



**[ HomeStreet ]**<sup>®</sup>

**2019 Annual Report to Shareholders**

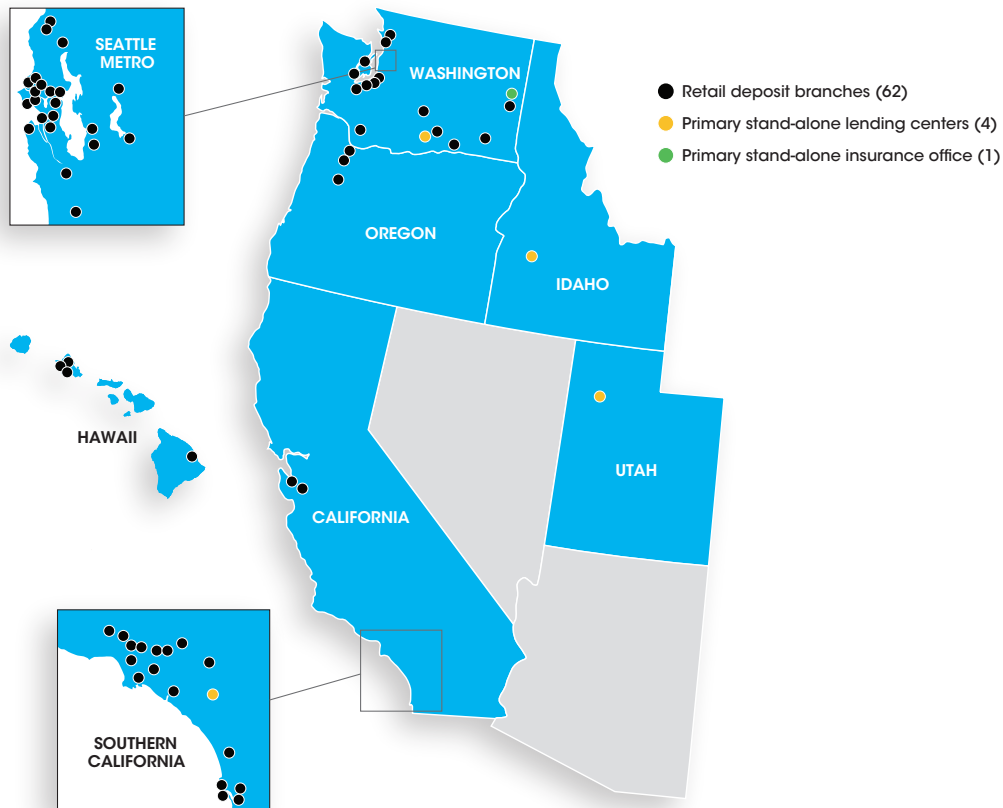


HomeStreet, Inc. (together with its consolidated subsidiaries, “HomeStreet,” the “Company,” “we,” “our” or “us”), a Washington corporation, is a diversified financial services company founded in 1921, headquartered in Seattle, Washington, serving customers primarily on the West Coast of the United States, including Hawaii. We are principally engaged in commercial banking, consumer banking, and real estate lending, including commercial real estate and single family mortgage lending. In addition to the banking and lending operations of our wholly owned subsidiaries, HomeStreet also sells insurance products and services for consumer clients under the name HomeStreet Insurance. Our primary subsidiaries are HomeStreet Bank and HomeStreet Capital Corporation.

HomeStreet Bank is a Washington state-chartered commercial bank providing commercial and consumer loans including mortgage loans, deposit products, private banking and cash management services. Our loan products include commercial business and agriculture loans, consumer loans, single family residential mortgages, loans secured by commercial real estate, and construction loans for residential and commercial real estate projects. Our branch network is primarily located in large metropolitan markets of the Western United States which promotes convenience for our customers and helps us build our market share through growth of commercial and consumer account deposits.

HomeStreet Capital Corporation, a Washington corporation, sells and services multifamily mortgage loans originated by HomeStreet Bank under the Fannie Mae Delegated Underwriting and Servicing Program (“DUS®”)<sup>1</sup>.

<sup>1</sup> DUS® is a registered trademark of Fannie Mae



The number of offices listed above does not include satellite offices with a limited number of staff who report to a manager located in a separate primary office.

To our fellow Shareholders,

At the time of this writing, our business, economy, and communities have been significantly impacted by the COVID-19 pandemic. This is a period of enormous stress on the global, national, regional, and local economies, and our Company will be adversely affected in ways we are still trying to quantify. The situation is changing rapidly, with a lot of unknowns, and our customers, employees and communities are all experiencing adverse impacts and personal tragedies. Moreover, we must acknowledge that there is the potential for permanent changes in the way we interact and do business. Nevertheless, I believe that our Company is well positioned as we face this crisis.

At present, we have a strong capital position, well in excess of the levels to be considered well-capitalized under regulatory standards for both the Bank and the Company. We have ample liquidity and access to more from our contingent sources. We believe our loan portfolio is conservatively underwritten, and that most of our borrowers are in an economic position that should allow them to persevere through this crisis. Where we have borrowers who are disproportionately impacted by the virus and its effects on our economy, we are working with them to defer or modify payments, pursue other forbearances and, where appropriate, extend additional credit. We have assisted many of these borrowers with Paycheck Protection Loans under the CARES Act which will provide additional assistance during this challenging time. Additionally, while we significantly reduced the size of our mortgage banking business in 2019, our continuing mortgage banking business is experiencing the benefits of lower interest rates and related high levels of refinancing. This additional income will, we believe, mitigate any negative impact to our earnings from credit losses and additional expenses incurred during this crisis.

With respect to our 2019 results, asset quality remained strong throughout the year, with nonperforming assets totaling 0.21 percent of total assets at the end of the year. As a result of the current COVID-19 pandemic, we expect to experience some deterioration of our loan portfolio credit quality with commercial loans most at risk. Our loan portfolio has, by design, limited concentrations by product type, industry, and geography in order to limit our risk of exposure to any one part of the market, however, to mitigate additional risk to our portfolio, we have temporarily suspended lending to certain borrowers operating in the most adversely affected businesses and industries. Much of our team that saw us through the great recession and helped us resolve a large portfolio of troubled assets and recapitalize the institution in 2012, remain at the Company in key positions. This experience will be invaluable as we navigate the current crisis.

During 2019 and the first quarter of 2020, before the advent of the COVID-19 related economic impacts, we implemented some significant changes at HomeStreet to achieve our strategy of greater efficiency and profitability while emerging as a leading West Coast regional bank.

After thoughtful consideration by the Board of Directors, in the first and second quarter of 2019 we executed on the Board's decision to substantially reduce our mortgage banking business, including the divestiture of our stand-alone home loan center-based mortgage origination business and related servicing. The successful completion of these divestitures avoided significant costs of liquidation, and most of our employees associated with these centers were transferred to the acquiror of the assets of the home loan centers. At the same time, we sold a majority of the mortgage servicing rights related to loan origination associated with those home loan centers. Finally, during the fourth quarter of 2019, we completed the sale of our ownership interest in our former mortgage joint venture, WMS Series, LLC.

In addition to reducing our exposure to mortgage banking and to focus on our commercial and consumer banking operations, we have also been executing a plan to meaningfully improve our operating efficiency and profitability. The plan identified a range of expense reduction opportunities that involves organizational, operational, technology, real estate, and personnel changes. We have forecasted substantial completion of this plan for some time in 2021, however, we do not yet know what the impact will be on the plan of changes to our economic conditions coming out of the COVID-19 pandemic.

Alongside these strategic, operational and cost structure changes, we continue to refresh our Board of Directors and add new members with business expertise and experience in banking and financial services who might also bring fresh perspectives to our Board. In October of 2019 we added Nancy D. Pellegrino, who brings over 30 years of wealth management and private banking experience and furthers our stated goals of increased diversity on our Board. In January of 2020, we also announced the appointment of James R. Mitchell to the Board. He is the founder and former chief executive of Puget Sound Bank, with over 40 years of commercial banking experience. We added these directors prior to our upcoming 2020 annual meeting of the shareholders to give the Board time to transition

as three of our current directors will not be standing for re-election at the Annual Meeting as they have reached the age limitation set forth in our Principles of Corporate Governance. We believe we are making great progress toward our Board diversification goals and we look forward to the contribution and fresh perspectives of our new Board members.

The Board recognizes that our shareholders have supported the development of the Company and the recent significant changes to our strategy, all of which were pursued with the goals of reducing earnings volatility, improving profitability and, ultimately, enhancing shareholder value. While some of these actions, and specifically the current initiative to improve operating efficiency, are obviously still a work in progress, and there is additional uncertainty in the near term as we work through the impacts of the COVID-19 pandemic on our economy, our customers and our industry, it is clear to the Board that the foundation for improvement has been laid. In 2019, the capital markets rewarded these actions as the total shareholder return of our stock price was 60.1% in comparison to the Keefe Bruyette & Woods Regional Bank Index return that was 23.9%.

Reflecting our progress in improving and stabilizing earnings, the Board initiated a quarterly common stock dividend that was paid on February 21, 2020. In determining this dividend, the Board considered numerous factors. First, the Board acknowledged that both the consistency and absolute level of the Company's current profitability continue to have much room for improvement. At the same time, the Board believes the strategic changes implemented have substantially reduced earnings volatility and presented a clearer path to continued improvement. While the Board will continue to assess the impact of economic changes, including those caused by the COVID-19 pandemic, on our ability to pay dividends and the amount of any dividends that might be declared, we have not suspended our dividend policy at this time.

During 2019 we established a common stock share repurchase program, repurchasing 3,187,259 shares during 2019 and an additional 580,278 shares during 2020. In total, these repurchases represent 13.9% of the total shares outstanding prior to the initiation of the repurchase program. On March 23, 2020, following the declaration of the COVID-19 pandemic, we suspended our share repurchase program as we believe it is prudent to preserve our capital to provide more protection against potential credit losses and provide more support for lending activities that may become crucial to supporting our communities. We anticipate restarting our share repurchase program when appropriate.

While HomeStreet is an essential business in our communities, providing banking products to our customers during this crisis, we recognize that our employees are taking significant risks in reporting to work and fulfilling these duties. We have instituted a work from home program for those functions that do not require an in office or customer facing presence. To keep our customers and employees safe, we have installed barriers where appropriate and implemented a comprehensive social distancing policy that contains robust sanitation and disinfecting protocols at locations for confirmed or presumed COVID-19 diagnoses throughout the Company. Acknowledging the potential hardships our frontline employees face, we have increased the benefits to our employees during this time to include: no out-of-pocket charges for COVID-19 related medical care; additional paid time off for employees that are required to interact with customers as part of their job duties; COVID Time Off if an employee is confirmed with a COVID-19 diagnosis, is quarantined by a healthcare provider, or is affected by a workplace closure, which does not get charged against an employee's sick or vacation time; and lastly, under certain circumstances, a furlough program that would allow employees to step away from their job without quitting while still retaining their medical benefits.

There is still much work ahead of us and the ultimate impact of the current COVID-19 pandemic is still largely unknown. Management is working closely with our Board, our regulators and our advisors as we plan and execute our response to the significant disruptions caused by the COVID-19 pandemic. On behalf of the entire Board of Directors, I want to commend the courage and dedication of our employees in pursuing our goals and serving our customers and communities during this time of personal risk and uncertainty. As a regional community bank, HomeStreet Bank plays an important role in supporting our local communities through this crisis. HomeStreet is well positioned to help our customers and communities weather the financial storm.

Finally, I want to thank you, our shareholders, for your continued support and confidence in our Company.

Mark K. Mason  
Chairman of the Board, President, and Chief Executive Officer  
HomeStreet, Inc.

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

FORM 10-K

(Mark One)

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

For the fiscal year ended December 31, 2019

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: 001-35424

**HOMESTREET, INC.**

(Exact name of registrant as specified in its charter)

Washington

91-0186600

(State or other jurisdiction of  
incorporation or organization)

(I.R.S. Employer  
Identification Number)

601 Union Street, Ste. 2000  
Seattle, WA 98101

(Address of principal executive offices) (Zip Code)

Registrant's telephone number, including area code: (206) 623-3050

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

Title of each class

Trading Symbol(s)

Name of each exchange on which registered

Common Stock, no par value

HMST

Nasdaq Stock Market LLC

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

None.

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

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

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

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

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

|                         |                          |                           |                                     |
|-------------------------|--------------------------|---------------------------|-------------------------------------|
| Large accelerated filer | <input type="checkbox"/> | Accelerated filer         | <input checked="" type="checkbox"/> |
| Non-accelerated filer   | <input type="checkbox"/> | Smaller reporting company | <input type="checkbox"/>            |
| Emerging growth Company | <input type="checkbox"/> |                           |                                     |

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 Act). Yes  No

As of June 28, 2019, the last business day of the registrant's most recently completed second fiscal quarter, the aggregate market value of common stock held by non-affiliates was approximately \$645.8 million, based on a closing price of \$29.64 per share of common stock on the Nasdaq Global Select Market on such date. Shares of common stock held by each executive officer and director and by each person known to the Company who beneficially owns more than 10% of the outstanding common stock have been excluded in that such persons may under certain circumstances be deemed to be affiliates. This determination of executive officer or affiliate status is not necessarily a conclusive determination for other purposes.

The number of outstanding shares of the registrant's common stock as of March 2, 2020 was 23,685,849.6.

**DOCUMENTS INCORPORATED BY REFERENCE**

The information required by Part III of this Report, to the extent not set forth herein, will be incorporated by reference from the registrant's definitive proxy statement relating to the annual meeting of the shareholders to be held in 2020, to be filed with the Securities and Exchange Commission within 120 days of the end of the fiscal year to which this Report relates. If a definitive proxy statement of the registrant is not filed within such period, the registrant will instead file such information on an amendment to this Report within such 120 days of the end of the registrant's fiscal year to which this report relates.

## TABLE OF CONTENTS

|   |     |
|---|-----|
| PART 1 .....  | 1   |
| FORWARD-LOOKING STATEMENTS .....  | 1   |
| ITEM 1    BUSINESS .....  | 1   |
| ITEM 1A   RISK FACTORS .....  | 16  |
| ITEM 1B   UNRESOLVED STAFF COMMENTS .....   | 34  |
| ITEM 2    PROPERTIES .....  | 34  |
| ITEM 3    LEGAL PROCEEDINGS .....   | 34  |
| ITEM 4    MINE SAFETY DISCLOSURES .....   | 34  |
| PART II .....   | 35  |
| ITEM 5    MARKET FOR REGISTRANT’S COMMON EQUITY, RELATED STOCKHOLDER<br>MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES ..... | 35  |
| ITEM 6    SELECTED FINANCIAL DATA .....   | 36  |
| ITEM 7    MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION<br>AND RESULTS OF OPERATIONS .....                        | 39  |
| ITEM 7A   QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK .....  | 81  |
| ITEM 8    FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA .....   | 85  |
| ITEM 9    CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING<br>AND FINANCIAL DISCLOSURE .....                         | 169 |
| ITEM 9A   CONTROLS AND PROCEDURES .....   | 169 |
| ITEM 9B   OTHER INFORMATION .....   | 172 |
| PART III .....  | 173 |
| ITEM 10   DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE .....  | 173 |
| ITEM 11   EXECUTIVE COMPENSATION .....  | 173 |
| ITEM 12   SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND<br>MANAGEMENT AND RELATED STOCKHOLDER MATTERS .....               | 173 |
| ITEM 13   CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS AND DIRECTOR<br>INDEPENDENCE .....                                     | 174 |
| ITEM 14   PRINCIPAL ACCOUNTANT FEES AND SERVICES .....  | 174 |
| PART IV .....   | 175 |
| ITEM 15   EXHIBITS AND FINANCIAL STATEMENT SCHEDULES .....  | 175 |
| SIGNATURES .....  | 179 |
| CERTIFICATIONS  |     |
| EXHIBIT 21  |     |
| EXHIBIT 31.1  |     |
| EXHIBIT 31.2  |     |
| EXHIBIT 32  |     |

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



## PART I

### FORWARD-LOOKING STATEMENTS

This Annual Report on Form 10-K (“Form 10-K”) and the documents incorporated by reference contain, in addition to historical information, “forward-looking statements” within the meaning of Section 27A of the Securities Act of 1933, as amended (the “Securities Act”) and Section 21E of the Securities Exchange Act of 1934, as amended (the “Exchange Act”), including statements relating to projections of revenues, estimated operating expenses or other financial items; management’s plans and objectives for future operations or programs; future operations, plans, regulatory compliance or approvals; anticipated restructuring or resource optimization plans and activities and expected cost savings from and timing of these plans and activities; proposed new products or services; expected or estimated performance of our loan portfolio; pending or potential expansion activities; pending or future mergers, acquisitions or other transactions; future economic conditions or performance; expectations relating to our industry, regulatory environment and the economy as a whole and underlying assumptions of any of the foregoing.

All statements other than statements of historical fact are “forward-looking statements” for the purpose of these provisions. When used in this Form 10-K, terms such as “anticipates,” “believes,” “continue,” “could,” “estimates,” “expects,” “intends,” “may,” “plans,” “potential,” “predicts,” “should,” or “will” or the negative of those terms or other comparable terms are intended to identify such forward-looking statements. These statements involve known and unknown risks, uncertainties and other factors that may cause us to fall short of our expectations or may cause us to deviate from our current plans, as expressed or implied by these statements. The known risks that could cause our results to differ, or may cause us to take actions that are not currently planned or expected, are described below and in Item 1A, Risk Factors.

Unless required by law, we do not intend to update any of the forward-looking statements after the date of this Form 10-K to conform these statements to actual results or changes in our expectations. Readers are cautioned not to place undue reliance on these forward-looking statements, which apply only as of the date of this Form 10-K.

Except as otherwise noted, references to “we,” “our,” “us” or “the Company” refer to HomeStreet, Inc. and its subsidiaries that are consolidated for financial reporting purposes.

### ITEM 1 BUSINESS

#### General

HomeStreet, Inc. (together with its consolidated subsidiaries, “HomeStreet,” the “Company,” “we,” “our” or “us”), a Washington corporation, is a diversified financial services company founded in 1921, headquartered in Seattle, Washington, serving customers primarily on the West Coast of the United States, including Hawaii. We are principally engaged in commercial banking, consumer banking, and real estate lending, including commercial real estate and single family mortgage lending. In addition to the banking and lending operations of our wholly owned subsidiaries, HomeStreet also sells insurance products and services for consumer clients under the name HomeStreet Insurance. Our primary subsidiaries are HomeStreet Bank and HomeStreet Capital Corporation.

HomeStreet Bank is a Washington state-chartered commercial bank providing commercial and consumer loans including mortgage loans, deposit products, private banking and cash management services. Our loan products include commercial business and agriculture loans, consumer loans, single family residential mortgages, loans secured by commercial real estate, and construction loans for residential and commercial real estate projects. Our branch network is primarily located in large metropolitan markets of the Western United States which promotes convenience for our customers and helps us build our market share through growth of commercial and consumer account deposits.

HomeStreet Capital Corporation, a Washington corporation, sells and services multifamily mortgage loans originated by HomeStreet Bank under the Fannie Mae Delegated Underwriting and Servicing Program (“DUS<sup>®</sup>”)<sup>1</sup>.

Shares of our common stock are traded on the Nasdaq Global Select Market under the symbol “HMST.” We also have outstanding \$65.0 million in aggregate principal amount of 6.5% senior notes due 2026, all of which are registered pursuant to Section 15(d) of the Securities Exchange Act of 1934, as amended.

---

<sup>1</sup> DUS<sup>®</sup> is a registered trademark of Fannie Mae

At December 31, 2019, we had total assets of \$6.81 billion, net loans held for investment of \$5.07 billion, deposits of \$5.34 billion and shareholders' equity of \$679.7 million.

We provide diversified financial products and services to our customers through bank branches, ATMs, online, mobile and telephone banking channels. These products and services include deposit products, single family residential mortgage loans, consumer, business and agricultural portfolio loans, insurance products and cash management services. We originate construction loans, bridge loans, and permanent loans for our portfolio on single family residences, and on office, retail, industrial and multifamily properties. We originate multifamily real estate loans through our Fannie Mae DUS<sup>®</sup> business, and after origination those loans are sold to or securitized by Fannie Mae, with the Company generally retaining the servicing rights. The majority of our mortgage loans are sold to or securitized by Fannie Mae, Freddie Mac or Ginnie Mae, with the right to service these loans retained. We are a rated originator and servicer of jumbo loans, allowing us to sell the loans to other securitizers. We also sell loans on a servicing-released and servicing-retained basis to securitizers and correspondent lenders. A small percentage of our loans are brokered to other lenders or sold on a servicing-released basis to correspondent lenders. On occasion, we may sell a portion of our mortgage servicing rights ("MSRs"). We manage the loan funding and the interest rate risk associated with the secondary market loan sales and the retained single family MSRs. In addition, through the Commercial Real Estate division of HomeStreet Bank, we originate permanent commercial real estate loans primarily up to \$15 million in size, a portion of which we pool for sale and sell into the secondary market.

### **Recent Developments**

The Board of Directors approved an addition to our share repurchase program for up to \$25 million of our common stock in January 2020, and our regulators have confirmed no objections to that repurchase. In February the Board increased the authorization by an additional \$10 million, conditional on the non-objection of our regulators. Assuming no objections from our regulators for the additional repurchase authorization, we expect to commence repurchases in the first or second quarter of 2020. This represents, in aggregate amount of shares of the Company's common stock, no par value, from shareholders, which represents approximately 5.2% of the Company's currently outstanding common stock based on the closing price of the stock as of March 2, 2020. This authorization is in addition to the 3.4 million shares of common stock that the Company repurchased in 2019 and early 2020.

In January 2020 HomeStreet's Board of Directors approved a new dividend policy that contemplates the payment of quarterly cash dividends on our common stock when, if and in an amount declared by the Board after taking into consideration, among other things, earnings, regulatory capital levels, the overall payout ratio and expected asset growth. The first dividend declared under this policy was a cash dividend of \$0.15 per share for the first quarter of 2020, which was paid on February 21, 2020 to shareholders of record as of the close of business on February 5, 2020. The dividend rate to be paid will be reassessed each quarter by the Board of Directors in accordance with the dividend policy.

### **Business Strategy**

Since our initial public offering (IPO) in February of 2012, we have steadily grown our banking presence to diversify our earnings and mitigate the impact of the earnings volatility of our mortgage banking business. As a part of our growth strategy we opened several de novo retail deposit branches between 2012 and 2019 to expand our branch network and increase our core deposit base, while also expanding our offerings of community banking products and services. We have focused our de novo branch openings in markets that we believe are underserved by community banks. From 2012 to 2015, we opened 10 de novo branches in the greater Seattle area. In 2016, we added six de novo branches in San Diego, Hawaii and Eastern Washington, and in 2017 we opened three de novo branches in Southern California, Eastern Washington and the greater Seattle area. In 2018, we added three de novo branches in the Puget Sound area. In 2019, we added two de novo branches in Northern California. Overall, from our IPO through December 31, 2019, we have added 24 de novo branches and acquired nine branches. At the same time, we grew and diversified the Bank through acquisitions of whole banks and retail deposit branches in attractive growth markets on the West Coast to increase our scale in existing markets, enter new markets and add to or acquire additional professionals for our commercial and consumer lending teams. Between 2013 and 2019, we acquired four banks, expanding our network in Eastern Washington and Southern California, and nine individual branches to complement our existing networks in Washington, Oregon and California. We believe that our acquisitions have accelerated our growth of interest-earning commercial banking assets, strengthened our core deposit base, increased our geographic diversification and added experienced commercial and consumer banking professionals in key target markets.



In 2019, we took additional steps to rebalance the mix of our business toward commercial and consumer banking by significantly reducing our presence in the mortgage banking industry. In late 2018 and early 2019 our Board of Directors reviewed the challenges that confronted our former single family Mortgage Banking segment and the mortgage industry in general and determined that it would be in the best interests of the Company and its shareholders to explore a potential sale of the home loan center (“HLC”)-based single family mortgage origination business and related MSR. These challenges included substantially lower origination volume due to changes in market interest rates resulting in lower revenue and increased regulations on loan underwriting and loan disclosures resulting in higher mortgage origination costs. Additionally, a persistently flat yield curve by historical standards made hedging the change in value of our MSRs less effective, thereby reducing our risk management results. The decision to exit the HLC-based mortgage banking business aligned with our long-term strategic goal of reducing the impact of this cyclical and volatile earnings stream and was made only after we felt we had substantially exhausted opportunities to improve the performance of the now former Mortgage Banking segment. Following this determination, the Board approved a plan to sell the Bank’s stand-alone home loan centers and related mortgage servicing rights, which was accomplished in three separate transactions. Our legacy Mortgage Banking segment was discontinued effective March 31, 2019 when the Bank’s Board of Directors adopted a plan of exit or disposal of our HLC-based mortgage banking business.

On March 29, 2019, HomeStreet Bank successfully closed and settled two separate sales of the rights to service an aggregate of \$14.26 billion in total unpaid principal balances of single family mortgage loans for Fannie Mae, Freddie Mac and Ginnie Mae, representing 71% of HomeStreet’s total single family mortgage loans serviced for others portfolio as of December 31, 2018. The Company finalized the servicing transfer for these loans to their respective buyers in the second and third quarters of 2019 and subserviced the loans until the transfer date.

In April 2019, the Bank entered into an agreement with Homebridge Financial Services Inc (“Homebridge”) to sell substantially all of the assets of the HLC-based mortgage origination business and transfer related personnel to Homebridge. In a series of closings in June and July 2019, the bank sold substantially all of the assets associated with the 47 HLC, satellite and fulfillment offices and facilitated the transfer of 464 related mortgage personnel. Homebridge paid the net book value of the acquired assets, which was approximately \$4.9 million, plus a premium of \$1.0 million, which was reduced by \$1.5 million for reimbursement by HomeStreet of certain transaction expenses incurred by Homebridge, as well as the assumption of certain home loan center and fulfillment office lease obligations. Additionally, in June 2019, we closed the remaining four stand-alone HLCs that were not sold to Homebridge, which left us with no remaining stand-alone single family residential lending centers.

In order to further reduce the Company’s exposure to the mortgage business and solidify its focus on commercial and consumer banking, in November 2019, we completed the sale of our ownership interest in WMS Series, LLC, an affiliated business arrangement that we had partially owned with various members of Windermere Real Estate Company franchises that operates a single family mortgage origination business from certain Windermere offices under the name Penrith Home Loans.

The assets sold or abandoned largely represented the majority of the Company’s prior Mortgage Banking segment, the activities of which related to originating, servicing, underwriting, funding and selling single family residential mortgage loans. The Bank has continued to originate mortgages through its bank locations, online banking and affinity lending relationships.

Any remaining activity for these HLCs, along with certain other mortgage banking-related assets and liabilities that are expected to be sold or abandoned, are classified as discontinued operations in the accompanying Consolidated Statements of Financial Condition and Consolidated Statements of Operations. Certain remaining components of the Company’s former Mortgage Banking segment, including MSRs on certain mortgage loans that were not sold as part of the MSR sales described above and our remaining single-family mortgage origination and servicing business, have been classified as continuing operations.

Our legacy Mortgage Banking segment was discontinued effective March 31, 2019 when the Bank’s Board of Directors adopted a plan of exit or disposal of our HLC-based mortgage banking business. Thus, discontinued operations reported in the first quarter of 2019 included our entire mortgage banking business as did all comparative periods presented. Effective April 1, 2019, the newly organized bank location-based mortgage banking business commenced operations and the associated revenues and expenses were reported as part of the Company’s continuing operations beginning in the second quarter of 2019.

After the successful 2019 sale of our home loan center-based mortgage origination business and servicing rights, our strategy continues to be growing our commercial and consumer banking business and diversifying our earnings. Included in our strategy is a focus on efficiency and profitability which has resulted in substantial organizational and operational changes, reflecting our more simplified business structure and lower growth goals.

We also plan to expand our commercial real estate business with a focus on multifamily mortgage origination through our existing commercial banking network as well as through our Fannie Mae DUS<sup>®</sup> origination and servicing relationships. We expect to continue to benefit from being one of only 25 companies nationally that is an approved Fannie Mae DUS<sup>®</sup> seller and servicer. We will continue to support our DUS<sup>®</sup> program by providing new construction and short-term bridge loans to experienced borrowers who intend to build or purchase apartment buildings for renovation, which we will then seek to replace with permanent financing upon completion of the projects. We also originate commercial real estate construction loans, bridge loans and permanent loans for our portfolio, primarily on office, retail, industrial and multifamily property types located within our geographic footprint and regularly sell those types of loans to other investors.

While we continue to focus on growing and strengthening our commercial banking business, we have suspended future de novo deposit branch openings while we execute our strategy of improving efficiency and overall profitability.

Our market focus is concentrated primarily in the major metropolitan markets in the Western United States, which are characterized by larger populations, lower unemployment and generally higher growth than many other metropolitan areas. These markets are the Seattle/Puget Sound and eastern areas of Washington, the Portland, Oregon area, the Hawaiian Islands, the San Francisco Bay Area of California, and Southern California, including Los Angeles, Orange, Riverside, and San Diego Counties. We believe there is a significant opportunity for a well-capitalized, community-focused bank to compete effectively in West Coast markets, especially those that are not well served by existing community banks. Our strategy is to offer responsive and personalized service while providing a full range of financial services to small- and middle-market commercial and consumer customers, to build loyalty and grow market share, both organically in our existing locations and teams opportunistically through strategic acquisitions.

In 2019, following the reduction of our mortgage banking business we took steps to improve productivity and reduce total corporate expenses, reflecting the substantial reduction in the size and complexity of our operations and our lower growth plan going forward. Since the second quarter of 2019, we have been working with an outside consulting firm that specializes in bank efficiency on an enterprise-wide profitability improvement project. The goal of this project is to analyze and improve all of our corporate expenses and business line processes, including contract terms, occupancy and technology costs, organization and staffing improvements, and other cost savings and efficiency proposals. The project includes the following initiatives:

- Simplify the organizational structure by reducing management levels and management redundancy
- Consolidate similar functions currently residing in multiple organizations
- Renegotiate, where possible, our technology contracts
- Identify and eliminate redundant or unnecessary systems and services
- Rationalize staffing levels to recognize the significant changes in work volumes and Company growth rates
- Eliminate excess occupancy costs consistent with reduced personnel

We began executing on the efficiency initiatives in the third quarter of 2019 and expect these reductions and enhancements will continue through 2020 and beyond.

## **Market and Competition**

We view our market as the major metropolitan coastal areas of the Western United States, including Hawaii. These metropolitan areas share a number of key demographic factors that are characteristic of growth markets, such as large and growing populations with above-average household incomes, a significant number of large and mid-sized companies, and diverse economies. These markets all share large populations that we believe are underserved due to the rapid consolidation of community banks since the financial crisis. We believe these markets can be well served by a strong regional bank like ours that is focused on providing consumers and businesses with quality customer service and a competitive array of deposit and lending products.

As of December 31, 2019, we operated 62 full service bank branches in the State of Washington, Northern California, Southern California, the Portland, Oregon area and the State of Hawaii, as well as four primary stand-alone commercial lending centers located in Central Washington, Southern California, Boise, Idaho, and Salt Lake City, Utah.

The financial services industry is highly competitive. We compete with other banks, credit unions, mortgage banking companies, insurance companies, finance companies, and investment and mutual fund companies. In particular, we compete with many financial institutions with greater resources, including the capacity to make larger loans, fund extensive advertising campaigns and offer a broader array of products and services. The number of competitors for lower and middle-market business customers has, however, decreased in recent years primarily due to consolidations. At the same time, national banks have been focused on larger customers to achieve economies of scale in lending and depository relationships and have also consolidated business banking operations and support and reduced service levels in many of our markets. We have taken advantage of industry consolidation by recruiting well-qualified employees and attracting new customers who seek long-term stability, local decision-making, quality products and outstanding expertise and customer service.

## **Employees**

As of December 31, 2019, we employed 1,071 full-time equivalent employees, compared to 2,036 full-time equivalent employees at December 31, 2018.

## **Where You Can Obtain Additional Information**

We file annual, quarterly, current and other reports with the Securities and Exchange Commission (the "SEC"). We make available free of charge on or through our website <http://www.homestreet.com> all of these reports (and all amendments thereto), as soon as reasonably practicable after we file these materials with the SEC. Please note that the contents of our website do not constitute a part of our reports, and those contents are not incorporated by reference into this Form 10-K or any of our other securities filings. The SEC's website, [www.sec.gov](http://www.sec.gov), contains reports, proxy and information statements, and other information that we file or furnish electronically with the SEC.

## REGULATION AND SUPERVISION

*The following is a brief description of certain laws and regulations that are applicable to us. The description of these laws and regulations, as well as descriptions of laws and regulations contained elsewhere in this Form 10-K, does not purport to be complete and is qualified in its entirety by reference to the applicable laws and regulations.*

*The bank regulatory framework to which we are subject is intended primarily for the protection of bank depositors and the Deposit Insurance Fund and not for the protection of shareholders or other security holders.*

### **General**

The Company is a bank holding company which has made an election to be a financial holding company. It is regulated by the Board of Governors of the Federal Reserve System (the “Federal Reserve”) and the Washington State Department of Financial Institutions, Division of Banks (the “WDFI”). The Company is required to register and file reports with, and otherwise comply with, the rules and regulations of the Federal Reserve and the WDFI.

The Bank is a Washington state-chartered commercial bank. The Bank is subject to regulation, examination and supervision by the WDFI and the Federal Deposit Insurance Corporation (the “FDIC”).

New statutes, regulations and guidance are regularly considered that could contain wide-ranging potential changes to the competitive landscape for financial institutions operating in our markets and in the United States generally. We cannot predict whether or in what form any proposed statute, regulation or other guidance will be adopted or promulgated, or the extent to which our business may be affected. Any change in policies, legislation or regulation, whether by the Federal Reserve, the WDFI, the FDIC, the Washington state legislature, the United States Congress or any other federal, state or local government branch or agency with authority over us, could have a material adverse impact on us and our operations and shareholders. In addition, the Federal Reserve, the WDFI and the FDIC have significant discretion in connection with their supervisory and enforcement activities and examination policies, including, among other things, policies with respect to the Bank’s capital levels, the classification of assets and establishment of adequate loan loss reserves for regulatory purposes.

Our operations and earnings will be affected by domestic economic conditions and the monetary and fiscal policies of the United States government and its agencies. In addition to its role as the regulator of bank holding companies, the Federal Reserve has, and is likely to continue to have, an important impact on the operating results of financial institutions through its power to implement national monetary and fiscal policy including, among other things, actions taken in order to curb inflation or combat a recession. The Federal Reserve affects the levels of bank loans, investments and deposits in various ways, including through its control over the issuance of United States government securities, its regulation of the discount rate applicable to member banks and its influence over reserve requirements to which banks are subject. From December 2015 through December 2018, the Federal Reserve increased short-term interest rates nine times. Since the beginning of 2019, however, the Federal Reserve has lowered short-term interest rates four times. We cannot predict the ultimate impact of these rate changes on the economy or our institution, or the nature or impact of future changes in monetary policies of the Federal Reserve.

### **Regulation of the Company**

#### ***General***

As a bank holding company, the Company is subject to Federal Reserve regulations, examinations, supervision and reporting requirements relating to bank holding companies. Among other things, the Federal Reserve is authorized to restrict or prohibit activities that are determined to be a serious risk to the financial safety, soundness or stability of a subsidiary bank. Since the Bank is chartered under Washington law, the WDFI has authority to regulate the Company generally relating to its conduct affecting the Bank.

#### ***Capital/Source of Strength***

During 2015, the Company was a savings and loan holding company and as such became subject to capital requirements under the Dodd-Frank Act, beginning in 2015. Following its conversion in 2016 to a bank holding company that has elected to be a financial holding company, the Company continues to be subject to these capital requirements. See “Regulation and Supervision of HomeStreet Bank — *Capital and Prompt Corrective Action Requirements — Capital Requirements*.”

Regulations and historical practices of the Federal Reserve have required bank holding companies to serve as a “source of strength” for their subsidiary banks. The Dodd-Frank Act codified this requirement and extended it to all companies that control an insured depository institution. Accordingly, the Company is required to act as a source of strength for the Bank.

### ***Restrictions Applicable to Bank Holding Companies***

Federal law generally prohibits a bank holding company, including the Company, directly or indirectly (or through one or more subsidiaries), from acquiring:

- control of another depository institution (or a holding company parent) without prior approval of the Federal Reserve (as “control” is defined under the Bank Holding Company Act);
- another depository institution (or a holding company thereof), through merger, consolidation or purchase of all or substantially all of the assets of such institution (or holding company) without prior approval from the Federal Reserve or FDIC;
- more than 5.0% of any class of the voting shares of a non-subsidiary depository institution or a holding company subject to certain exceptions; or
- control of any depository institution not insured by the FDIC (except through a merger with and into the holding company’s bank subsidiary that is approved by the FDIC).

In evaluating applications by holding companies to acquire depository institutions or holding companies, the Federal Reserve must consider the financial and managerial resources and future prospects of the company and the institutions involved, the effect of the acquisition on the risk to the insurance funds, the convenience and needs of the community and competitive factors. In addition, nonbank acquisitions by a bank holding company are generally limited to the acquisition of up to 5% of the outstanding share of any class of voting securities of a company unless the Federal Reserve has previously determined that the nonbank activities are closely related to banking or prior approval is obtained from the Federal Reserve.

### ***Acquisition of Control***

Under the federal Change in Bank Control Act, a notice must be submitted to the Federal Reserve if any person (including a company), or group acting in concert, seeks to acquire “control” of a bank holding company. An acquisition of control can occur upon the acquisition of 10.0% or more of the voting stock of a bank holding company or as otherwise defined by the Federal Reserve. Under the Change in Bank Control Act, the Federal Reserve has 60 days from the filing of a complete notice to act (the 60-day period may be extended), taking into consideration certain factors, including the financial and managerial resources of the acquirer and the antitrust effects of the acquisition. Control can also exist if an individual or company has, or exercises, directly or indirectly or by acting in concert with others, a controlling influence over the Bank. Washington law also imposes certain limitations on the ability of persons and entities to acquire control of banking institutions and their parent companies.

### ***Dividend Policy***

Under Washington law, the Company is generally permitted to make a distribution, including payments of dividends, only if, after giving effect to the distribution, in the judgment of the board of directors, (1) the Company would be able to pay its debts as they become due in the ordinary course of business and (2) the Company’s total assets would at least equal the sum of its total liabilities plus the amount that would be needed if the Company were to be dissolved at the time of the distribution to satisfy the preferential rights upon dissolution of shareholders whose preferential rights are superior to those receiving the distribution. In addition, it is the policy of the Federal Reserve that bank holding companies generally should pay dividends only out of net income generated over the past year and only if the prospective rate of earnings retention appears consistent with the organization’s capital needs, asset quality and overall financial condition. The policy also provides that bank holding companies should not maintain a level of cash dividends that places undue pressure on the capital of its subsidiary bank or that may undermine its ability to serve as a source of strength.



The Company's ability to pay dividends to shareholders is significantly dependent on the Bank's ability to pay dividends to the Company. Capital rules as well as regulatory policy impose additional requirements on the ability of the Company and the Bank to pay dividends. See "Regulation and Supervision of HomeStreet Bank — *Capital and Prompt Corrective Action Requirements — Capital Requirements.*"

### ***Compensation Policies***

Compensation policies and practices at the Company and the Bank are subject to regulation by their respective banking regulators and the SEC.

*Guidance on Sound Incentive Compensation Policies.* The Federal banking regulators have adopted the Sound Incentive Compensation Policies Final Guidance (the "Final Guidance") designed to help ensure that incentive compensation policies at banking organizations do not encourage imprudent risk-taking and are consistent with the safety and soundness of the organization. The Final Guidance applies to senior executives and others who are responsible for oversight of our company-wide activities and material business lines, as well as other employees who, either individually or as a part of a group, have the ability to expose the Bank to material amounts of risk.

*Dodd-Frank Act.* In addition to the Final Guidance, the Dodd-Frank Act contains a number of provisions relating to compensation applying to public companies such as the Company. The Dodd-Frank Act added a new Section 14A(a) to the Securities and Exchange Act of 1934, as amended (the "Exchange Act") that requires companies to include a separate non-binding resolution subject to shareholder vote in their proxy materials approving the executive compensation disclosed in the materials. In addition, a new Section 14A(b) to the Exchange Act requires any proxy or consent solicitation materials for a meeting seeking shareholder approval of an acquisition, merger, consolidation or disposition of all or substantially all of the company's assets to include a separate non-binding shareholder resolution approving certain "golden parachute" payments made in connection with the transaction. A new Section 10D to the Exchange Act requires the SEC to direct the national securities exchanges to require companies to implement a policy to "claw back" certain executive payments that were made based on improper financial statements.

In addition, Section 956 of the Dodd-Frank Act requires certain regulators (including the FDIC, SEC and Federal Reserve) to adopt regulations or guidelines prohibiting excessive compensation or compensation that could lead to material loss as well as rules relating to disclosure of compensation. On April 14, 2011, these regulators published a joint proposed rulemaking to implement Section 956 of Dodd-Frank for depository institutions, their holding companies and various other financial institutions with \$1 billion or more in assets. On June 10, 2016, these regulators published a modified proposed rule. Under the new proposed rule, the requirements and prohibitions will vary depending on the size and complexity of the covered institution. Generally, for covered institutions with less than \$50 billion in consolidated assets (such as the Company), the new proposed rule would (1) prohibit incentive-based compensation arrangements for covered persons that would encourage inappropriate risks by providing excessive compensation or by providing compensation that could lead to a material financial loss, (2) require oversight of an institution's incentive-based compensation arrangements by the institution's board of directors or a committee and approval by the board or committee of certain payments and awards and (3) require the creation on an annual basis and maintenance for at least seven years of records that (a) document the institution's incentive compensation arrangements, (b) demonstrate compliance with the regulation and (c) are disclosed to the institution's appropriate federal regulator upon request.

*FDIC Regulations.* We are further restricted in our ability to make certain "golden parachute" and "indemnification" payments under Part 359 of the FDIC regulations, and the FDIC also regulates payments to executives under Part 364 of its regulations relating to excessive executive compensation.

## **Regulation and Supervision of HomeStreet Bank**

### ***General***

As a commercial bank chartered under the laws of the State of Washington, HomeStreet Bank is subject to applicable provisions of Washington law and regulations of the WDFI. As a state-chartered commercial bank that is not a member of the Federal Reserve System, the Bank's primary federal regulator is the FDIC. It is subject to regulation and examination by the WDFI and the FDIC, as well as enforcement actions initiated by the WDFI and the FDIC, and its deposits are insured by the FDIC.



## ***Washington Banking Regulation***

As a Washington bank, the Bank's operations and activities are substantially regulated by Washington law and regulations, which govern, among other things, the Bank's ability to take deposits and pay interest, make loans on or invest in residential and other real estate, make consumer and commercial loans, invest in securities, offer various banking services to its customers and establish branch offices. Under state law, commercial banks in Washington also generally have, subject to certain limitations or approvals, all of the powers that Washington chartered savings banks have under Washington law and that federal savings banks and national banks have under federal laws and regulations.

Washington law also governs numerous corporate activities relating to the Bank, including the Bank's ability to pay dividends, to engage in merger activities and to amend its articles of incorporation, as well as limitations on change of control of the Bank. Under Washington law, the board of directors of the Bank generally may not declare a cash dividend on its capital stock in an amount greater than its retained earnings without the approval of the WDFI. This restriction is in addition to restrictions imposed by federal law. Mergers involving the Bank and sales or acquisitions of its branches are generally subject to the approval of the WDFI. No person or entity may acquire control of the Bank until 30 days after filing a notice or an application with the WDFI, which has the authority to disapprove the notice or application. Washington law defines "control" of an entity to mean directly or indirectly, alone or in concert with others, to own, control or hold the power to vote 25.0% or more of the outstanding stock or voting power of the entity. Any amendment to the Bank's articles of incorporation requires the approval of the WDFI.

The Bank is subject to periodic examination by and reporting requirements of the WDFI, as well as enforcement actions initiated by the WDFI. The WDFI's enforcement powers include the issuance of orders compelling or restricting conduct by the Bank and the authority to bring actions to remove the Bank's directors, officers and employees. The WDFI has authority to place the Bank under supervisory direction or to take possession of the Bank and to appoint the FDIC as receiver.

## ***Insurance of Deposit Accounts and Regulation by the FDIC***

The FDIC is the Bank's principal federal bank regulator. As such, the FDIC is authorized to conduct examinations of, and to require reporting by the Bank. The FDIC may prohibit the Bank from engaging in any activity determined by law, regulation or order to pose a serious risk to the institution, and may take a variety of enforcement actions in the event the Bank violates a law, regulation or order or engages in an unsafe or unsound practice or under certain other circumstances. The FDIC also has the authority to appoint itself as receiver of the Bank or to terminate the Bank's deposit insurance if it were to determine that the Bank has engaged in unsafe or unsound practices or is in an unsafe or unsound condition.

The Bank is a member of the Deposit Insurance Fund ("DIF") administered by the FDIC, which insures customer deposit accounts. The amount of federal deposit insurance coverage is \$250,000, per depositor, for each account ownership category at each depository institution. The \$250,000 amount is subject to periodic adjustments.

In order to maintain the DIF, member institutions, such as the Bank, are assessed insurance premiums. The Dodd-Frank Act required the FDIC to make numerous changes to the DIF and the manner in which assessments are calculated. As required by the Dodd-Frank Act, assessments are now based on an insured institution's average consolidated assets less tangible equity capital.

Each institution is provided an assessment rate, which is generally based on the risk that the institution presents to the DIF. Institutions with less than \$10 billion in assets generally have an assessment rate that can range from 1.5 to 30 basis points. However, the FDIC does have flexibility to adopt assessment rates without additional rule-making provided that the total base assessment rate increase or decrease does not exceed 2 basis points. In the future, if the reserve ratio reaches certain levels, these assessment rates will generally be lowered. As of December 31, 2019, the Bank's assessment rate was 4.96 basis points on average assets less average tangible equity capital.

In addition, in the past, all FDIC-insured institutions were required to pay a pro rata portion of the interest due on obligations issued by the Financing Corporation to fund the closing and disposal of failed thrift institutions by the Resolution Trust Corporation. The last of these obligations matured in 2019 and accordingly, FDIC-insured institutions are no longer required to make payments related to the obligations.

## ***Capital and Prompt Corrective Action Requirements***

### *Capital Requirements*

In July 2013, federal banking regulators (including the FDIC and the FRB) adopted new capital rules (the “Rules”). The Rules apply to both depository institutions (such as the Bank) and their holding companies (such as the Company). The Rules reflect, in part, certain standards initially adopted by the Basel Committee on Banking Supervision in December 2010 (which standards are commonly referred to as “Basel III”) as well as requirements contemplated by the Dodd-Frank Act. The Rules applied to both the Company and the Bank beginning in 2015.

The Rules recognize three components, or tiers, of capital: common equity Tier 1 capital, additional Tier 1 capital and Tier 2 capital. Common equity Tier 1 capital generally consists of retained earnings and common stock instruments (subject to certain adjustments), as well as accumulated other comprehensive income (“AOCI”) except to the extent that the Company and the Bank exercise a one-time irrevocable option to exclude certain components of AOCI. Both the Company and the Bank made this election in 2015. Additional Tier 1 capital generally includes non-cumulative preferred stock and related surplus subject to certain adjustments and limitations. Tier 2 capital generally includes certain capital instruments (such as subordinated debt) and portions of the amounts of the allowance for loan and lease losses, subject to certain requirements and deductions. The term

“Tier 1 capital” means common equity Tier 1 capital plus additional Tier 1 capital, and the term “total capital” means Tier 1 capital plus Tier 2 capital.

The Rules generally measure an institution’s capital using four capital measures or ratios. The common equity Tier 1 capital ratio is the ratio of the institution’s common equity Tier 1 capital to its Tier 1 risk-weighted assets. The Tier 1 capital ratio is the ratio of the institution’s Tier 1 capital to its total risk-weighted assets. The total capital ratio is the ratio of the institution’s total capital to its total risk-weighted assets. The leverage ratio is the ratio of the institution’s Tier 1 capital to its average total consolidated assets. To determine risk-weighted assets, assets of an institution are generally placed into a risk category as prescribed by the regulations and given a percentage weight based on the relative risk of that category. An asset’s risk-weighted value will generally be its percentage weight multiplied by the asset’s value as determined under generally accepted accounting principles. In addition, certain off-balance-sheet items are converted to balance-sheet credit equivalent amounts, and each amount is then assigned to one of the risk categories. An institution’s federal regulator may require the institution to hold more capital than would otherwise be required under the Rules if the regulator determines that the institution’s capital requirements under the Rules are not commensurate with the institution’s credit, market, operational or other risks.

To be adequately capitalized both the Company and the Bank are required to have a common equity Tier 1 capital ratio of at least 4.5% or more, a Tier 1 leverage ratio of 4.0% or more, a Tier 1 risk-based ratio of 6.0% or more and a total risk-based ratio of 8.0% or more. In addition to the preceding requirements, all financial institutions subject to the Rules, including both the Company and the Bank, are required to establish a “conservation buffer,” consisting of common equity Tier 1 capital, which is at least 2.5% above each of the preceding common equity Tier 1 capital ratio, the Tier 1 risk-based ratio and the total risk-based ratio. An institution that does not meet the conservation buffer will be subject to restrictions on certain activities including payment of dividends, stock repurchases and discretionary bonuses to executive officers.

The Rules set forth the manner in which certain capital elements are determined, including but not limited to, requiring certain deductions related to mortgage servicing rights and deferred tax assets. When the federal banking regulators initially proposed new capital rules in 2012, the rules would have phased out trust preferred securities as a component of Tier 1 capital. As finally adopted, however, the Rules permit holding companies with less than \$15 billion in total assets as of December 31, 2009 (which includes the Company) to continue to include trust preferred securities issued prior to May 19, 2010 in Tier 1 capital, generally up to 25% of other Tier 1 capital.

