estate | Consumer |
| Owner occupied commercial real estate | Construction | Senior lien | Total Consumer |
| Agriculture | Acquisition and development | Junior lien | |
| Energy | Multifamily | | |
| | Non-owner occupied | | |

Appropriate ALL levels are determined by segment and class utilizing risk ratings, loss history, peer loss history and qualitative adjustments. The qualitative adjustments consider the following risk factors:

- economic/external conditions;
- loan administration, loan structure and procedures;
- risk tolerance/experience;
- loan growth;
- trends;

concentrations; and
other.

Management derives an estimated annual loss rate adjusted for an estimated loss emergence period based on historical loss data categorized by segment and class. The loss rates are applied at the loan segment and class level. Our historical loss history began in 2012, resulting in minimal losses in our originated portfolio. In order to address this lack of historical data, we incorporate not only our own historical loss rates since the beginning of 2012, but we also utilize peer historical loss data, including a historical average net charge-off ratio on each loan type, relying on the Uniform Bank Performance Reports compiled by the Federal Financial Institutions Examinations Council (“FFIEC”). We may also apply a long-term estimated loss rate to pass rated credits as necessary to account for inherent risks to the portfolio. For originated loans, we assign a slightly higher portion of our loss history, but still rely on the peer loss history to account for our limited historical data. For acquired loans, we use solely our internal loss history as those loans are more seasoned and more of the actual losses in the portfolio have been from the acquired portfolio.

The collective resulting ALL for originated and acquired loans is calculated as the sum of the specific reserves and the general reserves. While these amounts are calculated by individual loan or segment and class, the entire ALL is available for any loan that, in our judgment, should be charged-off.

During the three and nine months ended September 30, 2018, we recorded \$0.8 million and \$2.5 million, respectively, of provision for loan losses for originated and acquired loans, for general reserves on loan growth. For originated and acquired loans the Company recorded net recoveries of \$0.8 million during the three months ended September 30, 2018 and net charge-offs of \$0.1 million. Specific reserves on impaired loans totaled \$1.5 million and \$1.5 million at September 30, 2018 and December 31, 2017, respectively.

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During the three and nine months ended September 30, 2017, we recorded \$4.0 million and \$9.9 million, respectively, of provision for loan losses for originated and acquired loans. The three months ended September 30, 2017 provision for loan losses included \$2.9 million related to one non-accrual energy loan and general reserves on net loan growth. The nine months ended September 30, 2017 provision included \$6.3 million of specific reserves on two previously identified energy loans and one previously identified commercial and industrial loan. The remaining provision for the nine months ended September 30, 2017 was for general reserves on loan growth. Net charge-offs for originated and acquired loans during the three and nine months ended September 30, 2017 totaled \$8.8 million and \$8.8 million, respectively, and were related to the loan relationships discussed above. Specific reserves on impaired loans totaled \$1.1 million at September 30, 2017.

Total ALL

After considering the above-mentioned factors, we believe that the ALL of \$33.8 million is adequate to cover probable losses inherent in the loan portfolio at September 30, 2018. However, it is likely that future adjustments to the ALL will be necessary and any changes to the assumptions, circumstances or estimates used in determining the ALL could adversely affect the Company's results of operations, liquidity or financial condition.

The following table presents, by class stratification, the changes in the ALL during the three months ended September 30, 2018 and 2017:

| | September 30, 2018 | | | September 30, 2017 | | |
|--|-------------------------------------|------------------------|-----------|-------------------------------------|------------------------|-----------|
| | Originated and acquired loans | ASC 310-30 loans | Total | Originated and acquired loans | ASC 310-30 loans | Total |
| Beginning allowance for loan losses | \$ 32,029 | \$ 201 | \$ 32,230 | \$ 34,817 | \$ 142 | \$ 34,959 |
| Charge-offs: | | | | | | |
| Commercial | — | — | — | (8,618) | — | (8,618) |
| Commercial real estate non owner-occupied | — | — | — | — | — | — |
| Residential real estate | (13) | — | (13) | (16) | — | (16) |
| Consumer | (381) | — | (381) | (209) | — | (209) |
| Total charge-offs | (394) | — | (394) | (8,843) | — | (8,843) |
| Recoveries | 1,170 | — | 1,170 | 51 | — | 51 |
| Net recoveries (charge-offs) | 776 | — | 776 | (8,792) | — | (8,792) |
| Provision (recoupment) for loan loss | 801 | 6 | 807 | 4,022 | (142) | 3,880 |
| Ending allowance for loan losses | \$ 33,606 | \$ 207 | \$ 33,813 | \$ 30,047 | \$ — | \$ 30,047 |

| | | | | | | |
|---|--------------|-----------|--------------|--------------|------------|--------------|
| Ratio of annualized (recoveries) net charge-offs to average total loans during the period, respectively | (0.08)% | 0.00% | (0.08)% | 1.18% | 0.00% | 1.13% |
| Average total loans outstanding during the period | \$ 3,748,630 | \$ 80,629 | \$ 3,829,259 | \$ 2,967,972 | \$ 127,752 | \$ 3,095,724 |

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The following table presents, by class stratification, the changes in the ALL during the nine months ended September 30, 2018 and 2017:

| | September 30, 2018 | | | September 30, 2017 | | |
|--|-------------------------------------|------------------------|--------------|-------------------------------------|------------------------|--------------|
| | Originated and acquired loans | ASC 310-30 loans | Total | Originated and acquired loans | ASC 310-30 loans | Total |
| Beginning allowance for loan losses | \$ 31,193 | \$ 71 | \$ 31,264 | \$ 28,949 | \$ 225 | \$ 29,174 |
| Charge-offs: | | | | | | |
| Commercial | (437) | (61) | (498) | (8,638) | — | (8,638) |
| Commercial real estate non-owner occupied | (11) | — | (11) | — | — | — |
| Residential real estate | (103) | — | (103) | (26) | — | (26) |
| Consumer | (894) | — | (894) | (510) | — | (510) |
| Total charge-offs | (1,445) | (61) | (1,506) | (9,174) | — | (9,174) |
| Recoveries | 1,335 | — | 1,335 | 347 | — | 347 |
| Net charge-offs | (110) | (61) | (171) | (8,827) | — | (8,827) |
| Provision (recoupment) for loan loss | 2,523 | 197 | 2,720 | 9,925 | (225) | 9,700 |
| Ending allowance for loan losses | \$ 33,606 | \$ 207 | \$ 33,813 | \$ 30,047 | \$ — | \$ 30,047 |
| Ratio of net charge-offs to average total loans during the period, respectively | 0.00% | 0.10% | 0.01% | 0.41% | 0.00% | 0.39% |
| Ratio of ALL to total loans outstanding at period end, respectively | 0.88% | 0.28% | 0.87% | 1.00% | 0.00% | 0.96% |
| Ratio of ALL to total non-performing loans at period end, respectively | 137.40% | 0.00% | 138.25% | 156.84% | 0.00% | 156.84% |
| Total loans | \$ 3,830,389 | \$ 74,922 | \$ 3,905,311 | \$ 2,994,947 | \$ 125,596 | \$ 3,120,543 |
| Average total loans outstanding during the period | \$ 3,673,565 | \$ 79,350 | \$ 3,752,915 | \$ 2,857,579 | \$ 135,485 | \$ 2,993,064 |
| Non-performing loans | \$ 24,458 | \$ — | \$ 24,458 | \$ 19,157 | \$ — | \$ 19,157 |

The following tables present the allocation of the ALL and the percentage of the total amount of loans in each loan category listed as of the dates presented:

September 30, 2018

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| | Total loans | % of total loans | Related ALL | ALL as a % of total ALL |
|---|--------------|------------------|----------------|----------------------------|
| Commercial | \$ 2,442,091 | 62.5% | \$ 25,294 | 74.8% |
| Commercial real estate non-owner occupied | 611,243 | 15.7% | 4,480 | 13.2% |
| Residential real estate | 825,227 | 21.1% | 3,721 | 11.0% |
| Consumer | 26,750 | 0.7% | 318 | 0.9% |
| Total | \$ 3,905,311 | 100.0% | \$ 33,813 | 100.0% |

December 31, 2017

| | Total loans | % of total loans | Related ALL | ALL as a % of total ALL |
|---|--------------|------------------|----------------|----------------------------|
| Commercial | \$ 1,874,605 | 59.0% | \$ 21,385 | 68.4% |
| Commercial real estate non-owner occupied | 563,049 | 17.7% | 5,609 | 17.9% |
| Residential real estate | 716,237 | 22.5% | 3,965 | 12.7% |
| Consumer | 25,056 | 0.8% | 305 | 1.0% |
| Total | \$ 3,178,947 | 100.0% | \$ 31,264 | 100.0% |

The ALL allocated to commercial loans increased to 74.8% at September 30, 2018 from 68.4% at December 31, 2017 due to the provision recorded during the period to support the increase in originated loans.

