National Bank Holdings Corp
Form 10-Q
May 04, 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 March 31, 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 incorporation or organization)	(I.R.S. Employer 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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes 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	(do not check if a smaller reporting company)	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 May 1, 2018, the registrant had outstanding 30,530,877 shares of Class A voting common stock, each with $0.01 par value per share, excluding 135,252 shares of restricted Class A common stock issued but not yet vested.

		Page
Part I. Financial Information		
Item 1.	Financial Statements (Unaudited)	3
	Consolidated Statements of Financial Condition as of March 31, 2018 and December 31, 2017	3
	Consolidated Statements of Operations for the three months ended March 31, 2018 and 2017	4
	Consolidated Statements of Comprehensive Income for the three months ended March 31, 2018 and 2017	5
	Consolidated Statements of Changes in Shareholders' Equity for the three months ended March 31, 2018 and 2017	6
	Consolidated Statements of Cash Flows for	7

	the three months ended March 31, 2018 and 2017	
	Notes to Consolidated Financial Statements	8
Item 2.	Management’s Discussion and Analysis of Financial Condition and Results of Operations	39
Item 3.	Quantitative and Qualitative Disclosures About Market Risk	65
Item 4.	Controls and Procedures	65
Part II. Other Information		
Item 1.	Legal Proceedings	66
Item 1A.	Risk Factors	66
Item 2.	Unregistered Sales of Equity Securities and Use of Proceeds	67
Item 5.	Other Information	67
Item 6.	Exhibits	67

Table of Contents

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," "t "continuing," "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;

Table of Contents

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.

Table of Contents

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)

	March 31, 2018	December 31, 2017
ASSETS		
Cash and due from banks	$ 260,731	$ 193,297
Interest bearing bank deposits	26,139	64,067
Cash and cash equivalents	286,870	257,364
Investment securities available-for-sale (at fair value)	917,865	855,345
Investment securities held-to-maturity (fair value of $278,716 and $256,771 at March 31, 2018 and December 31, 2017, respectively)	283,369	258,730
Non-marketable securities	14,088	15,030
Loans	3,702,334	3,178,947
Allowance for loan losses	(30,686)	(31,264)
Loans, net	3,671,648	3,147,683
Loans held for sale	51,050	4,629
Other real estate owned	11,875	10,491
Premises and equipment, net	112,038	93,708
Goodwill	114,909	59,630
Intangible assets, net	15,561	1,607
Other assets	178,310	139,248
Total assets	$ 5,657,583	$ 4,843,465
LIABILITIES AND SHAREHOLDERS' EQUITY		
Liabilities:		
Deposits:		
Non-interest bearing demand deposits	$ 1,083,245	$ 902,439
Interest bearing demand deposits	698,796	474,607
Savings and money market	1,779,817	1,484,463
Time deposits	1,147,452	1,118,050
Total deposits	4,709,310	3,979,559
Securities sold under agreements to repurchase	141,187	130,463
Federal Home Loan Bank advances	77,335	129,115
Other liabilities	83,888	71,921
Total liabilities	5,011,720	4,311,058
Shareholders' equity:		
Common stock, par value $0.01 per share: 400,000,000 shares authorized; 51,516,335 and 51,518,162 shares issued; 30,479,969 and 26,875,585	515	515

shares outstanding at March 31, 2018 and December 31, 2017, respectively		
Additional paid-in capital	1,012,268	970,668
Retained earnings	68,008	60,795
Treasury stock of 20,814,584 and 24,479,020 shares at March 31, 2018 and December 31, 2017, respectively, at cost	(420,040)	(493,329)
Accumulated other comprehensive loss, net of tax	(14,888)	(6,242)
Total shareholders’ equity	645,863	532,407
Total liabilities and shareholders’ equity	$ 5,657,583	$ 4,843,465

See accompanying notes to the consolidated interim financial statements.

3

Table of Contents

NATIONAL BANK HOLDINGS CORPORATION AND SUBSIDIARIES

Consolidated Statements of Operations (Unaudited)

(In thousands, except share and per share data)

	For the three months ended March 31,	
	2018	2017
Interest and dividend income:		
Interest and fees on loans	$ 45,280	$ 31,763
Interest and dividends on investment securities	6,526	6,613
Dividends on non-marketable securities	244	167
Interest on interest-bearing bank deposits	741	197
Total interest and dividend income	52,791	38,740
Interest expense:		
Interest on deposits	4,634	3,787
Interest on borrowings	510	231
Total interest expense	5,144	4,018
Net interest income before provision for loan losses	47,647	34,722
Provision for loan losses	41	1,795
Net interest income after provision for loan losses	47,606	32,927
Non-interest income:		
Service charges	4,510	3,326
Bank card fees	3,362	2,804
Mortgage banking income	7,971	454
Bank-owned life insurance income	452	470
Other non-interest income	1,150	1,414
OREO related income	390	228
Total non-interest income	17,835	8,696
Non-interest expense:		
Salaries and benefits	30,672	20,390
Occupancy and equipment	7,955	5,437
Telecommunications and data processing	4,366	1,587
Marketing and business development	1,224	651
FDIC deposit insurance	753	705
Bank card expense	2,136	883
Professional fees	2,819	416
Other non-interest expense	3,845	2,406
Problem asset workout	781	872
Loss (gain) on OREO sales, net	78	(112)
Core deposit intangible asset amortization	653	1,370
Total non-interest expense	55,282	34,605
Income before income taxes	10,159	7,018

Income tax expense (benefit)	1,695	(1,240)
Net income	$ 8,464	$ 8,258
Income per share—basic	$ 0.28	$ 0.31
Income per share—diluted	$ 0.27	$ 0.30
Weighted average number of common shares outstanding:		
Basic	30,493,689	26,801,773
Diluted	31,143,528	27,680,029

See accompanying notes to the consolidated interim financial statements.

Table of Contents

NATIONAL BANK HOLDINGS CORPORATION AND SUBSIDIARIES

Consolidated Statements of Comprehensive Income (Unaudited)

(In thousands)

	For the three months ended March 31,	
	2018	2017
Net income	$ 8,464	$ 8,258
Other comprehensive loss, net of tax:		
Securities available-for-sale:		
Net unrealized (losses) gains arising during the period, net of tax benefit (expense) of $2,301 and $(161) for the three months ended March 31, 2018 and 2017, respectively	(6,780)	263
Less: amortization of net unrealized holding gains to income, net of tax benefit of $70 and $218 for the three months ended March 31, 2018 and 2017, respectively	(387)	(357)
Other comprehensive loss	(7,167)	(94)
Comprehensive income	$ 1,297	$ 8,164

See accompanying notes to the consolidated interim financial statements.