The Rules made changes in the methods of calculating certain risk-based assets, which in turn affects the calculation of risk-based ratios. Higher or more sensitive risk weights are assigned to various categories of assets, among which are commercial real estate, credit facilities that finance the acquisition, development or construction of real property, certain exposures or credits that are 90 days past due or are nonaccrual, foreign exposures, certain corporate exposures, securitization exposures, equity exposures and in certain cases mortgage servicing rights and deferred tax assets.

We believe that the current capital levels of the Company and the Bank are in compliance with the standards under the Rules including the conservation buffer.

### *Prompt Corrective Action Regulations*

Section 38 of the Federal Deposit Insurance Act establishes a framework of supervisory actions for insured depository institutions that are not adequately capitalized, also known as “prompt corrective action” regulations. All of the federal banking agencies have promulgated substantially similar regulations to implement a system of prompt corrective action. These regulations apply to the Bank but not the Company. As modified by the Rules, the framework establishes five capital categories; under the Rules, a bank is:

- “well capitalized” if it has a total risk-based capital ratio of 10.0% or more, a Tier 1 risk-based capital ratio of 8.0% or more, a common equity Tier 1 risk-based ratio of 6.5% or more, and a leverage capital ratio of 5.0% or more, and is not subject to any written agreement, order or capital directive to meet and maintain a specific capital level for any capital measure;
- “adequately capitalized” if it has a total risk-based capital ratio of 8.0% or more, a Tier 1 risk-based capital ratio of 6.0% or more, a common equity Tier 1 risk-based ratio of 4.5% or more, and a leverage capital ratio of 4.0% or more;
- “undercapitalized” if it has a total risk-based capital ratio less than 8.0%, a Tier 1 risk-based capital ratio less than 6.0%, a common equity risk-based ratio less than 4.5% or a leverage capital ratio less than 4.0%;
- “significantly undercapitalized” if it has a total risk-based capital ratio less than 6.0%, a Tier 1 risk-based capital ratio less than 4.0%, a common equity risk-based ratio less than 3.0% or a leverage capital ratio less than 3.0%; and
- “critically undercapitalized” if it has a ratio of tangible equity to total assets that is equal to or less than 2.0%.

A bank that, based upon its capital levels, is classified as “well capitalized,” “adequately capitalized” or “undercapitalized” may be treated as though it were in the next lower capital category if the appropriate federal banking agency, after notice and opportunity for a hearing, determines that an unsafe or unsound condition, or an unsafe or unsound practice, warrants such treatment.

At each successive lower capital category, an insured bank is subject to increasingly severe supervisory actions. These actions include, but are not limited to, restrictions on asset growth, interest rates paid on deposits, branching, allowable transactions with affiliates, ability to pay bonuses and raises to senior executives and pursuing new lines of business. Additionally, all “undercapitalized” banks are required to implement capital restoration plans to restore capital to at least the “adequately capitalized” level, and the FDIC is generally required to close “critically undercapitalized” banks within a 90-day period.

### ***Capital Simplification Rule***

Following the enactment of the Economic Growth, Regulatory Relief, and Consumer Protection Act (the “EGRRCPA”) in May 2018, the federal banking regulators (including the FDIC and the Federal Reserve) issued a new rule, the Community Bank Leverage Ratio (“CBLR”), intended to simplify capital rules for certain community banks and their holding companies. Qualifying community banking organizations can elect to be under a new capital framework rather than the current capital framework. The new rule is effective beginning in 2020. We have elected to remain under the existing capital framework rather than under the new CLBR framework. Qualifying community banks have the right to opt into and out of the CLBR framework at any time and for any reason.

### ***Limitations on Transactions with Affiliates***

Transactions between the Bank and any affiliate are governed by Sections 23A and 23B of the Federal Reserve Act. An affiliate of the Bank is any company or entity which controls, is controlled by or is under common control with the Bank but which is not a subsidiary of the Bank. The Company and its non-bank subsidiaries are affiliates of the Bank. Generally, Section 23A limits the extent to which the Bank or its subsidiaries may engage in “covered

transactions” with any one affiliate to an amount equal to 10.0% of the Bank’s capital stock and surplus, and imposes an aggregate limit on all such transactions with all affiliates in an amount equal to 20.0% of such capital stock and surplus. Section 23B applies to “covered transactions” as well as certain other transactions and requires that all transactions be on terms substantially the same, or at least as favorable to the Bank, as those provided to a non-affiliate. The term “covered transaction” includes the making of loans to an affiliate, the purchase of or investment in the securities issued by an affiliate, the purchase of assets from an affiliate, the acceptance of securities issued by an affiliate as collateral security for a loan or extension of credit to any person or company, the issuance of a guarantee, acceptance or letter of credit on behalf of an affiliate, or certain transactions with an affiliate that involves the borrowing or lending of securities and certain derivative transactions with an affiliate.

In addition, Sections 22(g) and (h) of the Federal Reserve Act place restrictions on loans, derivatives, repurchase agreements and securities lending to executive officers, directors and principal shareholders of the Bank and its affiliates.

### ***Standards for Safety and Soundness***

The federal banking regulatory agencies have prescribed, by regulation, a set of guidelines for all insured depository institutions prescribing safety and soundness standards. These guidelines establish general standards for internal controls, information systems, internal audit systems, loan documentation, credit underwriting, interest rate risk exposure, asset growth, asset quality, earnings standards, compensation, fees and benefits. In general, the guidelines require appropriate systems and practices to identify and manage the risks and exposures specified in the guidelines before capital becomes impaired. The guidelines prohibit excessive compensation as an unsafe and unsound practice and describe compensation as excessive when the amounts paid are unreasonable or disproportionate to the services performed by an executive officer, employee, director, or principal shareholder.

Each insured depository institution must implement a comprehensive written information security program that includes administrative, technical and physical safeguards appropriate to the institution’s size and complexity and the nature and scope of its activities. The information security program also must be designed to ensure the security and confidentiality of customer information, protect against any unanticipated threats or hazards to the security or integrity of such information, protect against unauthorized access to or use of such information that could result in substantial harm or inconvenience to any customer and ensure the proper disposal of customer and consumer information. Each insured depository institution must also develop and implement a risk-based response program to address incidents of unauthorized access to customer information in customer information systems. If the FDIC determines that the Bank fails to meet any standard prescribed by the guidelines, it may require the Bank to submit an acceptable plan to achieve compliance with the standard. The Bank maintains a program to meet the information security requirements.

### ***Real Estate Lending Standards***

FDIC regulations require the Bank to adopt and maintain written policies that establish appropriate limits and standards for real estate loans. These standards, which must be consistent with safe and sound banking practices, must establish loan portfolio diversification standards, prudent underwriting standards (including loan-to-value ratio limits) that are clear and measurable, loan administration procedures and documentation, approval and reporting requirements. The Bank is obligated to monitor conditions in its real estate markets to ensure that its standards continue to be appropriate for market conditions. The Bank’s board of directors is required to review and approve the Bank’s standards at least annually.

The FDIC has published guidelines for compliance with these regulations, including supervisory limitations on loan-to-value ratios for different categories of real estate loans. Under the guidelines, the aggregate amount of all loans in excess of the supervisory loan-to-value ratios should not exceed 100.0% of total capital, and the total of all loans for commercial, agricultural, multifamily or other non-one-to-four family residential properties in excess of such ratios should not exceed 30.0% of total capital. Loans in excess of the supervisory loan-to-value ratio limitations must be identified in the Bank’s records and reported at least quarterly to the Bank’s board of directors.

The FDIC and the federal banking agencies have also issued guidance on sound risk management practices for concentrations in commercial real estate lending. The particular focus is on exposure to commercial real estate loans that are dependent on the cash flow from the real estate held as collateral and that are likely to be sensitive to conditions in the commercial real estate market (as opposed to real estate collateral held as a secondary source

of repayment or as an abundance of caution). The purpose of the guidance is not to limit a bank's commercial real estate lending but to guide banks in developing risk management practices and capital levels commensurate with the level and nature of real estate concentrations.

### ***Risk Retention***

The Dodd-Frank Act requires that, subject to certain exemptions, securitizers of mortgage and other asset-backed securities retain not less than five percent of the credit risk of the mortgages or other assets and that the securitizer not hedge or otherwise transfer the risk it is required to retain. Generally, the implemented regulations provide various ways in which the retention of risk requirement can be satisfied and also describes exemptions from the retention requirements for various types of assets, including mortgages.

### ***Volcker Rule***

Certain provisions of the Dodd-Frank Act are commonly known as the "Volcker Rule." Subject to certain exceptions, the Volcker Rule generally prohibits banks and affiliated companies from engaging in proprietary trading of certain securities, derivatives, commodity futures and options on those instruments, for their own account. The Volcker Rule also imposes restrictions on banks and their affiliates from acquiring or retaining an ownership interest in, sponsoring or having certain other relationships with hedge funds or private equity funds.

Section 203 of the EGRRCPA amends the Volker Rule to exempt any institution that does not have, or is not controlled by a company that has, more than \$10 billion in total consolidated assets and total trading assets and liabilities that are more than five percent of total consolidated assets. As a result, the Bank is exempt from the Volker Rule until such time that its assets exceed \$10 billion or its total trading assets and liabilities are more than five percent of total consolidated assets.

### ***Activities and Investments of Insured State-Chartered Financial Institutions***

Federal law generally prohibits FDIC-insured state banks from engaging as a principal in activities, and from making equity investments, other than those that are permissible for national banks. An insured state bank is not prohibited from, among other things, (1) acquiring or retaining a majority interest in certain subsidiaries, (2) investing as a limited partner in a partnership the sole purpose of which is direct or indirect investment in the acquisition, rehabilitation or new construction of a qualified housing project, provided that such limited partnership investments may not exceed 2.0% of the bank's total assets, (3) acquiring up to 10.0% of the voting stock of a company that solely provides or reinsures directors', trustees' and officers' liability insurance coverage or bankers' blanket bond group insurance coverage for insured depository institutions and (4) acquiring or retaining the voting shares of a depository institution if certain requirements are met.

Washington State has enacted a law regarding financial institution parity. The law generally provides that Washington-chartered commercial banks may exercise any of the powers of Washington-chartered savings banks, national banks or federally-chartered savings banks, subject to the approval of the Director of the WDFI in certain situations.

### ***Environmental Issues Associated with Real Estate Lending***

The Comprehensive Environmental Response, Compensation and Liability Act, or (the "CERCLA"), is a federal statute that generally imposes strict liability on all prior and present "owners and operators" of sites containing hazardous waste. However, Congress has acted to protect secured creditors by providing that the term "owner and operator" excludes a person whose ownership is limited to protecting its security interest in the site. Since the enactment of the CERCLA, this "secured creditor" exemption has been the subject of judicial interpretations which have left open the possibility that lenders could be liable for cleanup costs on contaminated property that they hold as collateral for a loan. To the extent that legal uncertainty exists in this area, all creditors, including the Bank, that have made loans secured by properties with potential hazardous waste contamination (such as petroleum contamination) could be subject to liability for cleanup costs, which costs often substantially exceed the value of the collateral property.



### ***Reserve Requirements***

The Bank is subject to Federal Reserve regulations pursuant to which depository institutions may be required to maintain non-interest-earning reserves against their deposit accounts and certain other liabilities. Reserves must be maintained against transaction accounts (primarily negotiable order of withdrawal and regular checking accounts). The regulations generally required in 2019 that reserves be maintained as follows:

- Net transaction accounts up to \$16.3 million are exempt from reserve requirements.
- A reserve of 3.0% for transaction accounts over \$16.3 million up to \$124.2 million.
- A reserve of 10% for any transaction accounts over \$124.2 million.

In 2020, the regulations generally require that reserves be maintained as follows:

- Net transaction accounts up to \$16.9 million are exempt from reserve requirements.
- A reserve of 3.0% of the aggregate is required for transaction accounts over \$16.9 million up to \$127.5 million.
- A reserve of 10% is required for any transaction accounts over \$127.5 million.

### ***Federal Home Loan Bank System***

The Federal Home Loan Bank system consists of 11 regional Federal Home Loan Banks. Among other benefits, each of these serves as a reserve or central bank for its members within its assigned region. Each of the Federal Home Loan Banks makes available loans or advances to its members in compliance with the policies and procedures established by its board of directors. The Bank is a member of the Federal Home Loan Bank of Des Moines (the “Des Moines FHLB”). As a member of the Des Moines FHLB, the Bank is required to own stock in the Des Moines FHLB. As of December 31, 2019, we owned \$22.4 million of stock in the FHLB based on this obligation.

### ***Community Reinvestment Act of 1977***

Banks are subject to the provisions of the CRA of 1977, which requires the appropriate federal bank regulatory agency to assess a bank’s record in meeting the credit needs of the assessment areas serviced by the bank, including low and moderate income neighborhoods. The regulatory agency’s assessment of the bank’s record is made available to the public. Further, these assessments are considered by regulators when evaluating mergers, acquisitions and applications to open or relocate a branch or facility. The Bank currently has a rating of “Satisfactory” under the CRA.

### ***Dividends***

Dividends from the Bank constitute an important source of funds for dividends that may be paid by the Company to shareholders. The amount of dividends payable by the Bank to the Company depends upon the Bank’s earnings and capital position and is limited by federal and state laws. Under Washington law dividends on the Bank’s capital stock generally may not be paid in an amount greater than its retained earnings without the approval of the WDFI.

The amount of dividends actually paid during any one period will be strongly affected by the Bank’s policy of maintaining a strong capital position. Federal law prohibits an insured depository institution from paying a cash dividend if this would cause the institution to be “undercapitalized,” as defined in the prompt corrective action regulations. Moreover, the federal bank regulatory agencies have the general authority to limit the dividends paid by insured banks if such payments are deemed to constitute an unsafe and unsound practice. Capital rules that went into effect in 2015 impose additional requirements on the Bank’s ability to pay dividends. See “Regulation and Supervision of HomeStreet Bank — *Capital and Prompt Corrective Action Requirements — Capital Requirements.*”

### ***Liquidity***

The Bank is required to maintain a sufficient amount of liquid assets to ensure its safe and sound operation. See “Management’s Discussion and Analysis — *Liquidity Risk and Capital Resources.*”



## ***Compensation***

The Bank is subject to regulation of its compensation practices. See “Regulation and Supervision — *Regulation of the Company — Compensation Policies.*”

## ***Bank Secrecy Act and USA Patriot Act***

The Company and the Bank are subject to the Bank Secrecy Act, as amended by the USA PATRIOT Act, which gives the federal government powers to address money laundering and terrorist threats through enhanced domestic security measures, expanded surveillance powers and mandatory transaction reporting obligations. By way of example, the Bank Secrecy Act imposes an affirmative obligation on the Bank to report currency transactions that exceed certain thresholds and to report other transactions determined to be suspicious. The Bank Secrecy Act requires financial institutions, including the Bank, to meet certain customer due diligence requirements, including obtaining a certification from the individual opening the account on behalf of the legal entity that identifies the beneficial owner(s) of the entity. The purpose of these requirements is to enable the Bank to be able to predict with relative certainty the types of transactions in which a customer is likely to engage which should in turn assist in determining when transactions are potentially suspicious.

Like all United States companies and individuals, the Company and the Bank are prohibited from transacting business with certain individuals and entities named on the Office of Foreign Asset Control’s list of Specially Designated Nationals and Blocked Persons. Failure to comply may result in fines and other penalties. The Office of Foreign Asset Control (“OFAC”) has issued guidance directed at financial institutions in which it asserted that it may, in its discretion, examine institutions determined to be high-risk or to be lacking in their efforts to comply with these prohibitions.

The Bank maintains a program to meet the requirements of the Bank Secrecy Act, USA PATRIOT Act and OFAC.

## ***Identity Theft***

Section 315 of the Fair and Accurate Credit Transactions Act (“FACT Act”) requires each financial institution or creditor to develop and implement a written Identity Theft Prevention Program to detect, prevent and mitigate identity theft “red flags” in connection with the opening of certain accounts or certain existing accounts.

The Bank maintains a program to meet the requirements of Section 315 of the FACT Act.

## ***Consumer Protection Laws and Regulations***

The Bank and its affiliates are subject to a broad array of federal and state consumer protection laws and regulations that govern almost every aspect of its business relationships with consumers. While this list is not exhaustive, these include the Truth-in-Lending Act, the Truth in Savings Act, the Electronic Fund Transfer Act, the Expedited Funds Availability Act, the Equal Credit Opportunity Act, the Fair Housing Act, the Secure and Fair Enforcement in Mortgage Licensing Act, the Real Estate Settlement Procedures Act, the Home Mortgage Disclosure Act, the Fair Credit Reporting Act, the Fair Debt Collection Practices Act, the Service Members’ Civil Relief Act, the Right to Financial Privacy Act, the Home Ownership and Equity Protection Act, the Consumer Leasing Act, the Fair Credit Billing Act, the Homeowners Protection Act, the Check Clearing for the 21<sup>st</sup> Century Act, laws governing flood insurance, laws governing consumer protections in connection with the sale of insurance, federal and state laws prohibiting unfair and deceptive business practices, foreclosure laws and various regulations that implement some or all of the foregoing. These laws and regulations mandate certain disclosure requirements and regulate the manner in which financial institutions must deal with customers when taking deposits, making loans, collecting loans and providing other services. Failure to comply with these laws and regulations can subject the Bank to various penalties, including but not limited to, enforcement actions, injunctions, fines, civil money penalties, civil liability, criminal penalties, punitive damages and the loss of certain contractual rights. The Bank has a compliance governance structure in place to help ensure its compliance with these requirements.

The Dodd-Frank Act established the Bureau of Consumer Financial Protection (“CFPB”) as a new independent bureau that is responsible for regulating consumer financial products and services under federal consumer financial laws. The CFPB has broad rulemaking authority with respect to these laws and exclusive examination and primary enforcement authority regarding such laws with respect to banks with assets of more than \$10 billion.

The Dodd-Frank Act also contains a variety of provisions intended to reform consumer mortgage practices. The provisions include (1) a requirement that lenders make a determination that at the time a residential mortgage loan is consummated the consumer has a reasonable ability to repay the loan and related costs, (2) a ban on loan originator compensation based on the interest rate or other terms of the loan (other than the amount of the principal), (3) a ban on prepayment penalties for certain types of loans, (4) bans on arbitration provisions in mortgage loans and (5) requirements for enhanced disclosures in connection with the making of a loan. The Dodd-Frank Act also imposed a variety of requirements on entities that service mortgage loans and significantly expanded mortgage loan application data collection and reporting requirements under the Home Mortgage Disclosure Act.

The Dodd-Frank Act contains provisions further regulating payment card transactions. The Dodd-Frank Act required the Federal Reserve to adopt regulations limiting any interchange fee for a debit transaction to an amount which is “reasonable and proportional” to the costs incurred by the issuer. The Federal Reserve has adopted final regulations limiting the amount of debit interchange fees that large bank issuers may charge or receive on their debit card transactions. There is an exemption from the rules for issuers with assets of less than \$10 billion.

### **Future Legislation or Regulation**

The Trump administration, Congress, the regulators and various states continue to focus attention on the financial services industry. Proposals that affect the industry will likely continue to be introduced. We cannot predict whether any of these proposals will be enacted or adopted or, if they are, the effect they would have on our business, our operations or our financial condition or on the financial services industry generally.

## **ITEM 1A RISK FACTORS**

*This Form 10-K contains forward-looking statements that involve risks and uncertainties. Our actual results could differ materially from those anticipated in these forward-looking statements as a result of certain factors, including the risks faced by us described below and elsewhere in this report.*

### **Risks Related to Our Operations**

***We may not be able to meet our cost reduction and efficiency goals on the timeline we have projected or on the scale we have anticipated.***

Beginning in the second quarter of 2019, following the divestiture of our HLC-based mortgage business, we turned our focus to improving corporate efficiency in our continuing operations and implementing cost cutting measures across the organization, including setting goals for cost savings based on reductions in technology expenses and personnel as well as organizational restructuring. In the first quarter of 2020 we revised our previously disclosed expectations for the timeline on which we expect to meet these goals. We believe that we will be able to meet most if not all of these goals and now expect to substantially complete implementation of the related cost-cutting and efficiency measures before the end of the third quarter of 2021. However, we can offer no assurances that all of the cost cutting measures identified can be fully implemented, that the implementation can be completed within that time frame, or that other developments will not arise in the interim to make these cost cutting measures less feasible or have less impact on the efficiency of the organization. We may not be successful in renegotiating contracts for technology services, which may limit our ability to effectively cut costs in that area. We may incur additional unexpected costs as a part of the process which may lower the benefit of the cost cutting initiatives. If the cost cutting initiatives take longer to implement, if we are not able to implement them on the scale we anticipate, or if developments occur that limit or offset those cost savings in whole or in part, we may not be able to meet the efficiency and cost reduction goals we have set for the Company on the projected timeline or at all, which could adversely impact our overall results of operations and our stock price. We may not be successful in reducing our overall expenses and improving our efficiency ratio to the level of our peers in the near term, or at all.

***Our recent and proposed stock repurchases may not enhance our long-term shareholder value.***

In the second quarter of 2019, we began repurchasing shares of our outstanding common stock in open market transactions pursuant to a series of stock repurchase plans that were approved by the Board of Directors of the Company, as well as a one time negotiated transaction with an investor group in the third quarter of 2019. Through December 31, 2019 we repurchased an aggregate 3,187,259 shares for a total return to shareholders of approximately

\$98.5 million in capital. In January 2020, the Board of Directors authorized an additional stock repurchase plan, conditioned on approval or non-objection from our regulators, which was recently obtained, of up to \$25 million in additional outstanding shares of our common stock, negotiated transactions and otherwise, which we expect to begin in the first quarter of 2020. In February the Board increased the authorization by an additional \$10 million conditional on the non-objection of our regulators. Assuming no objections from our regulators for the additional repurchase authorization, we expect to commence repurchases in the first or second quarter of 2020. While the intent of the repurchases is to return capital to shareholders to improve the long-term value of our stock, we cannot be assured that our stock repurchase programs will actually enhance long-term shareholder value. Repurchases pursuant to our stock repurchase programs may affect our stock price and increase its volatility in the short term, and the existence of a stock repurchase program may also cause our stock price to be higher than it would be in the absence of such a program and potentially may have reduced the market liquidity for our stock during the time the plan is in effect. Additionally, repurchases under our stock repurchase program have reduced our equity and regulatory capital ratios, which could impact our ability to pursue possible future strategic opportunities and acquisitions. There can be no assurance that any stock repurchases will enhance shareholder value because the market price of our common stock may decline below the levels at which we repurchased shares of stock. Although our stock repurchase program is intended to enhance long-term shareholder value, in the short term our stock price may fluctuate and shareholders may not immediately see an increase to the value of their holdings.

***If we are not able to retain or attract key employees, we could experience a disruption in our ability to implement our strategic plan which would have a material adverse effect on our business.***

The Company is going through a time of transition: in 2019 we divested our HLC-based mortgage business and have continued since that time to significantly reduce our employee headcount, slow the growth of our continuing operations and implement steps aimed at improving our profitability and efficiency. These transitions have resulted in some uncertainty among our continuing employees because we have also eliminated a number of corporate positions in order to improve the efficiency of our remaining operations and reduce our overhead expenses, which may cause some employees who we would want to retain, either in the near-term or long-term, to seek other opportunities. If a key employee or a substantial number of employees depart whom we were seeking to retain, it may negatively impact our ability to conduct business as usual. The low unemployment rates in many of our primary job markets, including Seattle, may leave us especially vulnerable to the loss of these employees. Similarly, this uncertainty may make it more challenging for us to attract and retain qualified and desirable candidates to fill open positions at the Company. The loss of key personnel or an inability to continue to attract, retain and motivate key personnel could adversely affect our business.

***Changes in interest rates, competition in our industry, operational costs and other factors beyond our control may adversely impact our profitability.***

Factors outside of our control, including changing interest rate environments, regulatory decisions, increased competition, a flattening yield curve and other forces of market volatility, can have a significant impact on our financial condition and results of operations, including decreasing net interest income, decreasing profitability, increasing the cost of loan origination and adversely impacting our hedging strategies. For instance, the declining interest rate environment in the third quarter of 2019, which resulted in a temporary inversion of the yield curve, had an adverse impact on our net interest margin. Lower rates prompted an increase in loan prepayments, which reduced the overall yield of our loan portfolio because higher interest loans were replaced with loans originated with lower interest rates, impacting our results of operations. On the other hand, increases in interest rates in 2018, combined with other factors, negatively impacted our origination volume, especially with respect to single family mortgages. While we are subject to these market forces, we do not have any control over them and may not be able to predict changes that could have a significant impact on us.

***We may incur significant losses as a result of ineffective hedging of interest rate risk related to our loans sold with retained servicing rights.***

Both the value of our single family mortgage servicing rights, or MSRs, and the value of our single family loans held for sale change due to market forces including, among other things, fluctuations in interest rates that can impact the changing expectations of mortgage prepayment activity and speed. To mitigate potential losses of fair value of single family loans held for sale and MSRs related to changes in interest rates, we actively hedge this risk with financial derivative instruments. Hedging is a complex process, requiring sophisticated models, experienced and

skilled personnel and continual monitoring. Changes in the value of our hedging instruments may not correlate with changes in the value of our single family loans held for sale and MSR's, and our hedging activities may be impacted by unforeseen or unexpected changes. Therefore, our hedging activities may be insufficient or fail to reduce the impact of interest rate fluctuations on single family loans held for sale and MSR's.

***Natural disasters or impacts of a pandemic in our geographic markets may negatively impact our financial results.***

Our primary markets are located in geographic regions that are at risk for earthquakes, wildfires, volcanic eruptions, floods, mudslides, outbreaks, epidemics, pandemics and other natural disasters. Certain communities in our markets have suffered significant losses from natural disasters, including devastating wildfires in California, Oregon and Washington, and volcanic eruptions and hurricanes in Hawaii. While the impacts of these natural disasters on our business have not been material to date, we have in the past had temporary office closures during these events and certain of our customers have experienced losses from these events.

In addition, our headquarters are located in King County, Washington, which has seen a higher initial infection and fatality rate from the COVID-19 virus than the rest of the United States, and most of our branches are located in states where cases of COVID-19 have already been identified. We may experience impacts from quarantines, market downturns and changes in consumer behavior related to pandemic fears and impacts on our workforce if the virus becomes widespread in any of our markets. We cannot predict the full impact of COVID-19 or any other future global pandemic on our business, but we could suffer financial losses as a result of the crisis. In addition, downturns in the global market related to pandemic fears could result in a lowering of interest rates as a stimulus to boost consumer spending, which could further negatively impact our results of operations.

If the COVID-19 pandemic becomes more pronounced in our markets, or if a more significant natural disaster or pandemic were to occur in the future, our operations in areas impacted by such events could experience an adverse financial impact due to office closures and market changes. In addition, our financial results could be impacted due to an inability of our customers to meet their loan commitments in a timely manner because of their losses, including a decrease in revenues for certain businesses in areas impacted by quarantines during a pandemic or other changes in consumer behavior, a reduction in housing inventory due to losses caused by natural disaster, and negative impacts to the local economy as it seeks to recover from these disasters.

***Our business is geographically confined to certain metropolitan areas of the Western United States, and events and conditions that disproportionately affect those areas may pose a more pronounced risk for our business.***

Although we presently have retail deposit branches in four states, with lending offices in these states and two others, a substantial majority of our revenues are derived from operations in the Puget Sound region of Washington, the Portland, Oregon metropolitan area, the San Francisco Bay Area, and the Los Angeles, Orange County, Riverside and San Diego metropolitan areas in Southern California. All of our markets are located in the Western United States. Each of our primary markets is subject to various types of natural disasters, and many have experienced disproportionately significant economic volatility compared to the rest of the United States in the past. In addition, many of these areas have experienced a constriction in the availability of houses for sale in recent periods as new home construction has not kept pace with population growth in our primary markets, in part due to limitations on permitting and land availability. Economic events or natural disasters that affect the Western United States and our primary markets in that region, may have an unusually pronounced impact on our business. Because our operations are not more geographically diversified, we may lack the ability to mitigate those impacts from operations in other regions of the United States.

***The significant concentration of real estate secured loans in our portfolio has had a negative impact on our asset quality and profitability in the past and there can be no assurance that it will not have such impact in the future.***

A substantial portion of our loans are secured by real property. Our real estate secured lending is generally sensitive to national, regional and local economic conditions, making loss levels difficult to predict. Declines in real estate sales and prices, significant increases in interest rates, unforeseen natural disasters and a decline in prevailing economic conditions may result in higher than expected loan delinquencies, foreclosures, problem loans, other real estate owned ("OREO"), net charge-offs and provisions for credit and OREO losses. Although real estate prices are currently stable in the markets in which we operate, if market values decline significantly, as they did in the

last recession, the collateral for our loans may provide less security and reduce our ability to recover the principal, interest and costs due on defaulted loans. Such declines may have a greater effect on our earnings and capital than on the earnings and capital of financial institutions whose loan portfolios are more diversified.

Deterioration in the real estate markets in which we operate and higher than normal delinquency and default rates on loans could cause other adverse consequences for us, including:

- Reduced cash flows and capital resources, as we are required to make cash advances to meet contractual obligations to investors, process foreclosures, and maintain, repair and market foreclosed properties;
- Declining mortgage servicing fee revenues because we recognize these revenues only upon collection;
- Increasing mortgage servicing costs;
- Declining fair value on our mortgage servicing rights; and
- Declining fair values and liquidity of securities held in our investment portfolio that are collateralized by mortgage obligations.

***Proxy contests commenced against the Company have caused us to incur substantial costs, diverted the attention of the Board of Directors and management, taken up management's attention and resources, caused uncertainty about the strategic direction of our business and adversely affected our business, operating results and financial condition, and future proxy contests could do so as well.***

A proxy contest or other activist campaign and related actions, such as the recent contest by Roaring Blue Lion Capital Management and related entities in 2018 and 2019, could have a material and adverse effect on us for the following reasons:

- Activist investors may attempt to effect changes in the Company's strategic direction and how the Company is governed, or to acquire control over the Company.
- While the Company welcomes the opinions of all shareholders, responding to proxy contests and related actions by activist investors could be costly and time-consuming, disrupt our operations, and divert the attention of our Board of Directors and senior management and employees away from their regular duties and the pursuit of business opportunities. In addition, there may be litigation in connection with a proxy contest, as was the case with our 2018 proxy fight, which would serve as a further distraction to our Board of Directors, senior management and employees and could require the Company to incur significant additional costs.
- Perceived uncertainties as to our future direction as a result of potential changes to the composition of the Board of Directors may lead to the perception of a change in the strategic direction of the business, instability or lack of continuity which may be exploited by our competitors; may cause concern to our existing or potential customers and employees; may result in the loss of potential business opportunities; and may make it more difficult to attract and retain qualified personnel and business partners.
- Proxy contests and related actions by activist investors could cause significant fluctuations in our stock price based on temporary or speculative market perceptions or other factors that do not necessarily reflect the underlying fundamentals and prospects of our business.

***We may have deficiencies in internal controls over financial reporting that we have not discovered which may result in our inability to maintain control over our assets or to identify and accurately report our financial condition, results of operations, or cash flows.***

Our internal controls over financial reporting are intended to ensure we maintain accurate records, promote the accurate and timely reporting of our financial information, maintain adequate control over our assets, and detect unauthorized acquisition, use or disposition of our assets. Effective internal and disclosure controls are necessary for us to provide reliable financial reports, effectively prevent fraud, and operate successfully as a public company. If we cannot provide reliable financial reports or prevent fraud, our reputation and operating results may be harmed.



As part of our ongoing monitoring of internal controls, from time to time we have discovered deficiencies in our internal controls that have required remediation. In the past, these deficiencies have included “material weaknesses,” defined as a deficiency or combination of deficiencies that results in more than a remote likelihood that a material misstatement of the annual or interim financial statements will not be prevented or detected.

Management has a process in place to document and analyze all identified internal control deficiencies and implement measures sufficient to remediate those deficiencies. To support our strategic initiatives, as well as to reflect the strategic shift in the business and to create operating efficiencies, we have implemented, and will continue to implement, new systems and processes. We will continue to realign our resources, including reductions in certain areas of corporate support operations, in line with our new strategies. If our change management processes are not sound and adequate resources are not deployed to support these implementations and changes, we may experience additional internal control deficiencies that could expose the Company to operating losses. Moreover, any failure to maintain effective controls or timely implement any necessary improvement of our internal and disclosure controls in the future could harm operating results or cause us to fail to meet our reporting obligations.

***Our allowance for credit losses may prove inadequate or we may be negatively affected by credit risk exposures. Future additions to our allowance for credit losses, as well as charge-offs in excess of reserves, will reduce our earnings.***

Our business depends on the creditworthiness of our customers. As with most financial institutions, we maintain an allowance for credit losses to reflect potential defaults and nonperformance, which represents management’s best estimate of probable incurred losses inherent in the loan portfolio. Management’s estimate is based on our continuing evaluation of specific credit risks and loan loss experience, current loan portfolio quality, present economic, political and regulatory conditions, industry concentrations and other factors that may indicate future loan losses. Generally, our nonperforming loans and OREO reflect operating difficulties of individual borrowers and weaknesses in the economies of the markets we serve. This allowance may not be adequate to cover actual losses, and future provisions for losses could materially and adversely affect our financial condition, results of operations and cash flows.

On January 1, 2020, the Company adopted ASU 2016-13, *Measurement of Credit Losses on Financial Instruments*, the new accounting standard promulgated by the Financial Accounting Standards Board (“FASB”), regarding the recognition of credit losses. This standard makes significant changes to the accounting and disclosures for credit losses on financial instruments recorded on an amortized cost basis, including our loans held for investment. The new current expected credit loss (“CECL”) impairment model requires an estimate of expected credit losses for financial assets measured over the contractual life of an instrument based on historical experience, current conditions and reasonable and supportable forecasts. The standard provides significant flexibility and requires a high degree of judgment in order to develop an estimate of expected lifetime losses. Providing for lifetime losses for our loan portfolio is a change to the previous method of allowances for loan losses that are based on probable and incurred losses over a short-term horizon. As it is a new model, we do not yet have experience with it and how it may perform in different business cycles or changes to our loan portfolio. The new methodology is likely to be much more sensitive to changes in inputs such as economic forecasts and other factors which may cause significant impact on the allowance, and could create volatility in the loan loss provision and net income particularly in periods of downturn. Regulators may impose additional capital buffers to absorb this volatility. Moreover, with the new model we have risk of complying with the new accounting standard which are still subject to review by our auditors and regulators.

In addition, as we acquired new operations, we added to our books the loans previously held by the acquired companies or related to the acquired branches, including loans acquired from Silvergate Bank in March 2019. If we make additional acquisitions in the future, we may bring additional loans originated by other institutions onto our books. Although we review loan quality as part of our due diligence in considering any acquisition involving loans, the addition of such loans may increase our credit risk exposure, require an increase in our allowance for credit losses, and adversely affect our financial condition, results of operations and cash flows stemming from losses on those acquired loans.



**Uncertainty relating to the London Interbank Offered Rate (LIBOR) calculation process and potential phasing out of LIBOR may adversely affect our results of operations.**

On July 27, 2017, the Chief Executive of the United Kingdom Financial Conduct Authority (FCA), which regulates LIBOR, announced that the FCA intends to stop persuading or compelling banks to submit rates for the calibration of LIBOR to the administrator of LIBOR after 2021. The announcement indicates that the continuation of LIBOR on the current basis cannot and will not be guaranteed after 2021. It is impossible to predict whether and to what extent banks will continue to provide LIBOR submissions to the administrator of LIBOR or whether any additional reforms to LIBOR may be enacted in the United Kingdom or elsewhere. At this time, no consensus exists as to what rate or rates may become acceptable alternatives to LIBOR and it is impossible to predict the effect of any such alternatives on the value of LIBOR-based securities and variable rate loans, subordinated debentures, or other securities or financial arrangements, given LIBOR's role in determining market interest rates globally. The Federal Reserve, in conjunction with the Alternative Reference Rates Committee, a steering committee comprised of large U.S. financial institutions, selected a new index calculated by short-term repurchase agreements, backed by Treasury securities (SOFR) to replace LIBOR. SOFR is observed and backward looking, which stands in contrast with LIBOR under the current methodology, which is an estimated forward-looking rate and relies, to some degree, on the expert judgment of submitting panel members. Given that SOFR is a secured rate backed government securities, it will be a rate that does not take into account bank credit risk (which is different for LIBOR). SOFR is therefore likely to be lower than LIBOR and is less likely to correlate with the funding costs of financial institutions. Whether or not SOFR attains market traction as a LIBOR replacement tool remains in question, although some transactions using SOFR have been completed in 2019, and the future of LIBOR remains uncertain at this time. Uncertainty as to the nature of alternative reference rates and as to potential changes or other reforms to LIBOR may adversely affect LIBOR rates and the value of LIBOR-based loans, and to a lesser extent, securities in our portfolio, and may impact the availability and cost of hedging instruments and borrowings, including the rates we pay on our subordinated debentures and trust preferred securities. If LIBOR rates are no longer available, and we are required to implement substitute indices for the calculation of interest rates under our loan agreements with our borrowers or our existing borrowings, we may incur significant expenses in effecting the transition, and may be subject to disputes or litigation with customers and creditors over the appropriateness or comparability to LIBOR of the substitute indices, which could have an adverse effect on our results of operations.

***Our accounting policies and methods are fundamental to how we report our financial condition and results of operations, and we use estimates in determining the fair value of certain of our assets, which estimates may prove to be imprecise and result in significant changes in valuation.***

A portion of our assets are carried on the balance sheet at fair value, including investment securities available for sale, mortgage servicing rights related to single family loans and single family loans held for sale. Generally, for assets that are reported at fair value, we use quoted market prices or internal valuation models that use observable market data inputs to estimate their fair value. In certain cases, observable market prices and data may not be readily available, or their availability may be diminished due to market conditions. We use financial models to value certain of these assets. These models are complex and use asset-specific collateral data and market inputs for interest rates. Although we have processes and procedures in place governing internal valuation models and their testing and calibration, such assumptions are complex because we must make judgments about the effect of matters that are inherently uncertain. Different assumptions could result in significant changes in valuation, which in turn could affect earnings or result in significant changes in the dollar amount of assets reported on the balance sheet. From time to time, we may choose to retire or replace existing financial models and reassess assumptions underlying the models, which may impact our valuation estimates.

***Our funding sources may prove insufficient to replace deposits and support our future growth.***

We must maintain sufficient funds to respond to the needs of depositors and borrowers. As a part of our liquidity management, we use a number of funding sources in addition to core deposit growth and repayments and maturities of loans and investments, including Federal Home Loan Bank advances, proceeds from the sale of loans, federal funds purchased, brokered certificates of deposit and issuance of equity or debt securities. Adverse operating results or changes in industry conditions could lead to difficulty or an inability to access these additional funding sources and could make our existing funds more volatile. Our financial flexibility may be materially constrained if we are unable to maintain our access to funding or if adequate financing is not available to accommodate future growth at acceptable interest rates. When interest rates change, the cost of our funding may change at a different rate than

our interest income, which may have a negative impact on our net interest income and, in turn, our financial results. If we are required to rely more heavily on more expensive funding sources to support future growth, our revenues may not increase proportionately to cover our costs. In that case, our operating margins and profitability would be adversely affected. Further, the volatility inherent in some of these funding sources, particularly brokered deposits, may increase our exposure to liquidity risk.

***Our management of capital could adversely affect profitability measures and the market price of our common stock and could dilute the holders of our outstanding common stock.***

Since our IPO in 2012, we have maintained our capital ratios at a level that is higher than regulatory minimums. We may choose to have lower capital ratios in the future in order to take advantage of growth opportunities, including acquisition and organic loan growth, to return additional capital to our shareholders or in order to take advantage of a favorable investment opportunity. On the other hand, we may again in the future elect to raise capital through a sale of our debt or equity securities in order to have additional resources to pursue our growth, including by acquisition, fund our business needs and meet our commitments, or as a response to changes in economic conditions that make capital raising a prudent choice. In the event the quality of our assets or our economic position were to deteriorate significantly, as a result of market forces or otherwise, we may also need to raise additional capital in order to remain compliant with capital standards.

We may not be able to raise such additional capital at the time when we need it, or on terms that are acceptable to us. Our ability to raise additional capital will depend in part on conditions in the capital markets at the time, which are outside our control, and in part on our financial performance. Further, if we need to raise capital in the future, especially if it is in response to changing market conditions, we may need to do so when many other financial institutions are also seeking to raise capital, which would create competition for investors. An inability to raise additional capital on acceptable terms when needed could have a material adverse effect on our business, financial condition, results of operations and prospects. In addition, any capital raising alternatives could dilute the holders of our outstanding common stock and may adversely affect the market price of our common stock.

***Changes in government-sponsored enterprises and their ability to insure or to buy our loans in the secondary market may result in significant changes in our ability to recognize income on sale of our loans to third parties.***

We originate a substantial portion of our single family mortgage loans for sale to government-sponsored enterprises (“GSE”) such as Fannie Mae, Freddie Mac and Ginnie Mae. Changes in the types of loans purchased by these GSEs or the program requirements for those entities could adversely impact our ability to sell certain of the loans we originate for sale. For example, as a result of Section 309 of the Economic Growth, Regulatory Relief, and Consumer Protection Act, which was enacted into law in May 2018, a few of our VA-qualified loans we had originated for sale to Ginnie Mae were deemed to be ineligible for sale to Ginnie Mae under the revised terms of that entity’s program and we were required to find a different way to sell these loans. Such changes are difficult to predict and can have a negative impact on our cash flow and results of operations.

***The integration of recent and future acquisitions could consume significant resources and may not be successful.***

We completed four whole-bank acquisitions and acquired nine stand-alone branches between September 2013 and December 31, 2019, all of which required substantial resources and costs related to the acquisition and integration process. There are certain risks related to the integration of operations of acquired banks and branches, which we may continue to encounter if we acquire other banks or branches in the future, including risks related to the investigation and consideration of the potential acquisition and the costs of undertaking such a transaction, as well as integrating acquired businesses into the Company, including risks that arise after the transaction is completed. Difficulties in pursuing or integrating any new acquisitions, and potential discoveries of additional losses or undisclosed liabilities with respect to the assets and liabilities of acquired companies, may increase our costs and adversely impact our financial condition and results of operations. Further, even if we successfully address these factors and are successful in closing acquisitions and integrating our systems with the acquired systems, we may nonetheless experience customer losses, or we may fail to grow the acquired businesses as we intend or to operate the acquired businesses at a level that would avoid losses or justify our investments in those companies.

***If we breach any of the representations or warranties we make to a purchaser or securitizer of our loans or MSRs, we may be liable to the purchaser or securitizer for certain costs and damages.***

When we sell or securitize loans, we are required to make certain representations and warranties to the purchaser about the loans and the manner in which they were originated. Our agreements require us to repurchase loans if we have breached any of these representations or warranties, in which case we may be required to repurchase such loan and record a loss upon repurchase and/or bear any subsequent loss on the loan. We may not have any remedies available to us against a third party for such losses, or the remedies available to us may not be as broad as the remedies available to the purchaser of the loan against us. In addition, if there are remedies against a third party available to us, we face further risk that such third party may not have the financial capacity to perform remedies that otherwise may be available to us. Therefore, if a purchaser enforces remedies against us, we may not be able to recover our losses from a third party and may be required to bear the full amount of the related loss.

In 2019, we sold a substantial portion of our MSRs related to our large scale mortgage business, which may increase our exposure to these risks in the short term due to the volume of MSR sales outside of our historical ordinary course of business.

If we experience increased repurchase and indemnity demands on loans or MSRs that we have sold or that we sell from our portfolios in the future, our liquidity, results of operations and financial condition may be adversely affected.

***If we breach any representations or warranties or fail to follow guidelines when originating a FHA/HUD-insured loan or a VA-guaranteed loan, we may lose the insurance or guarantee on the loan and suffer losses, pay penalties, and/or be subjected to litigation from the federal government.***

We originate and purchase, sell and thereafter service single family loans, some of which are insured by FHA/HUD or guaranteed by the VA. We certify to the FHA/HUD and the VA that the loans meet their requirements and guidelines. The FHA/HUD and VA audit loans that are insured or guaranteed under their programs, including audits of our processes and procedures as well as individual loan documentation. Violations of guidelines can result in monetary penalties or require us to provide indemnifications against loss or loans declared ineligible for their programs. In the past, monetary penalties and losses from indemnifications have not created material losses to the Bank. FHA/HUD perform regular audits, and HUD's Inspector General is active in enforcing FHA regulations with respect to individual loans, including partnering with the Department of Justice ("DOJ") to bring lawsuits against lenders for systemic violations. The penalties resulting from such lawsuits can be severe, since systemic violations can be applied to groups of loans and penalties may be subject to treble damages. The DOJ has used the Federal False Claims Act and other federal laws and regulations in prosecuting these lawsuits. Because of our significant origination of FHA/HUD insured and VA guaranteed loans, if the DOJ were to find potential violations by the Bank, we could be subject to material monetary penalties and/or losses, and may even be subject to lawsuits alleging systemic violations which could result in treble damages.

***Changes in fee structures by third party loan purchasers may decrease our loan production volume and the margin we can recognize on loans and may adversely impact our results of operations.***

Changes in the fee structures by third party loan purchasers may increase our costs of doing business and, in turn, increase the cost of loans to our customers and the cost of selling loans to third party loan purchasers. Increases in those costs could in turn decrease our margin and negatively impact our profitability. Were any of our third party loan purchasers to make such changes in the future, it may have a negative impact on our ability to originate loans to be sold because of the increased costs of such loans and may decrease our profitability with respect to loans held for sale. In addition, any significant adverse change in the level of activity in the secondary market or the underwriting criteria of these third party loan purchasers could negatively impact our results of business, operations and cash flows.

***We may incur additional costs in placing loans if our third party purchasers discontinue doing business with us for any reason.***

We rely on third party purchasers with whom we place loans as a source of funding for the loans we make to customers. Occasionally, third party loan purchasers may go out of business, elect to exit the market or choose to cease doing business with us for a variety of reasons, including but not limited to the increased burdens on purchasers related to compliance, adverse market conditions or other pressures on the industry. In the event that one

or more third party purchasers goes out of business, exits the market or otherwise ceases to do business with us at a time when we have loans that have been placed with such purchaser but not yet sold, we may incur additional costs to sell those loans to other purchasers or may have to retain such loans, which could negatively impact our results of operations and our capital position.

***Our real estate lending may expose us to environmental liabilities.***

In the course of our business, it is necessary to foreclose and take title to real estate, including commercial real estate which could subject us to environmental liabilities with respect to these properties. Hazardous substances or waste, contaminants, pollutants or sources thereof may be discovered on properties during our ownership or after a sale to a third party. We could be held liable to a governmental entity or to third parties for property damage, personal injury, investigation and clean-up costs incurred in connection with environmental contamination, or may be required to investigate or clean up hazardous or toxic substances or chemical releases at such properties. The costs associated with investigation or remediation activities could be substantial and could substantially exceed the value of the real property. In addition, if we were to be an owner or former owner of a contaminated site, we may be subject to common law claims by third parties based on damages and costs resulting from environmental contamination emanating from the property. We may be unable to recover costs from any third party. These occurrences may materially reduce the value of the affected property, and we may find it difficult or impossible to use or sell the property prior to or following any environmental remediation. If we become subject to significant environmental liabilities, our business, financial condition and results of operations could be materially and adversely affected.

**Market-Related Risks**

***Fluctuations in interest rates could adversely affect the value of our assets and reduce our net interest income and noninterest income, thereby adversely affecting our earnings and profitability.***

Interest rates may be affected by many factors beyond our control, including general and economic conditions and the monetary and fiscal policies of various governmental and regulatory authorities. For example, unexpected increases in interest rates can result in a higher percentage of rate lock customers closing loans, which would in turn increase our costs relative to income. On the other hand, decreases in interest rates may increase loan prepayment speeds, resulting in an overall decrease in the yield of our loan portfolio, and may have a negative impact on our net interest margins and results of operations. Changes in interest rates over the past year have impacted our business. Rising interest rates in 2018 reduced our mortgage revenues by reducing the market for refinancing, thereby negatively impacting demand for certain of our residential loan products and the revenue realized on the sale of loans and our noninterest income and, to a lesser extent, our net interest income. Subsequently, decreasing interest rates in 2019 negatively impacted our net interest margin while also reducing the overall yield of our loans held for investment portfolio because existing loans bearing higher interest rates were prepaid at a faster rate and replaced in the portfolio with lower interest rate loans.

Market volatility in interest rates also can be difficult to predict, as unexpected interest rate changes may result in a sudden impact while anticipated changes in interest rates generally impact the mortgage rate market prior to the actual rate change.

Our earnings are also dependent on the difference between the interest earned on loans and investments and the interest paid on deposits and borrowings. Changes in market interest rates impact the rates earned on loans and investment securities and the rates paid on deposits and borrowings and may negatively impact our ability to attract deposits, make loans, and achieve satisfactory interest rate spreads, which could adversely affect our financial condition or results of operations. In addition, changes to market interest rates may impact the level of loans, deposits and investments and the credit quality of existing loans.

Asymmetrical changes in interest rates, for example a greater increase in short term rates than in long term rates, could adversely impact our net interest income because our liabilities, including advances from the FHLB and interest payable on our deposits, tend to be more sensitive to short term rates while our assets tend to be more sensitive to long term rates. In addition, it may take longer for our assets to reprice to adjust to a new rate environment because fixed rate loans do not fluctuate with interest rate changes and adjustable rate loans often have a specified period of reset. As a result, a flattening or an inversion of the yield curve, such as occurred in the third quarter of 2019, is likely to have a negative impact on our net interest income.

Our securities portfolio also includes securities that are insured or guaranteed by U.S. government agencies or government-sponsored enterprises and other securities that are sensitive to interest rate fluctuations. The unrealized gains or losses in our available-for-sale portfolio are reported as a separate component of shareholders' equity until realized upon sale. Interest rate fluctuations may impact the value of these securities and as a result, shareholders' equity, and may cause material fluctuations from quarter to quarter. Failure to hold our securities until maturity or until market conditions are favorable for a sale could adversely affect our financial condition.