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Other Assets

Significant components of other assets were as follows as of the dates indicated:

| | September 30, 2018 | December 31, 2017 | Increase (decrease) | |
|--|--------------------|-------------------|---------------------|----------|
| | | | Amount | % Change |
| Bank-owned life insurance | \$ 65,722 | \$ 64,387 | \$ 1,335 | 2.1% |
| Deferred tax asset | 32,172 | 35,630 | (3,458) | (9.7)% |
| Derivative assets | 37,105 | 13,105 | 24,000 | 183.1% |
| Accrued interest on loans | 18,892 | 11,784 | 7,108 | 60.3% |
| Accrued income taxes receivable | 4,525 | 3,992 | 533 | 13.4% |
| Accrued interest on interest bearing bank deposits and investment securities | 2,544 | 2,471 | 73 | 3.0% |
| Other miscellaneous assets | 22,769 | 7,879 | 14,890 | 189.0% |
| Total other assets | \$ 183,730 | \$ 139,248 | \$ 44,482 | 31.9% |

Other assets totaled \$183.7 million and \$139.2 million at September 30, 2018 and December 31, 2017, respectively, representing an increase of \$44.5 million, or 31.9%, during the nine months ended September 30, 2018. Deferred tax asset decreased during the nine months ended September 30, 2018 due to normal activity. Derivative assets and accrued interest on loans increased during the nine months ended September 30, 2018 due to higher volumes of loans related to the Peoples acquisition. Included in other miscellaneous assets at September 30, 2018 is \$10.0 million of restricted cash related to the Peoples acquisition for certain potential liabilities, \$2.5 million of other assets acquired from Peoples and an increase in prepaid assets of \$2.0 million. Refer to note 17 of our consolidated financial statements for further discussion of the derivative asset.

Other Liabilities

Significant components of other liabilities were as follows as of the dates indicated:

| | September 30, 2018 | December 31, 2017 | Increase (decrease) | |
|----------------------------------|--------------------|-------------------|---------------------|----------|
| | | | Amount | % Change |
| Pending loan purchase settlement | \$ 18,986 | \$ 30,181 | \$ (11,195) | (37.1)% |
| Accrued expenses | 18,734 | 16,172 | 2,562 | 15.8% |
| Accrued interest payable | 7,729 | 5,776 | 1,953 | 33.8% |
| Derivative liabilities | 4,838 | 3,758 | 1,080 | 28.7% |

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| | | | | |
|---------------------------------|-----------|-----------|-----------|--------|
| Other miscellaneous liabilities | 47,485 | 15,346 | 32,139 | 209.4% |
| Participant interest in OREO | — | 688 | (688) | 100.0% |
| Total other liabilities | \$ 97,772 | \$ 71,921 | \$ 25,851 | 35.9% |

Other liabilities totaled \$97.8 million and \$71.9 million at September 30, 2018 and December 31, 2017, respectively, representing an increase of \$25.9 million, or 35.9%, during the nine months ended September 30, 2018. Pending loan purchase settlement decreased due to timing of loan settlements. Included in accrued expenses and accrued interest payable at September 30, 2018 is an increase of \$2.5 million from Peoples expenses. Included in other miscellaneous liabilities is an increase in derivative collateral reserves of \$15.6 million, a \$10.0 million contingent liability related to the Peoples acquisition, and a \$3.9 million mortgage repurchase reserve. Refer to note 17 and note 18 of our consolidated financial statements for further discussion of the derivative liability and mortgage repurchase reserve, respectively.

Deposits

Deposits from banking clients serve as a primary funding source for our banking operations and our ability to gather and manage deposit levels is critical to our success. Deposits not only provide a low cost funding source for our loans, but also provide a foundation for the client relationships that are critical to future loan growth.

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The following table presents information regarding our deposit composition at September 30, 2018 and December 31, 2017:

| | September 30, 2018 | | December 31, 2017 | | Increase (decrease) | |
|--------------------------------------|--------------------|--------|-------------------|--------|---------------------|----------|
| | Amount | % | Amount | % | Amount | % Change |
| Non-interest bearing demand deposits | \$ 1,089,631 | 23.6% | \$ 902,439 | 22.7% | \$ 187,192 | 20.7% |
| Interest bearing demand deposits | 675,213 | 14.6% | 474,607 | 11.9% | 200,606 | 42.3% |
| Savings accounts | 548,111 | 11.9% | 472,852 | 11.9% | 75,259 | 15.9% |
| Money market accounts | 1,181,452 | 25.6% | 1,011,611 | 25.4% | 169,841 | 16.8% |
| Total transaction deposits | 3,494,407 | 75.7% | 2,861,509 | 71.9% | 632,898 | 22.1% |
| Time deposits < \$100,000 | 636,468 | 13.8% | 637,789 | 16.0% | (1,321) | (0.2)% |
| Time deposits > \$100,000 | 483,157 | 10.5% | 480,261 | 12.1% | 2,896 | 0.6% |
| Total time deposits | 1,119,625 | 24.3% | 1,118,050 | 28.1% | 1,575 | 0.1% |
| Total deposits | \$ 4,614,032 | 100.0% | \$ 3,979,559 | 100.0% | \$ 634,473 | 15.9% |

The following table shows scheduled maturities of certificates of deposit with denominations greater than or equal to \$100,000 as of September 30, 2018:

| | September 30, 2018 |
|---------------------------------|--------------------|
| Three months or less | \$ 79,152 |
| Over 3 months through 6 months | 71,111 |
| Over 6 months through 12 months | 140,944 |
| Thereafter | 191,951 |
| Total time deposits > \$100,000 | \$ 483,157 |

Total deposits increased \$634.5 million during the nine months ended September 30, 2018, driven by the addition of \$730 million in total deposits from the Peoples acquisition on January 1, 2018 and transaction deposit growth. The mix of transaction deposits (defined as total deposits less time deposits) to total deposits improved to 75.7% at September 30, 2018, from 71.9% at December 31, 2017, due to the Peoples acquisition and our continued focus on developing long-term banking relationships.

At September 30, 2018 and December 31, 2017, time deposits that were scheduled to mature within 12 months totaled \$711.4 million and \$684.6 million, respectively. Of the \$711.4 million in time deposits scheduled to mature within 12 months at September 30, 2018, \$291.2 million were in denominations of \$100,000 or more, and \$420.2 million were in denominations less than \$100,000.

Other Borrowings

As of September 30, 2018 and December 31, 2017, the Company sold securities under agreements to repurchase totaling \$55.7 million and \$130.5 million, respectively. In addition, as a member of the FHLB, the Bank has access to a line of credit and term financing from the FHLB with total available credit of \$1.0 billion at September 30, 2018. At September 30, 2018 and December 31, 2017, the Bank had \$77.3 million and \$129.1 million in term advances from the FHLB, respectively. The term advances have fixed rates between 1.55% - 2.33%, with maturity dates of 2018 - 2020. At September 30, 2018 and December 31, 2017 the Bank had \$67.2 million and \$0.0 million in line of credit advances from the FHLB, respectively.

Results of Operations

Our net income depends largely on net interest income, which is the difference between interest income from interest earning assets and interest expense on interest bearing liabilities. Our results of operations are also affected by provisions for loan losses and non-interest income, such as service charges, bank card income, swap fee income, and gain on sale of mortgages, net. Our primary operating expenses, aside from interest expense, consist of salaries and benefits, occupancy costs, telecommunications data processing and marketing and business development. Any expenses related to the resolution of problem assets are also included in non-interest expense.