Table of Contents

NATIONAL BANK HOLDINGS CORPORATION AND SUBSIDIARIES

Consolidated Statements of Changes in Shareholders' Equity (Unaudited)

Three months ended March 31, 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	—	—	8,258	—	—	8,258
Stock-based compensation	—	902	—	—	—	902
Issuance of stock under purchase and equity compensation plans, including gain on reissuance of treasury stock of $4,883, net	—	(11,314)	—	5,577	—	(5,737)
Cash dividends declared ($0.07 per share)	—	—	(1,900)	—	—	(1,900)
Warrant exercise	—	(1,933)	—	1,933	—	—
Other comprehensive loss	—	—	—	—	(94)	(94)
Balance, March 31, 2017	$ 514	$ 971,742	$ 61,812	$ (494,594)	$ (1,856)	$ 537,618
Balance, December 31, 2017	$ 515	$ 970,668	$ 60,795	$ (493,329)	$ (6,242)	$ 532,407
Net income	—	—	8,464	—	—	8,464
Stock-based compensation	—	833	—	—	—	833
Issuance of stock under purchase and equity compensation plans, including gain on reissuance of treasury stock of $3,566, net	—	(1,476)	—	5,319	—	3,843
Reissuance of treasury stock of 3,398,477 for acquisition of Peoples, Inc.	—	42,243	—	67,970	—	110,213
Cash dividends declared ($0.09 per share)	—	—	(2,756)	—	—	(2,756)

Reclassification of certain tax effects from accumulated other comprehensive income(1)	—	—	1,479	—	(1,479)	—
Cumulative effect adjustment(2)	—	—	26	—	—	26
Other comprehensive loss	—	—	—	—	(7,167)	(7,167)
Balance, March 31, 2018	$ 515	$ 1,012,268	$ 68,008	$ (420,040)	$ (14,888)	$ 645,863

(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.

Table of Contents

NATIONAL BANK HOLDINGS CORPORATION AND SUBSIDIARIES

Consolidated Statements of Cash Flows (Unaudited)

(In thousands)

	For the three months ended March 31,	
	2018	2017
Cash flows from operating activities:		
Net income	$ 8,464	$ 8,258
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for loan losses	41	1,795
Depreciation and amortization	2,983	3,341
Current income tax receivable	(4,233)	444
Deferred income taxes	(609)	(1,734)
Net excess tax benefit on stock-based compensation	(371)	(2,845)
Discount accretion, net of premium amortization on securities	821	703
Loan accretion	(6,508)	(6,191)
Gain on sale of mortgages, net	(6,803)	(454)
Origination of loans held for sale, net of repayments	(219,584)	(14,925)
Proceeds from sales of loans held for sale	235,104	32,194
Bank-owned life insurance income	(452)	(470)
Loss (gain) on the sale of other real estate owned, net	78	(112)
Impairment on other real estate owned	38	46
Gain on fixed assets	—	(3)
Stock-based compensation	833	902
Change in other assets	(5,630)	(3,280)
Change in other liabilities	6,337	3,576
Net cash provided by operating activities	10,509	21,245
Cash flows from investing activities:		
Purchase of FHLB stock	(2,950)	—
Proceeds from redemption of FHLB stock	8,690	1,884
Proceeds from maturities of investment securities held-to-maturity	15,526	18,350
Proceeds from maturities of investment securities available-for-sale	55,152	59,155
Proceeds from sales of investment securities available-for-sale	33,202	—
Purchase of investment securities available-for-sale	(42,199)	(96,948)
Purchase of investment securities held-to-maturity	(40,735)	—
Net decrease (increase) in loans	9,136	(87,543)
Purchases of premises and equipment, net	(1,905)	(783)
Proceeds from sales of loans	—	20,269
Proceeds from sales of other real estate owned	36	755
Net cash activity from acquisition	68,983	—
Net cash provided by (used in) investing activities	102,936	(84,861)
Cash flows from financing activities:		
Net (decrease) increase in deposits	(160)	99,294

Increase (decrease) in repurchase agreements	10,724	(314)
Advances from FHLB	—	92,798
FHLB payoffs	(85,605)	(54,683)
Issuance of stock under purchase and equity compensation plans	(517)	(5,737)
Proceeds from exercise of stock options	4,360	—
Payment of dividends	(2,741)	(2,048)
Net cash (used in) provided by financing activities	(73,939)	129,310
Increase in cash, cash equivalents and restricted cash	39,506	65,694
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	$ 296,870	$ 218,430
Supplemental disclosure of cash flow information during the period:		
Cash paid for interest	$ 3,723	$ 2,745
Net tax refunds (payments)	$ 164	$ (7)
Supplemental schedule of non-cash investing activities:		
Loans transferred to other real estate owned at fair value	$ 127	$ 578
(Decrease) increase in loans purchased but not settled	$ (15,068)	$ 16,141
Loans transferred from loans held for sale to loans	$ 878	$ 3,825
Treasury stock reissued for acquisition	$ 110,213	$ —

See accompanying notes to the consolidated interim financial statements.

Table of Contents

NATIONAL BANK HOLDINGS CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

March 31, 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 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 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 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 and notes 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

current period mortgage banking income and, through a reduction in the valuation allowance, adjusts the carrying value of the MSRs 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 and by servicing mortgage loans to meet investor and secondary market standards.

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 FASB issued 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. 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 principals 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. A modified retrospective transition approach is required for lessees for capital and operating leases existing at, or entered into after, the beginning of the earliest comparative period presented in the financial statements. The Company expects to adopt ASU 2016-02 in the first quarter of 2019 and is currently in the process of evaluating the impact of the ASU's adoption on the Company's consolidated financial statements.

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

Table of Contents

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 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.

The company 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 does not expect the adoption of this pronouncement to have a material impact on its financial statements.

Note 3 Acquisition Activities

On January 1, 2018, the Company completed its acquisition of Peoples, Inc., 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 the Company is indemnified for pursuant to the merger agreement. The restricted cash is included in other assets in the Company's consolidated statements of financial condition at March 31, 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 $7.6 million were included in the Company's consolidated statements of operations for the three months ended March 31, 2018. The results of Peoples are included in the 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.

Table of Contents

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	1,409
Premises and equipment	18,584
Core deposit intangible asset	10,477
Mortgage servicing rights	4,301
Other assets	15,324
Total assets acquired	$ 875,543
Liabilities:	
Total deposits	729,911
FHLB borrowings	33,825
Other liabilities	20,683
Total liabilities assumed	$ 784,419
Identifiable net assets acquired	$ 91,124
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	$ 55,278

In connection with the Peoples acquisition, the Company recorded $55.3 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 FHLB borrowings of $33.9 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, none of the loans were accounted for under the guidance of ASC Topic 310-30, and the gross contractual amounts receivable, inclusive of all principal and interest, was $713.6 million. The Company's best estimate of the contractual 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. 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 $65.5 million and $61.6 million for the three months ended March 31, 2018 and 2017, respectively. Pro forma net income for the Company would have been approximately $14.5 million and $9.9 million for the three month ended March 31, 2018 and 2017, respectively. Pro forma basic and dilutive earnings per share for the Company would have been $0.48 and $0.47 for the three months ended March 31, 2018, respectively, and $0.33 and $0.32 for the three months ended March 31, 2017, respectively.