***The financial services industry is highly competitive.***

We face pricing competition for loans and deposits. We also face competition with respect to customer convenience, product lines, accessibility of service and service capabilities. Our most direct competition comes from other banks, credit unions, mortgage companies and savings institutions but more recently has also come from financial technology (or "fintech") companies that rely heavily on technology to provide financial services and often target a younger customer demographic. The significant competition in attracting and retaining deposits and making loans as well as in providing other financial services throughout our market area may impact future earnings and growth. Our success depends, in part, on the ability to adapt products and services to evolving industry standards and provide consistent customer service while keeping costs in line. There is increasing pressure to provide products and services at lower prices, which can reduce net interest income and non-interest income from fee-based products and services. New technology-driven products and services are often introduced and adopted, including innovative ways that customers can make payments, access products and manage accounts. We could be required to make substantial capital expenditures to modify or adapt existing products and services or develop new products and services. We may not be successful in introducing new products and services or those new products may not achieve market acceptance. We could lose business, be forced to price products and services on less advantageous terms to retain or attract clients, or be subject to cost increases if we do not effectively develop and implement new technology. In addition, advances in technology such as telephone, text and on-line banking, e-commerce and self-service automatic teller machines and other equipment, as well as changing customer preferences to access our products and services through digital channels, could decrease the value of our branch network and other assets. As a result of these competitive pressures, our business, financial condition or results of operations may be adversely affected.

***We have significantly decreased our home loan mortgage origination capacity with our new business model which may limit our ability to increase our volume significantly in the event of a significant improvement in the mortgage market.***

Due to increases in mortgage rates after many years of record low rates and a nationwide contraction in the number of homes available for sale, which is especially acute in our primary markets, we experienced a significant reduction in the overall number of mortgage products being purchased in the past two to three years as compared to prior periods. In response to those market conditions, in 2019 we sold or divested substantially all of the assets related to our stand alone home loan center-based mortgage origination business, including a significant portion of our mortgage servicing rights portfolio originated through those channels. We facilitated the transfer of a significant number of our related employees to the purchaser of those assets and terminated a number of other related positions. We also sold our interest in WMS Series LLC, an affiliated entity owned by us and Windermere Real Estate which originated single family loans that were generally immediately sold to HomeStreet pursuant to a correspondent purchase arrangement. Our branch based mortgage business which commenced operations on April 1, 2019 is significantly smaller than our legacy HLC based mortgage origination business. If the mortgage market were to significantly improve, we would not have the capacity to originate mortgages to the volume levels we have had in recent years, which would limit our ability to capitalize on that market.

***The price of our common stock is subject to volatility.***

The price of our common stock has fluctuated in the past and may face additional and potentially substantial fluctuations in the future. Among the factors that may impact our stock price are the following:

- Variances in our operating results;
- Disparity between our operating results and the operating results of our competitors;
- Changes in analyst's estimates of our earnings results and future performance, or variances between our actual performance and that forecast by analysts;



- News releases or other announcements of material events relating to the Company, including but not limited to mergers, acquisitions, expansion plans, restructuring activities or other strategic developments;
- Statements made by activist investors criticizing our strategy, our management team or our Board of Directors;
- Future securities offerings by us of debt or equity securities;
- Repurchase activity by us under our stock repurchase program;
- Addition or departure of key personnel;
- Market-wide events that may be seen by the market as impacting the Company;
- The presence or absence of short-selling of our common stock;
- General financial conditions of the country or the regions in which we operate;
- Trends in real estate in our primary markets;
- Trends relating to the economic markets generally; or
- Changes in laws and regulations affecting financial institutions.

The stock markets in general experience substantial price and trading fluctuations. Such changes may create volatility in the market as a whole or in the stock prices of securities related to particular industries or companies that are unrelated or disproportionate to changes in operating performance of the Company. Such volatility may have an adverse effect on the trading price of our common stock.

***A decline in certain economic conditions continue to pose significant challenges for us and could adversely affect our financial condition and results of operations.***

We generate revenue from the interest and fees we charge on the loans and other products and services we sell. A substantial amount of our revenue and earnings comes from the net interest income and noninterest income that we earn from our commercial lending and mortgage banking businesses. Our operations have been, and will continue to be, materially affected by the state of the U.S. economy, particularly unemployment levels and home prices. A prolonged period of slow growth or a pronounced decline in the U.S. economy, or any deterioration in general economic conditions and/or the financial markets resulting from these factors, or any other events or factors that may signal a return to a recessionary economic environment, could dampen consumer confidence, adversely impact the models we use to assess creditworthiness, and materially adversely affect our financial results and condition. A downturn in the economy and an increase in unemployment, which also would likely result in a decrease in consumer and business confidence and spending, may lead to a drop in demand for our credit products, including our mortgages, which will reduce our net interest income and noninterest income and our earnings. Significant and unexpected market developments may also make it more challenging for us to accurately forecast our expected financial results.

***A change in federal monetary policy could adversely impact our revenues from lending activities.***

The Federal Reserve Board is responsible for regulating the supply of money in the United States, and as a result, its monetary policies strongly influence our costs of funds for lending and investing, as well as the rate of return we are able to earn on those loans and investments, both of which impact our net interest income and net interest margin. Changes in interest rates may increase our cost of capital or decrease the income we receive from interest bearing assets. Asymmetrical changes in short term and long-term interest rates may result in a more rapid increase in the costs related to interest-bearing liabilities such as FHLB advances and interest-bearing deposit accounts without a correlated increase in the income from interest-bearing assets which are typically more sensitive to long-term interest rates. The Federal Reserve Board's interest rate policies can also materially affect the value of financial instruments we hold, including debt securities, MSRs and derivative instruments used to hedge against changes in the value of our MSRs. These monetary policies can also negatively impact our borrowers, which in turn may increase the risk that they will be unable to pay their loans according to the terms or be unable to pay their loans at all. We have no control over the Federal Reserve Board's policies and cannot predict when changes are expected or what the magnitude of such changes may be.



***A portion of our revenue is derived from residential mortgage lending which is a market sector that experiences significant volatility.***

Historically, a substantial portion of our consolidated net revenues (net interest income plus noninterest income) have been derived from originating and selling residential mortgages. While we have recently significantly decreased the size of our residential mortgage business through the sale of our HLC-based mortgage business and our interest in WMS Series LLC, we expect to continue to offer mortgage lending on a smaller scale, and therefore will remain subject to the volatility of that market sector. Residential mortgage lending in general has experienced substantial volatility in recent periods due to changes in interest rates, a significant lack of housing inventory caused by an increase in demand for housing at a time of decreased supply in our principal markets, and other market forces beyond our control. Lack of housing inventory limits our ability to originate purchase mortgages because it may take longer for loan applicants to find a home to buy after being pre-approved for a loan, which results in the Company incurring costs related to the pre-approval without being able to book the revenue from an actual loan. In addition, interest rate changes may result in lower rate locks and higher closed loan volume which can negatively impact our financial results because we book revenue at the time we enter into rate lock agreements after adjusting for the estimated percentage of loans that are not expected to actually close, which we refer to as “fallout.” When interest rates rise, the level of fallout as a percentage of rate locks declines, which results in higher costs relative to income for that period, which may adversely impact our earnings and results of operations. In addition, an increase in interest rates may materially and adversely affect our future loan origination volume, margins, and the value of the collateral securing our outstanding loans, may increase rates of borrower default, and may otherwise adversely affect our business.

***We may incur losses due to changes in prepayment rates.***

Our loan servicing rights carry interest rate risk because the total amount of servicing fees earned, as well as changes in fair-market value, fluctuate based on expected loan prepayments (affecting the expected average life of a portfolio of residential mortgage servicing rights). The rate of prepayment of loans generally may be impacted by changes in interest rates and general economic conditions while residential mortgage loans also may be influenced by pressures in the local real estate markets, among other things. During periods of declining interest rates, or increases in real estate values, many borrowers refinance their loans. Changes in prepayment rates are therefore difficult for us to predict. The loan servicing fee income (related to the loan servicing rights corresponding to a loan) decreases as loans are prepaid. Consequently, in the event of an increase in prepayment rates, we would expect the fair value of portfolios of loan servicing rights to decrease along with the amount of loan servicing income received. In the first quarter of 2019, we sold a significant portion of our mortgage servicing rights, however we continue to be exposed to such risks on a smaller scale with respect to the servicing rights we expect to retain going forward.

### **Regulatory-Related Risks**

***We are subject to extensive regulation that may restrict our activities, including declaring cash dividends or capital distributions or pursuing growth initiatives and acquisition activities, and imposes financial requirements or limitations on the conduct of our business.***

Our operations are subject to extensive regulation by federal, state and local governmental authorities, including the FDIC, the Washington Department of Financial Institutions and the Federal Reserve Board, and to various laws and judicial and administrative decisions imposing requirements and restrictions on part or all of our operations. The laws, rules and regulations to which we are subject evolve and change frequently, including changes that come from judicial or regulatory agency interpretations of laws and regulations outside of the legislative process that may be more difficult to anticipate. We are subject to various examinations by our regulators during the course of the year. Regulatory authorities who conduct these examinations have extensive discretion in their supervisory and enforcement activities, including the authority to restrict our operations, our growth and our acquisition activity, adversely reclassify our assets, determine the level of deposit insurance premiums assessed, require us to increase our allowance for loan losses, require customer restitution and impose fines or other penalties. For example, in November 2019, we entered into a Stipulation and Consent to the Issuance of an Order to Pay Civil Money Penalty (the “Stipulation and Consent”) with the FDIC based on alleged violations of the Real Estate Settlement Procedures Act raised by the FDIC during a 2016 compliance examination relating to certain marketing programs. These marketing programs, all of which we have terminated, were associated with the stand-alone home loan center mortgage origination business that we discontinued in 2019, and is accounted for in discontinued operations.

We paid a civil money penalty of \$1.35 million in connection with the Stipulation and Consent. We have fully resolved the matters that were at issue in the Stipulation and Consent without any additional sanctions. In addition, we have, in the past, been subject to specific regulatory orders that constrained our business and required us to take measures that investors may have deemed undesirable, and we may again in the future be subject to such orders if banking regulators were to determine that our operations require such restrictions or if they determine that remediation of operational or other legal or regulatory deficiencies is required.

In addition, recent political shifts in the United States may result in additional significant changes in legislation and regulations that impact us, although the possibility, nature and extent of any repeals or revisions to Dodd-Frank or any other regulations impacting financial institutions are not presently known and we cannot predict whether or not these changes will come to pass. These circumstances lead to additional uncertainty regarding our regulatory environment and the cost and requirements for compliance. We are unable to predict whether federal or state authorities, or other pertinent bodies, will enact legislations, laws, rules or regulations that will impact our business or operations. Further, an increasing amount of the regulatory authority that pertains to financial institutions is in the form of informal “guidance” such as handbooks, guidelines, examination manuals, field interpretations by regulators or similar provisions that will affect our business or require changes in our practices in the future even if they are not formally adopted as laws or regulations. Any such changes could adversely affect our cost of doing business and our profitability.

Changes in regulation of our industry have the potential to create higher costs of compliance, including short-term costs to meet new compliance standards, limit our ability to pursue business opportunities and increase our exposure to potential fines, penalties and litigation.

***Policies and regulations enacted by CFPB may negatively impact our residential mortgage loan business and increase our compliance risk.***

Our consumer business, including our mortgage, credit card, and other consumer lending and non-lending businesses, may be adversely affected by the policies enacted or regulations adopted by the Consumer Financial Protection Bureau (“CFPB”) which under the Dodd-Frank Act has broad rulemaking authority over consumer financial products and services. For example, in January 2014 federal regulations promulgated by the CFPB took effect which impact how we originate and service residential mortgage loans. Those regulations, among other things, require mortgage lenders to assess and document a borrower’s ability to repay their mortgage loan while providing borrowers the ability to challenge foreclosures and sue for damages based on allegations that the lender failed to meet the standard for determining the borrower’s ability to repay their loan. While the regulations include presumptions in favor of the lender based on certain loan underwriting criteria, they have not yet been challenged widely in courts and it is uncertain how these presumptions will be construed and applied by courts in the event of litigation. The ultimate impact of these regulations on the lender’s enforcement of its loan documents in the event of a loan default, and the cost and expense of doing so, is uncertain, but may be significant. In addition, the secondary market demand for loans that do not fall within the presumptively safest category of a “qualified mortgage” as defined by the CFPB is uncertain. Furthermore, the CFPB is considering allowing the “GSE Patch” provision of these regulations to expire. The “GSE Patch” grants a safe harbor to lenders, such as HomeStreet, to originate loans over a 43 percent debt to income (“DTI”) ratio and to use Fannie Mae and Freddie Mac standards for documentation. The impact of the expiration of this provision on HomeStreet and the U.S. mortgage market is uncertain. Finally, the 2014 regulations also require changes to certain loan servicing procedures and practices, which have resulted in increased foreclosure costs and longer foreclosure timelines in the event of loan default, and failure to comply with the new servicing rules may result in additional litigation and compliance risk.

The CFPB was also given authority over the Real Estate Settlement Procedures Act, or RESPA, under the Dodd-Frank Act and has, in some cases, interpreted RESPA requirements differently than other agencies, regulators and judicial opinions. As a result, certain practices that have been considered standard in the industry, including relationships that have been established between mortgage lenders and others in the mortgage industry such as developers, realtors and insurance providers, are now being subjected to additional scrutiny under RESPA. Our regulators, including the FDIC, review our practices for compliance with RESPA as interpreted by the CFPB. Changes in RESPA requirements and the interpretation of RESPA requirements by our regulators may result in adverse examination findings by our regulators, leading to enforcement actions, fines and penalties, such as those associated with the recent Stipulation and Consent discussed above.

In addition to RESPA compliance, the Bank is also subject to the CFPB's Final Integrated Disclosure Rule, commonly known as TRID, which became effective in October 2015. Among other things, TRID requires lenders to combine the initial Good Faith Estimate and Initial Truth in Lending disclosures into a single new Loan Estimate disclosure and the HUD-1 and Final TIL disclosures into a single new Closing Disclosure. The definition of an application and timing requirements has changed, and a new Closing Disclosure waiting period has been added. These changes, along with other changes required by TRID, require significant systems modifications, process and procedure changes. Failure to comply with these new requirements may result in payment of restitution to customers for disclosure defects, regulatory penalties for disclosure and other violations under RESPA and the Truth In Lending Act ("TILA"), and private right of action under TILA, and may impact our ability to sell or the price we receive for certain loans.

In addition, the CFPB has adopted and largely implemented additional rules under the Home Mortgage Disclosure Act ("HMDA") that are intended to improve information reported about the residential mortgage market and increase disclosure about consumer access to mortgage credit. The updates to the HMDA increase the types of dwelling-secured loans that are subject to the disclosure requirements of the rule and expand the categories of information that financial institutions such as the Bank are required to report with respect to such loans and such borrowers, including potentially sensitive customer information. Most of the rule's provisions went into effect on January 1, 2018. These changes increased our compliance costs due to the need for additional resources to meet the enhanced disclosure requirements as well as informational systems to allow the Bank to properly capture and report the additional mandated information. The volume of new data that is required to be reported under the updated rules will also cause the Bank to face an increased risk of errors in the processing of such information. More importantly, because of the sensitive nature of some of the additional customer information to be included in such reports, the Bank may face a higher potential for security breaches resulting in the disclosure of sensitive customer information in the event the HMDA reporting files were obtained by an unauthorized party.

***Interpretation of federal and state legislation, case law or regulatory action may negatively impact our business.***

Regulatory and judicial interpretation of existing and future federal and state legislation, case law, judicial orders and regulations could also require us to revise our operations and change certain business practices, impose additional costs, reduce our revenue and earnings and otherwise adversely impact our business, financial condition and results of operations. For instance, judges interpreting legislation and judicial decisions made during the recent financial crisis could allow modification of the terms of residential mortgages in bankruptcy proceedings which could hinder our ability to foreclose promptly on defaulted mortgage loans or expand assignee liability for certain violations in the mortgage loan origination process, any or all of which could adversely affect our business or result in our being held responsible for violations in the mortgage loan origination process. In addition, the exercise by regulators of revised and at times expanded powers under existing or future regulations could materially and negatively impact the profitability of our business, the value of assets we hold or the collateral available for our loans, require changes to business practices, limit our ability to pursue growth strategies or force us to discontinue certain business practices and expose us to additional costs, taxes, liabilities, penalties, enforcement actions and reputational risk.

Such judicial decisions or regulatory interpretations may affect the manner in which we do business and the products and services that we provide, restrict our ability to grow through acquisition, restrict our ability to compete in our current business or expand into any new business, and impose additional fees, assessments or taxes on us or increase our regulatory oversight.

***Federal, state and local consumer protection laws may restrict our ability to offer and/or increase our risk of liability with respect to certain products and services and could increase our cost of doing business.***

Federal, state and local laws have been adopted that are intended to eliminate certain practices considered "predatory" or "unfair and deceptive". These laws prohibit practices such as steering borrowers away from more affordable products, failing to disclose key features, limitations, or costs related to products and services, failing to provide advertised benefits, selling unnecessary insurance to borrowers, repeatedly refinancing loans, imposing excessive fees for overdrafts, and making loans without a reasonable expectation that the borrowers will be able to repay the loans irrespective of the value of the underlying property. It is our policy not to make predatory loans or engage in deceptive practices, but these laws and regulations create the potential for liability with respect to our lending, servicing, loan investment, deposit taking and other financial activities. As a company that originates single family mortgage loans, we also, inherently, have a significant amount of risk of noncompliance with fair

lending laws and regulations. These laws and regulations are complex and require vigilance to ensure that policies and practices do not create disparate impact on our customers or that our employees do not engage in overt discriminatory practices. Noncompliance can result in significant regulatory actions including, but not limited to, sanctions, fines or referrals to the Department of Justice and restrictions on our ability to execute our growth and expansion plans. If we offer products and services to customers in additional states, we may become subject to additional state and local laws designed to protect consumers. The additional laws and regulations may increase our cost of doing business and ultimately may prevent us from making certain loans, offering certain products, and may cause us to reduce the average percentage rate or the points and fees on loans and other products and services that we do provide.

***If our enterprise risk management framework is not effective at mitigating risk and loss to us, we could suffer unexpected losses and our results of operations could be materially adversely affected.***

Our enterprise risk management framework seeks to achieve an appropriate balance between risk and return, which is critical to optimizing stockholder value. We have established processes and procedures intended to identify, measure, monitor, report, analyze and control the types of risk to which we are subject. These risks include liquidity risk, credit risk, price risk, interest rate risk, operational risk, legal and compliance risk, strategic risk, and reputational risk, among others. We also maintain a compliance program to identify, measure, assess, and report on our adherence to applicable laws, policies and procedures. While we assess and improve these programs on an ongoing basis, there can be no assurance that our risk management or compliance programs, along with other related controls, will effectively mitigate all risk and limit losses in our business. However, as with any risk management framework, there are inherent limitations to our risk management strategies as there may exist, or develop in the future, risks that we have not appropriately anticipated or identified. If our risk management framework proves ineffective, we could suffer unexpected losses, our business financial condition and results of operations could be materially adversely affected, and we could be subject to regulatory criticism or restrictions.

***Significant legal or regulatory actions could subject us to substantial uninsured liabilities and reputational harm and have a material adverse effect on our business and results of operations.***

We are from time to time subject to claims and proceedings related to our operations. These claims and legal actions could include supervisory or enforcement actions by our regulators, or criminal proceedings by prosecutorial authorities, or claims by former and current employees, including class, collective and representative actions. Such actions are a substantial management distraction and could involve large monetary claims, including civil money penalties or fines imposed by government authorities and significant defense costs. For example, since 2016 we used considerable management time and resources and incurred additional legal and other costs associated with the matters resulting in the recent Stipulation and Consent Agreement with the FDIC in November 2019, pursuant to which we recently paid a penalty of \$1.35 million.

To mitigate the cost of some of these claims, we maintain insurance coverage in amounts and with deductibles that we believe are appropriate for our operations. However, our insurance coverage does not cover any civil money penalties or fines imposed by government authorities and may not cover all other claims that might be brought against us, including certain wage and hour class, collective and representative actions brought by employees or former employees. In addition, such insurance coverage may not continue to be available to us at a reasonable cost or at all. As a result, we may be exposed to substantial uninsured liabilities, which could adversely affect our business, prospects, results of operations and financial condition. Substantial legal liability or significant regulatory action against us could cause significant reputational harm to us and/or could have a material adverse impact on our business, financial condition, results of operations and prospects.

***We are subject to more stringent capital requirements under Basel III.***

As of January 1, 2015, we became subject to new rules relating to capital standards requirements, including requirements contemplated by Section 171 of the Dodd-Frank Act as well as certain standards initially adopted by the Basel Committee on Banking Supervision, which standards are commonly referred to as Basel III. Many of these rules apply to both the Company and the Bank, including increased common equity Tier 1 capital ratios, Tier 1 leverage ratios, Tier 1 risk-based ratios and total risk-based ratios. In addition, beginning in 2016, all institutions subject to Basel III, including the Company and the Bank are required to establish a “conservation buffer” that took full effect on January 1, 2019. This conservation buffer consists of common equity Tier 1 capital and is now

required to be 2.5% above existing minimum capital ratio requirements. This means that, in order to prevent certain regulatory restrictions, the common equity Tier 1 capital ratio requirement is now 7.0%, the Tier 1 risk-based ratio requirement is 8.5% and the total risk-based capital ratio requirement is 10.5%. Any institution that does not meet the conservation buffer will be subject to restrictions on certain activities including payment of dividends, stock repurchases and discretionary bonuses to executive officers.

Additional prompt corrective action rules implemented in 2015 also apply to the Bank, including higher and new ratio requirements for the Bank to be considered “well-capitalized.” The new rules also modify the manner for determining when certain capital elements are included in the ratio calculations, including but not limited to, requiring certain deductions related to MSRs and deferred tax assets. For more on these regulatory requirements and how they apply to the Company and the Bank, see “Business — Regulation and Supervision of HomeStreet Bank — Capital and Prompt Corrective Action Requirements — Capital Requirements” in our Annual Report on Form 10-K for the year ended December 31, 2018. The application of more stringent capital requirements could, among other things, result in lower returns on invested capital and result in regulatory actions if we were to be unable to comply with such requirements. In addition, if we need to raise additional equity capital in order to meet these more stringent requirements, our shareholders may be diluted.

***HomeStreet, Inc. primarily relies on dividends from the Bank, which may be limited by applicable laws and regulations.***

HomeStreet, Inc. is a separate legal entity from the Bank, and although we may receive some dividends from HomeStreet Capital Corporation, the primary source of our funds from which we service our debt, pay any dividends that we may declare to our shareholders and otherwise satisfy our obligations is dividends from the Bank. The availability of dividends from the Bank is limited by various statutes and regulations, capital rules regarding requirements to maintain a “well capitalized” ratio at the bank, as well as by our policy of retaining a significant portion of our earnings to support the Bank’s operations. See “Management’s Discussion and Analysis of Financial Condition and Results of Operations — Liquidity and Capital Resources Capital Management” as well as “Regulation and Supervision of HomeStreet Bank — Capital and Prompt Corrective Action Requirements” in this Annual Report on Form 10-K. If the Bank cannot pay dividends to us, we may be limited in our ability to service our debt, fund the Company’s operations and acquisition plans and pay dividends to the Company’s shareholders. In the first quarter of 2020, the Board of Directors adopted a policy to pay quarterly dividends to holders of our common stock, however, the declaration of such dividends in any quarter as well as the amount of any quarterly dividend remains subject to board approval, cash flow limitations, capital requirements, capital and strategic needs and other factors.

### **Risks Related to Information Systems and Security**

***A failure in or breach of our security systems or infrastructure, including breaches resulting from cyber-attacks, could disrupt our businesses, result in the disclosure or misuse of confidential or proprietary information, damage our reputation, increase our costs and cause losses.***

Information security risks for financial institutions have increased in recent years in part because of the proliferation of new technologies, the use of the Internet and telecommunications technologies to conduct financial transactions, and the increased sophistication and activities of organized crime, hackers, terrorists, activists, and other external parties. Those parties also may attempt to fraudulently induce employees, customers, or other users of our systems to disclose confidential information in order to gain access to our data or that of our customers. Our operations rely on the secure processing, transmission and storage of confidential information in our computer systems and networks, either managed directly by us or through our data processing vendors. In addition, to access our products and services, our customers may use personal computers, smartphones, tablet PCs, and other mobile devices that are beyond our control systems. Although we believe we have robust information security procedures and controls, we rely heavily on our third party vendors, technologies, systems, networks and our customers’ devices all of which may become the target of cyber-attacks, computer viruses, malicious code, unauthorized access, hackers or information security breaches that could result in the unauthorized release, gathering, monitoring, misuse, loss, theft or destruction of our confidential, proprietary and other information or that of our customers, or disrupt our operations or those of our customers or third parties.



To date we are not aware of any material losses that we have incurred relating to cyber-attacks or other information security breaches, but there can be no assurance that we will not suffer such attacks, breaches and losses in the future. Our risk and exposure to these matters remains heightened because of, among other things, the evolving nature of these threats, our plans to continue to evolve our Internet banking and mobile banking channel, our expanding operations and the outsourcing of a significant portion of our business operations. As a result, the continued development and enhancement of our information security controls, processes and practices designed to protect customer information, our systems, computers, software, data and networks from attack, damage or unauthorized access remain a priority for our management. As cyber threats continue to evolve, we may be required to expend significant additional resources to insure, modify or enhance our protective measures or to investigate and remediate important information security vulnerabilities or exposures; however, our measures may be insufficient to prevent all physical and electronic break-ins, denial of service and other cyber-attacks or security breaches.

Disruptions or failures in the physical infrastructure or operating systems that support our businesses and customers, or cyber-attacks or security breaches of the networks, systems or devices that our customers use to access our products and services could result in customer attrition, uninsured financial losses, the inability of our customers to transact business with us, employee productivity losses, technology replacement costs, incident response costs, violations of applicable privacy and other laws, regulatory fines, penalties or intervention, additional regulatory scrutiny, reputational damage, litigation, reimbursement or other compensation costs, and/or additional compliance costs, any of which could materially and adversely affect our results of operations or financial condition.

***We rely on third party vendors and other service providers for certain critical business activities, which creates additional operational and information security risks for us.***

Third parties with which we do business or that facilitate our business activities, including exchanges, clearing houses, financial intermediaries, agents or vendors that provide services or security solutions for our operations, could also be sources of operational and information security risk to us, including from interruptions or failures of their own systems, cybersecurity or ransomware attacks, capacity constraints or failures of their own internal controls. Specifically, we receive core systems processing, essential web hosting and other Internet systems and deposit and other processing services from third-party service providers. In late February 2018, one of our vendors provided notice to us that their independent auditors had determined their internal controls to be inadequate. While we do not believe this particular failure of internal controls would have an impact on us due to the strength of our own internal controls, future failures of internal controls of a vendor could have a significant impact on our operations if we do not have controls to cover those issues. Additionally, during the third quarter of 2019, we were advised by a third party providing services with access to certain of our systems that they had been subjected to a cybersecurity incident. We took measures to limit our vulnerability to such an attack and reviewed our own systems to determine that there was no apparent impact to our systems. However, the interruption caused by the breach in this third party's systems has limited their ability to provide us with contracted services which had the potential to increase our costs of doing business. To date, none of our third party vendors or service providers has notified us of any security breach in their systems that has breached the integrity of our confidential customer data. However, such third parties may also be targets of cyber-attacks, computer viruses, malicious code, unauthorized access, hackers, ransomware attacks or information security breaches that could compromise the confidential or proprietary information of HomeStreet and our customers.

In addition, if any third-party service providers experience difficulties or terminate their services and we are unable to replace them with other service providers, our operations could be interrupted and our operating expenses may materially increase. If an interruption were to continue for a significant period of time, our business financial condition and results of operations could be materially adversely affected.

Some of our primary third party service providers are subject to examination by banking regulators and may be subject to enhanced regulatory scrutiny due to regulatory findings during examinations of such service providers conducted by federal regulators. While we subject such vendors to higher scrutiny and monitor any corrective measures that the vendors are taking or would undertake, we cannot fully anticipate and mitigate all risks that could result from a breach or other operational failure of a vendor's system.

Others provide technology that we use in our own regulatory compliance, including our mortgage loan origination technology. If those providers fail to update their systems or services in a timely manner to reflect new or changing regulations, or if our personnel operate these systems in a non-compliant manner, our ability to meet regulatory requirements may be impacted and may expose us to heightened regulatory scrutiny and the potential for monetary penalties.

In addition, in order to safeguard our online financial transactions, we must provide secure transmission of confidential information over public networks. Our Internet banking system relies on third party encryption and authentication technologies necessary to provide secure transmission of confidential information. Advances in computer capabilities, new discoveries in the field of cryptology or other developments could result in a compromise or breach of the algorithms our third-party service providers use to protect customer data. If any such compromise of security were to occur, it could have a material adverse effect on our business, financial condition and results of operations.

***The failure to protect our customers' confidential information and privacy could adversely affect our business.***

We are subject to federal and state privacy regulations and confidentiality obligations that, among other things restrict the use and dissemination of, and access to, certain information that we produce, store or maintain in the course of our business. We also have contractual obligations to protect certain confidential information we obtain from our existing vendors and customers. These obligations generally include protecting such confidential information in the same manner and to the same extent as we protect our own confidential information, and in some instances may impose indemnity obligations on us relating to unlawful or unauthorized disclosure of any such information.

Recently passed legislation in the European Union (the General Data Protection Regulation, or GDPR) and in California (the California Privacy Act) may increase the burden and cost of compliance specifically in the realm of consumer data privacy. We are still evaluating the potential impact of these new regulations on our business and do not yet know exactly what the impact may be but anticipate that there will be at least some added cost and burden as a result of these measures. In addition, other federal, state or local governments may try to implement similar legislation, which could result in different privacy standards for different geographical regions, which could require significantly more resources for compliance.

If we do not properly comply with privacy regulations and contractual obligations that require us to protect confidential information, or if we experience a security breach or network compromise, we could experience adverse consequences, including regulatory sanctions, penalties or fines, increased compliance costs, remedial costs such as providing credit monitoring or other services to affected customers, litigation and damage to our reputation, which in turn could result in decreased revenues and loss of customers, all of which would have a material adverse effect on our business, financial condition and results of operations.

***The network and computer systems on which we depend could fail for reasons not related to security breaches.***

Our computer systems could be vulnerable to unforeseen problems other than a cyber-attack or other security breach. Because we conduct a part of our business over the Internet and outsource several critical functions to third parties, operations will depend on our ability, as well as the ability of third-party service providers, to protect computer systems and network infrastructure against damage from fire, power loss, telecommunications failure, physical break-ins or similar catastrophic events. Any damage or failure that causes interruptions in operations may compromise our ability to perform critical functions in a timely manner (or may give rise to perceptions of such compromise) and could have a material adverse effect on our business, financial condition and results of operations as well as our reputation and customer or vendor relationships.

***We continually encounter technological change, and we may have fewer resources than many of our competitors to invest in technological improvements.***

The financial services industry is undergoing rapid technological changes with frequent introductions of new technology-driven products and services. The effective use of technology increases efficiency and enables financial institutions to better serve customers and to reduce costs. Our future success will depend, in part, upon our ability to address the needs of our clients by using technology to provide products and services that will satisfy client demands for convenience, as well as to create additional efficiencies in our operations. Many national vendors provide turn-key services to community banks, such as Internet banking and remote deposit capture that allow smaller banks to compete with institutions that have substantially greater resources to invest in technological improvements. We may not be able, however, to effectively implement new technology-driven products and services or be successful in marketing these products and services to our customers.

## **Anti-Takeover Risk**

*Some provisions of our articles of incorporation and bylaws and certain provisions of Washington law may deter takeover attempts, which may limit the opportunity of our shareholders to sell their shares at a favorable price.*

Some provisions of our articles of incorporation and bylaws may have the effect of deterring or delaying attempts by our shareholders to remove or replace management, to commence proxy contests, or to effect changes in control. These provisions include:

- A phased-out classified Board of Directors so that until 2022, only a portion of our board of directors will be elected each year;
- Elimination of cumulative voting in the election of directors;
- Procedures for advance notification of shareholder nominations and proposals;
- The ability of our Board of Directors to amend our bylaws without shareholder approval; and
- The ability of our Board of Directors to issue shares of preferred stock without shareholder approval upon the terms and conditions and with the rights, privileges and preferences as the Board of Directors may determine.

In addition, as a Washington corporation, we are subject to Washington law which imposes restrictions on business combinations and similar transactions between a corporation and certain significant shareholders. These provisions, alone or together, could have the effect of deterring or delaying changes in incumbent management, proxy contests or changes in control. These restrictions may limit a shareholder's ability to benefit from a change-in-control transaction that might otherwise result in a premium unless such a transaction is favored by our Board of Directors.

## **ITEM 1B UNRESOLVED STAFF COMMENTS**

None.

## **ITEM 2 PROPERTIES**

We lease principal offices, which are located in downtown Seattle at 601 Union Street, Suite 2000, Seattle, WA 98101. This lease provides sufficient space to conduct the management of our business. The Company conducts its Commercial and Consumer Banking activities in locations in Washington, California, Oregon, Hawaii, Idaho, and Utah. As of December 31, 2019, we operated in four primary commercial lending centers, 62 retail deposit branches, and one insurance office. As of such date, we also operated three facilities for the purpose of administrative and other functions in addition to the principal offices: a call center and operations support facility located in Federal Way, Washington; a loan fulfillment center in Lynnwood, Washington, and an operations support center in Spokane, Washington. Of these properties, we own five of the retail deposit branches, the call center and operations support facility in Federal Way and we own 50% of a retail branch through a joint venture. All facilities are in a good state of repair and appropriately designed for use as banking or administrative office facilities.

## **ITEM 3 LEGAL PROCEEDINGS**

Because the nature of our business involves the collection of numerous accounts, the validity of liens and compliance with various state and federal lending laws, we are subject to various legal proceedings in the ordinary course of our business related to foreclosures, bankruptcies, condemnation and quiet title actions and alleged statutory and regulatory violations. We are also subject to legal proceedings in the ordinary course of business related to employment matters. We do not expect that these proceedings, taken as a whole, will have a material adverse effect on our business, financial position or our results of operations. There are currently no matters that, in the opinion of management, would have a material adverse effect on our consolidated financial position, results of operation or liquidity, or for which there would be a reasonable possibility of such a loss based on information known at this time.

## **ITEM 4 MINE SAFETY DISCLOSURES**

Not applicable.

## PART II

### ITEM 5 MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

#### Common Stock

Our common stock is traded on the Nasdaq Global Select Market under the symbol "HMST."

As of March 2, 2020, there were 2,326 shareholders of record of our common stock.

#### Dividend Policy

In January 2020 HomeStreet's Board of Directors approved a new dividend policy that contemplates the payment of quarterly cash dividends on our common stock when, if and in an amount declared by the Board after taking into consideration, among other things, earnings, regulatory capital levels, the overall payout ratio and expected asset growth. The first dividend declared under this policy was a cash dividend of \$0.15 per share for the first quarter of 2020, which was paid on February 21, 2020 to shareholders of record as of the close of business on February 5, 2020. The dividend rate to be paid will be reassessed each quarter by the Board of Directors in accordance with the dividend policy.

While the adoption of a quarterly dividend policy by the Board of Directors indicates the intention of the Board of Directors to consider a quarterly dividend going forward, our ability to pay dividends to shareholders is dependent on many factors, including those cited in the dividend policy as well as the Bank's ability to pay dividends to the Company. The Bank's ability to pay dividends will be limited to the extent necessary for the Bank to meet the regulatory requirements of a "well-capitalized" bank or other formal or informal guidance communicated by our principal regulators. See "Business Regulation and Supervision — Regulation and Supervision of HomeStreet Bank — *Capital and Prompt Corrective Action Requirements — Capital Requirements.*" Therefore, we cannot assure that we will be able to continue to pay a regular dividend in any future period.

#### Sales of Unregistered Securities

There were no sales of unregistered securities in the fourth quarter of 2019.

#### Purchases of Equity Securities by the Issuer

Shares repurchased, on a settlement-date basis, pursuant to the common equity repurchase program during the three months ended December 31, 2019, were as follows.

| <b>(in thousands, expect share and per share information)</b> | <b>Total shares of common stock purchased<sup>(1)</sup></b> | <b>Average price paid per share of common stock<sup>(2)</sup></b> | <b>Total number of shares purchased as part of publicly announced plan</b> | <b>Dollar value of remaining authorized for repurchase<sup>(3)</sup></b> |
|---|---|---|--|--|
| October . . . . .   | —   | \$ —  | —  | \$ 25,000  |
| November . . . . .  | 363,838   | 31.53   | 363,443  | 13,542   |
| December . . . . .  | 167,961   | 32.63   | 167,815  | 8,067  |
| Total . . . . .   | <u>531,799</u>  | \$ 31.87  | <u>531,258</u>   |  |

(1) Includes shares of the Company's common stock acquired by the Company in connection with satisfaction of tax withholding obligations on vested restricted stock units.

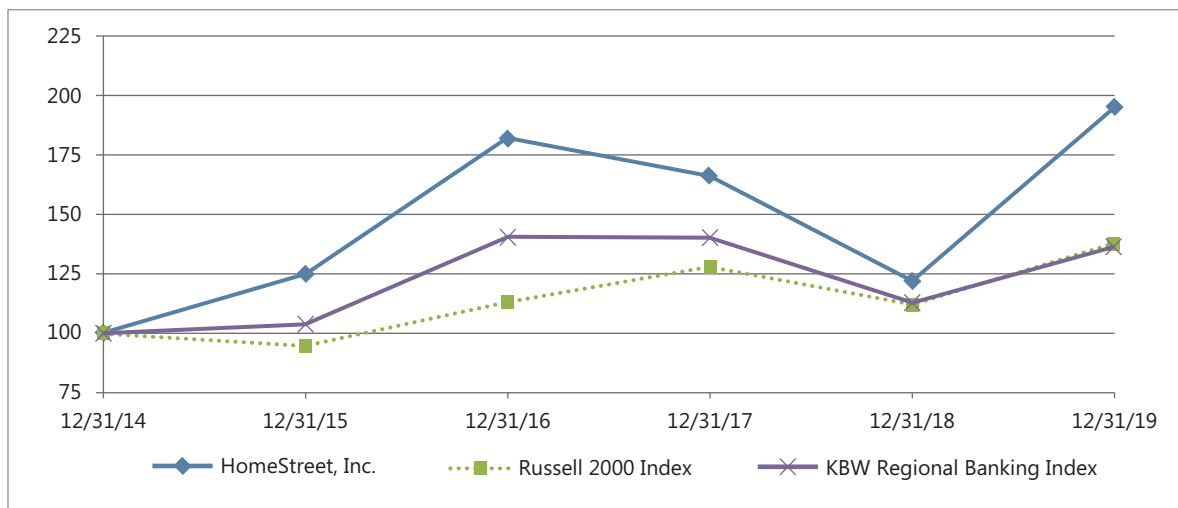
(2) Excludes commissions cost.

(3) Stock repurchases in the fourth quarter of 2019 were made pursuant to a Board authorized share repurchase program approved on September 26, 2019 pursuant to which the Company could purchase up to \$25.0 million of its issued and outstanding common stock, no par value, at prevailing market rates at the time of such purchase. In the first quarter of 2020, the Board authorized additional share repurchase programs pursuant to which the Company can repurchase up to an additional \$35 million of its common stock at prevailing market rates.

## Stock Performance Graph

*This performance graph shall not be deemed “soliciting material” or to be “filed” with the SEC for purposes of Section 18 of the Securities Exchange Act of 1934, as amended (Exchange Act), or otherwise subject to the liabilities under that Section, and shall not be deemed to be incorporated by reference into any filing of HomeStreet, Inc. under the Securities Act of 1933, as amended, or the Exchange Act.*

The following graph shows a comparison from December 31, 2014 through December 31, 2019 of the cumulative total return for our common stock, the Russell 2000 Index (RUT) and the KBW Regional Banking Index (KRX). The graph assumes that \$100 was invested at the market close on December 31, 2014 in the common stock of HomeStreet, Inc., the Russell 2000 Index, the KBW Regional Banking Index and data for HomeStreet, Inc., the Russell 2000 Index and the KBW Regional Banking Index assumes reinvestments of dividends. The stock price performance of the following graph is not necessarily indicative of future stock price performance.



## ITEM 6 SELECTED FINANCIAL DATA

The data set forth below should be read in conjunction with Item 7, “Management’s Discussion and Analysis of Consolidated Financial Condition and Results of Operations,” and the Consolidated Financial Statements and Notes thereto appearing at Item 8 of this Form 10-K.

The following table sets forth selected historical consolidated financial and other data for each of the periods ended as described below. The selected historical consolidated financial data as of December 31, 2019 and 2018 and for each of the years ended December 31, 2019, 2018 and 2017 have been derived from, and should be read together with, our audited consolidated financial statements and related notes included elsewhere in this Form 10-K. The selected historical consolidated financial data as of December 31, 2017, 2016 and 2015 and for each of the years ended December 31, 2017, 2016 and 2015 have been derived from our audited consolidated financial statements for those years, which are not included in this Form 10-K. Certain prior period amounts have been reclassified to conform to the current year’s presentation, including discontinued operations. You should read the summary selected historical consolidated financial and other data presented below in conjunction with “Management’s Discussion and Analysis of Financial Condition and Results of Operations” and our financial statements and the notes thereto, which are included elsewhere in this Form 10-K. We have prepared our unaudited information on the same basis as our audited consolidated financial statements and have included, in our opinion, all adjustments that we consider necessary for a fair presentation of the financial information set forth in that information.



| (dollars in thousands, except share data)   | At or for the Years Ended December 31, |            |              |            |            |
|---|--|------------|--------------|------------|------------|
|   | 2019                                   | 2018       | 2017         | 2016       | 2015       |
| Income statement data (for the period ended):                                       |  |            |              |            |            |
| Net interest income . . . . .   | \$ 189,390                             | \$ 189,963 | \$ 174,541   | \$ 154,015 | \$ 120,020 |
| (Reversal) provision for credit losses . . . . .                                    | (500)                                  | 3,000      | 750          | 4,100      | 6,100      |
| Noninterest income . . . . .  | 74,432                                 | 36,533     | 42,597       | 35,683     | 29,367     |
| Noninterest expense . . . . .   | 215,614                                | 195,241    | 190,614      | 178,029    | 156,293    |
| Income (loss) from continuing operations<br>before income taxes . . . . .           | 48,708                                 | 28,255     | 25,774       | 7,569      | (13,006)   |
| Income tax expense (benefit) from<br>continuing operations . . . . .                | 7,988                                  | 2,032      | (16,894)     | 3,503      | (8,882)    |
| Income (loss) from continuing operations . .  | 40,720                                 | 26,223     | 42,668       | 4,066      | (4,124)    |
| (Loss) income from discontinued<br>operations before income taxes . . . . .         | (28,285)                               | 17,610     | 40,415       | 83,208     | 69,913     |
| Income tax (benefit) expense from<br>discontinued operations . . . . .              | (5,077)                                | 3,806      | 14,137       | 29,123     | 24,470     |
| (Loss) income from discontinued<br>operations . . . . .                             | (23,208)                               | 13,804     | 26,278       | 54,085     | 45,443     |
| NET INCOME . . . . .  | \$ 17,512                              | \$ 40,027  | \$ 68,946    | \$ 58,151  | \$ 41,319  |
| Basic income (loss) per common share:   |  |            |              |            |            |
| Income (loss) from continuing operations . .  | 1.57                                   | 0.97       | 1.59         | \$ 0.17    | \$ (0.20)  |
| (Loss) income from discontinued<br>operations . . . . .                             | (0.91)                                 | 0.51       | 0.98         | \$ 2.20    | \$ 2.18    |
| Basic income (loss) per common share . . . . .                                      | \$ 0.66                                | \$ 1.48    | \$ 2.57      | \$ 2.36    | \$ 1.98    |
| Diluted income (loss) per common share:   |  |            |              |            |            |
| Income (loss) from continuing operations . .  | 1.55                                   | 0.97       | 1.57         | \$ 0.16    | \$ (0.20)  |
| (Loss) income from discontinued<br>operations . . . . .                             | (0.90)                                 | 0.51       | 0.97         | \$ 2.18    | \$ 2.18    |
| Diluted income (loss) per common share . . . . .                                    | \$ 0.65                                | \$ 1.47    | \$ 2.54      | \$ 2.34    | \$ 1.98    |
| Common shares outstanding . . . . .   | 23,890,855                             | 26,995,348 | 26,888,288   | 26,800,183 | 22,076,534 |
| Weighted average number of shares<br>outstanding:                                   |  |            |              |            |            |
| Basic . . . . .   | 25,573,488                             | 26,970,916 | 26,864,657   | 24,615,990 | 20,818,045 |
| Diluted . . . . .   | 25,770,783                             | 27,168,135 | 27,092,019   | 24,843,683 | 21,059,201 |
| Book value per share . . . . .  | \$ 28.45                               | \$ 27.39   | \$ 26.20     | \$ 23.48   | \$ 21.08   |
| Financial position (at year end):   |  |            |              |            |            |
| Cash and cash equivalents . . . . .   | \$ 57,880                              | \$ 57,982  | \$ 72,718    | \$ 53,932  | \$ 32,684  |
| Investment securities . . . . .   | 943,150                                | 923,253    | 904,304      | 1,043,851  | 572,164    |
| Loans held for sale . . . . .   | 208,177                                | 77,324     | 114,182      | 157,259    | 97,151     |
| Loans held for investment, net . . . . .  | 5,072,784                              | 5,075,371  | 4,506,466    | 3,819,027  | 3,192,720  |
| Mortgage servicing rights . . . . .   | 97,603                                 | 103,374    | 86,689       | 72,739     | 51,353     |
| Other real estate owned . . . . .   | 1,393                                  | 455        | 664          | 5,243      | 7,531      |
| Total assets . . . . .  | 6,812,435                              | 7,042,221  | 6,742,041    | 6,243,700  | 4,894,495  |
| Deposits . . . . .  | 5,339,959                              | 4,888,558  | 4,535,919    | 4,184,903  | 3,073,717  |
| Federal Home Loan Bank advances . . . . .   | 346,590                                | 932,590    | 979,201      | 868,379    | 1,018,159  |
| Federal funds purchased and securities<br>sold under agreements to repurchase . . . | 125,000                                | 19,000     | —            | —          | —          |
| Total shareholders' equity . . . . .  | \$ 679,723                             | \$ 739,520 | \$ 704,380   | \$ 629,284 | \$ 465,275 |
| Financial position (averages):  |  |            |              |            |            |
| Investment securities . . . . .   | \$ 850,695                             | \$ 916,840 | \$ 1,023,702 | \$ 834,671 | \$ 523,756 |
| Loans held for investment . . . . .   | 5,283,225                              | 4,866,210  | 4,178,326    | 3,668,263  | 2,834,511  |
| Total interest-earning assets . . . . .   | 6,483,937                              | 6,348,072  | 5,998,521    | 5,307,118  | 4,150,089  |
| Total interest-bearing deposits . . . . .   | 4,509,632                              | 4,051,903  | 3,588,515    | 3,145,137  | 2,499,538  |
| Federal Home Loan Bank advances . . . . .   | 407,071                                | 867,141    | 1,037,650    | 942,593    | 795,368    |
| Total interest-bearing liabilities . . . . .  | 5,096,550                              | 5,059,411  | 4,755,221    | 4,189,582  | 3,368,160  |
| Shareholders' equity . . . . .  | \$ 721,360                             | \$ 741,035 | \$ 675,877   | \$ 566,148 | \$ 442,105 |

| (dollars in thousands, except share data)                       | At or for the Years Ended December 31, |                      |                      |                      |                      |
|---|--|----------------------|----------------------|----------------------|----------------------|
|   | 2019                                   | 2018                 | 2017                 | 2016                 | 2015                 |
| Financial performance: <sup>(8)</sup>                           |  |                      |                      |                      |                      |
| Return on average shareholders' equity <sup>(1)</sup> . . . . . | 2.43%                                  | 5.40%                | 10.20%               | 10.27%               | 9.35%                |
| Return on average total assets . . . . .                        | 0.25%                                  | 0.57%                | 1.05%                | 1.01%                | 0.91%                |
| Net interest margin <sup>(2)</sup> . . . . .                    | 3.01%                                  | 3.23%                | 3.31%                | 3.45%                | 3.63%                |
| Efficiency ratio <sup>(3)</sup> . . . . .                       | 94.02%                                 | 88.88%               | 86.79%               | 82.40%               | 85.33%               |
| Asset quality:  |  |                      |                      |                      |                      |
| Allowance for credit losses. . . . . \$                         | 42,837                                 | \$ 42,913            | \$ 39,116            | \$ 35,264            | \$ 30,659            |
| Allowance for loan losses/total loans <sup>(4)</sup> . . . . .  | 0.82%                                  | 0.81%                | 0.83%                | 0.88%                | 0.91%                |
| Allowance for loan losses/nonaccrual loans . . . . .            | 324.80%                                | 356.92%              | 251.63%              | 165.52%              | 170.54%              |
| Total nonaccrual loans <sup>(5)(6)</sup> . . . . . \$           | 12,861                                 | \$ 11,619            | \$ 15,041            | \$ 20,542            | \$ 17,168            |
| Nonaccrual loans/total loans . . . . .                          | 0.25%                                  | 0.23%                | 0.33%                | 0.53%                | 0.53%                |
| Other real estate owned . . . . . \$                            | 1,393                                  | \$ 455               | \$ 664               | \$ 5,243             | \$ 7,531             |
| Total nonperforming assets. . . . . \$                          | 14,254                                 | \$ 12,074            | \$ 15,705            | \$ 25,785            | \$ 24,699            |
| Nonperforming assets/total assets . . . . .                     | 0.21%                                  | 0.17%                | 0.23%                | 0.41%                | 0.50%                |
| Net recoveries (charge-offs) . . . . . \$                       | 424                                    | \$ 797               | \$ 3,102             | \$ 505               | \$ 2,035             |
| Regulatory capital ratios for the Bank:                         |  |                      |                      |                      |                      |
| Tier 1 leverage capital (to average assets) . . . . .           | 10.56%                                 | 10.15%               | 9.67%                | 10.26%               | 9.46%                |
| Common equity Tier 1 capital (to risk-weighted assets). . . . . | 13.50%                                 | 13.82%               | 13.22%               | 13.92%               | 13.04%               |
| Tier 1 risk-based capital (to risk-weighted assets). . . . .    | 13.50%                                 | 13.82%               | 13.22%               | 13.92%               | 13.04%               |
| Total risk-based capital (to risk-weighted assets). . . . .     | 14.37%                                 | 14.72%               | 14.02%               | 14.69%               | 13.92%               |
| Regulatory capital ratios for the Company:                      |  |                      |                      |                      |                      |
| Tier 1 leverage capital (to average assets) . . . . .           | 10.16%                                 | 9.51%                | 9.12%                | 9.78%                | 9.95%                |
| Common equity Tier 1 capital (to risk-weighted assets). . . . . | 11.43%                                 | 11.26%               | 9.86%                | 10.54%               | 10.52%               |
| Tier 1 risk-based capital (to risk-weighted assets). . . . .    | 12.52%                                 | 12.37%               | 10.92%               | 11.66%               | 11.84%               |
| Total risk-based capital (to risk-weighted assets). . . . .     | 13.40%                                 | 13.27%               | 11.61%               | 12.34%               | 12.70%               |
| SUPPLEMENTAL DATA:  |  |                      |                      |                      |                      |
| Loans serviced for others                                       |  |                      |                      |                      |                      |
| Commercial . . . . . \$   | 1,618,876                              | \$ 1,542,477         | \$ 1,391,196         | \$ 1,177,363         | \$ 1,003,880         |
| Single family <sup>(7)(8)</sup> . . . . .                       | 7,023,441                              | 20,151,735           | 22,631,147           | 19,488,456           | 15,347,811           |
| Total loans serviced for others . . . . .                       | <u>\$ 8,642,317</u>                    | <u>\$ 21,694,212</u> | <u>\$ 24,022,343</u> | <u>\$ 20,665,819</u> | <u>\$ 16,351,691</u> |

- (1) Net earnings available to common shareholders divided by average shareholders' equity.
- (2) Net interest income divided by total average interest-earning assets on a tax equivalent basis.
- (3) Noninterest expense divided by total revenue (net interest income and noninterest income).
- (4) Includes loans acquired with bank acquisitions. Excluding acquired loans, allowance for loan losses/total loans was 0.86%, 0.85%, 0.90%, 1.00% and 1.10% at December 31, 2019, 2018, 2017, 2016 and 2015, respectively.
- (5) Generally, loans are placed on nonaccrual status when they are 90 or more days past due, unless payment is insured by the FHA or guaranteed by the VA.
- (6) Includes \$1.3 million and \$1.9 million of nonperforming loans at December 31, 2019 and 2018, respectively, which are guaranteed by the Small Business Administration ("SBA").
- (7) On March 29, 2019, the Company closed and settled two sales of the rights to service \$14.26 billion in total unpaid principal balance of single family mortgage loans representing 71% of single family mortgage loans serviced for others portfolio as of December 31, 2018.
- (8) Includes both continuing and discontinued operations.