Overview of Results of Operations

We recorded net income of \$18.2 million and \$44.2 million, or \$0.58 and \$1.41 per diluted share, during the three and nine months ended September 30, 2018, respectively, compared to net income of \$7.2 million and \$24.7 million, or \$0.26 and \$0.89 per diluted share, during the three and nine months ended September 30, 2017, respectively. Fully taxable equivalent net interest income totaled

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\$50.9 million and \$150.1 million for the three and nine months ended September 30, 2018, respectively, and increased \$11.5 million and \$36.4 million from the three and nine months ended September 30, 2017, respectively.

Provision for loan loss expense on originated and acquired loans was \$0.8 million and \$2.5 million during the three and nine months ended September 30, 2018, respectively, compared to \$4.0 million and \$9.9 million during the three and nine months ended September 30, 2017, respectively, a decrease of \$3.2 million and \$7.4 million, respectively. Annualized net (recoveries) charge-offs on originated and acquired loans totaled (0.08)% and 0.00% during the three and nine months ended September 30, 2018, respectively, compared to annualized net charge-offs of 1.18% and 0.41% during the three and nine months ended September 30, 2017, respectively.

Non-interest income totaled \$18.1 million and \$55.5 million for the three and nine months ended September 30, 2018, respectively, compared to \$9.6 million and \$30.2 million during the three and nine months ended September 30, 2017, respectively, an increase of \$8.5 million and \$25.3 million, respectively. Organic growth and the addition of the Peoples client base drove a \$1.6 million and \$4.7 million increase in service charges and bank card interchange fees during the three and nine months ended September 30, 2018, respectively. Mortgage banking income increased \$7.2 million and \$23.0 million during the three and nine months ended September 30, 2018, respectively, due to increased volume from the Peoples acquisition.

Non-interest expense totaled \$44.4 million and \$146.5 million for the three and nine months ended September 30, 2018, respectively, compared to \$34.6 million and \$102.7 million for the three and nine months ended September 30, 2017, respectively, increasing from the prior periods due to the Peoples acquisition. Included in total non-interest expense for the three and nine months ended September 30, 2018 were \$0.0 million and \$8.0 million of acquisition costs, respectively.

Income tax expense totaled \$4.4 million and \$8.8 million for the three and nine months ended September 30, 2018, respectively, compared to an expense of \$1.7 million and \$2.7 million for the three and nine months ended September 30, 2017, respectively. The tax expense recorded for the three and nine months ended September 30, 2018 was lowered by a \$0.1 million and \$1.3 million tax benefit from stock compensation activity, respectively. The tax expense recorded for the three and nine months ended September 30, 2017 was lowered by a \$0.1 million and \$3.4 million tax benefit from stock compensation activity, respectively. Without the discrete items related to stock compensation activity, the tax rates for the three and nine months ended September 30, 2018 were 19.8% and 19.1%, respectively and compared to 19.9% and 22.3% for the three and nine months ended September 30, 2017, respectively.

Net Interest Income

We regularly review net interest income metrics to provide us with indicators of how the various components of net interest income are performing. We regularly review: (i) our loan mix and the yield on loans; (ii) the investment portfolio and the related yields; (iii) our deposit mix and the cost of deposits; and (iv) net interest income simulations for various forecast periods.

The following tables present the components of net interest income for the periods indicated. The tables include: (i) the average daily balances of interest earning assets and interest bearing liabilities; (ii) the average daily balances of non-interest earning assets and non-interest bearing liabilities; (iii) the total amount of interest income earned on interest earning assets on a fully taxable equivalent basis; (iv) the total amount of interest expense incurred on interest bearing liabilities; (v) the resultant average yields and rates; (vi) net interest spread; and (vii) net interest margin, which represents the difference between interest income and interest expense, expressed as a percentage of interest earning assets. The effects of trade-date accounting of investment securities for which the cash had not settled are not considered interest earning assets and are excluded from this presentation for time frames prior to their cash settlement, as are the market value adjustments on the investment securities available-for-sale.

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The table below presents the components of net interest income on a fully taxable equivalent basis for the three months ended September 30, 2018 and 2017:

| | For the three months ended September 30, 2018 | | | For the three months ended September 30, 2017 | | |
|---|--|-----------|-----------------|--|-----------|-----------------|
| | Average balance | Interest | Average rate | Average balance | Interest | Average rate |
| Interest earning assets: | | | | | | |
| Originated loans | | | | | | |
| FTE(1)(2)(3) | \$ 3,215,369 | \$ 36,496 | 4.50% | \$ 2,857,318 | \$ 29,893 | 4.15% |
| Acquired loans | 533,261 | 7,891 | 5.87% | 110,654 | 1,894 | 6.79% |
| ASC 310-30 loans | 80,629 | 4,785 | 23.74% | 127,752 | 5,667 | 17.74% |
| Loans held for sale | 99,933 | 1,134 | 4.50% | 9,242 | 127 | 5.45% |
| Investment securities | | | | | | |
| available-for-sale | 858,469 | 4,482 | 2.09% | 848,847 | 4,011 | 1.89% |
| Investment securities held-to-maturity | 259,169 | 1,807 | 2.79% | 286,604 | 1,995 | 2.78% |
| Other securities | 18,048 | 269 | 5.96% | 16,843 | 234 | 5.56% |
| Interest earning deposits and securities purchased under agreements to resell | | | | | | |
| | 39,259 | 171 | 1.73% | 87,114 | 276 | 1.26% |
| Total interest earning assets FTE(2) | \$ 5,104,137 | \$ 57,035 | 4.43% | \$ 4,344,374 | \$ 44,097 | 4.03% |
| Cash and due from banks | \$ 80,334 | | | \$ 67,382 | | |
| Other assets | 424,873 | | | 313,630 | | |
| Allowance for loan losses | (33,024) | | | (35,103) | | |
| Total assets | \$ 5,576,320 | | | \$ 4,690,283 | | |
| Interest bearing liabilities: | | | | | | |
| Interest bearing demand, savings and money market deposits | | | | | | |
| | \$ 2,411,875 | \$ 2,269 | 0.37% | \$ 1,857,777 | \$ 1,503 | 0.32% |
| Time deposits | 1,126,377 | 3,183 | 1.12% | 1,131,326 | 2,565 | 0.90% |
| Securities sold under agreements to repurchase | | | | | | |
| | 59,214 | 51 | 0.34% | 91,737 | 46 | 0.20% |
| Federal Home Loan Bank advances | | | | | | |
| | 129,542 | 634 | 1.94% | 144,136 | 567 | 1.56% |
| Total interest bearing liabilities | \$ 3,727,008 | \$ 6,137 | 0.65% | \$ 3,224,976 | \$ 4,681 | 0.58% |
| Demand deposits | \$ 1,096,780 | | | \$ 874,750 | | |
| Other liabilities | 82,017 | | | 39,799 | | |
| Total liabilities | 4,905,805 | | | 4,139,525 | | |
| Shareholders' equity | 670,515 | | | 550,758 | | |
| Total liabilities and shareholders' equity | \$ 5,576,320 | | | \$ 4,690,283 | | |
| Net interest income FTE(2) | | \$ 50,898 | | | \$ 39,416 | |
| Interest rate spread FTE(2) | | | 3.78% | | | 3.45% |

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| | | | | |
|--|--------------|---------|--------------|---------|
| Net interest earning assets | \$ 1,377,129 | | \$ 1,119,398 | |
| Net interest margin FTE(2) | | 3.96% | | 3.60% |
| Average transaction deposits | \$ 3,508,655 | | \$ 2,732,527 | |
| Average total deposits | \$ 4,635,032 | | \$ 3,863,853 | |
| Ratio of average interest earning assets to average interest bearing liabilities | | 136.95% | | 134.71% |

- (1) Originated loans are net of deferred loan fees, less costs, which are included in interest income over the life of the loan.
- (2) Presented on a fully taxable equivalent basis using the statutory tax rate of 21% and 35% for the three months ended September 30, 2018 and 2017, respectively. The taxable equivalent adjustments included above are \$1,126 and \$1,518 for the three months ended September 30, 2018 and 2017, respectively.
- (3) Loan fees included in interest income totaled \$1,329 and \$1,066 for the three months ended September 30, 2018 and 2017, respectively.

Net interest income totaled \$49.8 million and \$37.9 million during the three months ended September 30, 2018 and 2017, respectively. Fully taxable equivalent net interest income totaled \$50.9 million for the three months ended September 30, 2018, and increased \$11.5 million, or 29.1%, from the three months ended September 30, 2017. The fully taxable equivalent net interest margin widened 0.36% to 3.96% as the yield on earning assets increased 0.40%, led by a 0.35% increase in the originated portfolio yields due to short-term rate increases, partially offset by an increase in the cost of deposits of 0.05%.