Table of Contents

For the three months ended March 31, 2018, the pro forma information reflects adjustments made to exclude acquisition-related expenses of the Company of $7.6 million. For the three months ended March 31, 2017, the pro-forma information reflects adjustments made to include estimated amortization and accretion of purchase discounts and premiums of $0.2 million and estimated amortization of acquired identifiable intangibles of $0.3 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 $1.2 billion at March 31, 2018 and included $0.9 billion of available-for-sale securities and $0.3 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.

Available-for-sale

At March 31, 2018 and December 31, 2017, the Company held $0.9 billion of available-for-sale investment securities. Available-for-sale securities are summarized as follows as of the dates indicated:

	March 31, 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	$ 189,430	$ 1,635	$ (2,435)	$ 188,630
Other residential MBS issued or guaranteed by U.S. Government agencies or sponsored enterprises	751,497	151	(23,919)	727,729

Municipal securities	1,054	—	(17)	1,037
Other securities	469	—	—	469
Total investment securities available-for-sale	$ 942,450	$ 1,786	$ (26,371)	$ 917,865

	December 31, 2017			
	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	$ 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 March 31, 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”).

Table of Contents

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:

	March 31, 2018					
	Less than 12 months		12 months or more		Total	
	Fair value	Unrealized losses	Fair value	Unrealized losses	Fair value	Unrealized losses
Mortgage-backed securities ("MBS"):						
Residential mortgage pass-through securities issued or guaranteed by U.S. Government agencies or sponsored enterprises	$ 99,713	$ (1,579)	$ 32,040	$ (856)	$ 131,753	$ (2,435)
Other residential MBS issued or guaranteed by U.S. Government agencies or sponsored enterprises	274,644	(3,894)	385,797	(20,025)	660,441	(23,919)
Municipal securities	503	(17)	—	—	503	(17)
Total	$ 374,860	$ (5,490)	$ 417,837	$ (20,881)	$ 792,697	$ (26,371)

	December 31, 2017					
	Less than 12 months		12 months or more		Total	
	Fair value	Unrealized losses	Fair value	Unrealized losses	Fair value	Unrealized losses
Mortgage-backed securities ("MBS"):						
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 March 31, 2018 were caused by changes in interest rates. The portfolio included 205 securities, having an aggregate fair value of $792.7 million, which were in an

unrealized loss position at March 31, 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 March 31, 2018 and December 31, 2017, and identified one municipal security with other-than-temporary impairment (OTTI), with an aggregate fair value of $0.3 million and $0.3 million, respectively. No OTTI charges were recorded during the three months ended March 31, 2018 and 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 Federal Home Loan Bank (“FHLB”), if needed. The fair value of available-for-sale investment securities pledged as collateral totaled $427.8 million and $334.6 million at March 31, 2018 and December 31, 2017, respectively. Certain investment securities may also be pledged as collateral for the line of credit at the FHLB; at March 31, 2018 or December 31, 2017, no securities were pledged for this purpose.

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 March 31, 2018 and December 31, 2017, respectively. This estimate is based on assumptions and actual results may differ. At March 31, 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 March 31, 2018, municipal securities with an amortized cost and fair value of $0.2 million were due after one year through five years, while municipal securities with an amortized cost and fair value of $0.5 million were due after five years through ten years. Other securities and municipal securities of $0.8 million as of March 31, 2018, have no stated contractual maturity date.

Table of Contents

Held-to-maturity

At March 31, 2018 and December 31, 2017, the Company held $283.4 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:

	March 31, 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	$ 191,136	$ 8	$ (2,535)	$ 188,609
Other residential MBS issued or guaranteed by U.S. Government agencies or sponsored enterprises	92,233	5	(2,131)	90,107
Total investment securities held-to-maturity	$ 283,369	$ 13	$ (4,666)	$ 278,716

	December 31, 2017			
	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	$ 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:

March 31, 2018					
Less than 12 months		12 months or more		Total	
Fair	Unrealized	Fair	Unrealized	Fair	Unrealized

	Fair value	Unrealized losses	Fair value	Unrealized losses	Fair value	Unrealized losses
Mortgage-backed securities ("MBS"):						
Residential mortgage pass-through securities issued or guaranteed by U.S. Government agencies or sponsored enterprises	$ 171,017	$ (2,059)	$ 16,202	$ (476)	$ 187,219	$ (2,535)
Other residential MBS issued or guaranteed by U.S. Government agencies or sponsored enterprises	6,018	(139)	43,350	(1,992)	49,368	(2,131)
Total	$ 177,035	$ (2,198)	$ 59,552	$ (2,468)	$ 236,587	$ (4,666)

	December 31, 2017					
	Less than 12 months		12 months or more		Total	
	Fair value	Unrealized losses	Fair value	Unrealized losses	Fair value	Unrealized losses
Mortgage-backed securities ("MBS"):						
Residential mortgage pass-through securities issued or guaranteed by U.S. Government agencies or sponsored enterprises	$ 149,182	$ (220)	$ 17,506	$ (235)	$ 166,688	$ (455)
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 48 securities, having an aggregate fair value of $236.6 million, which were in an unrealized loss position at March 31, 2018, compared to 36 securities, with a fair value of $219.4 million, at December 31, 2017.

Table of Contents

Management evaluated all of the held-to-maturity securities in an unrealized loss position and concluded that no OTTI existed at March 31, 2018 or December 31, 2017. The unrealized losses in the Company's investments at March 31, 2018 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.

The carrying value of held-to-maturity investment securities pledged as collateral totaled $140.8 million and $142.0 million at March 31, 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 March 31, 2018 and December 31, 2017 was 3.1 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 2.6 years and 2.8 years as of March 31, 2018 and December 31, 2017, respectively.

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 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 loans accounted for under ASC Topic 310-30, Receivables—Loans and Debt Securities Acquired with Deteriorated Credit Quality, and originated and acquired loans, as of the dates shown. The carrying value of originated and acquired loans is net of discounts, fees, cost and fair value marks of $11.2 million and $4.3 million as of March 31, 2018 and December 31, 2017, respectively.