## ITEM 7 MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

### NOTICE REGARDING FORWARD LOOKING STATEMENTS

The following discussion contains certain forward-looking statements, which are statements of expectations and not statements of historical fact. Many forward-looking statements can be identified as using words such as “anticipate,” “believe,” “could,” “estimate,” “expect,” “intend,” “may,” “plan,” “potential,” “should,” “will” and “would” and similar expressions (or the negative of these terms). Such statements involve inherent risks and uncertainties, many of which are difficult to predict and are generally beyond the control of the Company and are subject to risks and uncertainties, including, but not limited to, those discussed below and elsewhere in this Form 10-K, particularly in Item 1A “Risk Factors,” that could cause actual results to differ significantly from those projected. Although we believe that expectations reflected in the forward-looking statements are reasonable, we cannot guarantee future results, levels of activity, performance or achievements. We undertake no obligation to, and expressly disclaim any such obligation to update, or clarify any of the forward-looking statements after the date of this Form 10-K to reflect changed assumptions, the occurrence of anticipated or unanticipated events, new information or changes to future results over time of otherwise, except as required by law. Readers are cautioned not to place undue reliance on these forward-looking statements, which apply only as of the date of this Form 10-K.

*Management's Discussion and Analysis of Financial Condition and Results of Operations should be read in conjunction with “Selected Consolidated Financial Data” and the Consolidated Financial Statements and Notes included in Items 6 and 8 of this Form 10-K.*

### Executive Summary

HomeStreet is a diversified financial services company founded in 1921, headquartered in Seattle, Washington, serving customers primarily on the West Coast of the United States, including Hawaii. We are principally engaged in commercial banking, consumer banking, and real estate lending, including commercial real estate and single family mortgage banking operations.

HomeStreet, Inc. is a bank holding company that has elected to be treated as a financial holding company. Our primary subsidiaries are HomeStreet Bank and HomeStreet Capital Corporation. We also sell insurance products and services for consumer clients under the name HomeStreet Insurance.

HomeStreet Bank is a Washington state-chartered commercial bank providing commercial and consumer loans, mortgage loans, deposit products, private banking and cash management services and other banking services. Our loan products include commercial business loans and agriculture loans, consumer loans, single family residential mortgages, loans secured by commercial real estate and construction loans for residential and commercial real estate projects.

HomeStreet Capital Corporation, a Washington corporation, sells and services multifamily mortgage loans originated by HomeStreet Bank under the Fannie Mae Delegated Underwriting and Servicing Program (“DUS®”)<sup>1</sup>.

We generate revenue by earning net interest income and noninterest income. Net interest income is primarily the difference between interest income earned on loans and investment securities less the interest we pay on deposits and other borrowings. We also earn noninterest income from the origination, sale and servicing of loans and from fees earned on deposit services and insurance sales.

Since our IPO, we have been strategically focused on becoming a leading West Coast regional commercial bank, growing commercial banking to diversify our earnings and actively reducing our exposure to the single family lending mortgage business and its more cyclical and volatile earnings results. This includes the exit of our stand-alone home loan center (“HLC”)-based mortgage business and sale of related mortgage servicing rights in early 2019 (“HLC Business Sale”). In late 2019, we finalized the sale of our ownership interest in WMS Series LLC, our former joint venture. Following these transactions, we focused primarily on commercial and consumer banking including our smaller single family mortgage lending business conducted through our bank locations, online and affinity networks.

---

<sup>1</sup> DUS® is a registered trademark of Fannie Mae

In connection with the HLC Business Sale, we eliminated segment reporting in the first quarter of 2019 and classified all remaining activity for these HLCs, along with certain other mortgage banking related assets and liabilities that are expected to be sold or abandoned within approximately one year, as discontinued operations in the accompanying Consolidated Statements of Financial Condition and Consolidated Statements of Operations. Prior period financial statements have been reclassified to conform with this financial statement presentation. Certain components of the Company's former Mortgage Banking segment, including mortgage servicing rights ("MSRs") on certain mortgage loans that were not sold as part of this divestiture, along with our remaining single family mortgage origination and servicing business, were reported in continuing operations beginning on April 1, 2019 based on the Company's intent ("Retained MB Business").

We continue to take steps to improve productivity and reduce total corporate expenses, reflecting the substantial reduction in the size and complexity of our operations and our lower growth plan going forward. During 2019, we worked with an outside consulting firm that specializes in bank efficiency on an enterprise-wide profitability improvement project. The goal of this project is to analyze and improve all of our corporate expenses and business line processes, including contract terms, occupancy and technology costs, organization and staffing improvements, and other cost savings and efficiency proposals. The project includes the following initiatives:

- Simplify the organizational structure by reducing management levels and management redundancy
- Consolidate similar functions currently residing in multiple organizations
- Renegotiate, where possible, our technology contracts
- Identify and eliminate redundant or unnecessary systems and services
- Rationalize staffing levels to recognize the significant changes in work volumes and Company growth rates
- Eliminate excess occupancy costs consistent with reduced personnel

We began executing on the efficiency initiatives in the third quarter of 2019 and expect these reductions and enhancements will continue through 2020 and beyond.

In 2019, we made progress towards achieving these goals of improving efficiency and profitability with organizational and operational changes which resulted in substantial reductions in operating costs and headcount, with FTE falling to 1,027 at February 1, 2020. These reductions are meaningful progress toward achieving our efficiency and profitability improvement goals. However, our profitability goals have been challenged by reduced revenue from a lower interest rate environment and persistently flat yield curve, which have had an adverse impact on the balances of loans held for investment and our net interest margin. In addition, certain operational, technology and real estate cost reductions will occur later than originally anticipated impacting both our efficiency and profitability goals. We expect these reductions and enhancements will continue through 2020 and beyond.

In addition to proactively reducing our exposure to single family mortgage lending by exiting the HLC-based mortgage banking business, in 2019 we continued to grow our overall banking business. In 2019, we opened two de novo retail branches in San Jose and Santa Clara, CA and completed the acquisition of a retail bank branch and associated commercial lending team in San Diego County, CA. Our retail branch network continued to perform well, with total deposits from continuing operations increasing 9.2% over December 31, 2018.

As of December 31, 2019, we had 36 retail branches in Washington, 19 retail branches in California, four retail branches in Hawaii and three retail branches in Oregon. We also had four primary stand-alone commercial lending centers and one stand-alone insurance office. While we continue to focus on growing and strengthening our banking business, we have temporarily suspended future de novo deposit branch openings while we focus on our strategy of improving efficiency and profitability.

As part of our capital management strategy, in 2019, we repurchased a total of 3,187,259 shares of our common stock at an average price of \$30.75 per share. From January 2, 2020 through March 2, 2020, we repurchased 244,918 shares of our common stock at an average price of \$32.87 per share.

## Management’s Overview of 2019 Financial Performance

Results for 2019, 2018 and 2017 reflect the impact of the adoption in the first quarter of 2019 of a plan of exit or disposal with respect to the stand-alone home loan center-based mortgage origination and related servicing businesses, which comprised the bulk of our legacy mortgage banking business, as discontinued operations. Discontinued operations reported in the first quarter of 2019 included our entire former mortgage banking business as did all prior periods presented. Effective April 1, 2019, the newly organized bank location-based mortgage banking business commenced operations and the associated direct revenues and direct expenses were reported as part of the Company’s continuing operations beginning in the second quarter of 2019 (“Retained MB Business”).

### Recent Developments

The Board of Directors approved an addition to our share repurchase program for up to \$25 million of our common stock in January 2020, and our regulators have confirmed no objections to that repurchase. In February, the Board increased the authorization by an additional \$10 million conditional on the non-objection of our regulators. Assuming no objections from our regulators for the additional repurchase authorization, we expect to commence repurchases in the first or second quarter of 2020. This represents, in aggregate approximately 5.2% of the Company’s currently outstanding common stock based on the closing price of the stock as of March 2, 2020. This authorization is in addition to the 3.4 million shares of common stock that the Company repurchased in 2019 and early 2020.

On January 23, 2020, the Board declared a quarterly dividend for the first quarter of 2020 at \$0.15 per share, which was paid on February 21, 2020 to shareholders of record as of the close of the market on February 5, 2020.

### Consolidated Financial Performance

| (in thousands, except per share data and ratios)                         | At or for the Years Ended December 31, |            |            |
|--|--|------------|------------|
|  | 2019                                   | 2018       | 2017       |
| Selected statement of operations data                                    |  |            |            |
| Total net revenue <sup>(1)</sup> . . . . .                               | \$ 263,822                             | \$ 226,496 | \$ 217,138 |
| Total noninterest expense . . . . .                                      | 215,614                                | 195,241    | 190,614    |
| Provision for credit losses . . . . .                                    | (500)                                  | 3,000      | 750        |
| Income tax expense (benefit) from continuing operations . . . . .        | 7,988                                  | 2,032      | (16,894)   |
| Income from continuing operations . . . . .                              | 40,720                                 | 26,223     | 42,668     |
| (Loss) income from discontinued operations before income taxes . . . . . | (28,285)                               | 17,610     | 40,415     |
| Income tax (benefit) expense from discontinued operations . . . . .      | (5,077)                                | 3,806      | 14,137     |
| (Loss) income from discontinued operations . . . . .                     | (23,208)                               | 13,804     | 26,278     |
| Net income . . . . .   | \$ 17,512                              | \$ 40,027  | \$ 68,946  |
| Financial performance  |  |            |            |
| Diluted income (loss) per common share:                                  |  |            |            |
| Income from continuing operations . . . . .                              | \$ 1.55                                | \$ 0.97    | \$ 1.57    |
| (Loss) income from discontinued operations . . . . .                     | \$ (0.90)                              | \$ 0.51    | \$ 0.97    |
| Diluted income per common share . . . . .                                | \$ 0.65                                | \$ 1.47    | \$ 2.54    |
| Return on average common shareholders’ equity . . . . .                  | 2.43%                                  | 5.40%      | 10.20%     |
| Return on average assets . . . . .                                       | 0.25%                                  | 0.57%      | 1.05%      |
| Net interest margin . . . . .  | 3.01%                                  | 3.23%      | 3.31%      |

(1) Total net revenue is net interest income and noninterest income.

### Regulatory Matters

On January 1, 2015, the Company and the Bank became subject to new capital standards commonly referred to as “Basel III” which raised our minimum capital requirements. The Company and the Bank have remained above current “well-capitalized” regulatory minimums since the Company’s initial public offering in 2012, even with the implementation of the more stringent Basel III capital requirements.



Under the Basel III standards, the Bank's Tier 1 leverage and total risk-based capital ratios at December 31, 2019 were 10.56% and 14.37% and at December 31, 2018 were 10.15% and 14.72%, respectively. The Company's Tier 1 leverage and total risk-based capital ratios were 10.16% and 13.40% at December 31, 2019, and 9.51% and 13.27% at December 31, 2018, respectively.

For more on the Basel III requirements as they apply to us, please see "*Capital Management*" within the Liquidity and Capital Resources section and "Business — Regulation and Supervision" of this Form 10-K.

### **Critical Accounting Policies and Estimates**

The preparation of financial statements in accordance with the accounting principles generally accepted in the United States ("U.S. GAAP") requires management to make a number of judgments, estimates and assumptions that affect the reported amount of assets, liabilities, income and expense in the financial statements. Various elements of our accounting policies, by their nature, involve the application of highly sensitive and judgmental estimates and assumptions. Some of these policies and estimates relate to matters that are highly complex and contain inherent uncertainties. It is possible that, in some instances, different estimates and assumptions could reasonably have been made and used by management, instead of those we applied, which might have produced different results that could have had a material effect on the financial statements.

We have identified the following accounting policies and estimates that, due to the inherent judgments and assumptions and the potential sensitivity of the financial statements to those judgments and assumptions, are critical to an understanding of our financial statements. We believe that the judgments, estimates and assumptions used in the preparation of the Company's financial statements are appropriate. For a further description of our accounting policies, see Note 1, *Summary of Significant Accounting Policies* in the financial statements included in this Form 10-K.

#### ***Allowance for Loan Losses***

The allowance for loan losses represents management's estimate of incurred credit losses inherent within our loans held for investment portfolio. Determining the appropriateness of the allowance is complex and requires judgment by management about the effect of matters that are inherently uncertain. Subsequent evaluations of the loan portfolio, considering the factors then prevailing, may result in significant changes in the allowance for loan losses in those future periods.

We employ a disciplined process and methodology to establish our allowance for loan losses that has two basic components: first, an asset-specific component involving the identification of impaired loans and the measurement of impairment for each individual loan identified; and second, a formula-based component for estimating probable principal losses for all other loans.

Based upon this methodology, management establishes an asset-specific allowance for impaired loans based on the amount of impairment calculated on those loans and charging off amounts determined to be uncollectible. A loan is considered impaired when it is probable that all contractual principal and interest payments due will not be collected substantially in accordance with the terms of the loan agreement. Factors we consider in determining whether a loan is impaired include payment status, collateral value, borrower financial condition, guarantor support and the probability of collecting scheduled principal and interest payments when due.

When a loan is identified as impaired, we measure impairment as the difference between the recorded investment in the loan and the present value of expected future cash flows discounted at the loan's effective interest rate or based on the loan's observable market price. For impaired collateral-dependent loans, impairment is measured as the difference between the recorded investment in the loan and the fair value of the underlying collateral. The fair value of the collateral is adjusted for the estimated cost to sell if repayment or satisfaction of a loan is dependent on the sale (rather than only on the operation) of the collateral. In accordance with our appraisal policy, the fair value of impaired collateral-dependent loans is based upon independent third-party appraisals or on collateral valuations prepared by in-house appraisers, which generally are updated every twelve months. We require an independent third-party appraisal at least annually for substandard loans and other real estate owned ("OREO"). If our chief appraiser determines that market conditions, changes to the property, changes in intended use of the property or

other factors indicate that an appraisal is no longer reliable, a more frequent appraisal or internal collateral valuation may be required to assess whether a change in collateral value requires an additional adjustment to carrying value. A collateral valuation is a restricted appraisal report prepared by our internal appraisal staff in accordance with our appraisal policy. When we receive an updated appraisal or collateral valuation, management reassesses the need for adjustments to loan impairment measurements and, where appropriate, records an adjustment. If the calculated impairment is determined to be permanent, fixed or nonrecoverable, the impairment will be charged off. See “*Credit Risk Management — Asset Quality and Nonperforming Assets*” discussions within Management’s Discussion and Analysis of this Form 10-K.

In estimating the formula-based component of the allowance for loan losses, loans are segregated into loan pools. Loans are designated into loan pools based on product types and similar risk characteristics or areas of risk concentration. Credit loss assumptions are estimated using a model that categorizes loan pools based on loan type and asset risk rating or delinquency status. This model calculates an expected loss percentage for each loan category by considering the probability of default, based on the migration of loans from performing to loss by Asset Quality Rating (“AQR”) or delinquency status using two-year analysis periods for commercial portfolios and one-year analysis periods for consumer portfolios, and the potential severity of loss, based on the aggregate net lifetime losses incurred per loan class.

The formula-based component of the allowance for loan losses also considers qualitative factors (“Q-Factors”) for each loan pool, including changes in:

- lending policies and procedures;
- international, national, regional and local economic business conditions and developments that affect the collectability of the portfolio, including the condition of various markets;
- the nature of the loan portfolio, including the terms of the loans;
- the experience, ability and depth of the lending management and other relevant staff;
- the volume and severity of past due and adversely classified or graded loans and the volume of nonaccrual loans;
- the quality of our loan review system;
- the value of underlying collateral for collateral-dependent loans;
- the existence and effect of any concentrations of credit and changes in the level of such concentrations; and
- the effect of external factors such as competition and legal and regulatory requirements on the level of estimated credit losses in the existing portfolio.

Q-Factors are expressed in basis points and are adjusted downward or upward based on statistical analysis of economic drivers and management’s judgment as to the potential loss impact of each Q-Factor to a particular loan pool at the date of the analysis.

The provision for loan losses recorded through earnings is based on management’s assessment of the amount necessary to maintain the allowance for loan losses at a level appropriate to cover probable incurred losses inherent within the loans held for investment portfolio. The amount of provision and the corresponding level of allowance for loan losses are based on our evaluation of the collectability of the loan portfolio based on historical loss experience and other significant qualitative factors.

The allowance for loan losses, as reported in our consolidated statements of financial condition, is adjusted by a provision for loan losses, which is recognized in earnings, and reduced by the charge-off of loan amounts, net of recoveries. For further information on the allowance for loan losses, see Note 6, *Loans and Credit Quality* in the notes to the financial statements of this Form 10-K.

## ***Allowance for Credit Losses for Loans Held for Investment***

On January 1, 2020, the Company adopted ASU 2016-13 *Financial Instruments — Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments*, which replaces the incurred loss methodology with an expected loss methodology that is referred to as the current expected credit losses (“CECL”). The measurement of the expected credit losses under the CECL methodology, like the allowance, is complex and requires judgment by management about the effect of matters that are inherently uncertain. Many of the assumptions and judgments used in the CECL methodology are similar to those used in the Allowance for Loan Losses methodology. However, the CECL methodology incorporates the following differences:

### Amortized Cost Basis

The measurement of the expected credit losses under the CECL methodology is applicable to loans held for investment measured at amortized cost.

Amortized cost is the principal amount outstanding, net of cumulative charge-offs, interest applied to principal (for loans accounted for using the cost recovery method), unamortized net deferred loan origination fees and costs and unamortized premiums or discounts on purchased loans. Accrued interest receivable is reported separately in Other Assets in the Consolidated Statements of Financial Condition as the Bank has elected to exclude accrued interest receivable from the allowance for credit losses.

### Collectively Evaluated Component

In estimating the expected credit losses for loans collectively evaluated, loans are segregated into loan pools. Loans are designated into loan pools based on similar risk characteristics, such as product types, or areas of risk concentration. Credit loss assumptions are estimated using a model that further categorizes loan pools based on risk rating or delinquency status. This model calculates an expected loss percentage for each loan category by considering the probability of default, based on the migration of loans from performing to loss by risk rating or delinquency status using life of loan default rates.

### Life of Loan Loss Rates

Historical life of loan loss rates provide the basis for the estimation of expected credit losses. The model uses statistical analysis to determine the life of loan default rates for the quantitative component of the allowance for credit losses (“ACL”) and analyzes losses and recoveries over time without constraint.

### Qualitative Factors

The allowance for credit losses for loans held for investment that are collectively evaluated also considers qualitative factors (“Q-Factors”) for each loan pool. The Q-Factors adjust the expected historic loss rates for current and forecasted conditions that are not incorporated into the historical loss information. The Bank has established a methodology for adjusting historical expected loss rates based on these more recent or forecasted changes. The Q-Factor methodology is based on a blend of quantitative analysis and management judgment, including changes in:

- Portfolio Credit Quality
- Remaining Payments
- Volume & Nature
- Collateral Values
- Economic
- Credit Culture
- Business Environment
- Management Overlay

Management has assigned weightings for each Q-Factor as well as individual metrics within each Q-Factor with respect to the relative importance of that factor or metric specific to each portfolio type. The Q-Factors above are evaluated using a seven-point scale ranging from significant improvement to significant deterioration.

#### Current Conditions and Reasonable and Supportable Forecasts

Management estimates the allowance for credit losses balance using relevant available information, from internal and external sources relating to past events, current conditions, and reasonable and supportable forecasts.

The Bank has chosen two years as the forecast period based on management judgment and has determined that reasonable and supportable forecasts should be made for two of the Q-Factors: Economic and Collateral values.

The CECL Q-Factor methodology bounds the Q-Factor adjustments by a minimum and maximum range, based on the Bank's own expected loss pool history. The rating of the Q-Factor on the seven-point scale, along with the allocated weight, determines the final expected loss adjustment. The model is constructed so that the total of the Q-Factor adjustments plus the current expected loss rate cannot exceed the maximum or minimum historical two-year loss rate for that pool, which is aligned with the Bank's determined forecast period. Loss rates beyond two years are not adjusted in the Q-Factor process, and the model reverts to the historical mean loss rates.

#### Asset-Specific Component

For loans that do not share similar risk characteristics with other loans, the expected credit loss for individually evaluated loans is equal to the amount by which the net realizable value of the loan is less than the amortized cost basis of the loan, except when the loan is collateral dependent, which is when the borrower is experiencing financial difficulty and repayment is expected to be provided substantially through the operation or sale of the collateral. In these cases, the expected credit loss is measured as the difference between the amortized cost basis of the loan and the fair value of the collateral. The fair value of the collateral is adjusted for the estimated costs to sell if repayment or satisfaction of a loan is dependent on the sale (rather than only on the operation) of the collateral.

For further information on the allowance for loan losses, see Note 1, *Summary of Significant Accounting Policies* and Note 6, *Loans and Credit Quality* in the notes to the financial statements of this Form 10-K.

#### ***Fair Value of Financial Instruments and Single Family MSRs***

A portion of our assets are carried at fair value, including single family MSRs, single family loans held for sale, interest rate lock commitments, investment securities available for sale and derivatives used in our hedging programs. 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.

Fair value is based on quoted market prices, when available. If a quoted price for an asset or liability is not available, the Company uses valuation models to estimate its fair value. These models incorporate inputs such as forward yield curves, loan prepayment assumptions, expected loss assumptions, market volatilities, and pricing spreads utilizing market-based inputs where readily available. We believe our valuation methods are appropriate and consistent with those that would be used by other market participants. However, imprecision in estimating unobservable inputs and other factors may result in these fair value measurements not reflecting the amount realized in an actual sale or transfer of the asset or liability in a current market exchange.

A three-level valuation hierarchy has been established by the Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC") Topic 820 for disclosure of fair value measurements. The valuation hierarchy is based on the observability of inputs to the valuation of an asset or liability as of the measurement date. A financial instrument's categorization within the valuation hierarchy is based on the lowest level of input that is significant to the fair value measurement. The levels are defined as follows:

- Level 1 — Quoted prices (unadjusted) in active markets for identical assets or liabilities that the reporting entity can access at the measurement date. An active market for the asset or liability is a market in which transactions for the asset or liability take place with sufficient frequency and volume to provide pricing information on an ongoing basis.

- Level 2 — Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly. This includes quoted prices for similar assets and liabilities in active markets and inputs that are observable for the asset or liability for substantially the full term of the financial instrument.
- Level 3 — Unobservable inputs for the asset or liability. These inputs reflect the Company’s assumptions of what market participants would use in pricing the asset or liability.

Significant judgment is required to determine whether certain assets and liabilities measured at fair value are included in Level 2 or Level 3. When making this judgment, we consider all available information, including observable market data, indications of market liquidity and orderliness, and our understanding of the valuation techniques and significant inputs used. The classification of Level 2 or Level 3 is based upon the specific facts and circumstances of each instrument or instrument category and judgments are made regarding the significance of the Level 3 inputs to an instrument’s fair value measurement in its entirety. If Level 3 inputs are considered significant, the instrument is classified as Level 3.

As of December 31, 2019, our Level 3 recurring fair value measurements consisted of single family MSR’s, single family loans held for investment where fair value option was elected, certain single family loans held for sale, certain investment securities available for sale, and interest rate lock and purchase loan commitments.

On a quarterly basis, our Asset/Liability Management Committee (“ALCO”) and the Finance Committee of the Board review significant modeling variables used to measure the fair value of the Company’s financial instruments, including the significant inputs used in the valuation of single family MSR’s. Additionally, ALCO periodically obtains an independent review of the MSR valuation process and procedures, including a review of the model architecture and the valuation assumptions. We obtain an MSR valuation from an independent valuation firm monthly to assist with the validation of our fair value estimate and the reasonableness of the assumptions used in measuring fair value.

For further information on the fair value of financial instruments and single family MSR’s, see Note 1 *Summary of Significant Accounting Policies*; Note 13 *Mortgage Banking Operations*, and Note 19 *Fair Value Measurement*, in the notes to the financial statements of this Form 10-K.

## **Results of Operations**

### ***Average Balances and Rates***

Average balances, together with the total dollar amounts of interest income and expense, on a tax equivalent basis related to such balances and the weighted average rates, were as follows.



Years Ended December 31,

|  | 2019                |            |                    | 2018                |            |                    | 2017                |            |                    |
|--|---------------------|------------|--------------------|---------------------|------------|--------------------|---------------------|------------|--------------------|
|  | Average Balance     | Interest   | Average Yield/Cost | Average Balance     | Interest   | Average Yield/Cost | Average Balance     | Interest   | Average Yield/Cost |
| <b>Assets:</b>   |                     |            |                    |                     |            |                    |                     |            |                    |
| <b>Interest-earning assets:<sup>(1)</sup></b>  |                     |            |                    |                     |            |                    |                     |            |                    |
| Cash and cash equivalents . . . . .  | \$ 67,446           | \$ 793     | 1.18%              | \$ 76,855           | \$ 895     | 1.16%              | \$ 85,430           | \$ 567     | 0.67%              |
| Investment securities . . . . .  | 850,695             | 22,311     | 2.62               | 916,840             | 24,719     | 2.70               | 1,023,702           | 25,810     | 2.54               |
| Loans held for sale <sup>(4)</sup> . . . . .   | 282,571             | 12,101     | 4.28               | 488,167             | 22,234     | 4.55               | 711,063             | 28,732     | 4.05               |
| Loans held for investment . . . . .  | 5,283,225           | 252,272    | 4.73               | 4,866,210           | 225,730    | 4.64               | 4,178,326           | 187,281    | 4.46               |
| Total interest-earning assets . . . . .  | 6,483,937           | 287,477    | 4.40               | 6,348,072           | 273,578    | 4.30               | 5,998,521           | 242,390    | 4.03               |
| Noninterest-earning assets <sup>(2)(4)</sup> . . . . .                               | 605,822             |            |                    | 669,215             |            |                    | 591,561             |            |                    |
| Total assets . . . . .   | <u>\$ 7,089,759</u> |            |                    | <u>\$ 7,017,287</u> |            |                    | <u>\$ 6,590,082</u> |            |                    |
| <b>Liabilities and shareholders' equity:</b>   |                     |            |                    |                     |            |                    |                     |            |                    |
| <b>Deposits:<sup>(4)</sup></b>   |                     |            |                    |                     |            |                    |                     |            |                    |
| Interest-bearing demand accounts . . . . .   | \$ 382,333          | 1,506      | 0.39%              | \$ 426,610          | \$ 1,678   | 0.39%              | \$ 477,635          | \$ 1,964   | 0.41%              |
| Savings accounts . . . . .   | 229,924             | 530        | 0.23               | 280,358             | 820        | 0.29               | 306,151             | 1,013      | 0.33               |
| Money market accounts . . . . .  | 2,050,779           | 27,259     | 1.33               | 1,908,063           | 17,188     | 1.60               | 1,579,115           | 8,533      | 0.54               |
| Certificate accounts . . . . .   | 1,846,596           | 41,716     | 2.26               | 1,436,872           | 23,030     | 1.60               | 1,225,614           | 13,028     | 1.06               |
| Total interest-bearing deposits <sup>(5)</sup> . . . . .                             | 4,509,632           | 71,011     | 1.57               | 4,051,903           | 42,716     | 1.05               | 3,588,515           | 24,538     | 0.68               |
| Federal Home Loan Bank advances . . . . .  | 407,071             | 10,816     | 2.62               | 867,141             | 18,501     | 2.13               | 1,037,650           | 12,589     | 1.19               |
| Federal funds purchased and securities sold under agreements to repurchase . . . . . | 45,175              | 1,032      | 2.25               | 13,607              | 298        | 2.19               | 3,732               | 48         | 1.20               |
| Other borrowings . . . . .   | 9,122               | 342        | 3.75               | 1,398               | 62         | 4.40               | 96                  | 3          | 0.89               |
| Long-term debt . . . . .   | 125,550             | 6,822      | 5.41               | 125,362             | 6,646      | 5.30               | 125,228             | 6,067      | 4.83               |
| Total interest-bearing liabilities . . . . .   | 5,096,550           | 90,023     | 1.76               | 5,059,411           | 68,223     | 1.35               | 4,755,221           | 43,245     | 0.91               |
| Noninterest-bearing liabilities <sup>(4)</sup> . . . . .                             | 1,271,849           |            |                    | 1,216,841           |            |                    | 1,158,984           |            |                    |
| Total liabilities . . . . .  | 6,368,399           |            |                    | 6,276,252           |            |                    | 5,914,205           |            |                    |
| Temporary Shareholders' equity . . . . .   | 3,034               |            |                    | —                   |            |                    | —                   |            |                    |
| Permanent Shareholders' equity . . . . .   | 718,326             |            |                    | 741,035             |            |                    | 675,877             |            |                    |
| Total liabilities and shareholders' equity . . . . .                                 | <u>\$ 7,089,759</u> |            |                    | <u>\$ 7,017,287</u> |            |                    | <u>\$ 6,590,082</u> |            |                    |
| Net interest income <sup>(3)</sup> . . . . .   |                     | \$ 197,454 |                    |                     | \$ 205,355 |                    |                     | \$ 199,145 |                    |
| Net interest spread . . . . .  |                     |            | 2.64%              |                     |            | 2.95%              |                     |            | 3.12%              |
| Impact of noninterest-bearing sources . . . . .                                      |                     |            | 0.37%              |                     |            | 0.28%              |                     |            | 0.19%              |
| Net interest margin . . . . .  |                     |            | 3.01%              |                     |            | 3.23%              |                     |            | 3.31%              |

(1) The average balances of nonaccrual assets and related income, if any, are included in their respective categories.  
(2) Includes former loan balances that have been foreclosed and are now reclassified to OREO.  
(3) Includes taxable-equivalent adjustments primarily related to tax-exempt income on certain loans and securities of \$2.2 million, \$2.9 million and \$4.7 million for the years ended December 31, 2019, 2018 and 2017, respectively. The estimated federal statutory tax rate was 21% for both years ended 2019 and 2018 and 35% for the year ended 2017.  
(4) Includes average balances of discontinued operations, which were impractical to remove from the periods presented. Net interest margin related to discontinued operations is immaterial.  
(5) Cost of deposits of 1.29%, 0.84% and 0.53% for the years ended December 31, 2019, 2018 and 2017, respectively.

### Interest on Nonaccrual Loans

We do not include interest collected on nonaccrual loans in interest income. When we place a loan on nonaccrual status, we reverse the accrued but unpaid interest, reducing interest income, and we stop amortizing any net deferred fees. Additionally, if interest is received on nonaccrual loans, the interest collected on the loan is recognized as an adjustment to the cost basis of the loan. The net decrease to interest income due to adjustments made for nonaccrual loans, including the effect of additional interest income that would have been recorded during the period if the loans had been accruing, was \$1.9 million, \$1.4 million and \$1.5 million for the years ended December 31, 2019, 2018 and 2017, respectively.

### Rate and Volume Analysis

The following table presents the extent to which changes in interest rates and changes in the volume of our interest-earning assets and interest-bearing liabilities have affected our interest income and interest expense, excluding interest income from nonaccrual loans. Information is provided in each category with respect to: (1) changes attributable to changes in volume (changes in volume multiplied by prior rate), (2) changes attributable to changes in rate (changes in rate multiplied by prior volume), and (3) the net change.

| (in thousands)  | Years Ended December 31,      |                  |                   |                               |                  |                 |
|---|-------------------------------|------------------|-------------------|-------------------------------|------------------|-----------------|
|   | 2019 vs. 2018                 |                  |                   | 2018 vs. 2017                 |                  |                 |
|   | Increase (Decrease)<br>Due to |                  | Total<br>Change   | Increase (Decrease)<br>Due to |                  | Total<br>Change |
|   | Rate                          | Volume           |                   | Rate                          | Volume           |                 |
| Assets:   |                               |                  |                   |                               |                  |                 |
| Interest-earning assets   |                               |                  |                   |                               |                  |                 |
| Cash and cash equivalents . . . . .   | \$ 9                          | \$ (111)         | \$ (102)          | \$ 378                        | \$ (50)          | \$ 328          |
| Investment securities . . . . .   | (660)                         | (1,748)          | (2,408)           | 1,555                         | (2,646)          | (1,091)         |
| Loans held for sale . . . . .   | (1,259)                       | (8,874)          | (10,133)          | 4,357                         | (10,855)         | (6,498)         |
| Loans held for investment . . . . .   | 5,001                         | 21,541           | 26,542            | 7,358                         | 31,091           | 38,449          |
| Total interest-earning assets . . . . .   | 3,091                         | 10,808           | 13,899            | 13,648                        | 17,540           | 31,188          |
| Liabilities:  |                               |                  |                   |                               |                  |                 |
| Deposits  |                               |                  |                   |                               |                  |                 |
| Interest-bearing demand accounts . . . . .  | 2                             | (174)            | (172)             | (80)                          | (206)            | (286)           |
| Savings accounts . . . . .  | (157)                         | (133)            | (290)             | (111)                         | (82)             | (193)           |
| Money market accounts . . . . .   | 8,692                         | 1,379            | 10,071            | 6,608                         | 2,047            | 8,655           |
| Certificate accounts . . . . .  | 11,015                        | 7,671            | 18,686            | 7,484                         | 2,518            | 10,002          |
| Total interest-bearing deposits . . . . .   | 19,552                        | 8,743            | 28,295            | 13,901                        | 4,277            | 18,178          |
| Federal Home Loan Bank advances . . . . .   | 5,821                         | (13,506)         | (7,685)           | 7,468                         | (1,556)          | 5,912           |
| Federal funds purchased and securities sold<br>under agreements to repurchase . . . . . | 9                             | 725              | 734               | 60                            | 190              | 250             |
| Other borrowings . . . . .  | (8)                           | 288              | 280               | 13                            | 46               | 59              |
| Long-term debt . . . . .  | 164                           | 12               | 176               | 573                           | 6                | 579             |
| Total interest-bearing liabilities . . . . .  | 25,538                        | (3,738)          | 21,800            | 22,015                        | 2,963            | 24,978          |
| Total changes in net interest income . .  | <u>\$ (22,447)</u>            | <u>\$ 14,546</u> | <u>\$ (7,901)</u> | <u>\$ (8,367)</u>             | <u>\$ 14,577</u> | <u>\$ 6,210</u> |

### Net Income

#### Comparison of 2019 to 2018

Net income, which included both continuing and discontinued operations, was \$17.5 million in the year ended December 31, 2019, a decrease of \$22.5 million, or 56.2%, from \$40.0 million for the year ended December 31, 2018. The decrease in net income in 2019 was primarily due to the \$20.6 million loss on disposal and restructuring-related expenses, net of tax, taken in the year ended December 31, 2019 compared to the \$5.0 million in restructuring-related expenses, net of tax, taken in the year ended December 31, 2018, a \$4.9 million non-cash, tax benefit from the revaluation of our deferred tax liability related to the Tax Reform Act taken in 2018, a decline in

single-family mortgage servicing income related to the first quarter 2019 sales of single family mortgage servicing rights and a decline in single family net gain on mortgage loan sale and origination activities primarily from the HLC Business Sale. This decrease is partially offset by a reduction in noninterest expense from reduced salaries and commissions on lower closed loan volume, lower headcount, reductions in non-personnel costs from both cost savings initiatives and the HLC Business Sale.

#### *Comparison of 2018 to 2017*

For the year ended December 31, 2018, net income was \$40.0 million, a decrease of \$28.9 million, or 41.9%, from \$68.9 million for the year ended December 31, 2017. Included in net income for the year ended December 31, 2018 and 2017 was a non-cash, tax reform benefit from the revaluation of our deferred tax liability related to the Tax Reform Act of \$4.9 million and \$23.3 million, respectively, and restructuring and merger-related costs (net of tax) of \$5.0 million and \$2.8 million, respectively. The decrease in net income was primarily due to the reduction in tax reform benefit and the decline in mortgage loan production substantially driven by lower single-family mortgage loan volume. The decrease in net income was partially offset by a reduction in noninterest expense as a result of our 2018 and 2017 cost savings initiatives and reduced commissions on lower closed loan volume.

### **Net Income from Continuing Operations**

#### *Comparison of 2019 to 2018*

Net income from continuing operations increased in the year ended December 31, 2019 compared to the year ended December 31, 2018 primarily due to the inclusion, beginning in April 2019, of \$6.7 million after-tax, of income from the Retained MB Business. In the comparative period, income and expense associated with the legacy MB Business was in discontinued operations. Excluding this impact, the improvement resulted from an increase in gain on loan origination and sale activities related to higher volumes and improved margin of loans sold. The increase is partially offset by the \$4.9 million non-cash, tax benefit from the revaluation of our deferred tax liability related to the Tax Reform Act recorded in 2018 and savings related to reduced headcount and our cost saving initiatives.

#### *Comparison of 2018 to 2017*

Net income from continuing operations decreased in the year ended December 31, 2018 compared to the year ended December 31, 2017. Included in net income for the years ended December 31, 2018 and 2017 was a non-cash, tax benefit from the revaluation of our deferred tax liability related to the Tax Reform Act of \$4.9 million and \$23.3 million, respectively. The decrease in net income was primarily due to the reduction in tax reform benefit, a lower gain on loan origination and sale activities and an increase in noninterest expense. The decrease was partially offset by an increase in net interest income.

### **Net Income from Discontinued Operations**

#### *Comparison of 2019 to 2018*

During the year ended December 31, 2019, the Company completed the HLC Business Sale, which primarily comprised the Company's former Mortgage Banking segment. The Company determined that this sale met the criteria for classification as discontinued operations and the related operating results and financial condition are presented as discontinued operations on the consolidated financial statements.

Net loss from discontinued operations was \$23.2 million for the year ended December 31, 2019 compared to net income from discontinued operations of \$13.8 million for the year ended December 31, 2018. The decrease in net income from discontinued operations in the year ended December 31, 2019 was primarily due to an increase in restructuring and loss on disposal charges, the impact from revenues and expenses associated with the Retained MB Business, which were reflected in continuing operations beginning April 2019, a reduction in single family mortgage loan origination and sale activities and related noninterest expense as we wound down the operations of our stand-alone home loan center-based mortgage business and lower servicing income due to the first quarter sales of mortgage servicing rights. This decrease was partially offset by reduced commissions on lower closed loan volume, savings associated with lower headcount and other savings related to our cost reduction initiatives.

### *Comparison of 2018 to 2017*

The decrease in net income from discontinued operations in the year ended December 31, 2018 compared to the year ended December 31, 2017 was primarily due to a reduction in single family mortgage net gain on loan origination and sale activities and related noninterest expense on lower production volumes as the mortgage market weakened. This decrease was partially offset by reduced commissions on lower closed loan volume, savings associated with lower headcount and other savings related to our prior cost reduction initiatives.

### **Net Interest Income**

Our profitability depends significantly on net interest income, which is the difference between income earned on our interest-earning assets, primarily loans and investment securities, and interest paid on interest-bearing liabilities. Our interest-bearing liabilities consist primarily of deposits and borrowed funds, including our outstanding trust preferred securities, senior unsecured notes and advances from the Federal Home Loan Bank (“FHLB”).

### *Comparison of 2019 to 2018*

Net interest income on a tax equivalent basis for the year ended December 31, 2019 decreased \$7.9 million, or 3.8%, from December 31, 2018. The net interest margin decreased to 3.01% for the year ended December 31, 2019 from 3.23% for the year ended December 31, 2018. The decrease in both net interest income and net interest margin from the year ended December 31, 2018 was primarily due to a higher balance of high cost certificate of deposit accounts, partially offset by higher balances and yields on loans held for investment. The continued flattening of the yield curve during the period adversely affected our net interest margin because the cost of interest-bearing liabilities increased more quickly than the yield on our interest-earning assets.

Total average interest-earning assets increased by \$135.9 million, or 2.1%, in 2019 compared to 2018 as a result of both organic and acquired loan growth.

Total interest income on a tax equivalent basis in 2019 increased \$13.9 million, or 5.1%, from 2018 resulting from higher average balances of loans held for investment, which increased \$417.0 million, or 8.6%, from 2018.

Total interest expense in 2019 increased \$21.8 million, or 32.0%, from 2018. The increases resulted from higher rates paid on interest-bearing deposits, FHLB advances and wholesale deposits including brokered CDs as market interest rates rose.

### *Comparison of 2018 to 2017*

Net interest income on a tax equivalent basis for the year ended December 31, 2018 increased \$6.2 million, or 3.1%, from December 31, 2017 as a result of growth in loans held for investment. The net interest margin decreased to 3.23% for the year ended December 31, 2018 from 3.31% for the year ended December 31, 2017. The decrease in the net interest margin from the year ended December 31, 2017 was primarily due to our cost of interest-bearing liabilities, which increased more rapidly than our yield on interest-earning assets. The flattening of the yield curve during the period adversely affected our net interest margin because the cost of interest-bearing liabilities increased more quickly than the yield on our interest-earning assets.

Total average interest-earning assets increased by \$349.6 million, or 5.8%, in 2018 compared to 2017 primarily as a result of organic loan growth.

Total interest income on a tax equivalent basis in 2018 increased \$31.2 million, or 12.9%, from 2017 resulting from higher average balances of loans held for investment, which increased \$687.9 million, or 16.5%, from 2017 and repricing of interest earning assets due to higher market interest rates.

Total interest expense in 2018 increased \$25.0 million, or 57.8%, from 2017. The increase resulted from higher rates on interest-bearing deposits, FHLB advances and wholesale deposits including brokered CDs as market interest rates rose.

## Provision for Credit Losses

Management believes that our allowance for loan losses is at a level appropriate to cover estimated incurred losses inherent within the loans held for investment portfolio. Our credit risk profile has continued to improve since our initial public offering in 2012. Credit quality remained strong from December 31, 2019 and 2018.

### Comparison of 2019 to 2018

The Company had a reversal of provision for credit losses for the year ended December 31, 2019 of \$500 thousand compared to a \$3.0 million provision for credit losses for the year ended December 31, 2018. The decrease in credit loss provision was primarily due to a reduction in loan balances and continued recoveries.

Nonaccrual loans were \$12.9 million at December 31, 2019, an increase of \$1.2 million, or 10.7%, from \$11.6 million at December 31, 2018. Nonaccrual loans as a percentage of total loans increased to 0.25% at December 31, 2019 compared to 0.23% at December 31, 2018. Net loan recoveries were \$424 thousand in 2019 compared to net loan recoveries of \$797 thousand in 2018. Overall, the allowance for credit losses, which includes the reserve for unfunded commitments, was \$42.8 million, or 0.84% of loans held for investment at December 31, 2019, compared to \$42.9 million, or 0.84% of loans held for investment at December 31, 2018.

### Comparison of 2018 to 2017

The Company recorded a \$3.0 million provision for credit losses for the year ended December 31, 2018 compared to a \$750 thousand provision for credit losses for the year ended December 31, 2017. The increase in credit loss provision was due in part to lower net recoveries in the year ended December 31, 2018 as compared to the same period in 2017.

Nonaccrual loans were \$11.6 million at December 31, 2018, a decrease of \$3.4 million, or 22.8%, from \$15.0 million at December 31, 2017. Nonaccrual loans as a percentage of total loans decreased to 0.23% at December 31, 2018 compared to 0.33% at December 31, 2017. Net loan recoveries were \$797 thousand in 2018 compared to net loan recoveries of \$3.1 million in 2017. Overall, the allowance for credit losses, which includes the reserve for unfunded commitments, was \$42.9 million, or 0.84% of loans held for investment at December 31, 2018, compared to \$39.1 million, or 0.86% of loans held for investment at December 31, 2017.

For a more detailed discussion on our allowance for loan losses and related provision for loan losses, see “*Credit Risk Management — Asset Quality and Nonperforming Assets*” in this Form 10-K.

## Noninterest Income

Noninterest income from continuing operations consisted of the following.

| (dollars in thousands)  | Years Ended December 31, |                 |                |                 |                   |                | 2017            |
|---|--------------------------|-----------------|----------------|-----------------|-------------------|----------------|-----------------|
|   | 2019                     | Dollar Change   | Percent Change | 2018            | Dollar Change     | Percent Change |                 |
| Noninterest income  |                          |                 |                |                 |                   |                |                 |
| Net gain on loan origination and sale activities . . . . .                | \$44,122                 | \$32,256        | 272%           | \$11,866        | \$ (8,160)        | (41)%          | \$20,026        |
| Loan servicing income . . . . .   | 7,802                    | 4,131           | 113            | 3,671           | 340               | 10             | 3,331           |
| Depositor and other retail banking fees . . . . .                         | 7,926                    | (93)            | (1)            | 8,019           | 824               | 11             | 7,195           |
| Insurance agency commissions . . . . .                                    | 2,292                    | 99              | 5              | 2,193           | 289               | 15             | 1,904           |
| (Loss) gain on sale of investment securities available for sale . . . . . | (7)                      | (242)           | (103)          | 235             | (254)             | (52)           | 489             |
| Other . . . . .   | 12,297                   | 1,748           | 17             | 10,549          | 897               | 9              | 9,652           |
| Total noninterest income . . . . .  | <u>\$74,432</u>          | <u>\$37,899</u> | 104%           | <u>\$36,533</u> | <u>\$ (6,064)</u> | (14)%          | <u>\$42,597</u> |



### Comparison of 2019 to 2018

The increase in noninterest income in 2019 compared to 2018 was primarily due to \$31.0 million of noninterest income related to the inclusion, beginning in April 2019, of the revenues from the Retained MB Business. In the comparable period, noninterest income related to the legacy MB business was in discontinued operations. Excluding this impact, noninterest income increased primarily due to an increase in net gain on loan origination and sale activities related to an increase in volume and profit margin on loans sold.

### Comparison of 2018 to 2017

The decrease in noninterest income in 2018 compared to 2017 was primarily due to both lower volume and profit margin on DUS loan sales.

The significant components of our noninterest income are described in greater detail, as follows.

**Gain on loan origination and sale activities** consisted of the following.

| (in thousands)  | Years Ended December 31, |                   |                   |
|---|--------------------------|-------------------|-------------------|
|   | 2019                     | 2018              | 2017              |
| Commercial  | \$ 17,492                | \$ 11,776         | \$ 20,027         |
| Single family <sup>(1)</sup>                                      | 86,686                   | 174,473           | 235,849           |
| Total gain on loan origination and sale activities <sup>(2)</sup> | <u>\$ 104,178</u>        | <u>\$ 186,249</u> | <u>\$ 255,876</u> |

- (1) Includes \$60.1 million, \$174.4 million and \$235.9 million from discontinued operations for the years ended 2019, 2018 and 2017, respectively.
- (2) Includes loans originated as held for investment.

### Comparison of 2019 to 2018

The increase in gain on loan origination and sale activities from continuing operations in 2019 compared to 2018 is primarily due to \$26.9 million in gains related to the inclusion, beginning in April 2019, of the revenues from the Retained MB Business, (gain on sale associated with the legacy MB business was included in discontinued operations for the comparative period) and an increase in volume and profit margin on CRE HCC loans sold.