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Average loans comprised \$3.9 billion, or 77.0%, of total average interest earning assets during the three months ended September 30, 2018, compared to \$3.1 billion, or 71.5%, during the three months ended September 30, 2017. The increase in average loan balances from the three months ended September 30, 2017 was driven by an increase of \$422.6 million in acquired loans primarily from the Peoples acquisition and a \$358.1 million increase in originated loans. The originated loan portfolio yield increased to 4.50% during the three months ended September 30, 2018, compared to 4.15% during the three months ended September 30, 2017, benefitting from higher yields on variable rate loans, primarily driven by the short-term market rate increases. The yield on the ASC 310-30 loan portfolio was 23.7% and 17.74% during the three months ended September 30, 2018 and 2017, respectively, increasing due to \$0.4 million of accelerated accretion during the three months ended September 30, 2018.

Average investment securities comprised 21.9% and 26.1% of total interest earning assets during the three months ended September 30, 2018 and 2017, respectively. The decrease in the investment portfolio was a result of scheduled paydowns and reflects the re-mixing of the interest earning assets as we have utilized the paydowns of the investment portfolio to fund loan originations. Short-term investments, comprised of the interest earning deposits and securities purchased under agreements to resell, were 0.8% and 2.0% of interest earning assets during the three months ended September 30, 2018 and 2017, respectively.

Average balances of interest bearing liabilities increased \$502.0 million during the three months ended September 30, 2018, compared to the three months ended September 30, 2017. The Peoples acquisition added \$730 million in total deposits on January 1, 2018, coupled with transaction deposit growth, partially offset by the sale of four banking centers in the second quarter of 2017. Total interest bearing liabilities increased \$502.0 million due to increases of \$554.1 million in interest bearing demand, savings and money market deposits, offset by decreases in securities sold under agreements to repurchase of \$32.5 million, FHLB advances of \$14.6 million and time deposits of \$4.9 million. Total interest expense related to interest bearing liabilities was \$6.1 million and \$4.7 million during the three months ended September 30, 2018 and 2017, respectively, at an average cost of 0.65% and 0.58% during the three months ended September 30, 2018 and 2017, respectively. Additionally, the cost of deposits increased 0.05% to 0.47% during the three months ended September 30, 2018, compared to 0.42% during the three months ended September 30, 2017.

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The table below presents the components of net interest income on a fully taxable equivalent basis for the nine months ended September 30, 2018 and 2017:

| | For the nine months ended September 30, 2018 | | | For the nine months ended September 30, 2017 | | |
|--|---|------------|-----------------|---|------------|-----------------|
| | Average balance | Interest | Average rate | Average balance | Interest | Average rate |
| Interest earning assets: | | | | | | |
| Originated loans | | | | | | |
| FTE(1)(2)(3) | \$ 3,084,274 | \$ 102,115 | 4.43% | \$ 2,734,388 | \$ 82,495 | 4.03% |
| Acquired loans | 589,291 | 25,508 | 5.79% | 123,191 | 5,795 | 6.29% |
| ASC 310-30 loans | 96,904 | 15,009 | 20.65% | 135,485 | 17,718 | 17.44% |
| Loans held for sale | 79,350 | 2,650 | 4.47% | 8,668 | 406 | 6.26% |
| Investment securities | | | | | | |
| available-for-sale | 903,039 | 14,097 | 2.08% | 895,112 | 12,730 | 1.90% |
| held-to-maturity | 263,995 | 5,528 | 2.79% | 305,441 | 6,378 | 2.78% |
| Other securities | 16,959 | 761 | 5.98% | 15,307 | 619 | 5.39% |
| Interest earning deposits and securities purchased under agreements to resell | | | | | | |
| | 90,726 | 1,231 | 1.81% | 87,762 | 687 | 1.05% |
| Total interest earning assets FTE(2) | \$ 5,124,538 | \$ 166,899 | 4.35% | \$ 4,305,354 | \$ 126,828 | 3.94% |
| Cash and due from banks | \$ 91,914 | | | \$ 67,046 | | |
| Other assets | 418,753 | | | 317,702 | | |
| Allowance for loan losses | (32,026) | | | (32,208) | | |
| Total assets | \$ 5,603,179 | | | \$ 4,657,894 | | |
| Interest bearing liabilities: | | | | | | |
| Interest bearing demand, savings and money market deposits | | | | | | |
| | \$ 2,419,235 | \$ 6,042 | 0.33% | \$ 1,875,143 | \$ 4,294 | 0.31% |
| Time deposits | 1,144,051 | 8,908 | 1.04% | 1,152,550 | 7,465 | 0.87% |
| Securities sold under agreements to repurchase | 94,938 | 137 | 0.19% | 85,077 | 119 | 0.19% |
| Federal Home Loan Bank advances | 125,745 | 1,719 | 1.83% | 108,148 | 1,261 | 1.56% |
| Total interest bearing liabilities | \$ 3,783,969 | \$ 16,806 | 0.59% | \$ 3,220,918 | \$ 13,139 | 0.55% |
| Demand deposits | \$ 1,074,659 | | | \$ 852,913 | | |
| Other liabilities | 88,974 | | | 39,401 | | |
| Total liabilities | 4,947,602 | | | 4,113,232 | | |
| Stockholders' equity | 655,577 | | | 544,662 | | |

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| | | | |
|--|--------------|--------------|------------|
| Total liabilities and shareholders' equity | \$ 5,603,179 | \$ 4,657,894 | |
| Net interest income FTE(2) | \$ 150,093 | | \$ 113,689 |
| Interest rate spread FTE(2) | | 3.76% | 3.39% |
| Net interest earning assets | \$ 1,340,569 | \$ 1,084,436 | |
| Net interest margin FTE(2) | | 3.92% | 3.53% |
| Average transaction deposits | \$ 3,493,894 | \$ 2,728,056 | |
| Average total deposits | \$ 4,637,945 | \$ 3,880,606 | |
| Ratio of average interest earning assets to average interest bearing liabilities | 135.43% | 133.67% | |

- (1) Originated loans are net of deferred loan fees, less costs, which are included in interest income over the life of the loan.
- (2) Presented on a fully taxable equivalent basis using the statutory tax rate of 21% and 35% for the nine months ended September 30, 2018 and 2017, respectively. The taxable equivalent adjustments included above are \$3,288 and \$4,176 for the nine months ended September 30, 2018 and 2017, respectively.
- (3) Loan fees included in interest income totaled \$4,717 and \$3,009 for the nine months ended September 30, 2018 and 2017, respectively.

Net interest income totaled \$146.8 million and \$109.5 million for the nine months ended September 30, 2018 and 2017, respectively. Fully taxable equivalent net interest income totaled \$150.1 million for the nine months ended September 30, 2018 and increased \$36.4 million, or 32.0%, from the nine months ended September 30, 2017. The fully taxable equivalent net interest margin widened 0.39% to 3.92% as the yield on earnings assets increased 0.41%, led by a 0.40% increase in the originated portfolio yields due to short-term rate increases, partially offset by an increase in the cost of deposits of 0.02%.

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Average loans comprised \$3.8 billion, or 75.1%, of total average interest earning assets during the nine months ended September 30, 2018, compared to \$3.0 billion, or 69.7%, of total average interest earning assets during the nine months ended September 30, 2017. The increase in average loan balances was driven by an increase of \$466.1 million in acquired loans primarily from the Peoples acquisition and a \$349.9 million increase in originated loans. The originated loan portfolio yield increased to 4.43% during the nine months ended September 30, 2018, compared to 4.03% during the nine months ended September 30, 2017, benefitting from higher yields on variable rate loans, primarily driven by the short-term market rate increases. The yield on the ASC 310-30 loan portfolio was 20.65% and 17.44% during the nine months ended September 30, 2018 and 2017, respectively, increasing due to \$1.6 million of accelerated accretion during the nine months ended September 30, 2018.

Average investment securities comprised 22.8% and 27.9% of total interest earning assets during the nine months ended September 30, 2018 and 2017, respectively. The decrease in the investment portfolio was a result of scheduled paydowns and reflects the re-mixing of the interest earning assets as we have utilized the paydowns of the investment portfolio to fund loan originations. Short-term investments, comprised of interest earning deposits and securities purchased under agreements to resell, were 1.8% and 2.0% of interest earning assets during the nine months ended September 30, 2018 and 2017, respectively.