	March 31, 2018			
	ASC 310-30 loans	Originated and acquired loans	Total loans	% of total
Commercial	$ 24,702	$ 2,081,197	$ 2,105,899	56.9%
Commercial real estate non-owner occupied	75,277	635,438	710,715	19.2%

Residential real estate	12,000	847,155	859,155	23.2%
Consumer	330	26,235	26,565	0.7%
Total	$ 112,309	$ 3,590,025	$ 3,702,334	100.0%

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

Table of Contents

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

	March 31, 2018							
	30-59 days past due	60-89 days past due	Greater than 90 days past due	Total past due	Current	Total originated and acquired loans	Loans > 90 days past due and still accruing	Non-accrual
Originated and acquired loans:								
Commercial:								
Commercial and industrial	$ 1,083	$ 116	$ 1,214	$ 2,413	$ 1,492,675	$ 1,495,088	$ 150	$ 5,302
Owner occupied commercial real estate	440	534	2,790	3,764	380,483	384,247	535	7,202
Agriculture	151	—	734	885	160,764	161,649	16	2,103
Energy	—	—	923	923	39,290	40,213	—	923
Total commercial	1,674	650	5,661	7,985	2,073,212	2,081,197	701	15,530
Commercial real estate non-owner occupied:								
Construction	465	941	642	2,048	110,038	112,086	642	—
Acquisition/development	—	—	51	51	23,058	23,109	51	833
Multifamily	—	—	29	29	51,712	51,741	—	29
Non-owner occupied	—	10	—	10	448,492	448,502	—	613
Total commercial real estate	465	951	722	2,138	633,300	635,438	693	1,475
Residential real estate:								
Senior lien	2,535	309	1,517	4,361	744,083	748,444	238	5,918
Junior lien	1,002	238	40	1,280	97,431	98,711	—	710
Total residential real estate	3,537	547	1,557	5,641	841,514	847,155	238	6,628
Consumer	204	22	140	366	25,869	26,235	135	36
Total originated and acquired loans	$ 5,880	$ 2,170	$ 8,080	$ 16,130	$ 3,573,895	$ 3,590,025	$ 1,767	$ 23,669

	December 31, 2017						
	30-59	60-89	Greater than 90			Total originated and	Loans > 90 days past

	days past due	days past due	days past due	Total past due	Current	acquired loans	due and still accruing	Non-accrual
Originated and acquired loans:								
Commercial:								
Commercial and industrial	$ 554	$ 117	$ 1,389	$ 2,060	$ 1,373,962	$ 1,376,022	$ 150	$ 7,767
Owner occupied commercial real estate	696	—	1,983	2,679	270,074	272,753	—	3,478
Agriculture	585	—	701	1,286	137,609	138,895	—	2,003
Energy	—	—	1,645	1,645	55,815	57,460	—	1,645
Total commercial	1,835	117	5,718	7,670	1,837,460	1,845,130	150	14,893
Commercial real estate non-owner occupied:								
Construction	—	—	179	179	107,502	107,681	—	179
Acquisition/development	1,097	—	—	1,097	13,318	14,415	—	—
Multifamily	—	—	—	—	26,947	26,947	—	—
Non-owner occupied	56	—	574	630	335,468	336,098	—	605
Total commercial real estate	1,153	—	753	1,906	483,235	485,141	—	784
Residential real estate:								
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 accreting are generally considered to be performing and therefore are not included in the tables above. Non-accrual loans include troubled debt restructurings on non-accrual status.

Non-accrual originated and acquired loans totaled $23.7 million at March 31, 2018, increasing $2.7 million, or 12.7% from December 31, 2017, due to acquired Peoples loans on non-accrual of $5.7 million, partially offset by one previously identified commercial and industrial loan of $2.3 million placed back on accrual during the first quarter of 2018.

The Company’s internal risk rating system uses a series of grades which reflect our 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

16

Table of Contents

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.

Credit exposure for all loans as determined by the Company’s internal risk rating system was as follows at March 31, 2018 and December 31, 2017:

	March 31, 2018				
	Pass	Special mention	Substandard	Doubtful	Total
Originated and acquired loans:					
Commercial:					
Commercial and industrial	$ 1,460,896	$ 13,070	$ 20,219	$ 903	$ 1,495,088
Owner occupied commercial real estate	348,533	25,493	10,148	73	384,247
Agriculture	156,059	3,487	1,902	201	161,649
Energy	39,290	—	923	—	40,213
Total commercial	2,004,778	42,050	33,192	1,177	2,081,197
Commercial real estate non-owner occupied:					
Construction	110,850	—	1,236	—	112,086
Acquisition/development	22,276	—	833	—	23,109
Multifamily	49,605	—	2,136	—	51,741
Non-owner occupied	430,437	15,133	2,932	—	448,502
Total commercial real estate	613,168	15,133	7,137	—	635,438
Residential real estate:					
Senior lien	736,336	5,720	6,388	—	748,444
Junior lien	97,103	547	1,061	—	98,711
Total residential real estate	833,439	6,267	7,449	—	847,155
Consumer	26,197	1	37	—	26,235
Total originated and acquired loans	$ 3,477,582	$ 63,451	$ 47,815	$ 1,177	$ 3,590,025
Loans accounted for under ASC 310-30:					
Commercial	$ 19,846	$ 1,073	$ 3,783	$ —	$ 24,702
Commercial real estate non-owner occupied	48,174	912	26,191	—	75,277
Residential real estate	9,306	1,074	1,620	—	12,000
Consumer	208	8	114	—	330
Total loans accounted for under ASC 310-30	$ 77,534	$ 3,067	$ 31,708	$ —	$ 112,309

Total loans	$ 3,555,116	$ 66,518	$ 79,523	$ 1,177	$ 3,702,334

Table of Contents

	December 31, 2017				
	Pass	Special mention	Substandard	Doubtful	Total
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	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

Originated and acquired special mention loans increased $15.3 million from December 31, 2017, primarily due to increases in commercial and industrial, owner occupied commercial real estate and non-owner occupied commercial real estate sectors from the Peoples acquisition, offset by upgrades to pass within the agriculture sector. Originated and acquired substandard loans increased $14.2 million from December 31, 2017, primarily due to increases in the commercial and industrial and owner occupied commercial real estate sectors from the Peoples acquisition.

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 March 31, 2018, the Company measured $17.9 million of impaired loans based on the fair value of the collateral less selling costs and $2.3 million of impaired loans using discounted cash flows and the loan's initial contractual effective interest rate. Impaired loans totaling $8.7 million that individually were less than $250 thousand each, were measured through the general ALL reserves due to their relatively small size. Impaired loans acquired from Peoples totaling $5.8 million were marked to fair value at the date of acquisition.

At March 31, 2018 and December 31, 2017, the Company's recorded investment in impaired loans were $34.7 million and $30.9 million, respectively, of which $8.7 million and $8.5 million, respectively, were accruing TDRs. Impaired loans at March 31, 2018 were primarily comprised of seven relationships totaling $14.9 million. Three of the relationships were in the commercial and industrial sector totaling $7.5 million, two of the relationships were in the owner occupied commercial real estate sector totaling $4.9 million, one of the relationships was in the energy sector totaling $1.3 million and one relationship was in the agricultural sector totaling $1.2 million. Impaired loans had a collective related allowance for loan losses allocated to them of $1.2 million and $1.5 million at March 31, 2018 and December 31, 2017, respectively.