### Comparison of 2018 to 2017

The decrease in gain on loan origination and sale activities from continuing operations in 2018 compared to 2017 was due to both a lower volume and margin on DUS loan sales.

**Loans serviced for others** consisted of the following.

| (in thousands)                  | At December 31,     |                      |
|---------------------------------|---------------------|----------------------|
|                                 | 2019                | 2018                 |
| Commercial                      | \$ 1,618,876        | \$ 1,542,477         |
| Single family <sup>(1)(2)</sup> | 7,023,441           | 20,151,735           |
| Total loans serviced for others | <u>\$ 8,642,317</u> | <u>\$ 21,694,212</u> |

- (1) Includes both continuing and discontinued operations at December 31, 2018.
- (2) On March 29, 2019 the Company settled two sales of the rights to service \$14.26 billion in total unpaid principal balance of single family mortgage loans serviced representing 71% of the Company's total single family mortgage loans serviced for others portfolio as of December 31, 2018.

**Mortgage repurchase losses**, which management records an estimated liability for, have the effect of reducing gain on mortgage loan origination and sale activities. The following table presents the effect of changes in our mortgage repurchase liability within the respective line of gain on mortgage loan origination and sale activities. For further information on the Company's mortgage repurchase liability, see Note 14, *Commitments, Guarantees and Contingencies* to the financial statements in this Form 10-K.

| (in thousands)  | Years Ended December 31, |                 |               |
|---|--------------------------|-----------------|---------------|
|   | 2019                     | 2018            | 2017          |
| Effect of changes to the mortgage repurchase liability recorded in net gain on loan origination and sale activities: <sup>(1)</sup> |                          |                 |               |
| New loan sales <sup>(2)</sup> . . . . .   | \$ 648                   | \$ 1,092        | \$ 2,528      |
| Other changes in estimated repurchase losses <sup>(3)</sup> . . . . .   | (422)                    | 838             | (2,354)       |
|   | <u>\$ 226</u>            | <u>\$ 1,930</u> | <u>\$ 174</u> |

(1) Includes both continuing and discontinued operations.

(2) Represents the estimated fair value of the repurchase or indemnity obligation recognized as a reduction of proceeds on new loan sales.

(3) Represents changes in estimated probable future repurchase losses on previously sold loans.

*Loan servicing income* consisted of the following.

| (dollars in thousands)   | Years Ended December 31, |                   |                |                 |                  |                |                 |
|--|--------------------------|-------------------|----------------|-----------------|------------------|----------------|-----------------|
|  | 2019                     | Dollar Change     | Percent Change | 2018            | Dollar Change    | Percent Change | 2017            |
| Commercial loan servicing income, net:   |                          |                   |                |                 |                  |                |                 |
| Servicing fees and other . . . . .   | \$ 9,116                 | \$ 1,063          | 13%            | \$ 8,053        | \$ 790           | 11%            | \$ 7,263        |
| Amortization of capitalized MSR's . . . . .  | (5,219)                  | (836)             | 19             | (4,383)         | (451)            | 11             | (3,932)         |
| Commercial loan servicing income . . . . .   | <u>3,897</u>             | <u>227</u>        | 6              | <u>3,670</u>    | <u>339</u>       | 10             | <u>3,331</u>    |
| Single family servicing income, net:   |                          |                   |                |                 |                  |                |                 |
| Servicing fees and other . . . . .   | 28,442                   | (32,443)          | (53)           | 60,885          | 1,956            | 3              | 58,929          |
| Changes in fair value of single family MSR's due to amortization <sup>(1)</sup> . . . . .                  | (20,670)                 | 14,035            | (40)           | (34,705)        | 746              | (2)            | (35,451)        |
| Single family servicing income . . . . .   | <u>7,772</u>             | <u>(18,408)</u>   | (70)           | <u>26,180</u>   | <u>2,702</u>     | 12             | <u>23,478</u>   |
| Risk management, single family MSR's:  |                          |                   |                |                 |                  |                |                 |
| Changes in fair value of MSR due to changes in model inputs and/or assumptions <sup>(2)(3)</sup> . . . . . | (16,224)                 | (55,572)          | (141)          | 39,348          | 40,505           | (3,501)        | (1,157)         |
| Net (loss) gain from derivatives economically hedging MSR . . . . .  | <u>14,435</u>            | <u>54,909</u>     | (136)          | <u>(40,474)</u> | <u>(50,206)</u>  | (516)          | <u>9,732</u>    |
|  | <u>(1,789)</u>           | <u>(663)</u>      | 59             | <u>(1,126)</u>  | <u>(9,701)</u>   | (113)          | <u>8,575</u>    |
| Single family servicing income . . . . .   | <u>\$ 5,983</u>          | <u>\$(19,071)</u> | (76)%          | <u>\$25,054</u> | <u>\$(6,999)</u> | (22)%          | <u>\$32,053</u> |
| Total loan servicing income <sup>(4)</sup> . . . . .   | <u>\$ 9,880</u>          | <u>\$(18,844)</u> | (66)%          | <u>\$28,724</u> | <u>\$(6,660)</u> | (19)%          | <u>\$35,384</u> |

(1) Represents changes due to collection/realization of expected cash flows and curtailments.

(2) Principally reflects changes in market inputs, which include current market interest rates and prepayment model updates, both of which affect future prepayment speed and cash flow projections.

(3) Includes pre-tax loss of \$919 thousand and pre-tax gain of \$573 thousand, net of transaction costs and prepayment reserves, resulting from the sales of single family MSR for year ended December 31, 2019 and December 31, 2018, respectively.

(4) Includes \$3.0 million, \$25.1 million and \$32.1 million from discontinued operations for the years ended December 31, 2019, 2018 and 2017, respectively.

#### Comparison of 2019 to 2018

The decrease in loan servicing income in 2019 compared to 2018 was primarily due to a lower average unpaid principal balance of loans serviced for others due to our sales of single-family mortgage servicing rights and lower risk management results.

Risk management results fluctuate as market conditions change, including changes in interest rates and prepayment speed expectations. Loan servicing fees collected in 2019 decreased compared to 2018 primarily due to the sales of mortgage servicing rights. Our loans serviced for others portfolio decreased to \$8.64 billion at December 31, 2019 from \$21.69 billion at December 31, 2018. The reduction in balance from these periods was mainly due to the sale of \$14.26 billion of single-family loans serviced for others in the first quarter of 2019, partially offset by the growth of the portfolio in second half of 2019.

MSR risk management results represent changes in the fair value of single family MSR due to changes in model inputs and assumptions net of the gain/(loss) from derivatives economically hedging MSRs. The fair value of MSRs is sensitive to changes in interest rates, primarily due to the effect of prepayment speeds on underlying mortgage loans. MSRs typically increase in value when interest rates rise because rising interest rates tend to decrease mortgage prepayment speeds, and therefore increase the expected life of the net servicing cash flows of the MSR asset. Certain other changes in MSR fair value relate to factors other than interest rate changes and are generally not within the scope of the Company's MSR economic hedging strategy. These factors may include but are not limited to the impact of changes to the housing price index, prepayment model assumptions, the level of home sales activity, changes to mortgage spreads, valuation discount rates, costs to service and policy changes by U.S. government agencies.

#### *Comparison of 2018 to 2017*

The decrease in loan servicing income in 2018 compared to 2017 was primarily due to lower risk management results offset by higher servicing income. The lower risk management results were primarily driven by a more volatile interest rate environment, the flattening of the yield curve and increased negative convexity cost. The higher servicing income was primarily attributed to higher average balances of loans serviced for others. Loan servicing fees collected in 2018 increased compared to 2017 primarily as a result of higher average balances of loans serviced for others during the year. Although our loans serviced for others average balances were higher year over year, our loans serviced for others portfolio decreased to \$21.69 billion at December 31, 2018 from \$24.02 billion at December 31, 2017. The decrease in balance from these periods was mainly due to the sale of \$4.90 billion of single-family loans serviced for others in the second quarter of 2018, partially offset by the growth of the portfolio in second half of 2018.

**Depositor and other retail banking fees** for 2019 decreased slightly from 2018. The following table presents the composition of depositor and other retail banking fees for the periods indicated.

| <u>(dollars in thousands)</u>  | <u>Years Ended December 31,</u> |                      |                       |                 |                      |                       |                 |
|--|---------------------------------|----------------------|-----------------------|-----------------|----------------------|-----------------------|-----------------|
|  | <u>2019</u>                     | <u>Dollar Change</u> | <u>Percent Change</u> | <u>2018</u>     | <u>Dollar Change</u> | <u>Percent Change</u> | <u>2017</u>     |
| Fees:  |                                 |                      |                       |                 |                      |                       |                 |
| Monthly maintenance and deposit-related fees . . . . .                 | \$ 3,303                        | \$ (75)              | (2)%                  | \$ 3,378        | \$ 293               | 9%                    | \$ 3,085        |
| Debit Card/ATM fees . . . . .  | 4,370                           | (16)                 | —                     | 4,386           | 474                  | 12                    | 3,912           |
| Other fees . . . . .   | <u>261</u>                      | <u>(22)</u>          | (8)                   | <u>283</u>      | <u>59</u>            | 26                    | <u>224</u>      |
| Total depositor and other retail banking fees <sup>(1)</sup> . . . . . | <u>\$ 7,934</u>                 | <u>\$ (113)</u>      | (1)%                  | <u>\$ 8,047</u> | <u>\$ 826</u>        | 11%                   | <u>\$ 7,221</u> |

(1) Includes \$8 thousand, \$28 thousand and \$26 thousand from discontinued operations for the years ended December 31, 2019, 2018 and 2017, respectively.

## Noninterest Expense

*Noninterest expense* from continuing operations consisted of the following.

| (dollars in thousands)   | Years Ended December 31, |                 |                |                  |                 |                | 2017             |
|--|--------------------------|-----------------|----------------|------------------|-----------------|----------------|------------------|
|  | 2019                     | Dollar Change   | Percent Change | 2018             | Dollar Change   | Percent Change |                  |
| Noninterest expense  |                          |                 |                |                  |                 |                |                  |
| Salaries and related costs . . . . .                                   | \$122,189                | \$17,147        | 16%            | \$105,042        | \$ 3,251        | 3%             | \$101,791        |
| General and administrative . . . . .                                   | 33,862                   | 930             | 3              | 32,932           | (4,850)         | (13)           | 37,782           |
| Amortization of core deposit intangibles . . . . .                     | 1,634                    | 9               | 1              | 1,625            | (85)            | (5)            | 1,710            |
| Legal . . . . .  | 1,559                    | (1,814)         | (54)           | 3,373            | 2,070           | 159            | 1,303            |
| Consulting . . . . .   | 4,055                    | 1,586           | 64             | 2,469            | (213)           | (8)            | 2,682            |
| Federal Deposit Insurance Corporation assessments . . . . .            | 1,820                    | (1,988)         | (52)           | 3,808            | 810             | 27             | 2,998            |
| Occupancy . . . . .  | 22,242                   | 4,139           | 23             | 18,103           | 1,122           | 7              | 16,981           |
| Information services . . . . .   | 28,325                   | 297             | 1              | 28,028           | 2,131           | 8              | 25,897           |
| Net benefit of operation and sale of other real estate owned . . . . . | (72)                     | 67              | (48)           | (139)            | 391             | (74)           | (530)            |
| Total noninterest expense . . . . .                                    | <u>\$215,614</u>         | <u>\$20,373</u> | 10%            | <u>\$195,241</u> | <u>\$ 4,627</u> | 2%             | <u>\$190,614</u> |

### *Comparison of 2019 to 2018*

The increase in noninterest expense in 2019 compared to 2018 was primarily due to \$26.3 million of expenses related to the inclusion, beginning in April 2019, of the expenses from the Retained MB Business. In the comparable period, expenses related to the legacy MB business were in discontinued operations. Excluding this impact, noninterest expense decreased in both periods primarily due to savings related to reduced headcount and our cost saving initiatives.

Included in noninterest expense in 2019 and 2018 was \$4.5 million and \$22 thousand in restructuring-related costs, respectively.

**Salaries and related costs** increased primarily due to \$20.1 million in costs related to the inclusion, beginning in April 2019, of the expenses from the Retained MB Business. In the comparable period, salaries and related costs related to the legacy MB business were in discontinued operations, partially offset by a reduction in salaries primarily related to a decrease in full-time equivalent employees at December 31, 2019 compared to December 31, 2018.

**General and administrative and Information services costs** increased primarily due to the \$2.7 million in costs related to the inclusion, beginning in April 2019, of the expenses from the Retained MB Business. In the comparable period, general and administrative costs related to the legacy MB business were in discontinued operations. The increase was partially offset by a reduction in personnel associated expenses related to our cost savings initiatives.

### *Comparison of 2018 to 2017*

The increase in noninterest expense in 2018 compared to 2017 was primarily due to an increase in salaries and related costs, as well as an increase in information services costs. The increase was partially offset by a decrease in general and administrative costs.

**Salaries and related costs** increased primarily due to an increase in commissions on CRE loan sales.

**General and administrative and Information services costs** decreased primarily due to a reduction in office locations and a reduction in personnel related expenses related to our cost savings initiatives.

## Income Tax Expense

### *Comparison of 2019 to 2018*

For the year ended December 31, 2019, income tax expense from continuing operations was \$8.0 million with an effective tax rate of 16.4% (inclusive of discrete items) compared to income tax expense from continuing operations of \$2.0 million and an effective tax rate of 7.2% (inclusive of discrete items) for the year ended December 31, 2018.

The Company's effective income tax rate for the year ended December 31, 2019 differed from the Federal and state combined statutory tax rate of 23.5% primarily due to the benefit received from tax-exempt interest and BOLI income.

The increase in our 2019 effective income tax rate compared to 2018 is primarily related to the non-cash, benefit of \$4.9 million recorded in 2018 for the revaluation our net deferred tax liability position related to the Tax Reform Act.

### *Comparison of 2018 to 2017*

For the year ended December 31, 2018 income tax expense from continuing operations was \$2.0 million with an effective tax rate of 7.2% (inclusive of discrete items) compared to income tax benefit from continuing operations of \$16.9 million and an effective tax rate of (65.6)% (inclusive of discrete items) for the year ended December 31, 2017.

The Company's effective income tax rate for the year ended December 31, 2018 differed from the Federal and state combined statutory tax rate of 23.6% primarily due to a net tax benefit of \$3.7 million, comprised of a \$4.9 million tax benefit from the revaluation of our net deferred tax liability position related to the Tax Reform Act and a \$1.2 million expense related to the filing of our 2017 tax return, but unrelated to tax reform.

The increase in our 2018 effective income tax rate compared to 2017 is primarily related to the non-cash, benefit of \$23.3 million recorded at December 31, 2017 for the revaluation our net deferred tax liability position related to the Tax Reform Act. The increase was partially offset by the decrease in the Federal statutory rate from 35% to 21%.

## Capital Expenditures

### *Comparison of 2019 to 2018*

During 2019, our net expenditures for property and equipment were \$2.3 million, compared to net expenditures of \$9.7 million during 2018. The decrease was primarily due to the slower expansion of our commercial and consumer banking business as we focused on our strategy of improved efficiency and profitability.

### *Comparison of 2018 to 2017*

During 2018, our net expenditures for property and equipment were \$9.7 million, compared to net expenditures of \$42.3 million during 2017. The decrease was primarily due to the slower expansion of our commercial and consumer banking business.

## Review of Financial Condition — Comparison of December 31, 2019 to December 31, 2018

Total assets were \$6.81 billion at December 31, 2019 and \$7.04 billion at December 31, 2018, a decrease of \$229.8 million, or 3.3%, primarily due to a decline in assets related to discontinued operations.

Cash and cash equivalents were \$57.9 million at December 31, 2019 compared to \$58.0 million at December 31, 2018, a decrease of \$102 thousand, or 0.2%.

Investment securities were \$943.2 million at December 31, 2019 compared to \$923.3 million at December 31, 2018, an increase of \$19.9 million, or 2.2%, as we added to our investment portfolio in order to maintain our liquidity ratios after the decline in our loans held for sale balances related to the HLC Business Sale.



We primarily hold investment securities for liquidity purposes, while also creating a relatively stable source of interest income. We designate the vast majority of these securities as available for sale. We held securities having a carrying value of \$4.4 million at December 31, 2019, which were designated as held to maturity.

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

| (in thousands)   | At December 31,   |                   |                   |                   |
|--|-------------------|-------------------|-------------------|-------------------|
|  | 2019              |                   | 2018              |                   |
|  | Amortized Cost    | Fair Value        | Amortized Cost    | Fair Value        |
| Investment securities available for sale:                |                   |                   |                   |                   |
| Mortgage-backed securities:                              |                   |                   |                   |                   |
| Residential. . . . .                                     | \$ 93,283         | \$ 91,695         | \$ 112,852        | \$ 107,961        |
| Commercial. . . . .                                      | 37,972            | 38,025            | 34,892            | 34,514            |
| Collateralized mortgage obligations:                     |                   |                   |                   |                   |
| Residential. . . . .                                     | 292,370           | 291,618           | 171,412           | 166,744           |
| Commercial. . . . .                                      | 156,693           | 156,154           | 118,555           | 116,674           |
| Municipal bonds . . . . .                                | 333,303           | 341,318           | 393,463           | 385,655           |
| Corporate debt securities . . . . .                      | 18,391            | 18,661            | 21,177            | 19,995            |
| U.S. Treasury securities. . . . .                        | 1,296             | 1,307             | 11,211            | 10,900            |
| Agency debentures . . . . .                              | —                 | —                 | 9,876             | 9,525             |
| Total investment securities available for sale . . . . . | <u>\$ 933,308</u> | <u>\$ 938,778</u> | <u>\$ 873,438</u> | <u>\$ 851,968</u> |

Mortgage-backed securities (“MBS”) and collateralized mortgage obligations (“CMO”) primarily represent securities issued by government sponsored enterprises (“GSEs”). Most of the MBS and CMO securities in our investment portfolio are guaranteed by Fannie Mae, Ginnie Mae or Freddie Mac. Municipal bonds are comprised of general obligation bonds (i.e., backed by the general credit of the issuer) and revenue bonds (i.e., backed by either collateral or revenues from the specific project being financed) issued by various municipal corporations. As of December 31, 2019 and 2018, substantially all securities held were either agency quality or rated investment grade by at least one Nationally Recognized Statistical Rating Organization (“NRSRO”).

For information regarding the fair value of investment securities available for sale by contractual maturity along with the associated contractual yield for the periods, see Note 5, *Investment Securities* to the financial statements of this Form 10-K.

Investments in these instruments involve a risk that actual prepayments will vary from the estimated prepayments over the life of the security. This may require adjustments to the amortization of premiums or accretion of discounts relating to such instruments, thereby changing the net yield on such securities. At December 31, 2019, the aggregate net premium associated with our MBS portfolio was \$3.8 million, or 3.0%, of the aggregate unpaid principal balance, compared with \$5.9 million or 3.5% at December 31, 2018. The aggregate net premium associated with our CMO portfolio as of December 31, 2019 was \$4.4 million, or 1.0%, of the aggregate unpaid principal balance compared with \$3.4 million or 1.1% at December 31, 2018. There is also reinvestment risk associated with the cash flows from such securities and the market value of such securities may be adversely affected by changes in interest rates.

Management monitors the portfolio of securities classified as available for sale for impairment, primarily resulting from credit deterioration of the issuer or underlying collateral. We evaluate each investment security on a quarterly basis to assess if impairment is considered other than temporary. In conducting this evaluation, management considers many factors, including but not limited to whether we expect to recover the entire amortized cost basis of the security in light of adverse changes in expected future cash flows, the length of time the security’s fair value has been less than amortized cost and the severity of the unrealized loss. We also consider whether we intend to sell the security (or whether we will be required to sell the security) prior to recovery of its amortized cost basis, which may be at maturity.

Based on this evaluation, management concluded that unrealized losses as of December 31, 2019 were the result of changes in interest rates. Management does not intend to sell such securities nor is it likely it will be required to sell such securities prior to recovery of the securities' amortized cost basis. Accordingly, none of the unrealized losses as of December 31, 2019 were considered other than temporary.

*Loans held for sale* were \$208.2 million at December 31, 2019 compared to \$77.3 million at December 31, 2018, an increase of \$130.9 million, or 169.2%. Loans held for sale include single family and multifamily residential loans, typically sold within 30 days of origination or transfer to held for sale. The increase in the loans held for sale balance was primarily due to an increase in commercial loans.

*Loans held for investment, net* decreased \$2.6 million, or 0.1%, from December 31, 2018. The decrease was primarily due to a decline in single family loans. Included in the change were \$86.4 million of acquired commercial and industrial loans and \$23.5 million of acquired non-owner occupied commercial real estate loans.

Commercial real estate loans increased \$189.3 million, or 7.9%, commercial and industrial loans increased \$132.9 million, or 17.5% compared to 2018. These increases were primarily from acquired loans. Consumer loans decreased \$325.8 million, or 16.9% from 2018, this included a decrease in home equity loans of \$38.0 million, or 6.7%, and a \$287.8 million, or 21.2%, decrease in single family loans related to a decrease in interest rates and lower originations related to exit of the HLC business.

The following table details the composition of our loans held for investment portfolio by dollar amount and as a percentage of our total loan portfolio.

| (dollars in thousands)  | At December 31,             |           |                             |           |                             |           |                             |           |                     |           |
|---|-----------------------------|-----------|-----------------------------|-----------|-----------------------------|-----------|-----------------------------|-----------|---------------------|-----------|
|   | 2019                        |           | 2018                        |           | 2017                        |           | 2016                        |           | 2015                |           |
|   | Amount                      | Percent   | Amount                      | Percent   | Amount                      | Percent   | Amount                      | Percent   | Amount              | Percent   |
| Consumer loans:   |                             |           |                             |           |                             |           |                             |           |                     |           |
| Single family . . . . .   | \$ 1,070,332 <sup>(1)</sup> | 21%       | \$ 1,358,175 <sup>(1)</sup> | 27%       | \$ 1,381,366 <sup>(1)</sup> | 30%       | \$ 1,083,822 <sup>(1)</sup> | 28%       | \$ 1,203,180        | 37%       |
| Home equity and other. . . . .  | 532,926                     | 10        | 570,923                     | 11        | 453,489                     | 10        | 359,874                     | 9         | 256,373             | 8         |
|   | <u>1,603,258</u>            | <u>31</u> | <u>1,929,098</u>            | <u>38</u> | <u>1,834,855</u>            | <u>40</u> | <u>1,443,696</u>            | <u>37</u> | <u>1,459,553</u>    | <u>45</u> |
| Commercial real estate loans:   |                             |           |                             |           |                             |           |                             |           |                     |           |
| Non-owner occupied<br>commercial real estate. . . . .                             | 894,896                     | 18        | 701,928                     | 14        | 622,782                     | 14        | 588,672                     | 15        | 445,903             | 14        |
| Multifamily . . . . .   | 996,498                     | 20        | 908,015                     | 18        | 728,037                     | 16        | 674,219                     | 18        | 426,557             | 13        |
| Construction/land<br>development . . . . .  | 702,399                     | 14        | 794,544                     | 16        | 687,631                     | 15        | 636,320                     | 17        | 583,160             | 18        |
|   | <u>2,593,793</u>            | <u>52</u> | <u>2,404,487</u>            | <u>48</u> | <u>2,038,450</u>            | <u>45</u> | <u>1,899,211</u>            | <u>50</u> | <u>1,455,620</u>    | <u>45</u> |
| Commercial and industrial loans:  |                             |           |                             |           |                             |           |                             |           |                     |           |
| Owner occupied commercial<br>real estate . . . . .                                | 478,172                     | 9         | 429,158                     | 8         | 391,613                     | 9         | 282,891                     | 7         | 154,800             | 5         |
| Commercial business. . . . .  | 414,880                     | 8         | 331,004                     | 6         | 264,709                     | 6         | 223,653                     | 6         | 154,262             | 5         |
|   | <u>893,052</u>              | <u>17</u> | <u>760,162</u>              | <u>14</u> | <u>656,322</u>              | <u>15</u> | <u>506,544</u>              | <u>13</u> | <u>309,062</u>      | <u>10</u> |
| Total loans before allowance and<br>net deferred loan fees and<br>costs . . . . . | 5,090,103                   | 100%      | 5,093,747                   | 100%      | 4,529,627                   | 100%      | 3,849,451                   | 100%      | 3,224,235           | 100%      |
| Net deferred loan fees and costs . .  | 24,453                      |           | 23,094                      |           | 14,686                      |           | 3,577                       |           | (2,237)             |           |
|   | <u>5,114,556</u>            |           | <u>5,116,841</u>            |           | <u>4,544,313</u>            |           | <u>3,853,028</u>            |           | <u>3,221,998</u>    |           |
| Allowance for loan losses . . . . .   | (41,772)                    |           | (41,470)                    |           | (37,847)                    |           | (34,001)                    |           | (29,278)            |           |
|   | <u>\$ 5,072,784</u>         |           | <u>\$ 5,075,371</u>         |           | <u>\$ 4,506,466</u>         |           | <u>\$ 3,819,027</u>         |           | <u>\$ 3,192,720</u> |           |

(1) Includes \$3.5 million and \$4.1 million and \$5.5 million and \$18.0 million of loans at December 31, 2019, 2018, 2017 and 2016, respectively, where a fair value option election was made at the time of origination and; therefore, are carried at fair value with changes recognized in the consolidated statements of operations.

The following table shows the composition of the loan portfolio by fixed-rate and adjustable-rate loans.

| (dollars in thousands)                              | At December 31,     |             |                     |             |
|---|---------------------|-------------|---------------------|-------------|
|   | 2019                |             | 2018                |             |
|   | Amount              | Percent     | Amount              | Percent     |
| Adjustable-rate loans:                              |                     |             |                     |             |
| Single family . . . . .                             | \$ 783,754          | 15%         | \$ 1,011,877        | 20%         |
| Home equity and other . . . . .                     | 507,958             | 10          | 539,050             | 10          |
| Non-owner occupied commercial real estate . . . . . | 761,225             | 15          | 580,543             | 11          |
| Multifamily . . . . .                               | 972,804             | 19          | 871,809             | 17          |
| Construction/land development . . . . .             | 535,585             | 10          | 659,444             | 13          |
| Owner occupied commercial real estate . . . . .     | 333,495             | 7           | 285,485             | 5           |
| Commercial business . . . . .                       | 341,255             | 7           | 244,780             | 5           |
| Total adjustable-rate loans . . . . .               | <u>4,236,076</u>    | <u>83</u>   | <u>4,192,988</u>    | <u>81</u>   |
| Fixed-rate loans:                                   |                     |             |                     |             |
| Single family . . . . .                             | 286,578             | 6           | 346,298             | 7           |
| Home equity and other . . . . .                     | 24,968              | 1           | 31,873              | 1           |
| Commercial real estate loans:                       |                     |             |                     |             |
| Non-owner occupied commercial real estate . . . . . | 133,671             | 3           | 121,385             | 2           |
| Multifamily . . . . .                               | 23,694              | —           | 36,206              | 1           |
| Construction/land development . . . . .             | 166,814             | 3           | 135,100             | 3           |
| Owner occupied commercial real estate . . . . .     | 144,677             | 3           | 143,673             | 3           |
| Commercial business . . . . .                       | 73,625              | 1           | 86,224              | 2           |
| Total fixed-rate loans . . . . .                    | <u>854,027</u>      | <u>17</u>   | <u>900,759</u>      | <u>19</u>   |
| Total loans held for investment . . . . .           | <u>5,090,103</u>    | <u>100%</u> | <u>5,093,747</u>    | <u>100%</u> |
| Less:   |                     |             |                     |             |
| Net deferred loan fees and costs . . . . .          | 24,453              |             | 23,094              |             |
| Allowance for loan losses . . . . .                 | (41,772)            |             | (41,470)            |             |
| Loans held for investment, net . . . . .            | <u>\$ 5,072,784</u> |             | <u>\$ 5,075,371</u> |             |

The following tables show the contractual maturity of our loan portfolio by loan type.

| (in thousands)                                      | December 31, 2019 |                                   |                     |                     | Loans due after one year by rate characteristic |                     |
|---|-------------------|-----------------------------------|---------------------|---------------------|---|---------------------|
|   | Within one year   | After one year through five years | After five years    | Total               | Fixed-rate                                      | Adjustable-rate     |
|   |                   |                                   |                     |                     |   |                     |
| Consumer:   |                   |                                   |                     |                     |   |                     |
| Single family . . . . .                             | \$ 1,694          | \$ 1,880                          | \$1,066,758         | \$1,070,332         | \$ 286,208                                      | \$ 782,430          |
| Home equity and other . . . . .                     | 2,630             | 100                               | 530,196             | 532,926             | 22,338  | 507,958             |
| Total consumer . . . . .                            | <u>4,324</u>      | <u>1,980</u>                      | <u>1,596,954</u>    | <u>1,603,258</u>    | <u>308,546</u>                                  | <u>1,290,388</u>    |
| Commercial real estate loans:                       |                   |                                   |                     |                     |   |                     |
| Non-owner occupied commercial real estate . . . . . | 5,551             | 106,458                           | 782,887             | 894,896             | 133,398   | 755,946             |
| Multifamily . . . . .                               | 3,550             | 34,610                            | 958,338             | 996,498             | 21,996  | 970,952             |
| Construction/land development . . . . .             | 602,048           | 97,810                            | 2,541               | 702,399             | 77,022  | 23,329              |
| Total commercial real estate . . . . .              | <u>611,149</u>    | <u>238,878</u>                    | <u>1,743,766</u>    | <u>2,593,793</u>    | <u>232,416</u>                                  | <u>1,750,227</u>    |
| Commercial and industrial loans:                    |                   |                                   |                     |                     |   |                     |
| Owner occupied commercial real estate . . . . .     | 12,831            | 45,515                            | 419,826             | 478,172             | 133,105   | 332,237             |
| Commercial business . . . . .                       | 83,381            | 152,416                           | 179,083             | 414,880             | 70,771  | 260,728             |
| Total commercial and industrial . . . . .           | <u>96,212</u>     | <u>197,931</u>                    | <u>598,909</u>      | <u>893,052</u>      | <u>203,876</u>                                  | <u>592,965</u>      |
| Total loans held for investment . . . . .           | <u>\$ 711,685</u> | <u>\$ 438,789</u>                 | <u>\$ 3,939,629</u> | <u>\$ 5,090,103</u> | <u>\$ 744,838</u>                               | <u>\$ 3,633,580</u> |

| (in thousands)                                      | December 31, 2018  |  |                     |                    | Loans due after one year<br>by rate characteristic |                     |
|---|--------------------|--|---------------------|--------------------|--|---------------------|
|   | Within<br>one year | After<br>one year<br>through<br>five years | After<br>five years | Total              | Fixed-rate   | Adjustable-<br>rate |
|   |                    |  |                     |                    |  |                     |
| Consumer:   |                    |  |                     |                    |  |                     |
| Single family . . . . .                             | \$ 2,357           | \$ 2,602                                   | \$1,353,216         | \$1,358,175        | \$ 345,281   | \$1,010,537         |
| Home equity and other . . . . .                     | 1                  | 127  | 570,795             | 570,923            | 31,872   | 539,050             |
| Total consumer . . . . .                            | <u>2,358</u>       | <u>2,729</u>                               | <u>1,924,011</u>    | <u>1,929,098</u>   | <u>377,153</u>                                     | <u>1,549,587</u>    |
| Commercial real estate:                             |                    |  |                     |                    |  |                     |
| Non-owner occupied commercial real estate . . . . . | 8,829              | 66,477                                     | 626,622             | 701,928            | 114,882  | 578,217             |
| Multifamily . . . . .                               | 12,141             | 44,419                                     | 851,455             | 908,015            | 24,753   | 871,121             |
| Construction/land development . . . . .             | 606,758            | 156,674                                    | 31,112              | 794,544            | 96,292   | 91,494              |
| Total commercial real estate . . . . .              | <u>627,728</u>     | <u>267,570</u>                             | <u>1,509,189</u>    | <u>2,404,487</u>   | <u>235,927</u>                                     | <u>1,540,832</u>    |
| Commercial and industrial:                          |                    |  |                     |                    |  |                     |
| Owner occupied commercial real estate . . . . .     | 4,184              | 51,097                                     | 373,877             | 429,158            | 140,901  | 284,073             |
| Commercial business . . . . .                       | 61,375             | 147,195                                    | 122,434             | 331,004            | 82,081   | 187,548             |
| Total commercial and industrial . . . . .           | <u>65,559</u>      | <u>198,292</u>                             | <u>496,311</u>      | <u>760,162</u>     | <u>222,982</u>                                     | <u>471,621</u>      |
| Total loans held for investment . . . . .           | <u>\$ 695,645</u>  | <u>\$ 468,591</u>                          | <u>\$3,929,511</u>  | <u>\$5,093,747</u> | <u>\$ 836,062</u>                                  | <u>\$3,562,040</u>  |

The following table presents loan origination and loan sale volumes.

| (in thousands)  | Years Ended December 31, |                     |                      |
|---|--------------------------|---------------------|----------------------|
|   | 2019                     | 2018                | 2017                 |
| Loans originated                                      |                          |                     |                      |
| Real estate   |                          |                     |                      |
| Single family   |                          |                     |                      |
| Originated by HomeStreet <sup>(1)</sup> . . . . .     | \$ 3,105,664             | \$ 5,791,510        | \$ 7,525,248         |
| Originated by WMS Series LLC <sup>(2)</sup> . . . . . | 605,708                  | 517,461             | 566,152              |
| Total single family . . . . .                         | <u>3,711,372</u>         | <u>6,308,971</u>    | <u>8,091,400</u>     |
| Multifamily . . . . .                                 | 1,219,781                | 827,477             | 746,748              |
| Non-owner occupied commercial real estate . . . . .   | 144,339                  | 181,290             | 208,130              |
| Owner occupied commercial real estate . . . . .       | 90,363                   | 52,132              | 121,398              |
| Construction/land development . . . . .               | 800,539                  | 1,144,442           | 1,084,092            |
| Total real estate . . . . .                           | <u>5,966,394</u>         | <u>8,514,312</u>    | <u>10,251,768</u>    |
| Commercial business . . . . .                         | 210,784                  | 213,272             | 227,880              |
| Home equity and other . . . . .                       | 265,794                  | 506,633             | 361,043              |
| Total loans originated . . . . .                      | <u>\$ 6,442,972</u>      | <u>\$ 9,234,217</u> | <u>\$ 10,840,691</u> |
| Loans sold  |                          |                     |                      |
| Single family <sup>(1)</sup> . . . . .                | \$ 3,783,639             | \$ 6,057,784        | \$ 7,508,949         |
| Multifamily DUS <sup>®(3)</sup> . . . . .             | 214,124                  | 225,323             | 347,084              |
| SBA . . . . .   | 12,404                   | 19,414              | 26,841               |
| CRE Non-DUS <sup>®(4)</sup> . . . . .                 | 617,336                  | 346,384             | 321,699              |
| Single family <sup>(4)</sup> . . . . .                | 141,663                  | 243,054             | —                    |
| Total loans sold . . . . .                            | <u>\$ 4,769,166</u>      | <u>\$ 6,891,959</u> | <u>\$ 8,204,573</u>  |

(1) Includes both continuing and discontinued operations.

(2) Loans originated by WMS Series LLC and purchased by HomeStreet Bank.

(3) Fannie Mae Multifamily Delegated Underwriting and Servicing Program (“DUS<sup>®</sup>”) is a registered trademark of Fannie Mae.

(4) Loans originated as Held for Investment.

*Mortgage servicing rights from continuing operations* were \$97.6 million at December 31, 2019 compared to \$103.4 million at December 31, 2018, a decrease of \$5.8 million, or 5.6%. The decrease was primarily due to a decline in single family MSR fair value related to a decline in interest rates.

*Federal Home Loan Bank stock* was \$22.4 million at December 31, 2019 compared to \$45.5 million at December 31, 2018, a decrease of \$23.1 million, or 50.8%. FHLB stock is carried at par value and can only be purchased or redeemed at par value in transactions between the FHLB and its member institutions. Cash dividends received on FHLB stock are reported in other income.

Other assets were \$180.1 million at December 31, 2019, compared to \$171.3 million at December 31, 2018, an increase of \$8.8 million, or 5.2%.

## Deposits

Deposit balances were as follows for the periods indicated:

| (in thousands)  | At December 31, |              |              |
|---|-----------------|--------------|--------------|
|   | 2019            | 2018         | 2017         |
| Noninterest-bearing accounts – checking and savings . . . . . | \$ 704,743      | \$ 612,540   | \$ 579,504   |
| Interest-bearing transaction and savings deposits:            |                 |              |              |
| NOW accounts . . . . .  | 373,832         | 376,137      | 461,349      |
| Statement savings accounts due on demand . . . . .            | 219,182         | 245,795      | 293,858      |
| Money market accounts due on demand . . . . .                 | 2,224,494       | 1,935,516    | 1,834,154    |
| Total interest-bearing transaction and savings deposits . . . | 2,817,508       | 2,557,448    | 2,589,361    |
| Total transaction and savings deposits . . . . .              | 3,522,251       | 3,169,988    | 3,168,865    |
| Certificates of deposit . . . . .                             | 1,614,533       | 1,579,806    | 1,190,689    |
| Noninterest-bearing accounts – other <sup>(1)</sup> . . . . . | 203,175         | 301,614      | 401,398      |
| Total deposits . . . . .                                      | \$ 5,339,959    | \$ 5,051,408 | \$ 4,760,952 |

(1) Includes zero, \$162.8 million and \$225.0 million in servicing deposits related to discontinued operations for the periods ended December 31, 2019, 2018 and 2017, respectively.

Deposits at December 31, 2019 increased \$288.6 million, or 5.7%, from December 31, 2018. The increase in deposits from December 31, 2018 was a result of competitive rates offered on money markets accounts, which increased \$289.0 million, and noninterest bearing accounts — checking and savings, which increased \$92.2 million. The increase also included \$74.5 million in deposits related to the acquisition of a retail deposit branch in San Marcos, San Diego County, California from Silvergate Bank, which was completed in the first quarter of 2019, including \$42.7 million of noninterest-bearing accounts and \$31.8 million of money market and savings accounts. Certificates of deposit increased by \$34.7 million, or 2.2%, since December 31, 2018, with consumer and business accounts increasing \$496.8 million as a result of competitive rates offered and institutional accounts increasing \$57.2 million, offset by a \$518.9 million decline in brokered deposit balances. Consumer deposits can be sensitive to changes in interest rates, therefore, the Company continues to actively monitor the adequacy of its offered deposit rates.

At December 31, 2018, deposits increased \$290.5 million, or 6.1%, from December 31, 2017. Certificates of deposits increased by \$389.1 million, or 32.7% from December 31, 2017. This increase was offset by a decline in non-brokered deposits because rates paid on these deposits increased at a slower pace than market rates.

## Borrowings

FHLB advances were \$346.6 million at December 31, 2019 compared to \$932.6 million at December 31, 2018. FHLB advances may be collateralized by stock in the FHLB, cash, pledged mortgage-backed securities, real estate-secured commercial loans and unencumbered qualifying mortgage loans. The loan portfolio exhibits some seasonality and varies over time and is partly funded by FHLB advances to supplement bank deposit funding. The reduction in advances was largely due to an increase in brokered deposits as well as other deposits and the contraction of the balance sheet which reduced our reliance on wholesale borrowings. As of December 31, 2019, 2018 and 2017, FHLB borrowings had weighted average interest rates of 1.86%, 2.63% and 1.58%, respectively. Of the total FHLB borrowings outstanding as of December 31, 2019, \$341.0 million mature prior to December 31, 2020. We had \$943.3 million and \$492.7 million of additional borrowing capacity with the FHLB as of December 31, 2019 and 2018, respectively.

We may also borrow, on a collateralized basis, from the Federal Reserve Bank of San Francisco (“FRBSF” or “Federal Reserve Bank”). At December 31, 2019 and 2018, we did not have any outstanding borrowings from the FRBSF. Based on the amount of qualifying collateral available, borrowing capacity from the FRBSF was \$267.1 million and \$333.5 million at December 31, 2019 and 2018, respectively. The FRBSF is not contractually required to offer credit to us, and our access to this source for future borrowings may be discontinued at any time.

Long-term debt was \$125.7 million and \$125.5 million at December 31, 2019 and 2018, respectively. The balance at December 31, 2019 represented \$63.8 million of senior notes issued during 2016 and \$61.9 million of junior subordinated debentures issued in prior years. Such debentures were issued in connection with the sale of trust



preferred securities by HomeStreet Statutory Trusts, subsidiaries of HomeStreet, Inc. Trust preferred securities allow investors to buy subordinated debt through a variable interest entity trust that issues preferred securities to third-party investors and uses the cash received to purchase subordinated debt from the issuer. That debt is the sole asset of the trust and the coupon rate on the debt mirrors the dividend rate on the preferred securities. These securities are nonvoting and are not convertible into common stock, and the variable interest entity trust is not consolidated in our financial statements.

### Shareholders' Equity

Shareholders' equity was \$679.7 million at December 31, 2019 compared to \$739.5 million at December 31, 2018. This decrease was primarily related to share repurchases of \$98.5 million during the year ended December 31, 2019, partially offset by other comprehensive income of \$21.8 million and net income of \$17.5 million recognized during the year ended December 31, 2019. Other comprehensive income (loss) represents unrealized gains and losses on the valuation of our available for sale investment securities portfolio at December 31, 2019.

Shareholders' equity, on a per share basis, was \$28.45 per share at December 31, 2019, compared to \$27.39 per share at December 31, 2018.

### Return on Equity and Assets

The following table presents certain information regarding our returns on average equity and average total assets.

|   | Years Ended December 31, |        |        |
|---|--------------------------|--------|--------|
|   | 2019                     | 2018   | 2017   |
| Return on assets <sup>(1)(4)</sup> . . . . .    | 0.25%                    | 0.57%  | 1.05%  |
| Return on equity <sup>(2)(4)</sup> . . . . .    | 2.43%                    | 5.40%  | 10.20% |
| Equity to assets ratio <sup>(3)</sup> . . . . . | 10.17%                   | 10.56% | 10.26% |

- (1) Net income divided by average total assets.
- (2) Net income divided by average common shareholders' equity.
- (3) Average equity divided by average total assets.
- (4) Net income includes both continuing and discontinued operations.

### Off-Balance Sheet Arrangements

In the normal course of business, we are a party to financial instruments with off-balance sheet risk. These financial instruments (which include commitments to originate loans and commitments to purchase loans) include potential credit risk in excess of the amount recognized in the accompanying consolidated financial statements. These transactions are designed to (1) meet the financial needs of our customers, (2) manage our credit, market or liquidity risks, (3) diversify our funding sources, and/or (4) optimize capital.

For more information on off-balance sheet arrangements, see Note 14, *Commitments, Guarantees and Contingencies* to the financial statements of this Form 10-K.

### Commitments, Guarantees and Contingencies

We may incur liabilities under certain contractual agreements contingent upon the occurrence of certain events. Our known contingent liabilities include:

- *Unfunded loan commitments.* We make certain unfunded loan commitments as part of our lending activities that have not been recognized in the Company's financial statements. These include commitments to extend credit made as part of our lending activities on loans we intend to hold in our loans held for investment portfolio. The aggregate amount of these unrecognized unfunded loan commitments existing at December 31, 2019 and 2018 was \$52.8 million and \$33.8 million, respectively.
- *Credit agreements.* We extend secured and unsecured open-end loans to meet the financing needs of our customers. These commitments include unused consumer portfolio lines of \$485.1 million and \$462.0 million as of December 31, 2019 and 2018, respectively, and commercial portfolio lines of

\$722.2 million and \$852.9 million at December 31, 2019 and 2018, respectively. Within the commercial portfolio, undistributed construction loan proceeds, where the Company has an obligation to advance funds for construction progress payments, were \$435.2 million and \$607.2 million at December 31, 2019 and 2018, respectively. The total amounts of unused commitments do not necessarily represent future credit exposure or cash requirements in that commitments may expire without being drawn upon.

- *Interest rate lock commitments.* The Company writes options in the form of interest rate lock commitments on single family mortgage loans that are exercisable at the option of the borrower. We are exposed to market risk on interest rate lock commitments. The fair value of interest rate lock commitments existing at December 31, 2019 and 2018, was \$2.2 million and \$10.3 million, respectively. We mitigate the risk of future changes in the fair value of interest rate lock commitments primarily through the use of forward sale commitments.
- *Credit loss sharing.* We originate, sell and service multifamily loans through the Fannie Mae DUS<sup>®</sup> program. Multifamily loans are sold to Fannie Mae subject to a loss sharing arrangement. HomeStreet Capital services the loans for Fannie Mae and shares in the risk of loss with Fannie Mae under the terms of the DUS<sup>®</sup> contracts. Under the DUS<sup>®</sup> program, the Company and Fannie Mae share losses on a pro rata basis, where the Company is responsible for losses incurred up to one-third of the principal balance on each loan with two-thirds of the loss covered by Fannie Mae. The total principal balance of loans outstanding under the DUS<sup>®</sup> program as of December 31, 2019 and 2018 was \$1.55 billion and \$1.46 billion, respectively, and our loss reserves were \$2.8 million and \$2.5 million as of December 31, 2019 and 2018, respectively.
- *Mortgage repurchase liability.* In our single family lending business, we sell residential mortgage loans to government sponsored and other entities. In addition, the Company pools Federal Housing Administration (“FHA”)-insured and Department of Veterans’ Affairs (“VA”)-guaranteed mortgage loans into Ginnie Mae, Fannie Mae and Freddie Mac guaranteed mortgage-backed securities. We have made representations and warranties that the loans sold meet certain requirements. We may be required to repurchase mortgage loans or indemnify loan purchasers due to defects in the origination process of the loan, such as documentation errors, underwriting errors and judgments, early payment defaults and fraud.

These obligations expose us to mark-to-market and credit losses on the repurchased mortgage loans after accounting for any mortgage insurance that we may receive. Generally, the maximum amount of future payments we would be required to make for breaches of these representations and warranties would be equal to the unpaid principal balance of such loans that are deemed to have defects that were sold to investors plus, in certain circumstances, accrued and unpaid interest on such loans and certain expenses.

We do not typically receive repurchase requests from the FHA or VA. As an originator of FHA-insured or VA-guaranteed loans, we are responsible for obtaining the insurance with FHA or the guarantee with the VA. If we are not able to meet the requirements of FHA to get the loan insured by FHA or guaranteed by VA, we may be unable to sell the loan or be required to repurchase the loan. For loans that are found not to meet the requirements of FHA or VA, through required internal quality control reviews or through agency audits, we may be required to indemnify FHA or VA against loss. The loans remain in Ginnie Mae pools unless and until they qualify for voluntary repurchase by the Company. In general, once an FHA or VA loan becomes 90 days past due, we repurchase the FHA or VA loan to minimize the cost of interest advances on the loan. If the loan is cured through borrower efforts or through loss mitigation activities, the loan may be resold into another Ginnie Mae pool. The Company’s liability for mortgage loan repurchase losses incorporates probable losses associated with such indemnification.

As of December 31, 2019 and 2018, the total principal balance of loans sold on a servicing-retained basis that were subject to the terms and conditions of these representations and warranties totaled \$7.10 billion and \$20.24 billion, respectively. The recorded mortgage repurchase liability for loans sold on a servicing-retained and a servicing-released basis was \$2.9 million and \$3.1 million at December 31, 2019 and 2018, respectively. The Company’s mortgage repurchase liability reflects management’s estimate of losses for loans sold on a servicing-retained and servicing-released basis for which we could have a repurchase obligation. Actual repurchase losses of \$475 thousand, \$1.8 million and \$541 thousand were incurred for the years ended December 31, 2019, 2018 and 2017, respectively.

- *Leases.* Prior to the adoption of ASU No. 2016-02 in the first quarter of 2019, rental expense under non-cancelable operating leases totaled \$27.7 million and \$26.1 million for the years ended 2018 and 2017, respectively.
- *Small business investment company (“SBIC”) investment funds.* Between 2016 and 2019 we entered into agreements to invest \$24.9 million over time in SBIC investment funds. At December 31, 2019 and 2018 we had unfunded commitments of \$15.7 million and \$11.1 million, respectively, related to these agreements.
- *Low income housing tax credit partnerships.* We are entered into agreements to invest \$30.1 million in partnerships that encourage and assist corporations in investing in the ownership of residential rental property located throughout the United States that qualify for the Low-Income Housing Tax Credit. At December 31, 2019 and 2018, we had \$2.8 million and \$7.9 million, respectively, in unfunded commitments related to this agreement.
- *Tax exempt bond partnerships.* Between 2018 and 2019, we entered into partnerships to invest \$10.0 million in Tax Exempt LIHTC Debt Fund with anticipated Community Reinvestment Act consideration. At December 31, 2019 and 2018, we had \$5.0 million and \$4.9 million, respectively, in unfunded commitments related to this agreement.

### ***Derivative Counterparty Credit Risk***

Derivative financial instruments expose us to credit risk in the event of nonperformance by counterparties to such agreements. This risk consists primarily of the termination value of agreements where we are in a favorable position. Credit risk related to derivative financial instruments is considered within the fair value measurement of the instrument. We manage the credit risk associated with our various derivative agreements through counterparty credit review, counterparty exposure limits and monitoring procedures. From time to time, we may provide collateral to certain counterparties for amounts in excess of exposure limits as outlined by the counterparty credit policies of the parties. In addition, we obtain collateral in connection with our derivative contracts. Required collateral levels vary depending on the credit risk rating and the type of counterparty. Generally, we may accept collateral in the form of cash, U.S. Treasury securities and other marketable securities. Based on provisions contained in master netting agreements, we net cash collateral received against derivative assets. We also pledge collateral on our own derivative positions which can be applied against derivative liabilities. We have entered into agreements with derivative counterparties that include netting arrangements whereby the counterparties are entitled to settle certain positions on a net basis. At December 31, 2019 and 2018, our net exposure to the credit risk of derivative counterparties was \$8.8 million and \$19.8 million, respectively.