Average balances of interest bearing liabilities increased \$563.1 million during the nine months ended September 30, 2018, compared to the nine months ended September 30, 2017. The Peoples acquisition added \$730 million in total deposits on January 1, 2018, coupled with transaction deposit growth, partially offset by the sale of four banking centers in the second quarter of 2017. Total interest bearing liabilities increased \$563.1 million due to increases of \$544.1 million in interest-bearing demand, savings and money market deposits, increases of \$17.6 million in FHLB advances and increases of \$9.9 million in securities sold under agreements to repurchase, offset by a decrease in time deposits of \$8.5 million. Total interest expense related to interest bearing liabilities was \$16.8 million and \$13.1 million during the nine months ended September 30, 2018 and 2017, respectively, at an average cost of 0.59% and 0.55% during the nine months ended September 30, 2018 and 2017, respectively. Additionally, the cost of deposits increased 0.02% to 0.43% during the nine months ended September 30, 2018, compared to 0.41% during the nine months ended September 30, 2017.

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The following table summarizes the changes in net interest income on a fully taxable equivalent basis by major category of interest earning assets and interest bearing liabilities, identifying changes related to volume and changes related to rates for the three and nine months ended September 30, 2018 compared to the three and nine months ended September 30, 2017:

| | Three months ended September 30, 2018 compared to Three months ended September 30, 2017 Increase (decrease) due to | | | Nine months ended September 30, 2018 compared to Nine months ended September 30, 2017 Increase (decrease) due to | | |
|---|---|-----------------|------------------|---|------------------|------------------|
| | Volume | Rate | Net | Volume | Rate | Net |
| Interest income: | | | | | | |
| Originated loans FTE(1)(2)(3) | \$ 4,065 | \$ 2,539 | \$ 6,604 | \$ 11,585 | \$ 8,036 | \$ 19,621 |
| Acquired loans | 6,254 | (257) | 5,997 | 20,176 | (463) | 19,713 |
| ASC 310-30 loans | (2,797) | 1,915 | (882) | (5,976) | 3,267 | (2,709) |
| Loans held for sale | 1,029 | (22) | 1,007 | 2,361 | (117) | 2,244 |
| Investment securities available-for-sale | 50 | 421 | 471 | 124 | 1,243 | 1,367 |
| Investment securities held-to-maturity | (191) | 3 | (188) | (868) | 18 | (850) |
| Other securities | 18 | 17 | 35 | 74 | 68 | 142 |
| Interest earning deposits and securities purchased under agreements to resell | (208) | 102 | (106) | 40 | 504 | 544 |
| Total interest income | \$ 8,220 | \$ 4,718 | \$ 12,938 | \$ 27,516 | \$ 12,556 | \$ 40,072 |
| Interest expense: | | | | | | |
| Interest bearing demand, savings and money market deposits | \$ 521 | \$ 245 | \$ 766 | \$ 1,359 | \$ 389 | \$ 1,748 |
| Time deposits | (14) | 632 | 618 | (66) | 1,509 | 1,443 |
| Securities sold under agreements to repurchase | (28) | 33 | 5 | 14 | 5 | 19 |
| Federal Home Loan Bank advances | (71) | 138 | 67 | 241 | 217 | 458 |
| Total interest expense | 408 | 1,048 | 1,456 | 1,548 | 2,120 | 3,668 |
| Net change in net interest income | \$ 7,812 | \$ 3,670 | \$ 11,482 | \$ 25,968 | \$ 10,436 | \$ 36,404 |

- (1) Originated loans are net of deferred loan fees, less costs, which are included in interest income over the life of the loan.
- (2) Presented on a fully taxable equivalent basis using the statutory tax rate of 21% for the three and nine months ended September 30, 2018 and 35% for the three and nine months ended September 30, 2017. The taxable equivalent adjustments included above are \$1,126 and \$1,518 for the three months ended September 30, 2018 and 2017, respectively. The taxable equivalent adjustments included above are \$3,288 and \$4,176 for the nine months ended September 30, 2018 and 2017, respectively.
- (3)

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Loan fees included in interest income totaled \$1,329 and \$1,066 for the three months ended September 30, 2018 and 2017, respectively. Loan fees included in interest income totaled \$4,717 and \$3,009 for the nine months ended September 30, 2018 and 2017, respectively.

Below is a breakdown of average deposits and the average rates paid during the periods indicated:

| | For the three months ended | | | | For the nine months ended | | | |
|-----------------------------|----------------------------|-------------------------|--------------------|-------------------------|---------------------------|-------------------------|--------------------|-------------------------|
| | September 30, 2018 | | September 30, 2017 | | September 30, 2018 | | September 30, 2017 | |
| | Average balance | Average rate paid | Average balance | Average rate paid | Average balance | Average rate paid | Average balance | Average rate paid |
| Non-interest bearing demand | \$ 1,096,780 | 0.00% | \$ 874,750 | 0.00% | \$ 1,074,659 | 0.00% | \$ 852,913 | 0.00% |
| Interest bearing demand | 678,501 | 0.14% | 416,389 | 0.11% | 679,238 | 0.13% | 418,108 | 0.10% |
| Money market accounts | 1,174,205 | 0.49% | 998,403 | 0.39% | 1,170,144 | 0.43% | 1,037,201 | 0.38% |
| Savings accounts | 559,169 | 0.41% | 442,985 | 0.38% | 569,853 | 0.38% | 419,834 | 0.32% |
| Time deposits | 1,126,377 | 1.12% | 1,131,326 | 0.90% | 1,144,051 | 1.04% | 1,152,550 | 0.87% |
| Total average deposits | \$ 4,635,032 | 0.47% | \$ 3,863,853 | 0.42% | \$ 4,637,945 | 0.43% | \$ 3,880,606 | 0.41% |

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Provision for Loan Losses

The provision for loan losses represents the amount of expense that is necessary to bring the ALL to a level that we deem appropriate to absorb probable losses inherent in the loan portfolio as of the balance sheet date. The ALL is in addition to the remaining purchase accounting marks of \$9.2 million on acquired loans not accounted for under ASC 310-30 that were established at the time of acquisition. The Company recorded \$9.8 million of purchase accounting marks on January 1, 2018 related to the Peoples acquisition. Refer to note 3 of our consolidated financial statements for further discussion of the acquisition. The determination of the ALL, and the resultant provision for loan losses, is subjective and involves significant estimates and assumptions.

Below is a summary of the provision for loan losses recorded in the consolidated statements of operations for the periods indicated:

| | For the three months ended September 30, | | For the nine months ended September 30, | |
|---|--|----------|--|----------|
| | 2018 | 2017 | 2018 | 2017 |
| Provision (recoupment) for loans accounted for under ASC 310-30 | \$ 6 | \$ (142) | \$ 197 | \$ (225) |
| Provision for loan losses on originated and acquired loans | 801 | 4,022 | 2,524 | 9,925 |
| Total provision for loan losses | \$ 807 | \$ 3,880 | \$ 2,721 | \$ 9,700 |

Provision for loan loss expense was \$0.8 million and \$2.7 million during the three and nine months ended September 30, 2018, respectively, compared to \$3.9 million and \$9.7 million during the three and nine months ended September 30, 2017, respectively. To support loan growth, the Company recorded \$0.8 million and \$2.5 million of provision for loan losses on originated and acquired loans during the three and nine months ended September 30, 2018, respectively. Annualized net (recoveries) charge-offs on originated and acquired loans during the three and nine months ended September 2018 were (0.08)% and 0.00%, respectively, compared to annualized net charge-offs of 1.18% and 0.41% during the three and nine months ended September 30, 2017. The originated and acquired allowance for loan losses totaled 0.88% and 1.00% of originated and acquired loans at September 30, 2018 and 2017, respectively, and decreased as the acquired loans from the Peoples acquisition were recorded at fair value.

For the three and nine months ended September 30, 2018, we recorded a provision of \$6 thousand and \$197 thousand, respectively, of provision for loan losses accounted for under ASC 310-30 in connection with our re-measurements of expected cash flows. For the three and nine months ended September 30, 2017, we recorded a recoupment of \$142 and \$225, respectively, for loan losses accounted for under ASC 310-30 in connection with our re-measurements of expected cash flow.