Table of Contents

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

	March 31, 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	$ 7,036	$ 5,562	$ —	$ 6,481	$ 5,055	$ —
Owner occupied commercial real estate	7,726	7,464	—	4,186	3,934	—
Agriculture	1,508	1,259	—	1,502	1,245	—
Energy	6,889	2,171	—	8,661	3,861	—
Total commercial	23,159	16,456	—	20,830	14,095	—
Commercial real estate non-owner occupied:						
Construction	—	—	—	215	179	—
Acquisition/development	1,065	833	—	—	—	—
Multifamily	29	29	—	29	29	—
Non-owner occupied	962	845	—	901	853	—
Total commercial real estate	2,056	1,707	—	1,145	1,061	—
Residential real estate:						
Senior lien	1,738	1,563	—	333	309	—
Junior lien	393	300	—	—	—	—
Total residential real estate	2,131	1,863	—	333	309	—
Consumer	42	39	—	—	—	—
Total impaired loans with no related allowance recorded	$ 27,388	$ 20,065	$ —	$ 22,308	$ 15,465	$ —
With a related allowance recorded:						
Commercial:						
Commercial and industrial	$ 6,884	$ 4,284	$ 906	$ 7,919	$ 5,339	$ 1,329
Owner occupied commercial real estate	1,421	1,253	78	873	713	4
Agriculture	2,225	2,182	201	2,122	2,083	133
Energy	—	—	—	—	—	—
Total commercial	10,530	7,719	1,185	10,914	8,135	1,466
Commercial real estate non-owner occupied:						
Construction	—	—	—	—	—	—
Acquisition/development	—	—	—	—	—	—
Multifamily	—	—	—	—	—	—
Non-owner occupied	200	193	1	207	200	1
Total commercial real estate	200	193	1	207	200	1
Residential real estate:						

Senior lien	6,329	5,553	24	6,481	5,753	24
Junior lien	1,262	1,142	7	1,295	1,179	8
Total residential real estate	7,591	6,695	31	7,776	6,932	32
Consumer	—	—	—	146	141	1
Total impaired loans with a related allowance recorded	$ 18,321	$ 14,607	$ 1,217	$ 19,043	$ 15,408	$ 1,500
Total impaired loans	$ 45,709	$ 34,672	$ 1,217	$ 41,351	$ 30,873	$ 1,500

Table of Contents

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			
	March 31, 2018		March 31, 2017	
	Average recorded investment	Interest income recognized	Average recorded investment	Interest income recognized
With no related allowance recorded:				
Commercial:				
Commercial and industrial	$ 5,534	$ 83	$ 8,095	$ 48
Owner occupied commercial real estate	7,487	18	3,885	18
Agriculture	1,259	6	2,588	—
Energy	2,353	20	6,098	—
Total commercial	16,633	127	20,666	66
Commercial real estate non-owner occupied:				
Construction	—	—	—	—
Acquisition/development	886	—	—	—
Multifamily	—	—	—	—
Non-owner occupied	876	4	329	7
Total commercial real estate	1,762	4	329	7
Residential real estate:				
Senior lien	1,612	—	1,047	3
Junior lien	305	—	—	—
Total residential real estate	1,917	—	1,047	3
Consumer	14	—	4	—
Total impaired loans with no related allowance recorded	$ 20,326	$ 131	$ 22,046	$ 76
With a related allowance recorded:				
Commercial:				
Commercial and industrial	$ 4,339	$ —	$ 3,445	$ —
Owner occupied commercial real estate	1,265	5	678	5
Agriculture	2,126	1	156	1
Energy	—	—	6,589	—
Total commercial	7,730	6	10,868	6
Commercial real estate non-owner occupied:				
Construction	—	—	—	—
Acquisition/development	—	—	—	—
Multifamily	29	—	32	—
Non-owner occupied	196	2	223	3
Total commercial real estate	225	2	255	3
Residential real estate:				
Senior lien	5,601	13	5,791	21
Junior lien	1,151	9	1,625	13
Total residential real estate	6,752	22	7,416	34
Consumer	24	—	181	—
Total impaired loans with a related allowance recorded	$ 14,731	$ 30	$ 18,720	$ 43

Total impaired loans	$ 35,057	$ 161	$ 40,766	$ 119

Interest income recognized on impaired loans noted in the table above primarily represents interest earned on accruing troubled debt restructurings. Interest income recognized on impaired loans during the three months ended March 31, 2018 and 2017 was $0.2 million and $0.1 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.

Table of Contents

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.

During the three months ended March 31, 2018, the Company restructured four loans with a recorded investment of $0.9 million 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 March 31, 2018 and December 31, 2017:

	March 31, 2018			
	Recorded investment	Average year-to-date recorded investment	Unpaid principal balance	Unfunded commitments to fund TDRs
Commercial	$ 7,045	$ 6,985	$ 7,832	$ 1,902
Commercial real estate non-owner occupied	426	431	471	—
Residential real estate	1,205	1,213	1,214	2
Consumer	—	—	—	—
Total	$ 8,676	$ 8,629	$ 9,517	$ 1,904

	December 31, 2017			
	Recorded investment	Average year-to-date recorded investment	Unpaid principal balance	Unfunded commitments to fund TDRs
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 March 31, 2018 and December 31, 2017:

	March 31, 2018	December 31, 2017
Commercial	$ 3,113	$ 5,808
Commercial real estate non-owner occupied	29	—
Residential real estate	1,537	1,336

Consumer	—	111
Total non-accruing TDRs	$ 4,679	$ 7,255

At March 31, 2018 and December 31, 2017, the Company had $8.7 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 on non-accrual only after the loan has performed sufficiently. The Company had one TDR that was modified within the past twelve months and had defaulted on its restructured terms during the three months ended March 31, 2018. The defaulted TDR consisted of one commercial real estate non-owner occupied loan totaling $0.2 million. Non-accruing TDRs decreased $2.6 million from December 31, 2017 due to one previously identified commercial and industrial loan of $2.3 million placed back on accrual during the period. 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 troubled debt restructurings.

During the three months ended March 31, 2017, the Company had one TDR that was modified within the past twelve months and had defaulted on its restructured terms. For purposes of this disclosure, the Company considers "default" to mean 90 days or more past due on principal or interest.