### ***Contractual Obligations***

The following table summarizes our significant fixed and determinable contractual obligations, within the categories described below, by payment date or contractual maturity as of December 31, 2019. The payment amounts for financial instruments shown below represent principal amounts contractually due to the recipient and do not include any unamortized premiums or discounts, or other similar carrying value adjustments.

| <b>(in thousands)</b>                             | <b>Within<br/>one year</b> | <b>After one<br/>but within<br/>three years</b> | <b>After three<br/>but within<br/>five years</b> | <b>More than<br/>five years</b> | <b>Total</b>        |
|---|----------------------------|---|--|---------------------------------|---------------------|
| Deposits <sup>(1)</sup> . . . . .                 | \$ 5,007,837               | \$ 302,538                                      | \$ 29,455  | \$ 129                          | \$ 5,339,959        |
| FHLB advances . . . . .                           | 341,000                    | —   | —  | 5,590                           | 346,590             |
| Long term debt . . . . .                          | —                          | —   | —  | 65,000                          | 65,000              |
| Trust preferred securities <sup>(2)</sup> . . . . | —                          | —   | —  | 61,857                          | 61,857              |
| Interest <sup>(3)</sup> . . . . .                 | 23,689                     | 17,858  | 13,921   | 30,764                          | 86,232              |
| Operating and financing leases . .                | 16,668                     | 28,198  | 21,715   | 72,854                          | 139,435             |
| Purchase obligations <sup>(4)</sup> . . . . .     | 3,405                      | 2,200   | 14   | —                               | 5,619               |
| <b>Total . . . . .</b>                            | <b>\$ 5,392,599</b>        | <b>\$ 350,794</b>                               | <b>\$ 65,105</b>                                 | <b>\$ 236,194</b>               | <b>\$ 6,044,692</b> |

(1) Deposits with indeterminate maturities, such as demand, savings and money market accounts, are reflected as obligations due less than one year.

- (2) Trust preferred securities are included in long-term debt on the consolidated statements of financial condition.
- (3) Represents the future interest obligations related to interest-bearing time deposits and long-term debt in the normal course of business. These interest obligations assume no early debt redemption. We estimated variable interest rate payments using December 31, 2019 rates, which we held constant until maturity.
- (4) Represents agreements to purchase goods or services.

## Enterprise Risk Management

All financial institutions manage and control a variety of business and financial risks that can significantly affect their financial performance. Among these risks are credit risk; market risk, which includes interest rate risk and price risk; liquidity risk; and operational risk. We are also subject to risks associated with compliance/legal, strategic and reputational matters.

Our Board of Directors (the “Board”) and executive management have overall and ultimate responsibility for management of these risks. The Board, its committees and senior managers oversee the management of various risks. The Company utilizes a risk management framework which includes three lines of defense. The business units, which are the first line of defense, have responsibility to identify, monitor, control and escalate risks in their respective areas. The second line of defense, comprised of independent risk management functions, operating under the Chief Risk Officer, establishes the risk governance framework and assesses, tests and reports on risks by business unit and on an enterprise-wide basis. The legal department, under the supervision of our General Counsel, also operates as a part of our second line of defense. Our internal audit department provides independent assurance that the risk framework, policies, procedures and controls are appropriate and operating as intended and is considered the third line of defense. The Chief Risk Officer reports directly to the Enterprise Risk Management Committee of the Board and is responsible for oversight of enterprise risk management, compliance, Bank Secrecy Act, quality control, model risk management and regulatory affairs functions. The Chief Audit Officer reports directly to the Audit Committee of the Board.

The Board and its committees work closely with senior management in overseeing risk. Management recommends the appropriate level of risk in our strategic and business plans and in our board-approved credit and operating policies and has responsibility for measuring, managing, controlling and reporting on risks. The Board and its committees oversee the monitoring and controlling of significant risk exposures, including the policies governing risk management. The Board authorizes its committees to take any action on its behalf as described in their respective charter or as otherwise delegated by the Board, except as otherwise specifically reserved by law, regulation, other committees’ charters or the Company’s charter documents for action solely by the full board or another board committee. These committees include:

- *Audit Committee.* The Audit Committee oversees the policies and management activities relating to our financial reporting and internal and external audit.
- *Finance Committee.* The Finance Committee oversees the consolidated Company’s and subsidiaries’ activities related to balance sheet management, major financial risks including market, interest rate, liquidity and funding risks and counterparty risk management, including trading limits.
- *Credit Committee.* The Credit Committee oversees the annual Loan Review Plan, lending policies, credit performance and trends, the allowance for loan and lease losses policy, the allowance for credit losses policy, loan loss reserves, large borrower exposure and concentrations, and approval of counterparties.
- *Human Resources and Corporate Governance Committee.* The Human Resources and Corporate Governance Committee (the “HRCG”) of HomeStreet, Inc. reviews all matters concerning our human resources, compensation, benefits, and corporate governance. HRCG’s policy objectives are to ensure that HomeStreet and its operating subsidiaries meet their corporate objectives of attracting and retaining a well-qualified workforce, to oversee our human resource strategies and policies and to ensure processes are in place to assure compliance with employment laws and regulations.
- *Enterprise Risk Management Committee.* The Enterprise Risk Management Committee (the “ERM”) oversees the Company’s enterprise-wide risk management framework, including evaluating management’s identification and assessment of the significant risks and the related infrastructure to address such risks and monitors the Company’s compliance with its risk appetite and risk limit structures

and effective remediation of non-compliance on an ongoing, enterprise-wide, and individual entity basis. The ERMC also oversees policies and management activities relating to operational, regulatory, legal and compliance risks. The ERMC does not duplicate the risk oversight of the Board's other committees, but rather helps ensure end-to-end understanding and oversight of all risk issues in one Board committee and enhances the Board's and management's understanding of the Company's aggregate enterprise-wide risk profile.

The following is a discussion of our risk management practices. The risks related to credit, liquidity, interest rate and price warrant in-depth discussion due to the significance of these risks and the impact they may have on our business.

### **Credit Risk Management**

Credit risk is defined as the risk to current or anticipated earnings or capital arising from an obligor's failure to meet the terms of any contract with the Company, including those in the lending, securities and derivative portfolios, or otherwise perform as agreed. Factors relating to the degree of credit risk include the size of the asset or transaction, the contractual terms of the related documents, the credit characteristics of the borrower, the channel through which assets are acquired, the features of loan products or derivatives, the existence and strength of guarantor support, the availability, quality and adequacy of any underlying collateral and the economic environment after the loan is originated or the asset is acquired. Our overall portfolio credit risk is also impacted by asset concentrations within the portfolio.

Our credit risk management process is primarily centrally governed. Our overall credit process includes comprehensive credit policies, judgmental or statistical credit underwriting, frequent and detailed risk measurement and modeling, risk-based reporting and loan review, quality control and audit processes. In addition, we have an independent loan review function that reports directly to the Credit Committee of the Board, and internal auditors and regulatory examiners review and perform detailed tests of our credit underwriting, loan administration and allowance processes.

The Chief Credit Officer's primary responsibilities include directing the activities of the credit risk management function as it relates to the loan portfolio, overseeing loan portfolio performance, ensuring compliance with regulatory requirements and the Company's established credit policies, standards and limits, determining the reasonableness of our allowance for loan losses, reviewing and approving large credit exposures and delegating credit approval authorities. Credit administrators who oversee the lines of business have both transaction approval authority and governance authority for the approval of procedures within established policies, standards and limits. The Chief Credit Officer's role also includes direct oversight of appraisal and environmental functions. The Chief Credit Officer reports directly to the Chief Executive Officer.

The Loan Committee provides direction and oversight within our risk management framework. The committee seeks to ensure effective portfolio risk analysis and policy review and to support sound implementation of defined business and risk strategies. Additionally, the Loan Committee periodically approves credit larger than authority delegated to the members of the Loan Committee, either individually or in combination. The members of the Loan Committee are the Chief Executive Officer, Chief Credit Officer, and the Commercial Banking Director. The Deputy Chief Credit Officer serves as an Alternate Member of the Loan Committee.

The loan review department's primary responsibility includes the review of our loan portfolios to provide an independent assessment of credit quality, portfolio oversight and credit management, including accuracy of loan grading. Loan review also conducts targeted credit-related reviews and credit process reviews at the request of the Board and management and reviews a sample of newly originated loans for compliance with closing conditions and accuracy of loan grades. Loan review reports directly to the Credit Committee and administratively to the Chief Credit Officer.

Credit limits for capital markets counterparties, including derivative counterparties, are defined in the Company's Counterparty Risk policy, which is reviewed annually by the Bank Loan Committee, with final approval by the Board Credit Committee. The treasury function is responsible for directing the activities related to securities and derivative portfolios, including overseeing derivative portfolio performance and ensuring compliance with established credit policies, standards and limits. The Chief Investment Officer and Treasurer reports directly to both the Chief Executive Officer and Chief Financial Officer.



## *Appraisal Policy*

An integral part of our credit risk management process is the valuation of the collateral supporting the loan portfolio, which is primarily comprised of loans secured by real estate. We maintain a Board-approved appraisal policy for real estate appraisals that conforms to the Uniform Standards of Professional Appraisal Practice and FDIC regulatory requirements. Our Chief Appraiser, who is independent of the business units, is responsible for maintaining the appraisal policy and recommending changes to the policy subject to Loan Committee and Credit Committee approval.

### *Real Estate*

Our appraisal policy requires that market value appraisals or evaluations be prepared prior to new loan origination, subsequent loan transactions and for loan monitoring purposes. Our appraisals are prepared by independent third-party appraisers and our staff appraisers. Evaluations are prepared by independent and qualified third-party providers. We use state certified and licensed appraisers with appropriate expertise as it relates to the subject property type and location. All appraisals contain an “as is” market value estimate based upon the definition of market value as set forth in the FDIC appraisal regulations. For applicable property types, we may also obtain “upon completion” and “upon stabilization” values. The appraisal standard for non-tract development properties (four units or less) is the retail market value of individual units. For tract development properties with five or more units, the appraisal standard is the bulk market value of the tract as a whole.

We review all appraisals and evaluations prior to the closing of a loan transaction. Commercial and single family real estate appraisals and evaluations are reviewed by either our in-house appraisal staff or by independent and qualified third-party appraisers.

For loan monitoring and problem loan management purposes our appraisal practices are as follows:

- We generally do not perform valuation monitoring for pass-graded credits because we believe they carry minimal credit risk.
- For commercial loans secured by real estate that are graded special mention, an appraisal is performed at the time of loan downgrade, and an appraisal or evaluation is performed at least every two years thereafter, depending upon property complexity, market area, market conditions, intended use and other considerations.
- For commercial loans secured by real estate that are graded substandard or doubtful and for all OREO properties, we require an independent third-party appraisal at the time of downgrade or transfer to OREO and at least every twelve months thereafter until disposition or loan upgrade. For loans where foreclosure is probable, an appraisal or evaluation is prepared at the intervening six-month period prior to foreclosure.
- For performing consumer portfolio loans secured by real estate that are graded special mention or substandard, property values are determined quarterly from automated valuation model services employed by the Bank.
- In addition, if we determine that market conditions, changes to the property, changes in the intended use of the property or other factors indicate an appraisal is no longer reliable, we will also obtain an updated appraisal or evaluation and assess whether a change in collateral value requires an additional adjustment to carrying value.

### *Other*

Our appraisal requirements for loans not secured by real estate, such as business loans secured by equipment, include valuation methods ranging from evidence of sales price or verification with a recognized guide for new equipment to a valuation opinion by a professional appraiser for multiple pieces of used equipment.

## Loan Modifications

We have modified loans for various reasons for borrowers not experiencing financial difficulties. Those modifications generally are short-term extensions granted to allow time for receipt of appraisals and other financial reporting information to facilitate underwriting of loan extensions and renewals.

Our policy allows modifications for borrowers with financial difficulty when there is a well-conceived and prudent workout plan that supports the ultimate collection of principal and interest. We may enter into a loan modification to help maximize the likelihood of success for a given workout strategy. In each case we also assess whether it is in the best interests of the Company to foreclose or modify the terms. We have made concessions such as interest-only payment terms, interest rate reductions, principal and interest forgiveness and payment restructures. For single family mortgage borrowers, we have generally provided for granting payment restructures, and to a lesser extent, interest rate reductions for periods of three years or less to reduce payments and provide the borrower time to resolve their financial difficulties. In each case, we carefully analyze the borrower's current financial condition to assure that they can make the modified payment.

## Asset Quality and Nonperforming Assets

Our credit quality remained strong with nonperforming assets ("NPAs") remaining low at \$14.3 million, or 0.21% of total assets at December 31, 2019, compared to \$12.1 million, or 0.17% of total assets at December 31, 2018. The deterioration from December 31, 2018 was primarily due to an increase in commercial nonperforming loans.

Nonaccrual loans of \$12.9 million, or 0.25% of total loans at December 31, 2019, increased \$1.2 million, or 10.7%, from \$11.6 million, or 0.23% of total loans at December 31, 2018. Net recoveries in 2019 were \$424 thousand compared with net recoveries of \$797 thousand in 2018 and net recoveries of \$3.1 million in 2017.

At December 31, 2019, our loans held for investment portfolio, net of the allowance for loan losses, was \$5.07 billion, a decrease of \$2.6 million from December 31, 2018. The allowance for loan losses was \$41.8 million, or 0.82% of loans held for investment, compared to \$41.5 million, or 0.81% of loans held for investment at December 31, 2018.

The Company had a reversal of provision for credit losses of \$500 thousand for the year ended December 31, 2019 compared to a \$3.0 million of provision for credit losses for the year ended December 31, 2018 and a \$750 thousand provision for credit losses for the year ended December 31, 2017. Management considers the current level of the allowance for loan losses to be appropriate to cover estimated incurred losses inherent within our loans held for investment portfolio.

For information regarding the activity on our allowance for credit losses, which includes the reserves for unfunded commitments, and the amounts that were collectively and individually evaluated for impairment, see Note 6, *Loans and Credit Quality* to the financial statements of this Form 10-K.

The allowance for credit losses represents management's estimate of the incurred credit losses inherent within our loan portfolio. For further discussion related to credit policies and estimates see "*Critical Accounting Policies and Estimates — Allowance for Loan Losses*".

The following tables present the recorded investment, unpaid principal balance and related allowance for impaired loans, broken down by those with and those without a specific reserve.

| (in thousands)                                     | At December 31, 2019           |   |                   |
|--|--------------------------------|---|-------------------|
|  | Recorded Investment            | Unpaid Principal Balance <sup>(2)</sup> | Related Allowance |
| Impaired loans:                                    |                                |   |                   |
| Loans with no related allowance recorded . . . . . | \$ 66,326 <sup>(1)</sup>       | \$ 67,200                               | \$ —              |
| Loans with an allowance recorded . . . . .         | 2,425                          | 2,804                                   | 153               |
| Total . . . . .                                    | <u>\$ 68,751<sup>(1)</sup></u> | <u>\$ 70,004</u>                        | <u>\$ 153</u>     |

| (in thousands)                                     | At December 31, 2018           |   |                   |
|--|--------------------------------|---|-------------------|
|  | Recorded Investment            | Unpaid Principal Balance <sup>(2)</sup> | Related Allowance |
| Impaired loans:                                    |                                |   |                   |
| Loans with no related allowance recorded . . . . . | \$ 71,237 <sup>(1)</sup>       | \$ 73,113                               | \$ —              |
| Loans with an allowance recorded . . . . .         | 1,847                          | 1,847                                   | 233               |
| Total . . . . .                                    | <u>\$ 73,084<sup>(1)</sup></u> | <u>\$ 74,960</u>                        | <u>\$ 233</u>     |

| (in thousands)                                     | At December 31, 2017           |   |                   |
|--|--------------------------------|---|-------------------|
|  | Recorded Investment            | Unpaid Principal Balance <sup>(2)</sup> | Related Allowance |
| Impaired loans:                                    |                                |   |                   |
| Loans with no related allowance recorded . . . . . | \$ 78,696 <sup>(1)(3)</sup>    | \$ 80,904                               | \$ —              |
| Loans with an allowance recorded . . . . .         | 5,150                          | 5,288                                   | 289               |
| Total . . . . .                                    | <u>\$ 83,846<sup>(1)</sup></u> | <u>\$ 86,192</u>                        | <u>\$ 289</u>     |

- (1) Includes \$59.8 million, \$65.8 million and \$69.6 million in single family performing troubled debt restructurings (“TDRs”) at December 31, 2019, 2018 and 2017, respectively.
- (2) Unpaid principal balance does not include partial charge-offs, purchase discounts and premiums or nonaccrual interest paid. Related allowance is calculated on net book balances not unpaid principal balances.
- (3) Includes \$231 thousand of fair value option loans.

The Company had impaired loan balances of \$68.8 million, \$73.1 million and \$83.8 million at December 31, 2019, 2018 and 2017, respectively. At December 31, 2019 the Company had 313 impaired loan relationships compared to 349 at December 31, 2018. Included in the total impaired loan relationship amounts were 290 single family TDR loan relationships totaling \$61.5 million at December 31, 2019 and 320 single family TDR relationships totaling \$67.6 million at December 31, 2018. The decrease in the number of impaired loan relationships at December 31, 2019 from 2018 was primarily due to a decrease in the number of single family impaired loans. At December 31, 2019, there were 284 single family impaired relationships totaling \$59.8 million that were performing per their current contractual terms. Additionally, the impaired loan balance included \$48.9 million of loans insured by the FHA or guaranteed by the VA. The average recorded investment in these loans for the year ended December 31, 2019 was \$74.7 million, compared to \$75.8 million for the year ended December 31, 2018. Impaired loans of \$2.4 million and \$1.8 million had a valuation allowance of \$153 thousand and \$233 thousand at December 31, 2019 and 2018, respectively.

The following table presents the allowance for credit losses, including reserves for unfunded commitments, by loan class.

| (dollars in thousands)                              | At December 31,  |   |  |                  |   |  |                  |   |  |
|---|------------------|---|--|------------------|---|--|------------------|---|--|
|   | 2019             |   |  | 2018             |   |  | 2017             |   |  |
|   | Amount           | Percent of Allowance to Total Allowance | Loan Category as a % of Total Loans <sup>(1)</sup> | Amount           | Percent of Allowance to Total Allowance | Loan Category as a % of Total Loans <sup>(1)</sup> | Amount           | Percent of Allowance to Total Allowance | Loan Category as a % of Total Loans <sup>(1)</sup> |
| Consumer loans                                      |                  |   |  |                  |   |  |                  |   |  |
| Single family . . . . .                             | \$ 6,450         | 15%                                     | 21%  | \$ 8,217         | 19%                                     | 27%  | \$ 9,412         | 24%                                     | 30%  |
| Home equity and other . . . . .                     | 6,843            | 16                                      | 10   | 7,712            | 18                                      | 11   | 7,081            | 18                                      | 10   |
|   | <u>13,293</u>    | <u>31</u>                               | <u>31</u>  | <u>15,929</u>    | <u>37</u>                               | <u>38</u>  | <u>16,493</u>    | <u>42</u>                               | <u>40</u>  |
| Commercial real estate loans                        |                  |   |  |                  |   |  |                  |   |  |
| Non-owner occupied commercial real estate . . . . . | 7,249            | 17                                      | 18   | 5,496            | 13                                      | 14   | 4,755            | 12                                      | 14   |
| Multifamily . . . . .                               | 7,015            | 17                                      | 20   | 5,754            | 13                                      | 18   | 3,895            | 10                                      | 16   |
| Construction/land development . .                   | 8,679            | 20                                      | 14   | 9,539            | 22                                      | 16   | 8,677            | 22                                      | 15   |
|   | <u>22,943</u>    | <u>54</u>                               | <u>52</u>  | <u>20,789</u>    | <u>48</u>                               | <u>48</u>  | <u>17,327</u>    | <u>44</u>                               | <u>45</u>  |
| Commercial and industrial loans                     |                  |   |  |                  |   |  |                  |   |  |
| Owner occupied commercial real estate . . . . .     | 3,640            | 8                                       | 9  | 3,282            | 8                                       | 8  | 2,960            | 8                                       | 9  |
| Commercial business . . . . .                       | 2,961            | 7                                       | 8  | 2,913            | 7                                       | 6  | 2,336            | 6                                       | 6  |
|   | <u>6,601</u>     | <u>15</u>                               | <u>17</u>  | <u>6,195</u>     | <u>15</u>                               | <u>14</u>  | <u>5,296</u>     | <u>14</u>                               | <u>15</u>  |
| Total allowance for credit losses . . .             | <u>\$ 42,837</u> | <u>100%</u>                             | <u>100%</u>  | <u>\$ 42,913</u> | <u>100%</u>                             | <u>100%</u>  | <u>\$ 39,116</u> | <u>100%</u>                             | <u>100%</u>  |

(1) Excludes loans held for investment balances that are carried at fair value.

*Allowance for loan losses* (which excludes the allowance for unfunded commitments) represented 0.82% of loans held for investment at December 31, 2019 compared to 0.81% at December 31, 2018, which primarily reflected the continuing strong credit quality of the Company's loan portfolio. Excluding acquired loans, the allowance for loan losses was 0.86% of loans held for investment at December 31, 2019 compared to 0.85% at December 31, 2018. Nonperforming assets were \$14.3 million, or 0.21% of total assets at December 31, 2019, compared to \$12.1 million, or 0.17% of total assets at December 31, 2018.

The following tables present the composition of TDRs by accrual and nonaccrual status.

| (dollars in thousands)                 | At December 31, 2019 |                                 |                 |                                    |                  |                               |
|--|----------------------|---------------------------------|-----------------|------------------------------------|------------------|-------------------------------|
|  | Accrual              | Number of accrual relationships | Nonaccrual      | Number of nonaccrual relationships | Total            | Total number of relationships |
| Consumer                               |                      |                                 |                 |                                    |                  |                               |
| Single family <sup>(1)</sup> . . . . . | \$ 59,809            | 284                             | \$ 1,694        | 6                                  | \$ 61,503        | 290                           |
| Home equity and other . . . . .        | 853                  | 11                              | 9               | 1                                  | 862              | 12                            |
|  | <u>60,662</u>        | <u>295</u>                      | <u>1,703</u>    | <u>7</u>                           | <u>62,365</u>    | <u>302</u>                    |
| Commercial and industrial loans        |                      |                                 |                 |                                    |                  |                               |
| Commercial business . . . . .          | 48                   | 2                               | 222             | 1                                  | 270              | 3                             |
|  | <u>48</u>            | <u>2</u>                        | <u>222</u>      | <u>1</u>                           | <u>270</u>       | <u>3</u>                      |
|  | <u>\$ 60,710</u>     | <u>297</u>                      | <u>\$ 1,925</u> | <u>8</u>                           | <u>\$ 62,635</u> | <u>305</u>                    |

(1) Includes loan balances insured by the FHA or guaranteed by the VA of \$48.9 million at December 31, 2019.

| At December 31, 2018                               |                  |                                       |                 |  |                  |                                     |
|--|------------------|---------------------------------------|-----------------|--|------------------|-------------------------------------|
| (dollars in thousands)                             | Accrual          | Number<br>of accrual<br>relationships | Nonaccrual      | Number of<br>nonaccrual<br>relationships | Total            | Total<br>number of<br>relationships |
| Consumer   |                  |                                       |                 |  |                  |                                     |
| Single family <sup>(1)</sup> . . . . .             | \$ 65,835        | 314                                   | \$ 1,740        | 6  | \$ 67,575        | 320                                 |
| Home equity and other . . . . .                    | 1,237            | 16                                    | —               | —  | 1,237            | 16                                  |
|  | <u>67,072</u>    | <u>330</u>                            | <u>1,740</u>    | <u>6</u>                                 | <u>68,812</u>    | <u>336</u>                          |
| Commercial real estate loans                       |                  |                                       |                 |  |                  |                                     |
| Multifamily . . . . .                              | 492              | 1                                     | —               | —  | 492              | 1                                   |
| Construction/land development . .                  | 726              | 1                                     | —               | —  | 726              | 1                                   |
|  | <u>1,218</u>     | <u>2</u>                              | <u>—</u>        | <u>—</u>                                 | <u>1,218</u>     | <u>2</u>                            |
| Commercial and industrial loans                    |                  |                                       |                 |  |                  |                                     |
| Owner occupied commercial real<br>estate . . . . . | 846              | 1                                     | —               | —  | 846              | 1                                   |
| Commercial business . . . . .                      | 103              | 3                                     | 164             | 1  | 267              | 4                                   |
|  | <u>949</u>       | <u>4</u>                              | <u>164</u>      | <u>1</u>                                 | <u>1,113</u>     | <u>5</u>                            |
|  | <u>\$ 69,239</u> | <u>336</u>                            | <u>\$ 1,904</u> | <u>7</u>                                 | <u>\$ 71,143</u> | <u>\$ 343</u>                       |

(1) Includes loan balances insured by the FHA or guaranteed by the VA of \$52.4 million at December 31, 2018.

| At December 31, 2017                               |                  |                                       |                 |  |                  |                                     |
|--|------------------|---------------------------------------|-----------------|--|------------------|-------------------------------------|
| (in thousands)                                     | Accrual          | Number<br>of accrual<br>relationships | Nonaccrual      | Number of<br>nonaccrual<br>relationships | Total            | Total<br>number of<br>relationships |
| Consumer   |                  |                                       |                 |  |                  |                                     |
| Single family <sup>(1)</sup> . . . . .             | \$ 69,555        | 280                                   | \$ 2,451        | 11                                       | \$ 72,006        | 291                                 |
| Home equity and other . . . . .                    | 1,254            | 16                                    | 36              | 2  | 1,290            | 18                                  |
|  | <u>70,809</u>    | <u>296</u>                            | <u>2,487</u>    | <u>13</u>                                | <u>73,296</u>    | <u>309</u>                          |
| Commercial real estate loans                       |                  |                                       |                 |  |                  |                                     |
| Multifamily . . . . .                              | 507              | 1                                     | —               | —  | 507              | 1                                   |
| Construction/land development . .                  | 454              | 1                                     | —               | —  | 454              | 1                                   |
|  | <u>961</u>       | <u>2</u>                              | <u>—</u>        | <u>—</u>                                 | <u>961</u>       | <u>2</u>                            |
| Commercial and industrial loans                    |                  |                                       |                 |  |                  |                                     |
| Owner occupied commercial real<br>estate . . . . . | 876              | 1                                     | —               | —  | 876              | 1                                   |
| Commercial business . . . . .                      | 377              | 3                                     | 62              | 1  | 439              | 4                                   |
|  | <u>1,253</u>     | <u>4</u>                              | <u>62</u>       | <u>1</u>                                 | <u>1,315</u>     | <u>5</u>                            |
|  | <u>\$ 73,023</u> | <u>302</u>                            | <u>\$ 2,549</u> | <u>14</u>                                | <u>\$ 75,572</u> | <u>316</u>                          |

(1) Includes loan balances insured by the FHA or guaranteed by the VA of \$46.7 million at December 31, 2017.

The Company had TDR balances of \$62.6 million, \$71.1 million and \$75.6 million at December 31, 2019, 2018 and 2017, respectively. TDR balances continue to decline and included \$48.9 million, \$52.4 million and \$46.7 million of loan balances insured by the FHA or guaranteed by the VA as of December 31, 2019, 2018 and 2017, respectively. TDR loans within the loans held for investment portfolio and the related reserves are included in the impaired loan tables above. The Company had no unfunded commitments related to TDR loans at December 31, 2019, and 2017, and \$15 thousand at December 31, 2018.



| (in thousands)   | At December 31,  |                  |                  |                  |                  |
|--|------------------|------------------|------------------|------------------|------------------|
|  | 2019             | 2018             | 2017             | 2016             | 2015             |
| Loans accounted for on a nonaccrual basis: <sup>(1)</sup>            |                  |                  |                  |                  |                  |
| Consumer   |                  |                  |                  |                  |                  |
| Single family . . . . .  | \$ 5,364         | \$ 8,493         | \$ 11,091        | \$ 12,717        | \$ 12,119        |
| Home equity and other. . . . .                                       | 1,160            | 948              | 1,404            | 1,571            | 1,576            |
|  | <u>6,524</u>     | <u>9,441</u>     | <u>12,495</u>    | <u>14,288</u>    | <u>13,695</u>    |
| Commercial real estate loans   |                  |                  |                  |                  |                  |
| Non-owner occupied commercial real estate. . . . .                   | —                | —                | —                | 871              | —                |
| Multifamily . . . . .  | —                | —                | 302              | 337              | 119              |
| Construction/land development . . . . .                              | —                | 72               | 78               | 1,376            | 339              |
|  | <u>—</u>         | <u>72</u>        | <u>380</u>       | <u>2,584</u>     | <u>458</u>       |
| Commercial and industrial loans                                      |                  |                  |                  |                  |                  |
| Owner occupied commercial real estate . . . . .                      | 2,891            | 374              | 640              | 1,256            | 2,341            |
| Commercial business . . . . .  | 3,446            | 1,732            | 1,526            | 2,414            | 674              |
|  | <u>6,337</u>     | <u>2,106</u>     | <u>2,166</u>     | <u>3,670</u>     | <u>3,015</u>     |
| Total loans on nonaccrual . . . . .                                  | 12,861           | 11,619           | 15,041           | 20,542           | 17,168           |
| Other real estate owned . . . . .                                    | 1,393            | 455              | 664              | 5,243            | 7,531            |
| Total nonperforming assets . . . . .                                 | <u>\$ 14,254</u> | <u>\$ 12,074</u> | <u>\$ 15,705</u> | <u>\$ 25,785</u> | <u>\$ 24,699</u> |
| Loans 90 days or more past due and accruing <sup>(2)</sup> . . . . . | <u>\$ 19,702</u> | <u>\$ 39,116</u> | <u>\$ 37,171</u> | <u>\$ 40,486</u> | <u>\$ 36,612</u> |
| Accruing TDR loans . . . . .   | \$ 60,710        | \$ 69,239        | \$ 73,023        | \$ 76,581        | \$ 84,411        |
| Nonaccrual TDR loans. . . . .  | 1,925            | 1,904            | 2,549            | 4,874            | 3,931            |
| Total TDR loans . . . . .  | <u>\$ 62,635</u> | <u>\$ 71,143</u> | <u>\$ 75,572</u> | <u>\$ 81,455</u> | <u>\$ 88,342</u> |
| Allowance for loan losses as a percent of nonaccrual loans . . . . . | 324.80%          | 356.92%          | 251.63%          | 165.52%          | 170.54%          |
| Nonaccrual loans as a percentage of total loans . . . . .            | 0.25%            | 0.23%            | 0.33%            | 0.53%            | 0.53%            |
| Nonperforming assets as a percentage of total assets . . . . .       | 0.21%            | 0.17%            | 0.23%            | 0.41%            | 0.50%            |

(1) If interest on nonaccrual loans under the original terms had been recognized, such income is estimated to have been \$1.9 million, \$1.4 million and \$1.5 million for the years ended December 31, 2019, 2018 and 2017.

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

Delinquent loans and other real estate owned by loan type consisted of the following.

| (in thousands)                                  | At December 31, 2019  |                       |                  |                                       |                      |                         |
|---|-----------------------|-----------------------|------------------|---------------------------------------|----------------------|-------------------------|
|   | 30 – 59 Days Past Due | 60 – 89 Days Past Due | Nonaccrual       | 90 Days or More Past Due and Accruing | Total Past Due Loans | Other Real Estate Owned |
| Consumer loans                                  |                       |                       |                  |                                       |                      |                         |
| Single family . . . . .                         | \$ 5,694              | \$ 4,261              | \$ 5,364         | \$ 19,702 <sup>(1)</sup>              | \$ 35,021            | \$ 1,393                |
| Home equity and other. . . . .                  | 837                   | 372                   | 1,160            | —                                     | 2,369                | —                       |
|   | <u>6,531</u>          | <u>4,633</u>          | <u>6,524</u>     | <u>19,702</u>                         | <u>37,390</u>        | <u>1,393</u>            |
| Commercial and industrial loans                 |                       |                       |                  |                                       |                      |                         |
| Owner occupied commercial real estate . . . . . | —                     | —                     | 2,891            | —                                     | 2,891                | —                       |
| Commercial business . . . . .                   | 44                    | —                     | 3,446            | —                                     | 3,490                | —                       |
|   | <u>44</u>             | <u>—</u>              | <u>6,337</u>     | <u>—</u>                              | <u>6,381</u>         | <u>—</u>                |
| Total . . . . .                                 | <u>\$ 6,575</u>       | <u>\$ 4,633</u>       | <u>\$ 12,861</u> | <u>\$ 19,702</u>                      | <u>\$ 43,771</u>     | <u>\$ 1,393</u>         |

(1) FHA-insured and VA-guaranteed single family loans that are 90 days or more past due are maintained on accrual status if they are determined to have little to no risk of loss. At December 31, 2019, these past due loans totaled \$19.7 million.

| At December 31, 2018                               |                          |                          |                  |  |                            |                               |
|--|--------------------------|--------------------------|------------------|--|----------------------------|-------------------------------|
| (in thousands)                                     | 30 – 59 Days<br>Past Due | 60 – 89 Days<br>Past Due | Nonaccrual       | 90 Days<br>or More<br>Past Due<br>and Accruing | Total<br>Past Due<br>Loans | Other<br>Real Estate<br>Owned |
| Consumer loans                                     |                          |                          |                  |  |                            |                               |
| Single family . . . . .                            | \$ 9,725                 | \$ 3,653                 | \$ 8,493         | \$ 39,116 <sup>(1)</sup>                       | \$ 60,987                  | \$ 455                        |
| Home equity and other. . . . .                     | 145                      | 100                      | 948              | —  | 1,193                      | —                             |
|  | <u>9,870</u>             | <u>3,753</u>             | <u>9,441</u>     | <u>39,116</u>                                  | <u>62,180</u>              | <u>455</u>                    |
| Commercial real estate loans                       |                          |                          |                  |  |                            |                               |
| Construction/land development . .                  | —                        | —                        | 72               | —  | 72                         | —                             |
|  | —                        | —                        | 72               | —  | 72                         | —                             |
| Commercial and industrial loans                    |                          |                          |                  |  |                            |                               |
| Owner occupied commercial real<br>estate . . . . . | —                        | —                        | 374              | —  | 374                        | —                             |
| Commercial business. . . . .                       | —                        | —                        | 1,732            | —  | 1,732                      | —                             |
|  | —                        | —                        | 2,106            | —  | 2,106                      | —                             |
| <b>Total . . . . .</b>                             | <b>\$ 9,870</b>          | <b>\$ 3,753</b>          | <b>\$ 11,619</b> | <b>\$ 39,116</b>                               | <b>\$ 64,358</b>           | <b>\$ 455</b>                 |

(1) FHA-insured and VA-guaranteed single family loans that are 90 days or more past due are maintained on accrual status as they have little to no risk of loss. At December 31, 2018, these past due loans totaled \$39.1 million.

| At December 31, 2017                               |                          |                          |                  |  |                            |                               |
|--|--------------------------|--------------------------|------------------|--|----------------------------|-------------------------------|
| (in thousands)                                     | 30 – 59 Days<br>Past Due | 60 – 89 Days<br>Past Due | Nonaccrual       | 90 Days<br>or More<br>Past Due<br>and Accruing | Total<br>Past Due<br>Loans | Other<br>Real Estate<br>Owned |
| Consumer loans                                     |                          |                          |                  |  |                            |                               |
| Single family . . . . .                            | \$ 10,493                | \$ 4,437                 | \$ 11,091        | \$ 37,171 <sup>(1)</sup>                       | \$ 63,192                  | \$ 664                        |
| Home equity and other. . . . .                     | 750                      | 20                       | 1,404            | —  | 2,174                      | —                             |
|  | <u>11,243</u>            | <u>4,457</u>             | <u>12,495</u>    | <u>37,171</u>                                  | <u>65,366</u>              | <u>664</u>                    |
| Commercial real estate loans                       |                          |                          |                  |  |                            |                               |
| Multifamily . . . . .                              | —                        | —                        | 302              | —  | 302                        | —                             |
| Construction/land development . .                  | 641                      | —                        | 78               | —  | 719                        | —                             |
|  | <u>641</u>               | <u>—</u>                 | <u>380</u>       | <u>—</u>                                       | <u>1,021</u>               | <u>—</u>                      |
| Commercial and industrial loans                    |                          |                          |                  |  |                            |                               |
| Owner occupied commercial real<br>estate . . . . . | —                        | —                        | 640              | —  | 640                        | —                             |
| Commercial business. . . . .                       | 377                      | —                        | 1,526            | —  | 1,903                      | —                             |
|  | <u>377</u>               | <u>—</u>                 | <u>2,166</u>     | <u>—</u>                                       | <u>2,543</u>               | <u>—</u>                      |
| <b>Total . . . . .</b>                             | <b>\$ 12,261</b>         | <b>\$ 4,457</b>          | <b>\$ 15,041</b> | <b>\$ 37,171</b>                               | <b>\$ 68,930</b>           | <b>\$ 664</b>                 |

(1) FHA-insured and VA-guaranteed single family loans that are 90 days or more past due are maintained on accrual status as they have little to no risk of loss. At December 31, 2017, these past due loans totaled \$37.2 million.

The following tables present the single family loan held for investment portfolio by original FICO score.

| At December 31, 2019 |                       |                           |
|----------------------|-----------------------|---------------------------|
| Greater Than         | Less Than or Equal To | Percentage <sup>(1)</sup> |
| N/A <sup>(2)</sup>   | N/A <sup>(2)</sup>    | 1.9%                      |
| <                    | 500                   | 0.1%                      |
| 500                  | 549                   | 0.1%                      |
| 550                  | 599                   | 0.6%                      |
| 600                  | 649                   | 3.8%                      |
| 650                  | 699                   | 13.4%                     |
| 700                  | 749                   | 31.5%                     |
| 750                  | >                     | 48.6%                     |
|                      | TOTAL                 | 100.0%                    |

(1) Percentages based on aggregate loan amounts.

(2) Information is not available.

| At December 31, 2018 |                       |                           |
|----------------------|-----------------------|---------------------------|
| Greater Than         | Less Than or Equal To | Percentage <sup>(1)</sup> |
| N/A <sup>(2)</sup>   | N/A <sup>(2)</sup>    | 1.8%                      |
| <                    | 500                   | 0.1%                      |
| 500                  | 549                   | 0.1%                      |
| 550                  | 599                   | 0.5%                      |
| 600                  | 649                   | 4.2%                      |
| 650                  | 699                   | 12.7%                     |
| 700                  | 749                   | 31.4%                     |
| 750                  | >                     | 49.2%                     |
|                      | TOTAL                 | 100.0%                    |

(1) Percentages based on aggregate loan amounts.

(2) Information is not available.

### ***Loan Underwriting Standards***

Our underwriting standards for single family and home equity loans require evaluating and understanding a borrower's credit, collateral and ability to repay the loan. Credit is determined based on how well a borrower manages their current and prior debts, documented by a credit report that provides credit scores and the borrower's current and past information about their credit history. Collateral is based on the type and use of property, occupancy and market value, largely determined by property appraisals or evaluations in accordance with our appraisal policy. A borrower's ability to repay the loan is based on several factors, including employment, income, current debt, assets and level of equity in the property. We also consider loan-to-property value and debt-to-income ratios, amount of liquid financial reserves, loan amount and lien position in assessing whether to originate a loan. Single family and home equity borrowers are particularly susceptible to downturns in economic trends that negatively affect housing prices and demand and levels of unemployment.

For commercial, multifamily and construction loans, we consider the same factors with regard to the borrower and the guarantors. In addition, we evaluate liquidity, net worth, leverage, other outstanding indebtedness of the borrower, the quality and reliability of cash expected to flow through the borrower (including the outflow to other lenders) and prior known experiences with the borrower. We use this information to assess financial capacity, profitability and experience. Ultimate repayment of these loans is sensitive to interest rate changes, general economic conditions, liquidity and availability of long-term financing.

#### *Additional considerations for commercial permanent loans secured by real estate:*

Our underwriting standards for commercial permanent loans generally require that the loan-to-value ratio for these loans not exceed 75% of appraised value or discounted cash flow value, as appropriate, and that commercial properties attain debt coverage ratios (net operating income divided by annual debt servicing) of 1.25 or better.

Our underwriting standards for multifamily residential permanent loans generally require that the loan-to-value ratio for these loans not exceed 80% of appraised value, cost, or discounted cash flow value, as appropriate, and that multifamily residential properties attain debt coverage ratios of 1.15 or better. However, underwriting standards can be influenced by competition and other factors. We endeavor to maintain the highest practical underwriting standards while balancing the need to remain competitive in our lending practices.

*Additional considerations for commercial construction loans secured by real estate:*

We originate a variety of real estate construction loans. Underwriting guidelines for these loans vary by loan type but include loan-to-value limits, term limits, loan advance limits and pre-leasing requirements, as applicable.

Our underwriting guidelines for commercial real estate construction loans generally require that the loan-to-value ratio not exceed 75% and stabilized debt coverage ratios of 1.25 or better.

Our underwriting guidelines for multifamily residential construction loans generally require that the loan-to-value ratio not exceed 80% and stabilized debt coverage ratios of 1.20 or better.

Our underwriting guidelines for single family residential construction loans to builders generally require that the loan-to-value ratio not exceed 85%.

As noted above, underwriting standards can be influenced by competition and other factors. However, we endeavor to maintain the highest practical underwriting standards while balancing the need to remain competitive in our lending practices.

## **Liquidity and Capital Resources**

Liquidity risk management is primarily intended to ensure we are able to maintain sources of cash to adequately fund operations and meet our obligations, including demands from depositors, draws on lines of credit and paying any creditors, on a timely and cost-effective basis, in various market conditions. Our liquidity profile is influenced by changes in market conditions, the composition of the balance sheet and risk tolerance levels. HomeStreet, Inc., HomeStreet Capital (“HSC”) and the Bank have established liquidity guidelines and operating plans that detail the sources and uses of cash and liquidity.

HomeStreet, Inc., HSC and the Bank have different funding needs and sources of liquidity and separate regulatory capital requirements.

### ***HomeStreet, Inc.***

The main source of liquidity for HomeStreet, Inc. is proceeds from dividends from the Bank and HSC. HomeStreet, Inc. has raised capital through the issuance of common stock, senior debt and trust preferred securities. Additionally, we also have an available line of credit from which we can borrow up to \$30.0 million. At December 31, 2019, we did not have an outstanding balance on this line of credit.

Historically, the main cash outflows have been distributions to shareholders, interest and principal payments to creditors and payments of operating expenses. HomeStreet, Inc.’s ability to pay dividends to shareholders depends substantially on dividends received from the Bank. We did not pay a dividend to shareholders in 2019, 2018 or 2017. In January 2020, our Board of Directors adopted a dividend policy for the consideration of regular quarterly cash dividends on shares of HomeStreet, Inc. common stock and declared a quarterly dividend for the first quarter of 2020 at \$0.15 per share, and was paid on February 21, 2020 to shareholders of record as of the close of market on February 5, 2020.

In 2019, HomeStreet, Inc.’s Board of Directors authorized two stock repurchase programs of up to \$100 million of our common stock as well as a privately negotiated stock repurchase from a group of investors. The Bank completed dividends to HomeStreet, Inc. of \$110.0 million as the primary source of liquidity to fund the two repurchase programs, although repurchases may be funded from one or a combination of existing cash balances, free cash flow and other available liquidity sources. Under these programs in 2019 we repurchased 1,494,858 shares pursuant to those plans. In addition, on July 11, 2019 we repurchased 1,692,401 shares, outside of these repurchase plans, in a single transaction from an investor group. In the first quarter of 2020, the Board of Directors approved additional stock repurchase programs for up to \$35 million of our common stock, which we expect to begin implementing in the first or second quarter of 2020.

## ***HomeStreet Capital Corporation***

HomeStreet Capital generates positive cash flow from operations from its servicing fee income on the DUS<sup>®</sup> portfolio, net of its costs to service the DUS<sup>®</sup> portfolio. Additional uses are HomeStreet Capital's costs to purchase the servicing rights on new production from the Bank. Minimum liquidity and reporting requirements for DUS<sup>®</sup> lenders such as HomeStreet Capital are set by Fannie Mae. HomeStreet Capital's liquidity management therefore consists of meeting Fannie Mae requirements and its own operational requirements.

## ***HomeStreet Bank***

The Bank's primary sources of funds include deposits, advances from the FHLB, repayments and prepayments of loans, proceeds from the sale of loans and investment securities, interest from our loans and investment securities and capital contributions from HomeStreet, Inc. We have also raised short-term funds through the sale of securities under agreements to repurchase and federal funds purchased. While scheduled principal repayments on loans are a relatively predictable source of funds, deposit inflows and outflows and loan prepayments are greatly influenced by interest rates, economic conditions and competition. The Bank uses the primary liquidity ratio as a measure of liquidity. The primary liquidity ratio is defined as net cash, short-term investments and other marketable assets as a percent of net deposits and short-term borrowings. At December 31, 2019, our primary liquidity ratio was 18.7% compared with 19.4% at December 31, 2018 and 18.1% at December 31, 2017.

At December 31, 2019, 2018 and 2017, the Bank had available borrowing capacity of \$943.3 million, \$492.7 million and \$579.2 million, respectively, from the FHLB, and \$267.1 million, \$333.5 million and \$331.5 million, respectively, from the Federal Reserve Bank of San Francisco.

## ***Cash Flows***

For the years ended December 31, 2019, 2018 and 2017, cash, cash equivalents and restricted cash decreased \$706 thousand, decreased \$15.3 million and increased \$17.5 million, respectively. The following discussion highlights the major activities and transactions that affected our cash flows during these periods.

### *Cash flows from operating activities*

The Company's operating assets and liabilities are used to support our lending activities, including the origination and sale of mortgage loans. For the year ended December 31, 2019, net cash of \$258.8 million was provided by operating activities, primarily from proceeds from the sale of loans held for sale, partially offset by the net fair value adjustment and gain on sale of loans held for sale and the recognition of deferred taxes from the sale of mortgage servicing rights. We believe that cash flows from operations, available cash balances and our ability to generate cash through short-term debt are sufficient to fund our operating liquidity needs. For the year ended December 31, 2018, net cash of \$286.0 million was provided by operating activities, as our cash proceeds from the sale of loans exceeded cash used to fund loans held for sale production. For the year ended December 31, 2017, net cash of \$159.3 million was provided by operating activities, as our cash proceeds from the sale of loans exceeded cash used to fund loans held for sale production.

### *Cash flows from investing activities*

The Company's investing activities primarily include available-for-sale securities and loans originated as held for investment. For the year ended December 31, 2019, net cash of \$83.9 million was provided by investing activities, primarily due to \$769.4 million proceeds from sale of loans held for investment, \$184.9 million from proceeds from sale of investment securities, \$182.2 million proceeds from our disposal of discontinued operations and \$145.8 million from principal repayments and maturities of investment securities, partially offset by \$822.5 million cash used for the origination of portfolio loans net of principal repayments and \$330.5 million of cash used for the purchase of investment securities. For the year ended December 31, 2018, net cash of \$565.2 million was used in investing activities, primarily due to \$1.13 billion cash used for the origination of portfolio loans net of principal repayments and \$189.7 million of cash used for the purchase of investment securities, and \$9.7 million used for the purchase of property and equipment, partially offset by \$46.1 million from proceeds from sale of investment securities, \$548.8 million proceeds from sale of loans held for investment and \$106.8 million from principal repayments and maturities of investment securities. For the year ended December 31, 2017, net cash of



\$556.2 million was used in investing activities, primarily due to \$998.6 million cash used for the origination of portfolio loans net of principal repayments, \$368.1 million purchases of investment securities, and \$42.3 million used for the purchases of property and equipment, partially offset by \$397.5 million from proceeds from the sale of investment securities, \$324.7 million from proceeds from the sale of loans held for investment and \$105.8 million from principal repayments and maturities of investment securities.

#### *Cash flows from financing activities*

The Company's financing activities are primarily related to customer deposits and net proceeds from the FHLB. For the year ended December 31, 2019, net cash of \$343.5 million was used in financing activities, primarily resulting from \$586.0 million net repayment from FHLB advances, \$106.0 million net proceeds from Fed Funds purchased and \$98.5 million in repurchases of our common stock, partially offset by \$213.6 million growth in deposits. For the year ended December 31, 2018, net cash of \$263.9 million was provided by financing activities, primarily resulting from a \$290.2 million growth in deposits, partially offset by \$46.5 million net repayment from FHLB advances. For the year ended December 31, 2017, net cash of \$414.4 million was provided by financing activities, primarily resulting from \$309.8 million growth in deposits and \$111.0 million net proceeds from FHLB advances.

#### **Capital Management**

In July 2013, federal banking regulators (including the FDIC and the FRB) adopted new capital rules (as used in this section, the "Rules"). The Rules apply to both depository institutions (such as the Bank) and their holding companies (such as the Company). The Rules reflect, in part, certain standards initially adopted by the Basel Committee on Banking Supervision in December 2010 (which standards are commonly referred to as "Basel III") as well as requirements contemplated by the Dodd-Frank Act. Since 2015, the Rules have applied to both the Company and the Bank.

The Rules recognize three components, or tiers, of capital: common equity Tier 1 capital, additional Tier 1 capital and Tier 2 capital. Common equity Tier 1 capital generally consists of retained earnings and common stock instruments (subject to certain adjustments), as well as accumulated other comprehensive income ("AOCI") except to the extent that the Company and the Bank exercise a one-time irrevocable option to exclude certain components of AOCI. Both the Company and the Bank elected this one-time option in 2015 to exclude certain components of AOCI. Additional Tier 1 capital generally includes non-cumulative preferred stock and related surplus subject to certain adjustments and limitations. Tier 2 capital generally includes certain capital instruments (such as subordinated debt) and portions of the amounts of the allowance for loan and lease losses, subject to certain requirements and deductions. The term "Tier 1 capital" means common equity Tier 1 capital plus additional Tier 1 capital, and the term "total capital" means Tier 1 capital plus Tier 2 capital.