Non-Interest Income

The table below details the components of non-interest income for the periods presented:

| | For the three months ended September 30, | | For the nine months ended September 30, | | Three months Increase (decrease) | | Nine months Increase (decrease) | |
|----------------------------------|--|----------|---|-----------|----------------------------------|----------|---------------------------------|----------|
| | 2018 | 2017 | 2018 | 2017 | Amount | % Change | Amount | % Change |
| Service charges | \$ 4,592 | \$ 3,585 | \$ 13,473 | \$ 10,458 | \$ 1,007 | 28.1 % | \$ 3,015 | 28.8 % |
| Bank card fees | 3,686 | 3,076 | 10,720 | 9,014 | 610 | 19.8 % | 1,706 | 18.9 % |
| Mortgage banking income | 7,819 | 668 | 24,701 | 1,716 | 7,151 | >100.0% | 22,985 | >100.0% |
| Bank-owned life insurance income | 463 | 475 | 1,361 | 1,417 | (12) | (2.5)% | (56) | (4.0)% |
| Other non-interest income | 1,429 | 1,611 | 4,290 | 7,149 | (182) | (11.3)% | (2,859) | (40.0)% |
| OREO related income | 72 | 136 | 913 | 449 | (64) | (47.1)% | 464 | 103.3 % |
| Total non-interest income | \$ 18,061 | \$ 9,551 | \$ 55,458 | \$ 30,203 | \$ 8,510 | 89.1 % | \$ 25,255 | 83.6 % |

Non-interest income totaled \$18.1 million and \$55.5 million for the three and nine months ended September 30, 2018, respectively, compared to \$9.6 million and \$30.2 million for the three and nine months ended September 30, 2017, respectively. Service charges represent various fees charged to clients for banking services, including fees such as non-sufficient (“NSF”) charges and service charges on deposit accounts. Organic growth and the addition of the Peoples client base drove a \$1.6 million and \$4.7 million increase in service charges and bank card interchange fees during the three and nine months ended September 30, 2018, respectively. Mortgage banking income increased during the three and nine months ended September 30, 2018 due to increased volume from the Peoples acquisition. Other non-interest income decreased during the nine months ended September 30, 2018, primarily driven by a \$2.9 million gain from banking center divestitures during the three months ended September 30, 2017.

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OREO related income includes rental income and insurance proceeds received on OREO properties and write-ups to the fair value of collateral that exceed the loan balance at the time of foreclosure. During the three and nine months ended September 30, 2018, this income increased \$0.4 million and \$0.5 million, respectively, compared to prior periods.

Non-Interest Expense

The table below details the components of non-interest expense for the periods presented:

| | For the three months ended September 30, | | For the nine months ended September 30, | | Three months Increase (decrease) | | Nine months Increase (decrease) | |
|--|--|-----------|---|------------|----------------------------------|---------|---------------------------------|---------|
| | 2018 | 2017 | 2018 | 2017 | Amount | % | Amount | % |
| Salaries and benefits | \$ 28,127 | \$ 19,363 | \$ 87,910 | \$ 59,662 | \$ 8,764 | 45.3 % | \$ 28,248 | 47.3 % |
| Occupancy and equipment | 6,925 | 5,208 | 22,070 | 15,887 | 1,717 | 33.0 % | 6,183 | 38.9 % |
| Telecommunications and data processing | 2,186 | 1,702 | 8,653 | 4,841 | 484 | 28.4 % | 3,812 | 78.7 % |
| Marketing and business development | 1,128 | 683 | 3,589 | 1,878 | 445 | 65.2 % | 1,711 | 91.1 % |
| FDIC deposit insurance | 401 | 715 | 1,911 | 2,106 | (314) | (43.9)% | (195) | (9.3)% |
| Bank card expenses | 1,258 | 971 | 4,491 | 2,751 | 287 | 29.6 % | 1,740 | 63.2 % |
| Professional fees | 1,117 | 754 | 4,686 | 2,441 | 363 | 48.1 % | 2,245 | 92.0 % |
| Other non-interest expense | 2,564 | 2,700 | 9,515 | 7,839 | (136) | (5.0)% | 1,676 | 21.4 % |
| Problem asset workout | 665 | 1,636 | 2,221 | 3,389 | (971) | (59.4)% | (1,168) | (34.5)% |
| Gain on OREO sales, net | (450) | (497) | (386) | (2,254) | 47 | (9.5)% | 1,868 | (82.9)% |
| Core deposit intangible asset amortization | 511 | 1,370 | 1,817 | 4,110 | (859) | (62.7)% | (2,293) | (55.8)% |
| Total non-interest expense | \$ 44,432 | \$ 34,605 | \$ 146,477 | \$ 102,650 | \$ 9,827 | 28.4 % | \$ 43,827 | 42.7 % |

Non-interest expense totaled \$44.4 million and \$146.5 million for the three and nine months ended September 30, 2018, respectively, compared to \$34.6 million and \$102.7 million for the three and nine months ended September 30, 2017, respectively, increasing from the prior periods primarily due to the Peoples acquisition. Included in non-interest expense for the three and nine months ended September 30, 2018 are \$0.0 million and \$8.0 million of acquisition costs, respectively. Problem asset workout expense and gain on OREO sales decreased a combined \$0.9 million during the three months ended September 30, 2018 due to asset resolutions in the prior period and increased \$0.7 million during the nine months ended September 30, 2018, respectively, due to lower OREO gains in the current periods. The core deposits intangible asset amortization decreased during the three and nine months ended September 30, 2018 compared to prior periods, due to fully amortized core deposit intangibles from historic acquisitions.

Income taxes

Income tax expense attributable to income before income taxes was \$4.4 million and \$8.8 million for the three and nine months ended September 30, 2018, respectively, compared to an expense of \$1.7 million and \$2.7 million for the three and nine months ended September 30, 2017, respectively. The tax expense recorded for the three and nine months ended September 30, 2018 was lowered by a \$0.1 million and \$1.3 million tax benefit from stock compensation activity, respectively. The tax expense recorded for the three and nine months ended September 30, 2017 was lowered by a \$0.1 million and \$3.4 million tax benefit from stock compensation activity, respectively. Without the discrete items related to stock compensation activity, the tax rates for the three and nine months ended September 30, 2018 were 19.8% and 19.1%, respectively, and compared to 19.9% and 22.3% for the three and nine months ended September 30, 2017, respectively. The effective tax rate is lower compared to the prior year primarily due to the Tax Cuts and Jobs Act, which, among other items, reduced the federal corporate tax rate to 21% effective January 1, 2018. The effective tax rate differs from the federal statutory rate primarily due to tax benefits from stock compensation activity, interest income from tax-exempt lending, bank-owned life insurance income, and the relationship of these items to pre-tax income. The Company forecasts the full year estimated effective tax rate in accordance with ASC 740; as a result, the relationship between pre-tax income and tax-exempt income within each reporting period can create fluctuations in the effective tax rate from period-to-period.

The Company has unvested stock-based compensation awards outstanding at September 30, 2018, including stock options, restricted stock and performance stock units. The strike prices for options range from \$18.09 to \$40.51 with a large portion of the awards having strike prices of \$20.00. The option awards and restricted stock awards vest over a range of a 1-3 year period. The performance stock units cliff vest over 3 years and the number of shares issued is determined by the final performance results. Depending on the movement in our stock price, these stock-based compensation awards may create either an excess tax benefit or tax deficiency depending on the relationship between the fair value at the time of vesting or exercise and the estimated fair value recorded at the time of grant. As of September 30, 2018, the Company had \$2.7 million of deferred tax assets related to stock-based compensation, \$2.1 million of which is associated with executive officers still employed by the Company.

Additional information regarding income taxes can be found in note 16 of this Form 10-Q and 19 of our audited consolidated financial statements in our 2017 Annual Report on Form 10-K.