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

Table of Contents

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 three months ended March 31, 2018 and 2017:

	March 31, 2018	March 31, 2017
Accretable yield beginning balance	$ 46,568	$ 60,476
Reclassification from non-accretable difference	5,409	5,385
Reclassification to non-accretable difference	(1,390)	(399)
Accretion	(5,394)	(5,871)
Accretable yield ending balance	$ 45,193	$ 59,591

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

	March 31, 2018	December 31, 2017
Contractual cash flows	$ 488,637	$ 489,892
Non-accretable difference	(331,135)	(322,701)
Accretable yield	(45,193)	(46,568)
Loans accounted for under ASC 310-30	$ 112,309	$ 120,623

Note 6 Allowance for Loan Losses

The tables below detail the Company's allowance for loan losses and recorded investment in loans as of and for the three months ended March 31, 2018 and 2017:

	Three months ended March 31, 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)	—	—	(279)	(716)
Recoveries	42	—	2	53	97
Provision	540	(712)	(39)	211	—
Originated and acquired ending balance	21,485	4,871	3,928	290	30,574
ASC 310-30 beginning balance	45	26	—	—	71
Charge-offs	—	—	—	—	—
Recoveries	—	—	—	—	—
Provision (recoupment)	48	(7)	—	—	41
ASC 310-30 ending balance	93	19	—	—	112
Ending balance	$ 21,578	$ 4,890	$ 3,928	$ 290	$ 30,686
Ending allowance balance attributable to:					
Originated and acquired loans individually evaluated for impairment	$ 1,185	$ 2	$ 31	$ —	$ 1,218
Originated and acquired loans collectively evaluated for impairment	20,300	4,868	3,897	290	29,355
ASC 310-30 loans	93	20	—	—	113
Total ending allowance balance	$ 21,578	$ 4,890	$ 3,928	$ 290	$ 30,686
Loans:					
Originated and acquired loans individually evaluated for impairment	$ 24,175	$ 1,901	$ 8,558	$ 38	$ 34,672
Originated and acquired loans collectively evaluated for impairment	2,057,022	633,537	838,597	26,197	3,555,353
ASC 310-30 loans	24,702	75,277	12,000	330	112,309
Total loans	$ 2,105,899	$ 710,715	$ 859,155	$ 26,565	$ 3,702,334

Table of Contents

	Three months ended March 31, 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	(20)	—	(8)	(182)	(210)
Recoveries	11	10	3	67	91
Provision	1,727	167	(166)	72	1,800
Originated and acquired ending balance	20,539	5,599	4,216	276	30,630
ASC 310-30 beginning balance	—	220	—	5	225
Charge-offs	—	—	—	—	—
Recoveries	—	—	—	—	—
Recoupment	—	(4)	—	(1)	(5)
ASC 310-30 ending balance	—	216	—	4	220
Ending balance	$ 20,539	$ 5,815	$ 4,216	$ 280	$ 30,850
Ending allowance balance attributable to:					
Originated and acquired loans individually evaluated for impairment	$ 2,866	$ 1	$ 47	$ 2	$ 2,916
Originated and acquired loans collectively evaluated for impairment	17,673	5,598	4,169	274	27,714
ASC 310-30 loans	—	216	—	4	220
Total ending allowance balance	$ 20,539	$ 5,815	$ 4,216	$ 280	$ 30,850
Loans:					
Originated and acquired loans individually evaluated for impairment	$ 31,946	$ 574	$ 8,403	$ 180	$ 41,103
Originated and acquired loans collectively evaluated for impairment	1,572,715	450,577	722,582	26,614	2,772,488
ASC 310-30 loans	36,935	86,842	15,470	817	140,064
Total loans	$ 1,641,596	$ 537,993	$ 746,455	$ 27,611	$ 2,953,655

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 charge-offs on originated and acquired loans during the three months ended March 31, 2018 were $0.6 million. No provision was recorded for loan losses on originated and acquired loans during the three months ended March 31, 2018. During the three months ended March 31, 2017, the Company had $0.1 million of net charge offs on originated and acquired loans and recorded a provision for loan losses on originated and acquired loans of $1.8 million, driven by loan growth and increased reserves of $0.5 million for one energy sector credit previously placed on non-accrual.

During the three months ended March 31, 2018 and 2017, the Company re-estimated the expected cash flows of the loan pools accounted for under ASC 310-30. The re-measurement during the three months ended March 31, 2018 resulted in a net provision of $41 thousand. The re-measurement during the three months ended March 31, 2017 resulted in a net recoupment of $5 thousand for the three months ended March 31, 2017.

Table of Contents

Note 7 Other Real Estate Owned

A summary of the activity in the OREO balances during the three months ended March 31, 2018 and 2017 is as follows:

	For the three months ended March 31,	
	2018	2017
Beginning balance	$ 10,491	$ 15,662
Acquired through acquisition	1,409	—
Transfers from loan portfolio, at fair value	127	578
Impairments	(38)	(46)
Sales, net	(114)	(642)
Ending balance	$ 11,875	$ 15,552

The Company did not have any minority interest in participated other real estate owned at March 31, 2018. At December 31, 2017, OREO balances excluded $0.7 million of the Company's minority interests in OREO, which are held by outside banks where the Company was not the lead bank and does not have a controlling interest. The Company maintains a receivable in other assets for these minority interests. Included in Sales, net are losses of $78 thousand for the three months ended March 31, 2018 and gains of $112 thousand for the three months ended March 31, 2017.

Note 8 Goodwill and Intangible Assets

In connection with acquisitions, the Company recorded goodwill of $114.9 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 $55.3 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 assets acquired. No goodwill impairment was recorded during the three months ended March 31, 2018 or the year ended December 31, 2017.

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 $0.7 million and $1.4 million during the three months ended March 31, 2018 and 2017, respectively.

Mortgage servicing rights represent rights to service loans originated by the Company and sold to government sponsored enterprises including Freddie Mac (FHLMC), Fannie Mae (FNMA), Ginnie Mae(GNMA) and Federal Home Loan Bank (FHLB). Mortgage loans serviced for others were $441.0 million at March 31, 2018.

The gross carrying amount of intangible assets and the associated accumulated amortization at March 31, 2018 and December 31, 2017, are presented as follows:

	March 31, 2018			December 31, 2017		
	Gross carrying amount	Accumulated amortization	Net carrying amount	Gross carrying amount	Accumulated amortization	Net carrying amount
Core deposit intangible	$ 48,834	$ 37,403	$ 11,431	$ 38,357	$ 36,750	$ 1,607
Mortgage servicing rights	4,301	171	4,130	—	—	—
Total	$ 53,135	$ 37,574	$ 15,561	$ 38,357	$ 36,750	$ 1,607

Table of Contents

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

	For the three months ended March 31, 2018
Beginning balance	$ —
Purchased through acquisitions	4,301
Amortization	(171)
Ending balance	$ 4,130
Fair value of mortgage servicing rights	$ 4,712

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 during the three months ended March 31, 2018.

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 8.7% to 11.3% for the March 31, 2018 valuation.

Mortgage servicing rights are evaluated for impairment and recognized through a valuation allowance 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 is no valuation allowance at March 31, 2018.

Note 9 Borrowings

As of March 31, 2018 and December 31, 2017, the Company sold securities under agreements to repurchase totaling $141.2 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 $166.3 million and $136.1 million as of March 31, 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 March 31, 2018 and December 31, 2017, the Company had $25.1 million and $5.7 million of excess collateral pledged for repurchase agreements.