The Rules generally measure an institution's capital using four capital measures or ratios. The common equity Tier 1 capital ratio is the ratio of the institution's common equity Tier 1 capital to its total risk-weighted assets. The Tier 1 risk-based capital ratio is the ratio of the institution's total Tier 1 capital to its total risk-weighted assets. The total risk-based capital ratio is the ratio of the institution's total capital to its total risk-weighted assets. The Tier 1 leverage capital ratio is the ratio of the institution's Tier 1 capital to its average total consolidated assets. To determine risk-weighted assets, assets of an institution are generally placed into a risk category and given a percentage weight based on the relative risk of that category. The percentage weights range from 0% to 1,250%. An asset's risk-weighted value will generally be its percentage weight multiplied by the asset's value as determined under generally accepted accounting principles. In addition, certain off-balance-sheet items are converted to balance-sheet credit equivalent amounts, and each amount is then assigned to one of the risk categories. An institution's federal regulator may require the institution to hold more capital than would otherwise be required under the Rules if the regulator determines that the institution's capital requirements under the Rules are not commensurate with the institution's credit, market, operational or other risks.

The Rules set forth the manner in which certain capital elements are determined, including but not limited to, requiring certain deductions related to mortgage servicing rights and deferred tax assets. Holding companies with less than \$15 billion in total assets as of December 31, 2009 (which includes the Company) are permitted under the rules to continue to include trust preferred securities issued prior to May 19, 2010 in Tier 1 capital, generally up to 25% of other Tier 1 capital. Because our trust preferred securities were issued prior to May 19, 2010, we include those in our Tier 1 capital calculations.

The Rules made changes in the methods of calculating certain risk-based assets, which in turn affects the calculation of risk-based ratios. Higher or more sensitive risk weights are assigned to various categories of assets, including commercial real estate, credit facilities that finance the acquisition, development or construction of real property, certain exposures or credits that are 90 days past due or are nonaccrual, foreign exposures, certain corporate exposures, securitization exposures, equity exposures and in certain cases mortgage servicing rights and deferred tax assets.

Certain calculations under the rules related to deductions from capital had phase-in periods through 2017. Specifically, the capital treatment of mortgage servicing rights was to be phased in through the transition periods. Under the prior rules, the Bank deducted 10% of the value of MSR (net of deferred tax) from Tier 1 capital ratios. However, under Basel III, the Bank and Company must deduct a much larger portion of the value of MSR from Tier 1 capital.

- MSRs in excess of 10% of Tier 1 capital before threshold based deductions must be deducted from common equity. The disallowable portion of MSR was phased in incrementally (40% in 2015; 60% in 2016; 80% in 2017 and beyond).
- In addition, the combined balance of MSR and deferred tax assets is limited to approximately 15% of the Bank's and the Company's common equity Tier 1 capital. These combined assets must be deducted from common equity to the extent that they exceed the 15% threshold.
- Any portion of the Bank's and the Company's MSR that are not deducted from the calculation of common equity Tier 1 are subject to a 100% risk weight.

Both the Company and the Bank began compliance with the Rules on January 1, 2015. The phase-in of the conservation buffer began in 2016 and had it not been halted, it would have taken full effect on January 1, 2019. Certain calculations under the Rules will also have phase-in periods. We believe that the current capital levels of the Company and the Bank are in compliance with the standards under the Rules including the conservation buffer.

At December 31, 2019, the Bank's capital ratios continued to meet the regulatory capital category of "well capitalized" as defined by the FDIC's prompt corrective action rules.

The following tables present regulatory capital information for HomeStreet, Inc. and HomeStreet Bank for the December 31, 2019, 2018 and 2017 respectively, under Basel III.

| <b>At December 31, 2019</b>   |               |              |  |              |  |              |
|---|---------------|--------------|--|--------------|--|--------------|
| <b>HomeStreet Bank</b><br><b>(dollars in thousands)</b>             | <b>Actual</b> |              | <b>For Minimum Capital Adequacy Purposes</b> |              | <b>To Be Categorized As “Well Capitalized” Under Prompt Corrective Action Provisions</b> |              |
|   | <b>Amount</b> | <b>Ratio</b> | <b>Amount</b>                                | <b>Ratio</b> | <b>Amount</b>  | <b>Ratio</b> |
|   |               |              |  |              |  |              |
| Tier 1 leverage capital<br>(to average assets) . . . . .            | \$ 712,596    | 10.56%       | \$ 269,930                                   | 4.0%         | \$ 337,413   | 5.0%         |
| Common equity tier 1 capital<br>(to risk-weighted assets) . . . . . | 712,596       | 13.50        | 237,451                                      | 4.5          | 342,985  | 6.5          |
| Tier 1 risk-based capital<br>(to risk-weighted assets) . . . . .    | 712,596       | 13.50        | 316,602                                      | 6.0          | 422,136  | 8.0          |
| Total risk-based capital<br>(to risk-weighted assets) . . . . .     | 758,303       | 14.37        | 422,136                                      | 8.0          | 527,669  | 10.0         |

| <b>At December 31, 2019</b>   |               |              |  |              |  |              |
|---|---------------|--------------|--|--------------|--|--------------|
| <b>HomeStreet, Inc.</b><br><b>(dollars in thousands)</b>            | <b>Actual</b> |              | <b>For Minimum Capital Adequacy Purposes</b> |              | <b>To Be Categorized As “Well Capitalized” Under Prompt Corrective Action Provisions</b> |              |
|   | <b>Amount</b> | <b>Ratio</b> | <b>Amount</b>                                | <b>Ratio</b> | <b>Amount</b>  | <b>Ratio</b> |
|   |               |              |  |              |  |              |
| Tier 1 leverage capital<br>(to average assets) . . . . .            | \$ 691,323    | 10.16%       | \$ 272,253                                   | 4.0%         | \$ 340,316   | 5.0%         |
| Common equity tier 1 capital<br>(to risk-weighted assets) . . . . . | 631,323       | 11.43        | 248,523                                      | 4.5          | 358,977  | 6.5          |
| Tier 1 risk-based capital<br>(to risk-weighted assets) . . . . .    | 691,323       | 12.52        | 331,364                                      | 6.0          | 441,818  | 8.0          |
| Total risk-based capital<br>(to risk-weighted assets) . . . . .     | 739,812       | 13.40        | 441,818                                      | 8.0          | 552,273  | 10.0         |

| <b>At December 31, 2018</b>   |               |              |  |              |  |              |
|---|---------------|--------------|--|--------------|--|--------------|
| <b>HomeStreet Bank</b><br><b>(dollars in thousands)</b>             | <b>Actual</b> |              | <b>For Minimum Capital Adequacy Purposes</b> |              | <b>To Be Categorized As “Well Capitalized” Under Prompt Corrective Action Provisions</b> |              |
|   | <b>Amount</b> | <b>Ratio</b> | <b>Amount</b>                                | <b>Ratio</b> | <b>Amount</b>  | <b>Ratio</b> |
|   |               |              |  |              |  |              |
| Tier 1 leverage capital<br>(to average assets) . . . . .            | \$ 707,710    | 10.15%       | \$ 278,898                                   | 4.0%         | \$ 348,622   | 5.0%         |
| Common equity tier 1 capital<br>(to risk-weighted assets) . . . . . | 707,710       | 13.82        | 230,471                                      | 4.5          | 332,902  | 6.5          |
| Tier 1 risk-based capital<br>(to risk-weighted assets) . . . . .    | 707,710       | 13.82        | 307,295                                      | 6.0          | 409,726  | 8.0          |
| Total risk-based capital<br>(to risk-weighted assets) . . . . .     | 753,742       | 14.72        | 409,726                                      | 8.0          | 512,158  | 10.0         |

| At December 31, 2018  |  |            |  |            |  |            |
|---|--|------------|--|------------|--|------------|
| HomeStreet, Inc.<br>(dollars in thousands)                          | Actual   |            | For Minimum Capital<br>Adequacy Purposes |            | To Be Categorized As<br>“Well Capitalized” Under<br>Prompt Corrective<br>Action Provisions |            |
|   | Amount   | Ratio      | Amount                                   | Ratio      | Amount   | Ratio      |
|   | Tier 1 leverage capital<br>(to average assets) . . . . . | \$ 667,301 | 9.51%                                    | \$ 280,592 | 4.0%   | \$ 350,740 |
| Common equity tier 1 capital<br>(to risk-weighted assets) . . . . . | 607,388  | 11.26      | 242,832                                  | 4.5        | 350,757  | 6.5        |
| Tier 1 risk-based capital<br>(to risk-weighted assets) . . . . .    | 667,301  | 12.37      | 323,776                                  | 6.0        | 431,701  | 8.0        |
| Total risk-based capital<br>(to risk-weighted assets) . . . . .     | 715,848  | 13.27      | 431,701                                  | 8.0        | 539,626  | 10.0       |

| At December 31, 2017  |  |            |  |            |  |            |
|---|--|------------|--|------------|--|------------|
| HomeStreet Bank<br>(dollars in thousands)                           | Actual   |            | For Minimum Capital<br>Adequacy Purposes |            | To Be Categorized As<br>“Well Capitalized” Under<br>Prompt Corrective<br>Action Provisions |            |
|   | Amount   | Ratio      | Amount                                   | Ratio      | Amount   | Ratio      |
|   | Tier 1 leverage capital<br>(to average assets) . . . . . | \$ 649,864 | 9.67%                                    | \$ 268,708 | 4.0%   | \$ 335,885 |
| Common equity tier 1 capital<br>(to risk-weighted assets) . . . . . | 649,864  | 13.22      | 221,201                                  | 4.5        | 319,512  | 6.5        |
| Tier 1 risk-based capital<br>(to risk-weighted assets) . . . . .    | 649,864  | 13.22      | 294,935                                  | 6.0        | 393,246  | 8.0        |
| Total risk-based capital<br>(to risk-weighted assets) . . . . .     | 688,981  | 14.02      | 393,246                                  | 8.0        | 491,558  | 10.0       |

| At December 31, 2017  |  |            |  |            |  |            |
|---|--|------------|--|------------|--|------------|
| HomeStreet, Inc.<br>(dollars in thousands)                          | Actual   |            | For Minimum Capital<br>Adequacy Purposes |            | To Be Categorized As<br>“Well Capitalized” Under<br>Prompt Corrective<br>Action Provisions |            |
|   | Amount   | Ratio      | Amount                                   | Ratio      | Amount   | Ratio      |
|   | Tier 1 leverage capital<br>(to average assets) . . . . . | \$ 614,624 | 9.12%                                    | \$ 269,534 | 4.0%   | \$ 336,918 |
| Common equity tier 1 capital<br>(to risk-weighted assets) . . . . . | 555,120  | 9.86       | 253,293                                  | 4.5        | 365,868  | 6.5        |
| Tier 1 risk-based capital<br>(to risk-weighted assets) . . . . .    | 614,624  | 10.92      | 337,724                                  | 6.0        | 450,299  | 8.0        |
| Total risk-based capital<br>(to risk-weighted assets) . . . . .     | 653,741  | 11.61      | 450,299                                  | 8.0        | 562,873  | 10.0       |

### Impact of Inflation

The consolidated financial statements presented in this Form 10-K have been prepared in accordance with U.S. GAAP, which requires the measurement of financial position and operating results in terms of historical dollar amounts or market value without considering the changes in the relative purchasing power of money over time due to inflation. The impact of inflation is reflected in the cost of our operations as incurred. Unlike industrial companies, nearly all of our assets and liabilities are monetary in nature. As a result, interest rates have a greater impact on our performance than do the effects of general levels of inflation.

### Accounting Developments

See Financial Statements and Supplementary Data — Note 1, *Summary of Significant Accounting Policies* for a discussion of accounting developments.

## ITEM 7A QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

### Market Risk Management

Market risk is defined as the sensitivity of income, fair value measurements and capital to changes in interest rates, foreign currency exchange rates, commodity prices and other relevant market rates or prices. The primary market risks to which we are exposed are price and interest rate risks. Price risk is defined as the risk to current or anticipated earnings or capital arising from changes in the value of either assets or liabilities that are entered into as part of distributing or managing risk. Interest rate risk is defined as risk to current or anticipated earnings or capital arising from movements in interest rates.

For the Company, price and interest rate risks arise from the financial instruments and positions we hold. This includes loans, mortgage servicing rights, investment securities, deposits, borrowings, long-term debt and derivative financial instruments. Due to the nature of our current operations, we are not subject to foreign currency exchange or commodity price risk. Our real estate loan portfolio is subject to risks associated with the local economies of our various markets and, in particular, the regional economy of the western United States, including Hawaii.

Our price and interest rate risks are managed by the Bank's Asset/Liability Management Committee ("ALCO"), a management committee that identifies and manages the sensitivity of earnings or capital to changing interest rates to achieve our overall financial objectives. ALCO is a management-level committee whose members include the Chief Investment Officer, acting as the chair, the Chief Executive Officer, Chief Financial Officer and other members of management. The committee meets monthly and is responsible for:

- understanding the nature and level of the Company's interest rate risk and interest rate sensitivity;
- assessing how that risk fits within our overall business strategies;
- ensuring an appropriate level of rigor and sophistication in the risk management process for the overall level of risk;
- complying with and reviewing the asset/liability management policy; and
- formulating and implementing strategies to improve balance sheet mix and earnings.

The Finance Committee of the Bank's Board provides oversight of the asset/liability management process, reviews the results of interest rate risk analysis and approves submission of the relevant policies to the Board.

The spread between the yield on interest-earning assets and the cost of interest-bearing liabilities and the relative dollar amounts of these assets and liabilities are the principal items affecting net interest income. Changes in net interest rates (interest rate risk) are influenced to a significant degree by the repricing characteristics of assets and liabilities (timing risk), the relationship between various rates (basis risk), customer options (option risk) and changes in the shape of the yield curve (time-sensitive risk). We manage the available-for-sale investment securities portfolio while maintaining a balance between risk and return. The Company's funding strategy is to grow core deposits while we efficiently supplement using wholesale borrowings.

We estimate the sensitivity of our net interest income to changes in market interest rates using an interest rate simulation model that includes assumptions related to the level of balance sheet growth, deposit repricing characteristics and the rate of prepayments for multiple interest rate change scenarios. Interest rate sensitivity depends on certain repricing characteristics in our interest-earnings assets and interest-bearing liabilities, including the maturity structure of assets and liabilities and their repricing characteristics during the periods of changes in market interest rates. Effective interest rate risk management seeks to ensure both assets and liabilities respond to changes in interest rates within an acceptable timeframe, minimizing the impact of interest rate changes on net interest income and capital. Interest rate sensitivity is measured as the difference between the volume of assets and liabilities, at a point in time, that are subject to repricing at various time horizons, known as interest rate sensitivity gaps.



The following table presents sensitivity gaps for these different intervals.

| (dollars in thousands)  | December 31, 2019    |                            |                             |                             |                            |                     |                     | Non-Rate-Sensitive  | Total      |
|---|----------------------|----------------------------|-----------------------------|-----------------------------|----------------------------|---------------------|---------------------|---------------------|------------|
|   | 3 Mos. or Less       | More Than 3 Mos. to 6 Mos. | More Than 6 Mos. to 12 Mos. | More Than 12 Mos. to 3 Yrs. | More Than 3 Yrs. to 5 Yrs. | More Than 5 Yrs.    |                     |                     |            |
| Interest-earning assets:  |                      |                            |                             |                             |                            |                     |                     |                     |            |
| Cash & cash equivalents . . . . .   | \$ 57,880            | \$ —                       | \$ —                        | \$ —                        | \$ —                       | \$ —                | \$ —                | \$ —                | \$ 57,880  |
| FHLB Stock . . . . .  | —                    | —                          | —                           | —                           | —                          | 22,399              | —                   | —                   | 22,399     |
| Investment securities <sup>(1)</sup> . . . . .  | 69,452               | 39,517                     | 69,145                      | 198,061                     | 154,045                    | 412,930             | —                   | —                   | 943,150    |
| Mortgage loans held for sale . . . . .  | 208,177              | —                          | —                           | —                           | —                          | —                   | —                   | —                   | 208,177    |
| Loans held for investment <sup>(1)</sup> . . . . .  | 1,546,926            | 360,223                    | 590,862                     | 1,125,030                   | 900,890                    | 590,625             | —                   | —                   | 5,114,556  |
| Total interest-earning assets . . . . .   | 1,882,435            | 399,740                    | 660,007                     | 1,323,091                   | 1,054,935                  | 1,025,954           | —                   | —                   | 6,346,162  |
| Non-interest-earning assets . . . . .   | —                    | —                          | —                           | —                           | —                          | —                   | —                   | 437,645             | 437,645    |
| Assets of discontinued operations . . . . .   | —                    | —                          | —                           | —                           | —                          | —                   | —                   | \$ 28,628           | 28,628     |
| Total assets . . . . .  | <u>\$ 1,882,435</u>  | <u>\$ 399,740</u>          | <u>\$ 660,007</u>           | <u>\$ 1,323,091</u>         | <u>\$ 1,054,935</u>        | <u>\$ 1,025,954</u> | <u>\$ 466,273</u>   | <u>\$ 6,812,435</u> |            |
| Interest-bearing liabilities:   |                      |                            |                             |                             |                            |                     |                     |                     |            |
| NOW accounts <sup>(2)</sup> . . . . .   | \$ 373,832           | \$ —                       | \$ —                        | \$ —                        | \$ —                       | \$ —                | \$ —                | \$ —                | \$ 373,832 |
| Statement savings accounts <sup>(2)</sup> . . . . .   | 219,182              | —                          | —                           | —                           | —                          | —                   | —                   | —                   | 219,182    |
| Money market accounts <sup>(2)</sup> . . . . .  | 2,224,494            | —                          | —                           | —                           | —                          | —                   | —                   | —                   | 2,224,494  |
| Certificates of deposit . . . . .   | 779,445              | 202,196                    | 335,823                     | 268,785                     | 28,282                     | 2                   | —                   | —                   | 1,614,533  |
| Federal funds purchased and securities sold under agreements to repurchase . . . . .                    | 125,000              | —                          | —                           | —                           | —                          | —                   | —                   | —                   | 125,000    |
| FHLB advances . . . . .   | 341,000              | —                          | —                           | —                           | —                          | 5,590               | —                   | —                   | 346,590    |
| Long-term debt <sup>(3)</sup> . . . . .   | 60,650               | —                          | —                           | —                           | —                          | 65,000              | —                   | —                   | 125,650    |
| Total interest-bearing liabilities . . . . .  | 4,123,603            | 202,196                    | 335,823                     | 268,785                     | 28,282                     | 70,592              | —                   | —                   | 5,029,281  |
| Non-interest bearing liabilities . . . . .  | —                    | —                          | —                           | —                           | —                          | —                   | —                   | 1,100,828           | 1,100,828  |
| Liabilities of discontinued operations . . . . .  | —                    | —                          | —                           | —                           | —                          | —                   | —                   | 2,603               | 2,603      |
| Equity . . . . .  | —                    | —                          | —                           | —                           | —                          | —                   | —                   | 679,723             | 679,723    |
| Total liabilities and shareholders' equity . . . . .  | <u>\$ 4,123,603</u>  | <u>\$ 202,196</u>          | <u>\$ 335,823</u>           | <u>\$ 268,785</u>           | <u>\$ 28,282</u>           | <u>\$ 70,592</u>    | <u>\$ 1,783,154</u> | <u>\$ 6,812,435</u> |            |
| Interest sensitivity gap . . . . .  | <u>\$(2,241,168)</u> | <u>\$ 197,544</u>          | <u>\$ 324,184</u>           | <u>\$ 1,054,306</u>         | <u>\$ 1,026,653</u>        | <u>\$ 955,362</u>   | —                   | —                   |            |
| Cumulative interest sensitivity gap . . . . .   | <u>\$(2,241,168)</u> | <u>\$(2,043,624)</u>       | <u>\$(1,719,440)</u>        | <u>\$( 665,134)</u>         | <u>\$ 361,519</u>          | <u>\$ 1,316,881</u> | —                   | —                   |            |
| Cumulative interest sensitivity gap as a percentage of total assets . . . . .                           | (33)%                | (30)%                      | (25)%                       | (10)%                       | 5%                         | 19%                 | —                   | —                   |            |
| Cumulative interest-earning assets as a percentage of cumulative interest-bearing liabilities . . . . . | 46%                  | 53%                        | 63%                         | 87%                         | 107%                       | 126%                | —                   | —                   |            |

- (1) Based on contractual maturities, repricing dates and forecasted principal payments assuming normal amortization and, where applicable, prepayments.
- (2) Assumes 100% of interest-bearing non-maturity deposits are subject to repricing in three months or less.
- (3) Based on contractual maturity.

As of December 31, 2019, the Bank's cumulative interest sensitivity gap was positive, resulting in an asset-sensitive position. Therefore, net interest income would be expected to rise in the long term if interest rates were to rise without changing the slope of the yield curve. The Bank is liability-sensitive in the "three months or less" period which generally indicates that net interest income would be expected to fall in the short term if interest rates were to rise, though deposit interest rate increases generally lag market rate increases.

Changes in the mix of interest-earning assets or interest-bearing liabilities can either increase or decrease the net interest margin, without affecting interest rate sensitivity. In addition, the interest rate spread between an earning asset and its funding liability can vary significantly, while the timing of repricing for both the asset and the liability remains the same, thereby impacting net interest income. This characteristic is referred to as basis risk. Varying interest rate environments can create unexpected changes in prepayment levels of assets and liabilities that are not

reflected in the interest rate sensitivity analysis. These prepayments may have a significant impact on our net interest margin. Because of these factors, an interest sensitivity gap analysis may not provide an accurate assessment of our actual exposure to changes in interest rates.

The estimated impact on our net interest income over a time horizon of one year and the change in net portfolio value as of December 31, 2019 and 2018 are provided in the table below. For the scenarios shown, the interest rate simulation assumes an instantaneous and sustained shift in market interest rates and no change in the composition or size of the balance sheet.

| Change in Interest Rates (basis points) <sup>(1)</sup> | December 31, 2019                  |                                    | December 31, 2018                  |                                    |
|--|------------------------------------|------------------------------------|------------------------------------|------------------------------------|
|  | Percentage Change                  |                                    |                                    |                                    |
|  | Net Interest Income <sup>(2)</sup> | Net Portfolio Value <sup>(3)</sup> | Net Interest Income <sup>(2)</sup> | Net Portfolio Value <sup>(3)</sup> |
| +200 .....   | (7.2)%                             | (2.5)%                             | (8.3)%                             | (13.5)%                            |
| +100 .....   | (3.4)                              | 0.1                                | (4.1)                              | (7.0)                              |
| -100 .....   | 2.7                                | (6.4)                              | 5.0                                | (0.8)                              |
| -200 .....   | 2.2%                               | (21.2)%                            | 9.0%                               | (7.0)%                             |

- (1) For purposes of our model, we assume interest rates will not go below zero. This “floor” limits the effect of a potential negative interest rate shock in a low rate environment like the one we are currently experiencing.
- (2) This percentage change represents the impact to net interest income for a one-year period, assuming there is no change in the structure of the balance sheet.
- (3) This percentage change represents the impact to the net present value of equity, assuming there is no change in the structure of the balance sheet.

At December 31, 2019 and 2018 we believe our net interest income sensitivity did not exhibit a strong bias to either an increase in interest rates or a decline in interest rates. The changes in sensitivity reflect the impact of both lower market interest rates and changes to overall balance sheet composition. Some of the assumptions made in the simulation model may not materialize and unanticipated events and circumstances will occur. Modeling results in extreme interest rate decline scenarios and may encounter negative rate assumptions which may cause the results to be inherently unreliable. In addition, the simulation model does not take into account any future actions that we could undertake to mitigate an adverse impact due to changes in interest rates from those expected, in the actual level of market interest rates or competitive influences on our deposits.

### ***Risk Management Instruments***

We originate fixed-rate residential home mortgages primarily for sale into the secondary market. These loans are hedged against interest rate fluctuations from the time of the loan commitment until the loans are sold.

We have been able to manage interest rate risk by matching both on- and off-balance sheet assets and liabilities, within reasonable limits, through a range of potential rate and repricing characteristics. Where appropriate, we also use hedging techniques, including the use of forward sale commitments, option contracts and interest rate swaps.

In order to protect the economic value of our mortgage servicing rights, we employ hedging strategies utilizing derivative financial instruments including interest rate swaps, forward interest rate swaps, options on interest rate swap contracts and commitments to purchase mortgage backed securities. We utilize these instruments as economic hedges and changes in the fair value of these instruments are recognized in current income as a component of mortgage servicing income. Our mortgage servicing rights hedging policy requires management to hedge the impact on the value of our mortgage servicing rights for a low-probability, extreme and sudden increase in interest rates.

The following table presents the financial instruments classified as derivatives.

| <b>(in thousands)</b>                    | <b>At December 31, 2019</b> |                              |                                  |
|--|-----------------------------|------------------------------|----------------------------------|
|  | <b>Notional<br/>amount</b>  | <b>Fair value</b>            |                                  |
|  |                             | <b>Asset<br/>derivatives</b> | <b>Liability<br/>derivatives</b> |
| Forward sale commitments . . . . .       | \$ 651,838                  | \$ 830                       | \$ (492)                         |
| Interest rate lock commitments . . . . . | 124,379                     | 2,281                        | (58)                             |
| Interest rate swaps . . . . .            | 688,516                     | 27,097                       | (10,889)                         |
| Eurodollar futures . . . . .             | 2,232,000                   | 3                            | —                                |
|  | <u>\$ 3,696,733</u>         | <u>\$ 30,211</u>             | <u>\$ (11,439)</u>               |

We may implement other hedge transactions using forward loan sales, futures, option contracts and interest rate swaps, interest rate floors, financial futures, forward rate agreements and U.S. Treasury options on futures or bonds. Prior to considering any hedging activities, we analyze the costs and benefits of the hedge in comparison to other viable alternative strategies.

## ITEM 8 FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

### REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the shareholders and the Board of Directors of HomeStreet, Inc.

#### Opinion on the Financial Statements

We have audited the accompanying consolidated statements of financial condition of HomeStreet, Inc. and subsidiaries (the “Company”) as of December 31, 2019 and 2018, and the related consolidated statements of operations, comprehensive income, shareholders’ equity, and cash flows for each of the three years in the period ended December 31, 2019, and the related notes (collectively referred to as the “financial statements”). In our opinion, the financial statements present fairly, in all material respects, the financial position of the Company as of December 31, 2019 and 2018, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2019, in conformity with accounting principles generally accepted in the United States of America.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States) (PCAOB), the Company’s internal control over financial reporting as of December 31, 2019, based on criteria established in *Internal Control — Integrated Framework* (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated March 6, 2020, expressed an unqualified opinion on the Company’s internal control over financial reporting.

#### Emphasis of Matter — Discontinued Operations

As discussed in Note 1 and Note 2 to the financial statements, the Company sold or abandoned operations associated with the Company’s former home loan center-based mortgage origination business and related servicing during the year ended December 31, 2019. The results of the former home loan center-based mortgage origination business and related servicing have been presented as discontinued operations in the accompanying consolidated financial statements.

#### Basis for Opinion

These financial statements are the responsibility of the Company’s management. Our responsibility is to express an opinion on the Company’s financial statements based on our audits. We are a public accounting firm registered with the PCAOB and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether due to error or fraud. Our audits included performing procedures to assess the risks of material misstatement of the financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the financial statements. We believe that our audits provide a reasonable basis for our opinion.

/s/ Deloitte & Touche LLP

Seattle, Washington  
March 6, 2020

We have served as the Company’s auditor since 2013.

**HOMESTREET, INC. AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION**

| (in thousands, except share data)   | At December 31, |              |
|---|-----------------|--------------|
|   | 2019            | 2018         |
| <u>ASSETS</u>   |                 |              |
| Cash and cash equivalents (includes interest-earning instruments of \$28,489 and \$28,534) . . . . .  | \$ 57,880       | \$ 57,982    |
| Investment securities (includes \$938,778 and \$851,968 carried at fair value) . . . . .  | 943,150         | 923,253      |
| Loans held for sale (includes \$79,335 and \$52,186 carried at fair value) . . . . .  | 208,177         | 77,324       |
| Loans held for investment (net of allowance for loan losses of \$41,772 and \$41,470; includes \$3,468 and \$4,057 carried at fair value) . . . . . | 5,072,784       | 5,075,371    |
| Mortgage servicing rights (includes \$68,109 and \$75,047 carried at fair value) . . . . .  | 97,603          | 103,374      |
| Other real estate owned . . . . .   | 1,393           | 455          |
| Federal Home Loan Bank stock, at cost . . . . .   | 22,399          | 45,497       |
| Premises and equipment, net . . . . .   | 76,973          | 88,112       |
| Lease right-of-use assets . . . . .   | 94,873          | —            |
| Goodwill . . . . .  | 28,492          | 22,564       |
| Other assets . . . . .  | 180,083         | 171,255      |
| Assets of discontinued operations . . . . .   | 28,628          | 477,034      |
| Total assets . . . . .  | \$ 6,812,435    | \$ 7,042,221 |
| <u>LIABILITIES AND SHAREHOLDERS' EQUITY</u>   |                 |              |
| Liabilities:  |                 |              |
| Deposits . . . . .  | \$ 5,339,959    | \$ 4,888,558 |
| Federal Home Loan Bank advances . . . . .   | 346,590         | 932,590      |
| Accounts payable and other liabilities . . . . .  | 79,818          | 169,970      |
| Federal funds purchased and securities sold under agreements to repurchase . . . . .  | 125,000         | 19,000       |
| Long-term debt . . . . .  | 125,650         | 125,462      |
| Lease liabilities . . . . .   | 113,092         | —            |
| Liabilities of discontinued operations . . . . .  | 2,603           | 167,121      |
| Total liabilities . . . . .   | 6,132,712       | 6,302,701    |
| Commitments and contingencies (Note 14)   |                 |              |
| Shareholders' equity:   |                 |              |
| Preferred stock, no par value, authorized 10,000 shares, issued and outstanding, 0 shares and 0 shares . . . . .                                    | —               | —            |
| Common stock, no par value, authorized 160,000,000 shares, issued and outstanding, 23,890,855 shares and 26,995,348 shares . . . . .                | 511             | 511          |
| Additional paid-in capital . . . . .  | 300,218         | 342,439      |
| Retained earnings . . . . .   | 374,673         | 412,009      |
| Accumulated other comprehensive income (loss) . . . . .   | 4,321           | (15,439)     |
| Total shareholders' equity . . . . .  | 679,723         | 739,520      |
| Total liabilities and shareholders' equity . . . . .  | \$ 6,812,435    | \$ 7,042,221 |

See accompanying notes to consolidated financial statements.

**HOMESTREET, INC. AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF OPERATIONS**

| (in thousands, except share data)   | Years Ended December 31, |            |            |
|---|--------------------------|------------|------------|
|   | 2019                     | 2018       | 2017       |
| <b>Interest income:</b>   |                          |            |            |
| Loans . . . . .   | \$ 256,192               | \$ 228,350 | \$ 190,345 |
| Investment securities . . . . .   | 20,531                   | 22,645     | 21,753     |
| Other . . . . .   | 883                      | 467        | 222        |
|   | 277,606                  | 251,462    | 212,320    |
| <b>Interest expense:</b>  |                          |            |            |
| Deposits . . . . .  | 70,389                   | 41,995     | 23,912     |
| Federal Home Loan Bank advances . . . . .   | 9,342                    | 12,374     | 7,624      |
| Federal funds purchased and securities sold under agreements to repurchase . . . . .  | 1,033                    | 298        | 5          |
| Long-term debt . . . . .  | 6,822                    | 6,647      | 6,067      |
| Other . . . . .   | 630                      | 185        | 171        |
|   | 88,216                   | 61,499     | 37,779     |
| Net interest income . . . . .   | 189,390                  | 189,963    | 174,541    |
| (Reversal) provision for credit losses . . . . .  | (500)                    | 3,000      | 750        |
| Net interest income after provision for credit losses . . . . .   | 189,890                  | 186,963    | 173,791    |
| <b>Noninterest income:</b>  |                          |            |            |
| Net gain on loan origination and sale activities . . . . .  | 44,122                   | 11,866     | 20,026     |
| Loan servicing income . . . . .   | 7,802                    | 3,671      | 3,331      |
| Depositor and other retail banking fees . . . . .   | 7,926                    | 8,019      | 7,195      |
| Insurance agency commissions . . . . .  | 2,292                    | 2,193      | 1,904      |
| (Loss) gain on sale of investment securities available for sale . . . . .   | (7)                      | 235        | 489        |
| Other . . . . .   | 12,297                   | 10,549     | 9,652      |
|   | 74,432                   | 36,533     | 42,597     |
| <b>Noninterest expense:</b>   |                          |            |            |
| Salaries and related costs . . . . .  | 122,189                  | 105,042    | 101,791    |
| General and administrative . . . . .  | 33,862                   | 32,932     | 37,782     |
| Amortization of core deposit intangibles . . . . .  | 1,634                    | 1,625      | 1,710      |
| Legal . . . . .   | 1,559                    | 3,373      | 1,303      |
| Consulting . . . . .  | 4,055                    | 2,469      | 2,682      |
| Federal Deposit Insurance Corporation assessments . . . . .   | 1,820                    | 3,808      | 2,998      |
| Occupancy . . . . .   | 22,242                   | 18,103     | 16,981     |
| Information services . . . . .  | 28,325                   | 28,028     | 25,897     |
| Net benefit from operation and sale of other real estate owned . . . . .  | (72)                     | (139)      | (530)      |
|   | 215,614                  | 195,241    | 190,614    |
| Income from continuing operations before income taxes . . . . .   | 48,708                   | 28,255     | 25,774     |
| Income tax expense (benefit) from continuing operations . . . . .   | 7,988                    | 2,032      | (16,894)   |
| <b>Income from continuing operations</b> . . . . .  | 40,720                   | 26,223     | 42,668     |
| (Loss) income from discontinued operations before income taxes (includes net loss on disposal of \$21.6 million in 2019 and zero in both 2018 and 2017) . . . . . | (28,285)                 | 17,610     | 40,415     |
| Income tax (benefit) expense from discontinued operations . . . . .   | (5,077)                  | 3,806      | 14,137     |
| <b>(Loss) income from discontinued operations</b> . . . . .   | (23,208)                 | 13,804     | 26,278     |
| <b>NET INCOME</b> . . . . .   | \$ 17,512                | \$ 40,027  | \$ 68,946  |
| <b>Basic earnings per common share:</b>   |                          |            |            |
| Income from continuing operations . . . . .   | \$ 1.57                  | \$ 0.97    | \$ 1.59    |
| (Loss) income from discontinued operations . . . . .  | (0.91)                   | 0.51       | 0.98       |
| <b>Basic earnings per share</b> . . . . .   | \$ 0.66                  | \$ 1.48    | \$ 2.57    |
| <b>Diluted earnings per common share</b>  |                          |            |            |
| Income from continuing operations . . . . .   | \$ 1.55                  | \$ 0.97    | \$ 1.57    |
| (Loss) income from discontinued operations . . . . .  | (0.90)                   | 0.51       | 0.97       |
| <b>Diluted income per share</b> . . . . .   | \$ 0.65                  | \$ 1.47    | \$ 2.54    |
| Basic weighted average number of shares outstanding . . . . .   | 25,573,488               | 26,970,916 | 26,864,657 |
| Diluted weighted average number of shares outstanding . . . . .   | 25,770,783               | 27,168,135 | 27,092,019 |

See accompanying notes to consolidated financial statements.



**HOMESTREET, INC. AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME**

| <b>(in thousands)</b>   | <b>Years Ended December 31,</b> |             |             |
|---|---------------------------------|-------------|-------------|
|   | <b>2019</b>                     | <b>2018</b> | <b>2017</b> |
| Net income . . . . .  | \$ 17,512                       | \$ 40,027   | \$ 68,946   |
| Other comprehensive income (loss), net of tax:  |                                 |             |             |
| Unrealized gain (loss) on investment securities available for sale:   |                                 |             |             |
| Unrealized holding gain (loss) arising during the year, net of tax<br>expense (benefit) of \$5,656, \$(2,163) and \$1,942 . . . . .         | 21,834                          | (8,132)     | 3,607       |
| Reclassification adjustment for net losses (gains) included in net<br>income, net of tax expense (benefit) of \$(2), \$49 and \$172 . . . . | 6                               | (185)       | (317)       |
| Other comprehensive income (loss) . . . . .   | 21,840                          | (8,317)     | 3,290       |
| Comprehensive income . . . . .  | \$ 39,352                       | \$ 31,710   | \$ 72,236   |

See accompanying notes to consolidated financial statements.

**HOMESTREET, INC. AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY**

| (in thousands, except share data)                            | Number of<br>shares | Common<br>stock | Additional<br>paid-in<br>capital | Retained<br>earnings | Accumulated<br>other<br>comprehensive<br>income (loss) | Total<br>temporary<br>equity | Total<br>permanent<br>equity |
|--|---------------------|-----------------|----------------------------------|----------------------|--|------------------------------|------------------------------|
| Balance, December 31, 2016                                   | 26,800,183          | \$ 511          | \$ 336,149                       | \$ 303,036           | \$ (10,412)  | \$ —                         | \$ 629,284                   |
| Net income   | —                   | —               | —                                | 68,946               | —  | —                            | 68,946                       |
| Share-based compensation expense                             | —                   | —               | 2,502                            | —                    | —  | —                            | 2,502                        |
| Common stock issued  | 88,105              | —               | 358                              | —                    | —  | —                            | 358                          |
| Other comprehensive income                                   | —                   | —               | —                                | —                    | 3,290  | —                            | 3,290                        |
| Balance, December 31, 2017                                   | 26,888,288          | 511             | 339,009                          | 371,982              | (7,122)  | —                            | 704,380                      |
| Net income   | —                   | —               | —                                | 40,027               | —  | —                            | 40,027                       |
| Share-based compensation expense                             | —                   | —               | 3,012                            | —                    | —  | —                            | 3,012                        |
| Common stock issued  | 107,060             | —               | 418                              | —                    | —  | —                            | 418                          |
| Other comprehensive loss                                     | —                   | —               | —                                | —                    | (8,317)  | —                            | (8,317)                      |
| Balance, December 31, 2018                                   | 26,995,348          | 511             | 342,439                          | 412,009              | (15,439)   | —                            | 739,520                      |
| Net income   | —                   | —               | —                                | 17,512               | —  | —                            | 17,512                       |
| Share-based compensation recovery                            | —                   | —               | (434)                            | —                    | —  | —                            | (434)                        |
| Cumulative effect of adoption of new<br>accounting standards | —                   | —               | —                                | 1,532                | (2,080)  | —                            | (548)                        |
| Common stock issued  | 104,080             | —               | 376                              | —                    | —  | —                            | 376                          |
| Other comprehensive income                                   | —                   | —               | —                                | —                    | 21,840   | —                            | 21,840                       |
| Common stock repurchased and<br>retired                      | (3,208,573)         | —               | (20,287)                         | (25,521)             | —  | (52,735)                     | (98,543)                     |
| Reclassification to temporary equity                         | —                   | —               | (21,876)                         | (30,859)             | —  | 52,735                       | —                            |
| Balance, December 31, 2019                                   | <u>23,890,855</u>   | <u>\$ 511</u>   | <u>\$ 300,218</u>                | <u>\$ 374,673</u>    | <u>\$ 4,321</u>  | <u>\$ —</u>                  | <u>\$ 679,723</u>            |

See accompanying notes to consolidated financial statements.

**HOMESTREET, INC. AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**

| (in thousands)  | Years Ended December 31, |             |             |
|---|--------------------------|-------------|-------------|
|   | 2019                     | 2018        | 2017        |
| <b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>  |                          |             |             |
| Net income . . . . .  | \$ 17,512                | \$ 40,027   | \$ 68,946   |
| Adjustments to reconcile net income to net cash provided by operating activities:                     |                          |             |             |
| Depreciation, amortization and accretion . . . . .  | 39,499                   | 24,893      | 22,645      |
| (Reversal ) provision for credit losses . . . . .   | (500)                    | 3,000       | 750         |
| Net fair value adjustment and gain on sale of loans held for sale . .                                 | (78,994)                 | (93,766)    | (218,331)   |
| Gain on sale of mortgage servicing rights, gross . . . . .  | (6,206)                  | —           | —           |
| Loss on sale of HLC mortgage originations assets, net . . . . .                                       | 1,036                    | —           | —           |
| Fair value adjustment of loans held for investment . . . . .  | (282)                    | (107)       | (1,030)     |
| Origination of mortgage servicing rights . . . . .  | (34,606)                 | (61,871)    | (78,412)    |
| Change in fair value of mortgage servicing rights . . . . .   | 35,902                   | (6,711)     | 36,615      |
| Net loss (gain) on sale of investment securities . . . . .  | 7                        | (235)       | (489)       |
| Net gain on sale of loans originated as held for investment . . . . .                                 | (9,534)                  | (1,956)     | (4,600)     |
| Net fair value adjustment, gain on sale and provision for losses on other real estate owned . . . . . | (144)                    | (171)       | (383)       |
| Loss on disposal of fixed assets . . . . .  | 124                      | 244         | 215         |
| Loss on lease abandonment and exit costs . . . . .  | 16,619                   | 5,096       | 5,054       |
| Net deferred income tax (benefit) expenses . . . . .  | (29,903)                 | 12,777      | (2,094)     |
| Share-based compensation (recovery) expense . . . . .   | (163)                    | 3,361       | 2,856       |
| Origination of loans held for sale . . . . .  | (3,757,549)              | (6,075,290) | (7,763,844) |
| Proceeds from sale of loans originated as held for sale . . . . .                                     | 4,097,511                | 6,448,808   | 8,084,916   |
| Changes in operating assets and liabilities:  |                          |             |             |
| Decrease (increase) in accounts receivable and other assets . . . . .                                 | 14,198                   | (8,030)     | 26,470      |
| Decrease in accounts payable and other liabilities . . . . .  | (32,547)                 | (4,058)     | (19,957)    |
| Decrease in lease liability . . . . .   | (13,150)                 | —           | —           |
| Net cash provided by operating activities . . . . .   | 258,830                  | 286,011     | 159,327     |
| <b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>  |                          |             |             |
| Purchase of investment securities . . . . .   | (330,532)                | (189,660)   | (368,071)   |
| Proceeds from sale of investment securities . . . . .   | 184,871                  | 46,081      | 397,492     |
| Principal repayments and maturities of investment securities . . . . .                                | 145,771                  | 106,798     | 105,801     |
| Proceeds from sale of other real estate owned . . . . .   | 1,138                    | 836         | 6,105       |
| Proceeds from sale of loans originated as held for investment . . . . .                               | 769,354                  | 548,770     | 324,745     |
| Loans purchased from other third parties . . . . .  | —                        | (1,953)     | —           |
| Proceeds from sale of mortgage servicing rights . . . . .   | 3,269                    | 65,373      | —           |
| Mortgage servicing rights purchased from third parties . . . . .                                      | (14)                     | (4)         | (565)       |
| Capital expenditures related to other real estate owned . . . . .                                     | —                        | —           | (57)        |
| Net cash provided by disposal of discontinued operations . . . . .                                    | 182,189                  | —           | —           |
| Origination of loans held for investment and principal repayments, net . . . . .                      | (822,474)                | (1,132,521) | (998,638)   |
| Proceeds from sale of property and equipment . . . . .  | —                        | 808         | —           |
| Purchase of property and equipment . . . . .  | (2,257)                  | (9,724)     | (42,286)    |
| Net cash (paid) acquired from acquisitions . . . . .  | (47,389)                 | —           | 19,285      |
| Net cash provided by (used in) investing activities . . . . .   | 83,926                   | (565,196)   | (556,189)   |

**HOMESTREET, INC. AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS – (continued)**

| (in thousands)   | Years Ended December 31, |                  |                  |
|--|--------------------------|------------------|------------------|
|  | 2019                     | 2018             | 2017             |
| <b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>   |                          |                  |                  |
| Increase in deposits, net . . . . .  | \$ 213,572               | \$ 290,152       | \$ 309,798       |
| Proceeds from Federal Home Loan Bank advances . . . . .  | 7,598,300                | 11,729,500       | 10,972,200       |
| Repayment of Federal Home Loan Bank advances . . . . .   | (8,184,300)              | (11,776,000)     | (10,861,200)     |
| Proceeds from federal funds purchased and securities sold under agreements to repurchase . . . . . | 11,051,703               | 3,511,070        | 875,166          |
| Repayment of federal funds purchased and securities sold under agreements to repurchase . . . . .  | (10,945,703)             | (3,492,070)      | (875,166)        |
| Proceeds from line of credit draws . . . . .   | 20,000                   | 30,000           | —                |
| Repayment of line of credit draws . . . . .  | (20,000)                 | (30,000)         | —                |
| Repayment of lease principal . . . . .   | (1,694)                  | —                | —                |
| Proceeds from Federal Home Loan Bank stock repurchase . . . . .                                    | 161,254                  | 179,789          | 187,766          |
| Purchase of Federal Home Loan Bank stock . . . . .   | (138,156)                | (178,647)        | (194,058)        |
| Proceeds from debt issuance, net . . . . .   | —                        | —                | (65)             |
| Payments from equity raise, net . . . . .  | —                        | —                | (45)             |
| Stock repurchased . . . . .  | (98,543)                 | —                | —                |
| Proceeds from stock issuance, net . . . . .  | 105                      | 68               | 11               |
| Net cash (used in) provided by financing activities . . . . .                                      | (343,462)                | 263,862          | 414,407          |
| <b>NET (DECREASE) INCREASE IN CASH, CASH EQUIVALENTS AND RESTRICTED CASH . . . . .</b>             | <b>(706)</b>             | <b>(15,323)</b>  | <b>17,545</b>    |
| <b>CASH, CASH EQUIVALENTS AND RESTRICTED CASH:</b>   |                          |                  |                  |
| Cash, cash equivalents and restricted cash, beginning of year . . . . .                            | 58,586                   | 73,909           | 56,364           |
| Cash, cash equivalents and restricted cash, end of year . . . . .                                  | 57,880                   | 58,586           | 73,909           |
| Less restricted cash included in other assets . . . . .  | —                        | 604              | 1,191            |
| <b>CASH AND CASH EQUIVALENTS AT END OF YEAR . . . . .</b>  | <b>\$ 57,880</b>         | <b>\$ 57,982</b> | <b>\$ 72,718</b> |
| <b>SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:</b>  |                          |                  |                  |
| Cash paid during the period for:   |                          |                  |                  |
| Interest paid . . . . .  | \$ 93,325                | \$ 67,552        | \$ 42,889        |
| Federal and state income taxes paid (refunded), net . . . . .                                      | 33,625                   | (5,785)          | (21,885)         |
| Non-cash activities:   |                          |                  |                  |
| Loans held for investment foreclosed and transferred to other real estate owned . . . . .          | 915                      | 455              | 1,125            |
| Loans transferred from held for investment to held for sale . . . . .                              | 916,483                  | 634,205          | 419,494          |
| Loans transferred from held for sale to held for investment . . . . .                              | 8,705                    | 71,584           | 100,049          |
| Ginnie Mae loans recognized with the right to repurchase, net . . . . .                            | (28,281)                 | (1,674)          | 3,534            |
| Receivable from sale of mortgage servicing rights . . . . .  | 2,117                    | 3,337            | —                |
| Acquisition:   |                          |                  |                  |
| Assets acquired . . . . .  | 116,402                  | —                | —                |
| Liabilities assumed . . . . .  | 74,941                   | —                | —                |
| Goodwill . . . . .   | 5,928                    | —                | —                |
| Right-of-use assets obtained in exchange for lease obligations:                                    |                          |                  |                  |
| Operating leases . . . . .   | (7,805)                  | —                | —                |
| Finance leases . . . . .   | (1,033)                  | —                | —                |

See accompanying notes to consolidated financial statements.

**HOMESTREET, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 1 — SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:**

HomeStreet, Inc. and its wholly owned subsidiaries (the “Company”) is a diversified financial services company serving customers primarily on the West Coast of the United States, including Hawaii. The Company is principally engaged in commercial banking, mortgage banking, and consumer/retail banking activities. The Company’s consolidated financial statements include the accounts of HomeStreet, Inc. and its wholly owned subsidiaries, HomeStreet Capital Corporation, HomeStreet Statutory Trusts and HomeStreet Bank (the “Bank”), and the Bank’s subsidiaries, HomeStreet Reinsurance, Ltd., Continental Escrow Company, HomeStreet Foundation, HS Properties, Inc., HS Evergreen Corporate Center LLC, Union Street Holdings LLC, HS Cascadia Holdings LLC and YNB Real Estate LLC. HomeStreet Bank was formed in 1986 and is a state-chartered commercial bank.

The Company’s accounting and financial reporting policies conform to accounting principles generally accepted in the United States of America (U.S. GAAP). Inter-company balances and transactions have been eliminated in consolidation. In preparing the consolidated financial statements, the Company is required to make estimates and assumptions that affect the reported amounts of assets and liabilities as of the date of the financial statements and revenues and expenses during the reporting periods and related disclosures. These estimates that require application of management’s most difficult, subjective or complex judgments often result in the need to make estimates about the effect of matters that are inherently uncertain and may change in future periods. Management has made significant estimates in several areas, including the fair value of assets acquired and liabilities assumed in business combinations (Note 3, *Business Combinations*), allowance for credit losses (Note 6, *Loans and Credit Quality*), valuation of residential mortgage servicing rights and loans held for sale (Note 13, *Mortgage Banking Operations*), valuation of certain loans held for investment (Note 6, *Loans and Credit Quality*), valuation of investment securities (Note 5, *Investment Securities*), valuation of derivatives (Note 12, *Derivatives and Hedging Activities*), and taxes (Note 15, *Income Taxes*). Actual results could differ materially from those estimates. Certain amounts in the financial statements from prior periods have been reclassified to conform to the current financial statement presentation. These reclassifications are immaterial and have no effect on net income, comprehensive income, cash flows, total assets or total shareholders’ equity as previously reported.