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Liquidity and Capital Resources

Liquidity is monitored and managed to ensure that sufficient funds are available to operate our business and pay our obligations to depositors and other creditors, while providing ample available funds for opportunistic and strategic investments. On-balance sheet liquidity is represented by our cash and cash equivalents, and unencumbered investment securities, and is detailed in the table below as of September 30, 2018 and December 31, 2017:

| | September 30, 2018 | December 31, 2017 |
|---|--------------------|-------------------|
| Cash and due from banks | \$ 110,959 | \$ 193,297 |
| Cash segregated for Peoples acquisition | — | (36,189) |
| Unsegregated cash and due from banks | 110,959 | 157,108 |
| Interest bearing bank deposits | 500 | 64,067 |
| Unencumbered investment securities, at fair value | 582,697 | 637,048 |
| Total | \$ 694,156 | \$ 858,223 |

Total on-balance sheet liquidity decreased \$164.1 million at September 30, 2018 compared to December 31, 2017. The decrease was due to lower interest bearing bank deposits of \$63.6 million, lower unencumbered available-for-sale and held-to-maturity securities balances of \$54.4 million and lower unsegregated cash and due from banks of \$46.1 million.

Our primary sources of funds are deposits, securities sold under agreements to repurchase, prepayments and maturities of loans and investment securities, the sale of investment securities, and funds provided from operations. We anticipate having access to other third party funding sources, including the ability to raise funds through the issuance of shares of our common stock or other equity or equity-related securities, incurrence of debt, and federal funds purchased, that may also be a source of liquidity. We anticipate that these sources of liquidity will provide adequate funding and liquidity for at least a twelve-month period.

Our primary uses of funds are loan originations, investment security purchases, withdrawals of deposits, settlement of repurchase agreements, capital expenditures, operating expenses, and dividend payments. For additional information regarding our operating, investing, and financing cash flows, see our consolidated statements of cash flows in the accompanying unaudited consolidated financial statements.

Exclusive from the investing activities related to acquisitions, our primary investing activities are originations and pay-offs and pay downs of loans and purchases and sales of investment securities. At September 30, 2018, pledgeable investment securities represented a significant source of liquidity. Our available-for-sale investment securities are

carried at fair value and our held-to-maturity securities are carried at amortized cost. Our collective investment securities portfolio totaled \$1.0 billion at September 30, 2018, inclusive of pre-tax net unrealized losses of \$30.8 million on the available-for-sale securities portfolio and net unrealized losses of \$7.1 million in our held-to-maturity securities portfolio at September 30, 2018. The gross unrealized gains and losses are detailed in note 4 of our consolidated financial statements. As of September 30, 2018, our investment securities portfolio consisted primarily of mortgage-backed securities, all of which were issued or guaranteed by U.S. Government agencies or sponsored enterprises. The anticipated repayments and marketability of these securities offer substantial resources and flexibility to meet new loan demand, reinvest in the investment securities portfolio, or provide optionality for reductions in our deposit funding base.

At present, financing activities primarily consist of changes in deposits and repurchase agreements, and advances from the FHLB, in addition to the payment of dividends and the repurchase of our common stock. Maturing time deposits represent a potential use of funds. As of September 30, 2018, \$711.4 million of time deposits were scheduled to mature within twelve months. Based on the current interest rate environment, market conditions, and our consumer banking strategy focusing on both lower cost transaction accounts and term deposits, our strategy is to replace a significant portion of those maturing time deposits with transaction deposits and market-rate time deposits.

Through our membership with the FHLB, we have pledged qualifying loans and investment securities allowing us to obtain additional liquidity through FHLB advances and lines of credit. FHLB advances and lines of credit available totaled \$1.0 billion, of which \$144.5 million was used at September 30, 2018. We can obtain additional liquidity through FHLB advances if required. The Bank also has access to federal funds lines of credit with corresponding banks.

The Basel III Capital rules, effective January 1, 2015, changed the components of regulatory capital, changed the way in which risk ratings are assigned to various categories of bank assets, and defined a new Tier 1 common risk-based ratio. In addition, a capital

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conservation buffer requirement, designed to strengthen an institution's financial resilience during economic cycles through the restriction of capital distributions and other payments, became effective in 2017 with full phase-in beginning January 1, 2019. When fully phased-in, the capital conservation buffer adds a 2.5% capital requirement above existing regulatory minimum ratios. Under the Basel III requirements, at September 30, 2018, the Company and the Bank met all capital adequacy requirements and the Bank had regulatory capital ratios in excess of the levels established for well-capitalized institutions, including the fully phased-in capital conservation buffer. For more information on regulatory capital, see note 10 in our consolidated financial statements.

Our shareholders' equity is impacted by earnings, changes in unrealized gains and losses on securities, net of tax, stock-based compensation activity, share repurchases and the payment of dividends.

The Board of Directors has authorized multiple programs to repurchase shares of the Company's common stock from time to time either in open market or in privately negotiated transactions in accordance with applicable regulations of the SEC.

On August 5, 2016, the Company announced that its Board of Directors authorized a program to repurchase up to \$50.0 million of the Company's common stock. The remaining authorization under this program as of September 30, 2018 was \$12.6 million. During the three and nine months ended September 30, 2018, we did not repurchase any shares of our common stock.

On November 7, 2018, our Board of Directors declared a quarterly dividend of \$0.17 per common share, payable on December 14, 2018 to shareholders of record at the close of business on November 30, 2018.

Asset/Liability Management and Interest Rate Risk

Management and the Board of Directors are responsible for managing interest rate risk and employing risk management policies that monitor and limit this exposure. Interest rate risk is measured using net interest income simulations and market value of portfolio equity analyses. These analyses use various assumptions, including the nature and timing of interest rate changes, yield curve shape, prepayments on loans and securities, deposit decay rates, pricing decisions on loans and deposits, and reinvestment/replacement of asset and liability cash flows.

The principal objective of the Company's asset and liability management function is to evaluate the interest rate risk within the balance sheet and pursue a controlled assumption of interest rate risk while maximizing earnings and preserving adequate levels of liquidity and capital. The asset and liability management function is under the guidance of the Asset Liability Committee from direction of the Board of Directors. The Asset Liability Committee meets

monthly to review, among other things, the sensitivity of the Company's assets and liabilities to interest rate changes, local and national market conditions and rates. The Asset Liability Committee also reviews the liquidity, capital, deposit mix, loan mix and investment positions of the Company.

Instantaneous parallel rate shift scenarios are modeled and utilized to evaluate risk and establish exposure limits for acceptable changes in net interest margin. These scenarios, known as rate shocks, simulate an instantaneous change in interest rates and use various assumptions, including, but not limited to, prepayments on loans and securities, deposit decay rates, pricing decisions on loans and deposits, reinvestment and replacement of asset and liability cash flows.

We also analyze the economic value of equity as a secondary measure of interest rate risk. This is a complementary measure to net interest income where the calculated value is the result of the market value of assets less the market value of liabilities. The economic value of equity is a longer term view of interest rate risk because it measures the present value of the future cash flows. The impact of changes in interest rates on this calculation is analyzed for the risk to our future earnings and is used in conjunction with the analyses on net interest income.

Our interest rate risk model indicated that the Company was asset sensitive in terms of interest rate sensitivity at September 30, 2018. During the nine months ended September 30, 2018, we decreased our asset sensitivity as a result of the changes in beta assumptions for our interest bearing deposits. The table below illustrates the impact of an immediate and sustained 200 and 100 basis point increase

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and a 100 basis point decrease in interest rates on net interest income based on the interest rate risk model at September 30, 2018 and December 31, 2017:

| Hypothetical shift in interest rates (in bps) | % change in projected net interest income | |
|---|---|-------------------|
| | September 30, 2018 | December 31, 2017 |
| 200 | 6.84% | 6.93% |
| 100 | 3.49% | 4.82% |
| (100) | (5.42)% | (7.75)% |

Many assumptions are used to calculate the impact of interest rate fluctuations. Actual results may be significantly different than our projections due to several factors, including the timing and frequency of rate changes, market conditions and the shape of the yield curve. The computations of interest rate risk shown above do not include actions that management may undertake to manage the risks in response to anticipated changes in interest rates and actual results may also differ due to any actions taken in response to the changing rates.

As part of the asset/liability management strategy to manage primary market risk exposures expected to be in effect in future reporting periods, management has emphasized the origination of shorter duration loans as well as variable rate loans to limit the negative exposure to a rate increase. The strategy with respect to liabilities has been to emphasize transaction accounts, particularly non-interest or low interest bearing non-maturing deposit accounts which are less sensitive to changes in interest rates. Non-maturing deposit accounts have grown \$632.9 million during the nine months September 30, 2018, and totaled 75.7% of total deposits at September 30, 2018 compared to 71.9% at December 31, 2017. We currently have no brokered time deposits and intend to continue to focus on our strategy of increasing non-interest or low-cost interest bearing non-maturing deposit accounts.