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 $847.9 million at March 31, 2018. At March 31, 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 pledged as collateral for FHLB advances in the amount of $27.8 million at March 31, 2018 and $28.1 million at December 31, 2017. Interest expense related to FHLB advances totaled $460 thousand and $197 thousand for the three months ended March 31, 2018 and 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, 2016, 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.

Under the Basel III requirements, at March 31, 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.

Table of Contents

	March 31, 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	9.6%	$ 527,873	N/A	N/A	4.0%	$ 220,218
NBH Bank	8.8%	482,069	5.0%	$ 273,067	4.0%	218,454
Common equity tier 1 risk-based capital:						
Consolidated	12.4%	$ 527,873	N/A	N/A	7.0%	$ 385,382
NBH Bank	11.4%	482,069	6.5%	$ 354,987	7.0%	382,294
Tier 1 risk-based capital ratio:						
Consolidated	12.4%	$ 527,873	N/A	N/A	8.5%	$ 361,114
NBH Bank	11.4%	482,069	8.0%	$ 338,103	8.5%	359,234
Total risk-based capital ratio:						
Consolidated	13.2%	$ 559,623	N/A	N/A	10.5%	$ 446,082
NBH Bank	12.2%	513,819	10.0%	$ 422,628	10.5%	443,760

	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 Customers

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.

Table of Contents

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 months ended March 31, 2018 and 2017.

	For the three months ended March 31,	
	2018	2017
Non-interest income		

In-scope of Topic 606:		
Service Charges and other fees	$ 5,175	$ 3,791
Bank card fees	3,362	2,804
Non-interest income (in-scope of Topic 606)	8,537	6,595
Non-interest income (out-of-scope of Topic 606)	9,298	2,101
Total non-interest income	$ 17,835	$ 8,696
Non-interest expense		
In-scope of Topic 606:		
Loss (gain) on OREO sales, net	78	(112)
Total revenue in-scope of Topic 606	$ 8,615	$ 6,483

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 March 31, 2018 and December 31, 2017, the Company did not have any contract balances.

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 customer 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 customer 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 three months ended March 31, 2018 and 2017 in accordance with the 2014 Plan, which are time-vesting with 1/3 vesting on each of the first, second and third anniversary of the date of grant.

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 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 three months ended March 31, 2018:

	Options	Weighted average exercise price	Weighted average remaining contractual term in years	Aggregate intrinsic value
Outstanding at December 31, 2017	1,598,318	$ 20.62	4.07	$ 19,017
Granted	148,198	32.74		
Exercised	(220,877)	19.74		
Forfeited	(9,595)	27.69		
Outstanding at March 31, 2018	1,516,044	$ 21.89	4.38	$ 17,295
Options exercisable at March 31, 2018	1,152,875	$ 19.85	2.95	$ 15,450
Options vested and expected to vest	1,477,364	$ 21.64	4.24	$ 17,220

Stock option expense is a component of salaries and benefits in the consolidated statements of operations and totaled $0.2 million for the three months ended March 31, 2018 and 2017, respectively. At March 31, 2018, there was $1.2 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 2.7 years.

Restricted stock awards

The Company issued time based restricted stock awards during the three months ended March 31, 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.

Table of Contents

No market-based stock awards were granted during the first quarter of 2018 or 2017. During the three months ended March 31, 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 had 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 0.9 years.

Performance stock units

During the three months ended March 31, 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 three months ended March 31, 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 three months ended March 31, 2018:

	Restricted	Weighted average grant-	Performance	Weighted average grant-

	stock shares	date fair value	stock units	date fair value
Unvested at December 31, 2017	163,557	$ 22.60	125,082	$ 23.90
Granted	66,321	32.84	77,125	30.38
Vested	(182)	18.48	—	—
Forfeited	(7,914)	28.20	(5,351)	28.05
Unvested at March 31, 2018	221,782	$ 25.47	196,856	$ 26.33

As of March 31, 2018, the total unrecognized compensation cost related to the non-vested restricted stock awards and performance stock units totaled $2.5 million and $3.1 million, respectively, and is expected to be recognized over a weighted average period of approximately 2.6 years and 2.3 years, respectively. Expense related to non-vested restricted stock awards totaled $0.4 million and $0.6 million during the three months ended March 31, 2018 and 2017, respectively. Expense related to non-vested performance stock units totaled $0.2 million and $0.1 million during the three months ended March 31, 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 September 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 349,199 was available for issuance.

Under the ESPP, employees purchased 5,960 shares and 5,373 shares during the three months ended March 31, 2018 and 2017, respectively.

Table of Contents

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 30,479,969 and 26,875,585 shares of Class A common stock outstanding at March 31, 2018 and December 31, 2017, respectively. Additionally, the Company had 221,782 and 163,557 shares outstanding at March 31, 2018 and December 31, 2017, respectively, of restricted Class A common stock issued but not yet vested under the 2014 Omnibus Incentive 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 from time to time in either the open market or through privately negotiated transactions. The remaining authorization under this program as of March 31, 2018 was $12.6 million.

Note 15 Income Per Share

The Company calculates income 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.

The Company had 30,479,969 and 26,715,532 shares of Class A common stock outstanding as of March 31, 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 income per share because to do so would have been anti-dilutive for the three months ended March 31, 2018 and 2017.

The following table illustrates the computation of basic and diluted income per share for the three months ended March 31, 2018 and 2017:

	For the three months ended	
	March 31, 2018	March 31, 2017
Net income	$ 8,464	$ 8,258
Less: income allocated to participating securities	(13)	(8)
Income allocated to common shareholders	$ 8,451	$ 8,250
Weighted average shares outstanding for basic income per common share	30,493,689	26,801,773
Dilutive effect of equity awards	649,839	844,473
Dilutive effect of warrants	—	33,783
Weighted average shares outstanding for diluted income per common share	31,143,528	27,680,029
Basic income per share	$ 0.28	$ 0.31
Diluted income per share	$ 0.27	$ 0.30

The Company had 1,516,044 and 1,719,701 outstanding stock options to purchase common stock at weighted average exercise prices of $21.89 and $20.56 per share at March 31, 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 418,638 and 490,528 unvested restricted shares and units issued as of March 31, 2018 and 2017, respectively, 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.