Off-Balance Sheet Activities

In the normal course of business, we are a party to various contractual obligations, commitments and other off-balance sheet activities that contain credit, market, and operational risk that are not required to be reflected in our consolidated financial statements. The most significant of these are the loan commitments that we enter into to meet the financing needs of clients, including commitments to extend credit, commercial and consumer lines of credit and standby letters of credit. As of September 30, 2018 and December 31, 2017, we had loan commitments totaling \$765.4 million and \$680.8 million, respectively, and standby letters of credit that totaled \$8.5 million and \$7.2 million, respectively. Unused commitments do not necessarily represent future credit exposure or cash requirements, as commitments often expire without being drawn upon. We do not anticipate any material losses arising from commitments or contingent liabilities, and we do not believe that there are any material commitments to extend credit that represent risks of an unusual nature.

Item 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The information called for by this item is provided under the caption Asset/Liability Management and Interest Rate Risk in Part I, Item 2-Management's Discussion and Analysis of Financial Condition and Results of Operations and is incorporated herein by reference.

Item 4. CONTROLS AND PROCEDURES

Our management, with the participation of our principal executive officer and principal financial officer, conducted an evaluation of the effectiveness of our disclosure controls and procedures, as such term is defined in Rule 13a-15(e) under the Securities Exchange Act of 1934, as of September 30, 2018. Based on this evaluation, our principal executive officer and our principal financial officer concluded that our disclosure controls and procedures were effective as of September 30, 2018.

During the most recently completed fiscal quarter, there were no changes made in the Company's internal controls over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

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PART II: OTHER INFORMATION

Item 1. LEGAL PROCEEDINGS

From time to time, we are a party to various litigation matters incidental to the conduct of our business. We are not presently party to any legal proceedings the resolution of which we believe would have a material adverse effect on our business, prospects, financial condition, liquidity, results of operation, cash flows or capital levels.

Item 1A. RISK FACTORS

There have been no material changes to the risk factors disclosed in Item 1A. Risk Factors in our Annual Report on Form 10-K for the year ended December 31, 2017, except for the addition of:

The value of our mortgage servicing rights can decline during periods of falling interest rates, and we may be required to take a charge against earnings for the decreased value.

A mortgage servicing right is the right to service a mortgage loan for a fee. We capitalize MSR's when we originate mortgage loans and retain the servicing rights after we sell the loans. We carry MSR's at the lower of amortized cost or estimated fair value. Fair value is the present value of estimated future net servicing income, calculated based on a number of variables, including assumptions about the likelihood of prepayment by borrowers. Changes in interest rates can affect prepayment assumptions. When interest rates fall, borrowers are more likely to prepay their mortgage loans by refinancing them at a lower rate. As the likelihood of prepayment increases, the fair value of our MSR's can decrease. Each quarter we evaluate our MSR's for impairment based on the difference between the carrying amount and fair value, and, if a temporary impairment exists, we establish a valuation allowance through a charge that negatively affects our earnings.

We may be required to repurchase mortgage loans or reimburse investors and others as a result of breaches in contractual representations and warranties.

We sell residential mortgage loans to various parties, including GSEs and other financial institutions that purchase mortgage loans for investment or private label securitization. The agreements under which we sell mortgage loans and the insurance or guaranty agreements with the FHA and VA contain various representations and warranties regarding the origination and characteristics of the mortgage loans, including ownership of the loan, compliance with loan

criteria set forth in the applicable agreement, validity of the lien securing the loan, absence of delinquent taxes or liens against the property securing the loan, and compliance with applicable origination laws. We may be required to repurchase mortgage loans, indemnify the investor or insurer, or reimburse the investor or insurer for credit losses incurred on loans in the event of a breach of contractual representations or warranties that is not remedied within a period (usually 90 days or less) after we receive notice of the breach. Contracts for mortgage loan sales to the GSEs include various types of specific remedies and penalties that could be applied to inadequate responses to repurchase requests. Similarly, the agreements under which we sell mortgage loans require us to deliver various documents to the investor, and we may be obligated to repurchase any mortgage loan as to which the required documents are not delivered or are defective. We establish a mortgage repurchase liability related to the various representations and warranties that reflect management's estimate of losses for loans which we have a repurchase obligation. Our mortgage repurchase liability represents management's best estimate of the probable loss that we may expect to incur for the representations and warranties in the contractual provisions of our sales of mortgage loans. Because the level of mortgage loan repurchase losses depends upon economic factors, investor demand strategies and other external conditions that may change over the life of the underlying loans, the level of the liability for mortgage loan repurchase losses is difficult to estimate and requires considerable management judgment. If economic conditions and the housing market deteriorate or future investor repurchase demand and our success at appealing repurchase requests differ from past experience, we could experience increased repurchase obligations and increased loss severity on repurchases, requiring additions to the repurchase liability.

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

Under U.S. GAAP, we are required to record loans acquired through acquisitions, including purchase credit impaired loans, at fair value. Estimating the fair value of such loans requires management to make estimates based on available information, facts, and circumstances on the acquisition date. Any discount, which is the excess of the amount of reasonably estimable and probable discounted future cash collections over the purchase price, is accreted into interest income over the weighted average remaining contractual life of the loans. Therefore, our net interest margins may initially increase due to the discount accretion. We expect the yields on the total loan portfolio

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will decline as our acquired loan portfolios pay down or mature and the corresponding accretion of the discount decreases. We expect downward pressure on our interest income to the extent that the runoff of our acquired loan portfolios is not replaced with comparable high-yielding loans. This could result in higher net interest margins and interest income in current periods and lower net interest margins and interest income in future periods.

We have recorded goodwill as a result of acquisitions that can significantly affect our earnings if it becomes impaired.

Under current accounting standards, goodwill is not amortized but, instead, is subject to impairment tests on at least an annual basis or more frequently if an event occurs or circumstances change that reduce the fair value of a reporting unit below its carrying value.

Item 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

| Period | Total number of shares (or units) purchased | Average price paid per share (or unit) | Total number of shares (or units) purchased as part of publicly announced plans or programs | Maximum number (or approximate dollar value) of shares (or units) that may yet be purchased under the plans or programs (2) |
|-------------------------------------|---|--|---|---|
| July 1 - July 31, 2018(1) | 3,553 | \$ 39.43 | — | \$ 12,562,825 |
| August 1 - August 31, 2018(1) | 3,729 | 40.23 | — | 12,562,825 |
| September 1 - September 30, 2018(1) | 370 | 37.76 | — | 12,562,825 |
| Total | 7,652 | \$ 39.74 | — | \$ 12,562,825 |

- (1) These shares represent shares purchased other than through publicly announced plans and were purchased pursuant to the Company's stock incentive plans. Pursuant to the plans, shares were purchased from plan participants at the then current market value in satisfaction of stock option exercise prices, settlements of restricted stock and tax withholdings.
- (2) On August 5, 2016, the Company's Board of Directors authorized the repurchase of up to an additional \$50.0 million of common stock. Under this authorization, \$12,562,825 remained available for purchase at September 30, 2018.

Item 5. OTHER INFORMATION

None.

Item 6. EXHIBITS

- 3.1 Second Amended and Restated Certificate of Incorporation (incorporated herein by reference to Exhibit 3.1 to our Form S-1 Registration Statement (Registration No. 333-177971), filed August 22, 2012)
- 3.2 Second Amended and Restated By-Laws (incorporated herein by reference to Exhibit 3.2 to our Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2014, filed November 7, 2014)
- 31.1 Certification of CEO pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- 31.2 Certification of CFO pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- 32 Certifications of CEO and CFO pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
- 101 Interactive data files pursuant to Rule 405 of Regulation S-T: (i) the Consolidated Statements of Financial Condition, (ii) the Consolidated Statements of Operations, (iii) the Consolidated Statements of Comprehensive Income, (iv) the Consolidated Statements of Changes in Shareholders' Equity, (v) the Consolidated Statements of Cash Flows and (vi) the Notes to Consolidated Financial Statements, tagged as blocks of text and in detail

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SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

National Bank Holdings Corporation

By /s/ Aldis Birkans
Aldis Birkans
Chief Financial Officer and Treasurer
(principal financial officer)

Date: November 7, 2018

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