Table of Contents

Note 16 Income Taxes

Income tax expense attributable to income before income taxes was $1.7 million for the three months ended March 31, 2018 compared to an income tax benefit of $(1.2) million for the three month ended March 31, 2017, calculated based on a full year forecast method, resulting in an effective income tax rate of 16.7% for the three months ended March 31, 2018 and an effective income tax benefit of (17.7)% for the three months ended March 31, 2017. The tax expense recorded for the three months ended March 31, 2018 and March 31, 2017 was lowered by a $0.4 million and $2.8 million discrete tax benefit from stock compensation activity during the respective periods. 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 March 31, 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 March 31, 2018	December 31, 2017	Balance Sheet location	Liability derivatives fair value March 31, 2018	December 31, 2017
Derivatives designated as hedging instruments:						
Interest rate products	Other assets	$ 21,496	$ 10,489	Other liabilities	$ 121	$ 1,167
Total derivatives designated as hedging instruments		$ 21,496	$ 10,489		$ 121	$ 1,167
Derivatives not designated as hedging instruments:						
Interest rate products	Other assets	$ 3,199	$ 2,483	Other liabilities	$ 3,179	$ 2,584
Interest rate lock commitments	Other assets	1,219	128	Other liabilities	312	—
Forward contracts	Other assets	97	5	Other liabilities	289	7
Total derivatives not designated as hedging instruments		$ 4,515	$ 2,616		$ 3,780	$ 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 March 31, 2018, the Company had interest rate swaps with a notional amount of $462.9 million that were designated as fair value hedges of interest rate risk associated with $507.8 million of the Company’s fixed-rate loans, included in loans receivable on the statements of financial condition, before a $(20.5) million fair value hedge adjustment in the carrying amount. 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.

Table of Contents

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 March 31, 2018, the Company had matched interest rate swap transactions with an aggregate notional amount of $184.0 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 $110.7 million and forward contracts with a notional value of $131.4 million at March 31, 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.

Table of Contents

Effect of derivative instruments on the consolidated statements of operations

The tables below present the effect of the Company’s derivative financial instruments in the consolidated statements of operations for the three months ended March 31, 2018 and 2017:

Derivatives in fair value hedging relationships	Location of gain (loss) recognized in income on derivatives	Amount of gain or (loss) recognized in income on derivatives For the three months ended March 31,	
		2018	2017
Interest rate products	Interest and fees on loans	$ 12,052	$ —
Interest rate products	Other non-interest income	—	1,064
Total		$ 12,052	$ 1,064

Hedged items	Location of gain (loss) recognized in income on hedged items	Amount of gain or (loss) recognized in income on hedged items For the three months ended March 31,	
		2018	2017
Interest rate products	Interest and fees on loans	$ (11,917)	$ —
Interest rate products	Other non-interest income	—	(1,241)
Total		$ (11,917)	$ (1,241)

Derivatives not designated as hedging instruments	Location of gain (loss) recognized in income on derivatives	Amount of gain or (loss) recognized in income on derivatives For the three months ended March 31,	
		2018	2017
Interest rate products	Other non-interest expense	$ 122	$ (32)
Interest rate lock commitments	Mortgage banking income	375	123
Forward contracts	Mortgage banking income	1,108	(193)
Total		$ 1,605	$ (102)

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 March 31, 2018, the termination value of derivatives in a net liability position related to these agreements was $3.3 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 March 31, 2018 the Company had posted $0.2 million in eligible collateral. If the Company had breached any of these provisions at March 31, 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 March 31, 2018 and December 31, 2017, the Company had loan commitments totaling $786.9 million and $680.8 million, respectively, and standby letters of credit that totaled $8.1 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.

Table of Contents

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

	March 31, 2018	December 31, 2017
Commitments to fund loans	$ 235,078	$ 181,904
Unfunded commitments under lines of credit	551,838	498,857
Commercial and standby letters of credit	8,143	7,185
Total unfunded commitments	$ 795,059	$ 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.

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 $4.3 million at March 31, 2018, which is included in other liabilities on the consolidated statements of financial condition.

Contingencies

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 inputs to 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

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 three months ended March 31, 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 March 31, 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 classifies 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.

Table of Contents

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

	March 31, 2018			
	Level 1	Level 2	Level 3	Total
Assets:				
Investment securities available-for-sale:				
Mortgage-backed securities ("MBS"):				
Residential mortgage pass-through securities issued or guaranteed by U.S. Government agencies or sponsored enterprises	$ —	$ 188,630	$ —	$ 188,630
Other residential MBS issued or guaranteed by U.S. Government agencies or sponsored enterprises	—	727,729	—	727,729
Municipal securities	—	818	—	818
Loans held for sale	—	51,050	—	51,050
Interest rate swap derivatives	—	24,695	—	24,695
Mortgage banking derivatives	—	—	1,316	1,316
Total assets at fair value	$ —	$ 992,922	$ 1,316	$ 994,238
Liabilities:				
Interest rate swap derivatives	$ —	$ 3,300	$ —	$ 3,300
Mortgage banking derivatives	—	—	601	601
Total liabilities at fair value	$ —	$ 3,300	$ 601	$ 3,901

	December 31, 2017			
	Level 1	Level 2	Level 3	Total
Assets:				
Investment securities available-for-sale:				
Mortgage-backed securities ("MBS"):				
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

The table below details the changes in level 3 financial instruments during the three months ended March 31, 2018:

	Mortgage banking derivatives, net
Balance at December 31, 2017	$ 126
Gain included in earnings, net	589
Balance at March 31, 2018	$ 715

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.

Table of Contents

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 March 31, 2018, the Company measured six originated and acquired loans at fair value on a non-recurring basis, with a carrying balance of $6.4 million and specific reserve balance of $1.2 million. At March 31, 2017, the Company measured three loans with a carrying balance of $10.6 million and specific reserve balance of $2.9 million.

OREO is recorded at the lower of the cost basis or 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 $38 thousand and $46 thousand of OREO impairments in its consolidated statements of operations during the three months ended March 31, 2018 and 2017, respectively. The fair values of OREO 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 values of OREO 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 March 31, 2018 and prepayment speed assumption ranges of 8.7% to 11.3% at March 31, 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 no valuation allowance recorded at March 31, 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 tables below provide information regarding the assets recorded at fair value on a non-recurring basis during the three months ended March 31, 2018 and 2017:

	March 31, 2018
	Total

		Losses from fair value changes
Other real estate owned	$ 11,875	$ 38
Impaired loans	34,672	715

	March 31, 2017	
	Total	Losses from fair value changes
Other real estate owned	$ 15,552	$ 46
Impaired loans	41,103	209

The Company did not record any liabilities measured at fair value on a non-recurring basis during the three months ended March 31, 2018.

Table of Contents

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 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 March 31, 2018 and December 31, 2017, including methods and assumptions utilized for determining fair value of financial instruments, are set forth below:

	Level in fair value measurement hierarchy	March 31, 2018		December 31, 2017	
		Carrying amount	Estimated fair value	Carrying amount	Estimated fair value
ASSETS					
Cash and cash equivalents	Level 1	$ 286,870	$ 286,870	$ 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	188,630	188,630	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	727,729	727,729	685,230	685,230
Municipal securities	Level 2	818	818	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	191,136	188,609	204,352	204,048
Mortgage-backed securities—other residential mortgage-backed securities	Level 2	92,233	90,107	54,378	

issued or guaranteed by U.S.
Government agencies or sponsored
enterprises held-to-maturity