Discontinued Operations

During 2019, the Company’s Board of Directors (the “Board”) adopted a Resolution of Exit or Disposal of Home Loan Center (“HLC”) Based Mortgage Banking Operations to sell or abandon the assets and transfer or terminate the personnel associated with the Company’s high-volume HLC-based mortgage origination business and related servicing. The Company also successfully closed and settled two separate sales of the rights to service \$14.26 billion in total unpaid principal balance of single family mortgage loans serviced for others, representing in the aggregate approximately 71% of HomeStreet’s total single family mortgage loans serviced for others portfolio at December 31, 2018. These two actions largely represent the Company’s former Mortgage Banking segment. In accordance with Accounting Standards Codification (ASC) 205-20, the Company determined that the Board’s decision to sell or abandon the assets and personnel associated with the Company’s HLC-based mortgage business and the related mortgage servicing rights (“MSR”) sales met the criteria to be classified as discontinued operations and its operating results and financial condition are presented as discontinued operations in the consolidated financial statements for the current and all comparative periods which have been recast to conform to the new presentation (see Note 2, *Discontinued Operations* for additional information). Unless otherwise indicated, information included in these notes to the consolidated financial statements are presented on a consolidated operations basis, which includes results from both continuing and discontinued operations, for all periods presented.

At the end of the second quarter 2019, we also entered into a non-binding letter of interest to sell our ownership interest in WMS LLC at which time related operations also met the criteria to be included in discontinued operations and were reported for all periods presented.

**HOMESTREET, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 1 — SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:** (cont.)

Cash and Cash Equivalents

Cash and cash equivalents include cash, interest-earning overnight deposits at other financial institutions, and other investments with original maturities equal to three months or less. For the consolidated statements of cash flows, the Company considered cash equivalents to be investments that are readily convertible to known amounts, so near to their maturity that they present an insignificant risk of change in fair value due to changes in interest rates, and purchased in conjunction with cash management activities. Restricted cash of \$5.1 million and \$4.7 million at December 31, 2019 and 2018, respectively, is included in cash and cash equivalents for FNMA DUS<sup>®</sup> pledged securities and related reserves. In addition, we had restricted cash of \$604 thousand at December 31, 2018 and is included in accounts receivable and other assets for reinsurance-related reserves, with no similar balance at December 31, 2019.

Investment Securities

We classify investment securities as trading, held to maturity (“HTM”), or available for sale (“AFS”) at the date of acquisition. Purchases and sales of securities are generally recorded on a trade-date basis. We include and record certain certificates of deposit that meet the definition of a security as HTM investments.

Investment securities that we might not hold until maturity are classified as AFS and are reported at fair value in the statement of financial condition. Fair value measurement is based upon quoted market prices in active markets, if available. If quoted prices in active markets are not available, fair value is measured using pricing models or other model-based valuation techniques such as the present value of future cash flows, which consider prepayment assumptions and other factors such as credit losses and market liquidity. Unrealized gains and losses are excluded from earnings and reported, net of tax, in other comprehensive income (“OCI”). Purchase premiums and discounts are recognized in interest income using the effective interest method over the life of the securities. Purchase premiums or discounts related to mortgage-backed securities are amortized or accreted using projected prepayment speeds. Gains and losses on the sale of securities are recorded on the trade date and are determined using the specific identification method.

AFS investment securities in unrealized loss positions are evaluated for other-than-temporary impairment (“OTTI”) at least quarterly. For AFS debt securities, a decline in fair value is considered to be other-than-temporary if the Company does not expect to fully recover the amortized cost basis of the security.

Debt securities are classified as HTM if the Company has both the intent and ability to hold those securities to maturity regardless of changes in market conditions, liquidity needs or changes in general economic conditions. These securities are carried at cost adjusted for amortization of purchase premiums and accretion of purchase discounts.

Transfers of securities from available for sale to held to maturity are accounted for at fair value as of the date of the transfer. The difference between the fair value and the par value at the date of transfer is considered a premium or discount and is accounted for accordingly. Any unrealized gain or loss at the date of the transfer is reported in OCI, and is amortized over the remaining life of the security as an adjustment to yield in a manner consistent with the amortization of any premium or discount, and will offset or mitigate the impact on interest income of the amortization of the premium or discount for that held to maturity security.

Impairment may result from credit deterioration of the issuer or collateral underlying the security. In performing an assessment of recoverability, all relevant information is considered, including the length of time and extent to which fair value has been less than the amortized cost basis, the cause of the price decline, credit performance of the issuer and underlying collateral, and recoveries or further declines in fair value subsequent to the balance sheet date.



**HOMESTREET, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 1 — SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:** (cont.)

For debt securities, the Company measures and recognizes OTTI losses through earnings if (1) the Company has the intent to sell the security or (2) it is more likely than not that the Company will be required to sell the security before recovery of its amortized cost basis. In these circumstances, the impairment loss is equal to the full difference between the amortized cost basis and the fair value of the security. For securities that are considered other-than-temporarily-impaired that the Company has the intent and ability to hold in an unrealized loss position, the OTTI write-down is separated into an amount representing the credit loss, which is recognized in earnings, and the amount related to other factors, which is recognized as a component of OCI.

Federal Home Loan Bank Stock

As a borrower from the Federal Home Loan Bank of Des Moines (“FHLB”), the Company is required to purchase an amount of FHLB stock based on our membership and outstanding borrowings with the FHLB. This stock is used as collateral to secure the borrowings from the FHLB and is accounted for as a cost-method investment. FHLB stock is reviewed at least quarterly for possible OTTI, which includes an analysis of the FHLB’s cash flows, capital needs and long-term viability.

Loans Held for Sale

Loans originated for sale in the secondary market, which is our principal market, or as whole loan sales are classified as loans held for sale. Management has elected the fair value option for all single family loans held for sale (originated with the intent to market for sale) and records these loans at fair value. The fair value of loans held for sale is generally based on observable market prices from other loans in the secondary market that have similar collateral, credit, and interest rate characteristics. If quoted market prices are not readily available, the Company may consider other observable market data such as dealer quotes for similar loans or forward sale commitments. In certain cases, the fair value may be based on a discounted cash flow model. Gains and losses from changes in fair value on loans held for sale are recognized in net gain on mortgage loan origination and sale activities within noninterest income. Direct loan origination costs and fees for single family loans originated as held for sale are recognized in earnings. The change in fair value of loans held for sale is primarily driven by changes in interest rates subsequent to loan funding and changes in fair value of the related servicing asset, resulting in revaluation adjustments to the recorded fair value. The use of the fair value option allows the change in the fair value of loans to more effectively offset the change in the fair value of derivative instruments that are used as economic hedges of loans held for sale.

Multifamily and SBA loans held for sale are accounted for at the lower of amortized cost or fair value (LOCOM). Fair values for loans are based on committed sale prices or calculated internally for loans not committed to a future sale. LOCOM valuations are performed quarterly or at the time of transfer to or from loans held for sale. Related gains and losses are recognized in net gain on mortgage loan origination and sale activities. Direct loan origination costs and fees for multifamily and SBA loans classified as held for sale are deferred at origination and recognized in earnings at the time of sale.

Loans Held for Investment

Loans held for investment are reported at the principal amount outstanding, net of cumulative charge-offs, interest applied to principal (for loans accounted for using the cost recovery method), unamortized net deferred loan origination fees and costs and unamortized premiums or discounts on purchased loans. Deferred fees and costs and premiums and discounts are amortized over the contractual terms of the underlying loans using the constant effective yield (the interest method) or straight-line method. Interest on loans is accrued and recognized as interest income at the contractual rate of interest. A determination is made as of the loan commitment date as to whether a loan will be held for sale or held for investment. This determination is based primarily on the type of loan or loan program and its related profitability characteristics.

**HOMESTREET, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 1 — SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:** (cont.)

When a loan is designated as held for investment, the intent is to hold these loans for the foreseeable future or until maturity or pay-off. If subsequent changes occur as part of the balance sheet management process, the Company may change its intent to hold these loans. Once a determination has been made to sell such loans, they are immediately transferred to loans held for sale and carried at the lower of cost or fair value.

*Nonaccrual Loans*

Loans are placed on nonaccrual status when the full and timely collection of principal and interest is doubtful, generally when the loan becomes 90 days or more past due for principal or interest payment or if part of the principal balance has been charged off.

All payments received on nonaccrual loans are accounted for using the cost recovery method. Under the cost recovery method, all cash collected is applied first to reduce the outstanding principal balance. A loan may be returned to accrual status if all delinquent principal and interest payments are brought current and the collectability of the remaining principal and interest payments in accordance with the loan agreement is reasonably assured. Loans that are well-secured and in the process of collection are maintained on accrual status, even if they are 90 days or more past due. Loans whose repayments are insured by the Federal Housing Administration (“FHA”) or guaranteed by the Department of Veterans’ Affairs (“VA”) are maintained on accrual status even if 90 days or more past due.

*Impaired Loans*

A loan is considered impaired when it is probable that all contractual principal and interest payments due will not be collected in accordance with the terms of the loan agreement. Factors considered by management in determining whether a loan is impaired include payment status, collateral value and the probability of collecting scheduled principal and interest payments when due.

*Troubled Debt Restructurings*

A loan is accounted for and reported as a troubled debt restructuring (“TDR”) when, for economic or legal reasons, we grant a concession to a borrower experiencing financial difficulty that we would not otherwise consider.

A restructuring that results in only an insignificant delay in payment is not considered a concession. A delay may be considered insignificant if the payments subject to the delay are insignificant relative to the unpaid principal or collateral value and the contractual amount due, or the delay in timing of the restructured payment period is insignificant relative to the frequency of payments, the debt’s original contractual maturity or original expected duration.

TDRs are designated as impaired because interest and principal payments will not be received in accordance with original contract terms. TDRs that are performing and on accrual status as of the date of the modification remain on accrual status. TDRs that are nonperforming as of the date of modification generally remain as nonaccrual until the prospect of future payments in accordance with the modified loan agreement is reasonably assured, generally demonstrated when the borrower maintains compliance with the restructured terms for a predetermined period, normally at least six months. TDRs with temporary below-market concessions remain designated as a TDR and deemed impaired regardless of the accrual or performance status until the loan is paid off. However, if the TDR loan has been further modified in a subsequent restructuring with market terms and the borrower is not currently experiencing financial difficulty, then the loan may be de-designated as a TDR.

Allowance for Credit Losses

Credit quality within the loans held for investment portfolio is continuously monitored by management and is reflected within the allowance for credit losses. Included in the allowance for credit losses is both the allowance for loan loss reserves and unfunded commitment reserves. The allowance for credit losses is maintained at a level that, in management’s judgment, is appropriate to cover losses inherent within the Company’s loans held for investment

**HOMESTREET, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 1 — SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:** (cont.)

portfolio, including unfunded loan commitments, as of the balance sheet date. The allowance for loan losses, as reported in our consolidated statements of financial condition, is adjusted by a provision for loan losses, which is recognized in earnings, and reduced by the charge-off of loan principal amounts, net of recoveries.

The loss estimation process involves procedures to appropriately consider the unique characteristics of its two loan portfolios, the consumer loan portfolio and the commercial loan portfolio. These two portfolios are further disaggregated into loan classes, the level at which credit risk is monitored. When computing allowance levels, credit loss assumptions are estimated using a model that categorizes loan pools based on loss history, delinquency status and other credit trends and risk characteristics. Determining the appropriateness of the allowance is complex and requires judgment by management about the effect of matters that are inherently uncertain. Subsequent evaluations of the overall loan portfolio, in light of the factors then prevailing, may result in significant changes in the allowance for credit losses in those future periods.

Credit quality is assessed and monitored by evaluating various attributes and utilizes such information in our evaluation of the adequacy of the allowance for credit losses. The following provides the credit quality indicators and risk elements that are most relevant and most carefully considered and monitored for each loan portfolio.

*Consumer Loan Portfolio*

The consumer loan portfolio is comprised of the single family and home equity loan classes, which are underwritten after evaluating a borrower's capacity, credit, and collateral. Capacity refers to a borrower's ability to make payments on the loan. Several factors are considered when assessing a borrower's capacity, including the borrower's employment, income, current debt, assets, and level of equity in the property. Credit refers to how well a borrower manages their current and prior debts as documented by a credit report that provides credit scores and the borrower's current and past information about their credit history. Collateral refers to the type and use of property, occupancy, and market value. Property appraisals are obtained to assist in evaluating collateral. Loan-to-property value and debt-to-income ratios, loan amount, and lien position are also considered in assessing whether to originate a loan. These borrowers are particularly susceptible to downturns in economic trends such as conditions that negatively affect housing prices and demand and levels of unemployment.

*Commercial Loan Portfolio*

The commercial loan portfolio is comprised of the commercial real estate, non-owner occupied, multifamily residential, construction/land development, owner occupied and commercial business loan classes, whose underwriting standards consider the factors described for single family and home equity loan classes as well as others when assessing the borrower's and associated guarantors or other related party's financial position. These other factors include measuring liquidity, the level and composition of net worth and leverage, evaluating all other lender amounts and positions, analyzing expected cash flow through the obligors including the outflow to other lenders and considering prior experience with the borrower. This information is used to assess adequate financial capacity, profitability, and experience. Ultimate repayment of these loans is sensitive to interest rate changes, general economic conditions, liquidity, and availability of long-term financing.

*Loan Loss Measurement*

Allowance levels are influenced by loan volumes, loan asset quality ratings ("AQR") migration or delinquency status, historic loss experience and other conditions influencing loss expectations, such as economic conditions. The methodology for evaluating the adequacy of the allowance for loan losses has two basic components: first, an asset-specific component involving the identification of impaired loans and the measurement of impairment for each individual loan identified; and second, a formula-based component for estimating probable loan principal losses for all other loans.

**HOMESTREET, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 1 — SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:** (cont.)

*Impaired Loans*

When a loan is identified as impaired, impairment is measured based on net realizable value, or the difference between the discounted value of the expected future cash flows, based on the original effective interest rate, and the recorded investment balance of the loan. For impaired loans, we recognize impairment if we determine that the net realizable value of the impaired loan is less than the recorded investment of the loan (net of previous charge-offs and deferred loan fees and costs), except when the sole remaining source of collection is the underlying collateral. In these cases impairment is measured as the difference between the recorded investment balance of the loan and the fair value of the collateral. The fair value of the collateral is adjusted for the estimated cost to sell if repayment or satisfaction of a loan is dependent on the sale (rather than only on the operation) of the collateral.

The starting point for determining the fair value of collateral is through obtaining external appraisals. Generally, collateral values for impaired loans are updated every twelve months, either from external third parties or in-house certified appraisers. We require an independent third-party appraisal at least annually for substandard loans and other real estate owned (“OREO”). Third party appraisals are obtained from a pre-approved list of independent, third party, local appraisal firms. Approval and addition to the list is based on experience, reputation, character, consistency and knowledge of the respective real estate market. Generally, appraisals are internally reviewed by the appraisal services group to ensure the quality of the appraisal and the expertise and independence of the appraiser. For performing consumer loans secured by real estate that are classified as collateral dependent, the Bank determines the fair value estimates quarterly using automated valuation services. Once the impairment amount is determined, an asset-specific allowance is provided for equal to the calculated impairment and included in the allowance for loan losses. If the calculated impairment is determined to be permanent or not recoverable, the impairment will be charged off. Factors considered by management in determining if impairment is permanent or not recoverable include whether management judges the loan to be uncollectible, repayment is deemed to be protracted beyond reasonable time frames or the loss becomes evident owing to the borrower’s lack of assets or, for single family loans, the loan is 180 days or more past due unless both well-secured and in the process of collection.

*Estimate of Probable Loan Losses*

In estimating the formula-based component of the allowance for loan losses, loans are segregated into loan classes. Loans are designated into loan classes based on loans pooled by product types and similar risk characteristics or areas of risk concentration.

In determining the allowance for loan losses we derive an estimated credit loss assumption from a model that categorizes loan pools based on loan type and AQR or delinquency bucket. This model calculates an expected loss percentage for each loan category by considering the probability of default, based on the migration of loans from performing to loss by AQR or delinquency status using two-year analysis periods for the commercial portfolio and one-year analysis periods for the consumer portfolio, and the potential severity of loss, based on the aggregate net lifetime losses incurred per loan class.

The formula-based component of the allowance for loan losses also considers qualitative factors for each loan class, including changes in the following: (1) lending policies and procedures; (2) international, national, regional and local economic business conditions and developments that affect the collectability of the portfolio, including the condition of various markets; (3) the nature and volume of the loan portfolio including the terms of the loans; (4) the experience, ability, and depth of the lending management and other relevant staff; (5) the volume and severity of past due and adversely classified or graded loans and the volume of nonaccrual loans; (6) the quality of our loan review system; (7) the value of underlying collateral for collateral-dependent loans. Additional factors include (8) the existence and effect of any concentrations of credit, and changes in the level of such concentrations and (9) the effect of external factors such as competition and legal and regulatory requirements on the level of estimated credit losses in the existing portfolio. Qualitative factors are expressed in basis points and are adjusted downward or upward based on management’s judgment as to the potential loss impact of each qualitative factor to a particular loan pool at the date of the analysis.

**HOMESTREET, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 1 — SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:** (cont.)

*Unfunded Loan Commitments*

The Company maintains a separate allowance for losses on unfunded loan commitments, which is included in accounts payable and other liabilities on the consolidated statements of financial condition. Management estimates the amount of probable losses by calculating a one-year commitment usage factor and applying the loss factors used in the allowance for loan loss methodology to the results of the usage calculation to estimate the liability for credit losses related to unfunded commitments for each loan type.

Other Real Estate Owned

Other real estate owned (“OREO”) represents real estate acquired for debts previously contracted with the Company, generally through the foreclosure of loans. In certain cases, such as foreclosures on loans involving both the Company and other participating lenders, other real estate owned may be held in the form of an investment in an unconsolidated legal entity that is in-substance real estate. These properties are initially recorded at the net realizable value (fair value of collateral less estimated costs to sell). Upon transfer of a loan to other real estate owned, an appraisal is obtained and any excess of the loan balance over the net realizable value is charged against the allowance for loan losses. The Company allows up to 90 days after foreclosure to finalize determination of net realizable value. Subsequent declines in net realizable value identified from the ongoing analysis of such properties are recognized in current period earnings within noninterest expense as a provision for losses on other real estate owned. The net realizable value of these assets is reviewed and updated at least every six months depending on the type of property, or more frequently as circumstances warrant.

As part of our subsequent events analysis process, we review updated independent third-party appraisals received and internal collateral valuations received subsequent to the reporting period-end to determine whether the fair value of loan collateral or OREO has changed. Additionally, we review agreements to sell OREO properties executed prior to and subsequent to the reporting period-end to identify changes in the fair value of OREO properties. If we determine that current valuations have changed materially from the prior valuations, we record any additional loan impairments or adjustments to OREO carrying values as of the end of the prior reporting period.

Mortgage Servicing Rights

We initially record all mortgage servicing rights (“MSRs”) at fair value. For subsequent measurement of MSRs, accounting standards permit the election of either fair value or the lower of amortized cost or fair value. Management has elected to account for single family MSRs at fair value during the life of the MSR, with changes in fair value recorded through current period earnings. Fair value adjustments encompass market-driven valuation changes as well as modeled amortization involving the run-off of value that occurs due to the passage of time as individual loans are paid by borrowers. We account for multifamily and SBA MSRs at the lower of amortized cost or fair value.

MSRs are recorded as separate assets on our consolidated statements of financial condition upon purchase of the rights or when we retain the right to service loans that we have sold. Net gains on mortgage loan origination and sale activities depend, in part, on the initial fair value of MSRs, which is based on a discounted cash flow model.

Mortgage servicing income includes the changes in fair value over the reporting period of both our single family MSRs and the derivatives used to economically hedge our single family MSRs. Subsequent fair value measurements of single family MSRs, which are not traded in an active market with readily observable market prices, are determined by considering the present value of estimated future net servicing cash flows. Changes in the fair value of single family MSRs result from changes in (1) model inputs and assumptions and (2) modeled amortization, representing the collection and realization of expected cash flows and curtailments over time. The significant model inputs used to measure the fair value of single family MSRs include assumptions regarding market interest rates, projected prepayment speeds, discount rates, estimated costs of servicing and other income and additional expenses associated with the collection of delinquent loans.



**HOMESTREET, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 1 — SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:** (cont.)

Market expectations about loan duration, and correspondingly the expected term of future servicing cash flows, may vary from time to time due to changes in expected prepayment activity, especially when interest rates rise or fall. Market expectations of increased loan prepayment speeds may negatively impact the fair value of the single family MSRs. Fair value is also dependent on the discount rate used in calculating present value, which is imputed from observable market activity and market participants. Management reviews and adjusts the discount rate on an ongoing basis. An increase in the discount rate would reduce the estimated fair value of the single family MSRs asset.

For further information on how the Company measures the fair value of its single family MSRs, including key economic assumptions and the sensitivity of fair value to changes in those assumptions, see Note 13, *Mortgage Banking Operations*.

Investment in WMS Series LLC

In November 2019, HomeStreet, Inc. finalized the sale of our ownership interest in WMS Series, LLC Limited Liability Company (“WMS LLC”). Prior to this, HomeStreet/WMS, Inc. (Windermere Mortgage Services, Inc.), was a wholly owned and consolidated subsidiary of the Bank, with an affiliated business arrangement with WMS LLC. The Company and Windermere Real Estate each had 50% joint control over the governance of WMS LLC and the underlying series. The operations of WMS LLC, which was subdivided into 27 individual operating series, were recorded using the equity method of accounting. Prior to the sale, the Company recognized its proportionate share of the results of operations of WMS LLC as income from WMS Series LLC in discontinued operations within the Company’s consolidated statements of operations.

The equity method investment income from WMS LLC was \$1.2 million, \$160 thousand, and \$598 thousand for the years ended December 31, 2019, 2018, and 2017, respectively. The Company’s investment in WMS LLC, which is included in discontinued operations was \$1.8 million, at December 31, 2018. We had no similar investment at December 31, 2019 due to the sale of our ownership interest in WMS LLC.

Prior to the sale and subsequent as transition services, the Company provided contracted services to WMS LLC related to accounting, loan shipping, loan underwriting and insuring, quality control, secondary marketing, and information systems support performed by Company employees on behalf of WMS LLC. The Company recorded contracted and transition services income of \$888 thousand, \$853 thousand, and \$844 thousand for the years ended December 31, 2019, 2018 and 2017, respectively. Income related to WMS LLC contracted services prior to the sale is classified in discontinued operations. Income related to WMS LLC transition contracted services is classified in noninterest expense.

The Company purchased \$612.6 million, \$530.9 million and \$574.3 million of single family mortgage loans from WMS LLC for the years ended December 31, 2019, 2018 and 2017, respectively. The outstanding balance of the secured line of credit was \$12.6 million and \$5.4 million at December 31, 2019 and 2018, respectively. The highest outstanding balance of the secured line of credit was \$18.3 million and \$11.5 million during 2019 and 2018, respectively. The line of credit was paid off and matured on January 15, 2020.

Premises and Equipment

Furniture and equipment and leasehold improvements are reported at historical cost less accumulated depreciation or amortization and depreciated or amortized over the shorter of the useful life of the related asset or the term of the lease, generally 3 to 39 years, using the straight-line method. Management periodically evaluates furniture and equipment and leasehold improvements for impairment.



**HOMESTREET, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 1 — SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:** (cont.)

Leases

We determine if an arrangement is a lease at inception. Operating and finance leases are included in lease right-of-use (“ROU”) assets, and lease liabilities in our consolidated balance sheets. ROU assets represent our right to use an underlying asset for the lease term and lease liabilities represent our obligation to make lease payments arising from the lease. The lease liability is recognized at commencement date based on the present value of lease payments over the lease term. The right-of-use asset is based on the lease liability adjusted for the reclassification of certain balance sheet amounts such as prepaid rent, lease incentives and deferred rent. As the rate implicit in most of our leases are not readily determinable, we generally use our incremental borrowing rate based on the estimated rate of interest for collateralized borrowing over a similar term of the lease payments at commencement date. Our lease terms may include options to extend or terminate the lease when it is reasonably certain that we will exercise that option. We have lease agreements with lease and non-lease components, which are generally accounted for separately. For certain equipment leases we account for the lease and non-lease components as a single lease component.

Lease expense for operating leases is recognized on a straight-line basis over the non-cancelable lease term and renewal periods that are considered reasonably certain. Lease expense for our financing leases is comprised of the amortization of the right-of-use asset and interest expense recognized based on the effective interest method.

Goodwill

Goodwill is recorded upon completion of a business combination as the difference between the purchase price and the fair value of net identifiable assets acquired. Subsequent to initial recognition, the Company tests goodwill for impairment during the third quarter of each fiscal year, or more often if events or circumstances, such as adverse changes in the business climate, indicate there may be impairment. Goodwill was not impaired at December 31, 2019 or 2018, nor was any goodwill written off due to impairment during 2019, 2018 or 2017.

Changes in the carrying amount of goodwill are detailed in the following table:

|   | <b>(in thousands)</b> |
|---|-----------------------|
| Goodwill balance at December 31, 2017 ..... | \$ 22,564             |
| Acquisitions .....                          | —                     |
| Goodwill balance at December 31, 2018 ..... | 22,564                |
| Acquisitions .....                          | 5,928                 |
| Goodwill balance at December 31, 2019 ..... | \$ 28,492             |

Trust Preferred Securities

Trust preferred securities allow investors the ability to invest in subordinated debentures of the Company, which provide the Company with long-term financing. The transaction begins with the formation of a Variable Interest Entity (“VIE”) established as a trust by the Company. This trust issues two classes of securities: common securities, all of which are purchased and held by the Company and recorded in other assets on the consolidated statements of financial position, and trust preferred securities, which are sold to third-party investors. The trust holds subordinated debentures (debt) issued by the Company, which the Company records in long-term debt on the consolidated statement of financial position. The trust finances the purchase of the subordinated debentures with the proceeds from the sale of its common and preferred securities.

The subordinated debentures are the sole assets of the trust, and the coupon rate on the debt mirrors the dividend payment on the preferred security. The Company also has the right to defer interest payments for up to five years and has the right to call the preferred securities quarterly five years after issuance. These preferred securities are non-voting and do not have the right to convert to shares of the issuer. The trust’s common securities issued to the Company are not considered to be equity at risk because the equity securities were financed by the trust through the purchase of the subordinated debentures from the Company. As a result, the Company holds no variable interest in the trust, and therefore, is not the trust’s primary beneficiary.

**HOMESTREET, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 1 — SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:** (cont.)

Federal Funds Purchased and Securities Sold Under Agreements to Repurchase

From time to time, the Company may enter into federal funds transactions involving purchasing reserve balances on a short-term basis, or sales of securities under agreements to repurchase the same securities (“repurchase agreements”). Repurchase agreements are accounted for as secured financing arrangements with the obligation to repurchase securities sold reflected as a liability in the consolidated statements of financial condition. The dollar amount of securities underlying the repurchase agreements remains in investment securities available for sale. For short-term instruments, including securities sold under agreements to repurchase and federal funds purchased, the carrying amount is a reasonable approximation of the fair value.

Income Taxes

Our income tax expense is the total of current year income tax due or refundable; change in deferred tax assets and liabilities; and unrecognized tax positions; and reflects management’s best assessment of estimated current and future taxes to be paid. We are subject to federal income tax and also state income taxes in a number of different states. Significant judgments and estimates are required in determining the consolidated income tax expense.

Deferred income taxes arise from temporary differences between the tax basis of assets and liabilities and their reported amounts in the financial statements, which will result in taxable or deductible amounts in the future. Changes in tax laws and rates may affect recorded deferred tax assets and liabilities and our effective tax rate in the future. Such changes are accounted for in the period of enactment and are reflected as discrete tax items in the Company’s tax provision.

The Company records net deferred tax assets to the extent it is believed that these assets will more likely than not be realized. In making this determination, the Company considers all available positive and negative evidence, including future reversals of existing taxable temporary differences, projected future taxable income, tax planning strategies, and recent financial operations. After reviewing and weighing all of the positive and negative evidence, if the positive evidence outweighs the negative evidence, then the Company does not record a valuation allowance for deferred tax assets. If the negative evidence outweighs the positive evidence, then a valuation allowance for all or a portion of the deferred tax assets is recorded.

The calculation of our tax liabilities involves dealing with uncertainties in the application of complex tax laws and regulations in different jurisdictions. Accounting Standards Codification (“ASC”) 740 states that a tax benefit from an uncertain tax position may be recognized when it is more likely than not that the position will be sustained upon examination, including resolution of any related appeals or litigation, on the basis of its technical merits.

We record unrecognized tax positions as liabilities in accordance with ASC 740 (including any potential interest and penalties) and we adjust these liabilities when our judgment changes as a result of the evaluation of new information not previously available. Because of the complexity of some of these uncertainties, the ultimate resolution may result in a payment that is materially different from our current estimate of the unrecognized tax benefit liabilities. These differences will be reflected as increases or decreases to income tax expense in the period in which new information is available.

Derivatives and Hedging Activities

In order to reduce the risk of significant interest rate fluctuations on the value of certain assets and liabilities, such as certain mortgage loans held for sale or mortgage servicing rights, the Company utilizes derivatives, such as forward sale commitments, interest rate futures, Eurodollar futures, option contracts, interest rate swaps and swaptions as risk management instruments in its hedging strategy.

All free-standing derivatives are required to be recorded on the consolidated statements of financial condition at fair value. As permitted under U.S. GAAP, the Company nets derivative assets and liabilities, and related collateral, when a legally enforceable master netting agreement exists between the Company and the derivative counterparty.

**HOMESTREET, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 1 — SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:** (cont.)

The accounting for changes in fair value of a derivative depends on whether or not the instrument has been designated and qualifies for hedge accounting. Derivatives that are not designated as hedges are reported and measured at fair value through earnings. The Company does not use derivatives for trading purposes.

Before initiating a position where hedge accounting treatment is desired, the Company formally documents the relationship between the hedging instrument(s) and the hedged item(s), as well as its risk management objective and strategy.

For derivative instruments qualifying for hedge accounting treatment, the instrument is designed as either: (1) a hedge of changes in fair value of a recognized asset or liability or of an unrecognized firm commitment (a fair value hedge), or (2) a hedge of the variability in expected future cash flows associated with an existing recognized asset or liability or a probable forecasted transaction (a cash flow hedge).

Derivatives where the Company has not attempted to achieve or attempted but did not achieve hedge accounting treatment are referred to as economic hedges. The changes in fair value of these instruments are recorded in our consolidated statements of operations in the period in which the change occurs.

In a fair value hedge, changes in the fair value of the derivative and, to the extent that it is effective, changes in the fair value of the hedged asset or liability attributable to the hedged risk are recorded through current period earnings in the same financial statement category as the hedged item.

In a cash flow hedge, the entire change in fair value of the derivative is deferred in OCI and will be released to earnings when the hedged item/transaction impacts earnings.

The Company discontinues hedge accounting when (1) it determines that the derivative is no longer expected to be highly effective in offsetting changes in fair value or cash flows of the designated item; (2) the derivative expires or is sold, terminated, or exercised; (3) the derivative is de-designated from the hedge relationship; or (4) it is no longer probable that a hedged forecasted transaction will occur by the end of the originally specified time period.

If the Company determines that the derivative no longer qualifies as a fair value or cash flow hedge and therefore hedge accounting is discontinued, the derivative (if retained) will continue to be recorded on the balance sheet at its fair value with changes in fair value included in current earnings. For a discontinued fair value hedge, the previously hedged item is no longer adjusted for changes in fair value.

When the Company discontinues hedge accounting because it is not probable that a forecasted transaction will occur, the derivative will continue to be recorded on the balance sheet at its fair value with changes in fair value included in current earnings, and the gains and losses in accumulated other comprehensive income will be recognized immediately in earnings. When the Company discontinues hedge accounting because the hedging instrument is sold, terminated, or de-designated as a hedge, the amount reported in accumulated other comprehensive income through the date of sale, termination, or de-designation will continue to be reported in accumulated other comprehensive income until the forecasted transaction affects earnings. For fair value hedges that are de-designated, the net gain or loss on the underlying transactions being hedged is amortized to other noninterest income over the remaining contractual life of the loans at the time of de-designation. Changes in the fair value of these derivative instruments after de-designation of fair value hedge accounting are recorded in noninterest income in the Consolidated Statements of Operations. As of December 31, 2019 and December 31, 2018 the Company had no derivatives that were designated as fair value hedges or cash flow hedges.

Interest rate lock commitments (“IRLCs”) for single family mortgage loans that we intend to sell are considered free-standing derivatives. For determining the fair value measurement of IRLCs we consider several factors including the fair value in the secondary market of the underlying loan resulting from the exercise of the commitment, the expected net future cash flows related to the associated servicing of the loan and the probability that the loan will not fund according to the terms of the commitment (referred to as a fall-out factor). The value of the underlying loan is affected primarily by changes in interest rates. Management uses forward sales commitments to hedge the interest rate exposure from IRLCs. A forward loan sale commitment protects the Company from losses

**HOMESTREET, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 1 — SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:** (cont.)

on sales of loans arising from the exercise of the loan commitments by securing the ultimate sales price and delivery date of the loan. The Company takes into account various factors and strategies in determining the portion of the mortgage pipeline to hedge economically. Realized and unrealized gains and losses on derivative contracts utilized for economically hedging the mortgage pipeline are recognized as part of the net gain on mortgage loan origination and sale activities within noninterest income.

The Company is exposed to credit risk if derivative counterparties to derivative contracts do not perform as expected. This risk consists primarily of the termination value of agreements where the Company is in a favorable position. The Company minimizes counterparty credit risk through credit approvals, limits, monitoring procedures, and obtaining collateral, as appropriate.

The Company also executes interest rate swaps with commercial banking customers to facilitate their respective risk management strategies. Those interest rate swaps are hedged by simultaneously entering into an offsetting interest rate swap that the Company executes with a third party, such that the Company minimizes its net risk exposure.

Share-Based Employee Compensation

The Company has share-based employee compensation plans as more fully discussed in Note 18, *Share-Based Compensation Plans*. Under the accounting guidance for stock compensation, compensation expense recognized includes the cost for share-based awards, such as nonqualified stock options and restricted stock grants, which are recognized as compensation expense over the requisite service period (generally the vesting period) on a straight line basis. For stock awards that vest upon the satisfaction of a market condition, the Company estimates the service period over which the award is expected to vest. If all conditions required for the vesting of an award are satisfied prior to the end of the estimated vesting period, any unrecognized compensation costs associated with the portion of the award that vested earlier than expected are immediately recognized in earnings.

Fair Value Measurement

The term “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. A fair value measurement assumes that the transaction to sell the asset or transfer the liability occurs in the principal market for the asset or liability or, in the absence of a principal market, the most advantageous market for the asset or liability. The Company’s approach is to maximize the use of observable inputs and minimize the use of unobservable inputs when developing fair value measurements. The degree of management judgment involved in estimating the fair value of a financial instrument or other asset is dependent upon the availability of quoted market prices or observable market value inputs for internal valuation models, used for estimating fair value. For financial instruments that are actively traded in the marketplace or whose values are based on readily available market data, little judgment is necessary when estimating the instrument’s fair value. When observable market prices and data are not readily available, significant management judgment often is necessary to estimate fair value. In those cases, different assumptions could result in significant changes in valuation. See Note 19, *Fair Value Measurement*.

Commitments, Guarantees, and Contingencies

U.S. GAAP requires that a guarantor recognize, at the inception of a guarantee, a liability in an amount equal to the fair value of the obligation undertaken in issuing the guarantee. A guarantee is a contract that contingently requires the guarantor to pay a guaranteed party based upon: (a) changes in an underlying asset, liability or equity security of the guaranteed party; or (b) a third party’s failure to perform under a specified agreement. The Company initially records guarantees at the inception date fair value of the obligation assumed and records the amount in other liabilities. For indemnifications provided in sales agreements, a portion of the sale proceeds is allocated to the guarantee, which adjusts the gain or loss that would otherwise result from the transaction. For these indemnifications, the initial liability is amortized to income as the Company’s risk is reduced (i.e., over time as the Company’s exposure is reduced or when the indemnification expires).

**HOMESTREET, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 1 — SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:** (cont.)

Contingent liabilities, including those that exist as a result of a guarantee or indemnification, are recognized when it becomes probable that a loss has been incurred and the amount of the loss is reasonably estimable. The contingent portion of a guarantee is not recognized if the estimated amount of loss is less than the carrying amount of the liability recognized at inception of the guarantee (as adjusted for any amortization).

The Company typically sells residential mortgage loans servicing retained in either a pooled loan securitization transaction with a government-sponsored enterprise (“GSE”), a whole loan sale to a GSE, or a whole loan sale to market participants such as other financial institutions, who purchase the loans for investment purposes or include them in a private label securitization transaction, or the loans are pooled and sold into a conforming loan securitization with a GSE, provided loan origination parameters conform to GSE guidelines. Substantially all of the Company’s residential mortgage loan sales are whole loan sale transactions with GSEs such as Fannie Mae, Ginnie Mae and Freddie Mac.

The Company may be required to repurchase residential mortgage loans or indemnify loan purchasers due to defects in the origination process of the loan, such as documentation errors, underwriting errors and judgments, early payment defaults and fraud. These obligations expose the Company to any credit loss on the repurchased mortgage loans after accounting for any mortgage insurance that it may receive. Generally, the maximum amount of future payments the Company would be required to make for breaches of these representations and warranties would be equal to the unpaid principal balance of such loans that are deemed to have defects that were sold to purchasers plus, in certain circumstances, accrued and unpaid interest on such loans and certain expenses. See Note 14, *Commitments, Guarantees, and Contingencies*.

The Company sells multifamily loans through the Fannie Mae Delegated Underwriting and Servicing Program (“DUS”<sup>®</sup>, DUS<sup>®</sup> is a registered trademark of Fannie Mae) that are subject to a credit loss sharing arrangement. Under the DUS loss sharing arrangement, a liability is recorded based on the estimated fair value of the obligation under the accounting guidance for guarantees. These liabilities are included within other liabilities. See Note 14, *Commitments, Guarantees, and Contingencies*.

Earnings per Share

The Company calculates earnings per common share (“EPS”) using the two-class method. The two-class method is an earnings allocation formula that treats a participating security as having rights to earnings that otherwise would have been available to common shareholders but does not require the presentation of basic and diluted EPS for securities other than common shares. Under the two-class method, basic EPS is computed by dividing earnings allocated to common shareholders by the weighted average number of common shares outstanding for the period. Earnings allocated to common shareholders represents net income reduced by earnings allocated to participating securities. Diluted EPS is computed in the same manner as basic earnings per share except that the denominator is increased to include the effect of common stock equivalents (for example, stock options and unvested restricted stock) unless those additional shares are anti-dilutive. For the diluted EPS computation, the treasury stock method is applied and compared to the two-class method and whichever method results in a more dilutive impact is used to calculate diluted EPS.

Segment Reporting

In connection with the MSR sales and Board resolution regarding the former Mortgage Banking segment, the Company reassessed its reportable operating segments given these changes and associated changes made to its Chief Operating Decision Maker (CODM) package as of March 31, 2019. The Company concluded that as of March 31, 2019 the CODM evaluates the Company’s performance on a consolidated, entity-wide basis and accordingly has resulted in the elimination of segment reporting. The Company will no longer disclose operating results below the consolidated entity level which is now the reportable segment.



**HOMESTREET, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 1 — SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES: (cont.)**

Advertising Expense

Advertising costs, which consists of media and marketing materials, are expensed as incurred. We incurred \$5.9 million, \$6.9 million and \$6.8 million in advertising expense during the years ended December 31, 2019, 2018 and 2017, respectively.

Recently Adopted Accounting Pronouncements

In October 2018, FASB issued ASU 2018-16, *Derivatives and Hedging (Topic 815): Inclusion of the Secured Overnight Financing Rate (“SOFR”) Overnight Index Swap (“OIS”) Rate as a Benchmark Interest Rate for Hedge Accounting Purposes*. ASU 2018-16 expands the list of U.S. benchmark interest rates permitted in the application of hedge accounting by adding the OIS rate based on SOFR as an eligible benchmark interest rate. We adopted ASU 2018-16 on January 1, 2019 and it did not have a material impact on the Company’s consolidated financial statements.

In July 2018, the FASB issued ASU No. 2018-11, *Leases (Topic 842): Targeted Improvements to Provide Entities with Relief from the Costs of Implementing Certain Aspects of the New Leasing Standard*, ASU No. 2016-02. Specifically, under the amendments in ASU 2018-11: (1) entities may elect not to recast the comparative periods presented when transitioning to the new leasing standard, and (2) lessors may elect to not separate lease and non-lease components from leases when certain conditions are met. The Company adopted this ASU on January 1, 2019 and elected both transition options.

In February 2018, the FASB issued ASU No. 2018-02, *Income Statement — Reporting Comprehensive Income (Topic 220): Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income*, or ASU 2018-02. The amendments in this update allow a reclassification from accumulated other comprehensive income to retained earnings for stranded tax effects resulting from the Tax Cuts and Jobs Act (“Tax Act”). The update does not have any impact on the underlying ASC 740 guidance that requires the effect of a change in tax law be included in income from continuing operations. The Company adopted this ASU in the first quarter of 2019 and reclassified \$1.5 million of stranded tax effects from AOCI to retained earnings at that time.

In August 2017, the FASB issued ASU No. 2017-12, *Derivatives and Hedging (Topic 815): Targeted Improvements to Accounting for Hedging Activities*. This standard better aligns an entity’s risk management activities and financial reporting for hedging relationships through changes to both the designation and measurement guidance for qualifying hedging relationships and the presentation of hedge results. To meet that objective, the amendments expand and refine hedge accounting for both nonfinancial and financial risk components and align the recognition and presentation of the effects of the hedge instruments and the hedged item in the financial statements. The Company adopted the provisions of this guidance on January 1, 2019 and transferred approximately \$66.2 million in held to maturity securities to available for sale and recognized \$548 thousand in AOCI.

In February 2016, the FASB issued ASU 2016-02, *Leases (Topic 842)*. Under the new guidance, lessees are required to recognize the following for all leases: 1) a lease liability, which is the present value of a lessee’s obligation to make lease payments, and 2) a right-of-use asset, which is an asset that represents the lessee’s right to use, or control the use of, a specified asset for the lease term. All entities will classify leases to determine how to recognize lease-related revenue and expense. Quantitative and qualitative disclosures are required by lessees and lessors to meet the objective of enabling users of financial statements to assess the amount, timing, and uncertainty of cash flows arising from leases. The intention is to require enough information to supplement the amounts recorded in the financial statements so that users can understand more about the nature of an entity’s leasing activities. The Company elected the transition option provided in ASU No. 2018-11 (see above), the modified retrospective approach on January 1, 2019.

The Company elected certain relief options offered in ASU 2016-02, including the package of practical expedients (no reassessment of whether any expired or existing contracts contain a lease, no reassessment of lease classification for any expired or existing leases and no reassessment of initial direct costs for existing leases), and the option



**HOMESTREET, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 1 — SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES: (cont.)**

not to recognize right-of-use assets and lease liabilities that arise from short-term leases (i.e., leases with original terms of twelve months or less). The Company elected the hindsight practical expedient, which allows entities to reassess their assumptions used when determining lease term and impairment of right-of-use assets. The Company had facility and equipment lease agreements which were previously being accounted for as operating leases and therefore not being recognized on the Company's consolidated statement of condition. The new guidance required these lease agreements to be recognized on the consolidated statements of condition as a right-of-use asset and a corresponding lease liability. The provisions of ASU No. 2016-02 impacted the Company's consolidated statements of financial condition, along with the Company's regulatory capital ratios. On January 1, 2019, upon adoption of this standard, the Company recognized \$120.8 million and \$136.9 million increase in right-of-use assets and lease liabilities, respectively, based on the present value of the expected remaining lease payments. As most of our leases do not provide an implicit rate, the Company uses the FHLB Des Moines rate at lease commencement date in determining the present value of lease payments. There was no related adjustment to retained earnings. Please see Note 21, Leases for the impact of the adoption of this guidance.

Recent Accounting Pronouncements — Issued Not Yet Adopted

In December 2019, the Financial Accounting Standards Board ("FASB") issued ASU No 2019-12, "Income Taxes (Topic 740): Simplifying the Accounting for Income Taxes" ("ASU 2019-12"). ASU 2019-12 removes certain exceptions to the general principles in Topic 740 in Generally Accepted Accounting Principles. ASU 2019-12 is effective for public entities for fiscal years beginning after December 15, 2020, with early adoption permitted. The Company does not expect ASU 2019-12 to have a material effect on the Company's current financial position, results of operations or financial statement disclosures.

In August 2018, the FASB issued ASU No. 2018-13, *Fair Value Measurement (Topic 820): Disclosure Framework — Changes to the Disclosure Requirements for Fair Value Measurement*. This ASU adds, eliminates, and modifies certain disclosure requirements for fair value measurements. Among the changes, entities will no longer be required to disclose the amount of and reasons for transfers between Level 1 and Level 2 of the fair value hierarchy, but will be required to disclose the range and weighted average used to develop significant unobservable inputs for Level 3 fair value measurements. ASU No. 2018-13 is effective for interim and annual reporting periods beginning after December 15, 2019; early adoption is permitted. Entities are also allowed to elect early adoption of the eliminated or modified disclosure requirements and delay adoption of the added disclosure requirements until their effective date. As ASU No. 2018-13 only revises disclosure requirements, it will not impact the Company's consolidated financial statements.

In January 2017, the FASB issued ASU No. 2017-04, *Intangibles — Goodwill and Other (Topic 350): Simplifying the Test for Goodwill Impairment*, or ASU 2017-04, which eliminates Step 2 from the goodwill impairment test. ASU 2017-04 also eliminates the requirements for any reporting unit with a zero or negative carrying amount to perform a qualitative assessment and, if it fails that qualitative test, to perform Step 2 of the goodwill impairment test. An entity still has the option to perform the qualitative assessment for a reporting unit to determine if the quantitative impairment test is necessary. Adoption of ASU 2017-04 is required for annual or interim goodwill impairment tests in fiscal years beginning after December 15, 2019 with early adoption permitted for annual or interim goodwill impairment tests performed after January 1, 2017. The Company does not expect the adoption of ASU 2017-04 to have a material impact on its consolidated financial statements.

In June 2016, FASB issued ASU No. 2016-13, *Measurement of Credit Losses on Financial Instruments*. Current U.S. GAAP requires an "incurred loss" methodology for recognizing credit losses that delay recognition until it is probable a loss has been incurred. The main objective of this ASU is to provide financial statement users with more decision-useful information about the expected credit losses on financial instruments and other commitments to extend credit held by a reporting entity at each reporting date. The amendment affects loans, debt securities, trade receivables, net investments in leases, off-balance-sheet credit exposures, reinsurance receivables, and any other financial asset not excluded from the scope that has the contractual right to receive cash. The amendments in this ASU replace the incurred loss impairment model in current U.S. GAAP with a methodology that reflects expected credit losses and requires consideration of a broader range of reasonable and supportable information to inform

**HOMESTREET, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 1 — SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:** (cont.)

credit loss estimates. The amendments in this ASU require a financial asset (or group of financial assets) measured at amortized cost to be presented at the net amount expected to be collected. The allowance for credit losses is a valuation account that is deducted from the amortized cost basis of the financial asset(s) to present the net carrying value at the amount expected to be collected on the financial asset. Our allowance for credit losses includes both the allowance for loan losses and a separate allowance for losses related to unfunded loan commitments. The measurement of expected credit losses will be based on relevant information about past events, including historical experience, current conditions, and reasonable and supportable forecasts that affect the collectability of the reported amount. The amendments in this ASU broaden the information that an entity must consider in developing its expected credit loss estimate for assets measured either collectively or individually. The use of forecasted information incorporates more timely information in the estimate of expected credit loss, which will be more decision relevant to users of the financial statements. The amendments in this ASU will be effective for fiscal years beginning after December 15, 2019, including interim periods within those fiscal years. The Company adopted this ASU on January 1, 2020.

The Company has completed the development of the credit loss models for all loan portfolios and has tested these models and validated data inputs, as well as developed the policies, systems and controls that will be required to implement CECL. Based on forecasted economic conditions and portfolio composition at December 31, 2019, the adoption of the CECL standard is estimated to result in an increase in our allowance for credit losses of approximately \$3.7 million at January 1, 2020, a 9% increase, as compared to our December 31, 2019 aggregate reserve levels. The estimated increase is driven by the fact that the allowance will cover expected credit losses over the full expected life of the loan portfolios and will also consider forecasts of expected future economic conditions. The extent of the impact of the adoption of CECL on the Company's consolidated financial statements may vary and will depend on, completion of the Company's models, policies and management judgment's, and the composition of the loan portfolios. At adoption, on January 1, 2020, we recorded a cumulative-effect adjustment to retained earnings equal to the change in the allowance for credit losses.

In addition, the current accounting policy and procedures for other-than-temporary impairment on investment securities classified as available for sale will be replaced with an allowance approach. Based on the credit quality of our existing debt securities portfolio, the Company determined the CECL allowance for credit losses for HTM and AFS debt securities is not material.

**NOTE 2 — DISCONTINUED OPERATIONS:**

On March 31, 2019, based on mortgage market conditions and the operating environment, the Board adopted a Resolution of Exit or Disposal of HLC Based Mortgage Banking Operations to sell or abandon the assets and related personnel associated with those operations. The assets that were sold or abandoned largely represented the Company's former Mortgage Banking segment, the activities of which related to originating, servicing, underwriting, funding and selling single family residential mortgage loans.

The Company determined that the above actions constituted commitment to a plan of exit or disposal of certain long-lived assets (through sale or abandonment) and termination of employees. Further, the Company determined that the shift from a large-scale HLC based originator and servicer to a branch-focused product offering represented a strategic shift as we moved away from a higher cost, high volume sales-focused origination business to a lower cost, lower volume model that targeted our bank customers. As a result, the HLC-related mortgage banking operations are reported separately from the continuing operations as discontinued operations. In addition, the former Mortgage Banking operating segment and reporting unit was eliminated. This has resulted in a recast of the financial statements in the current and all comparative periods as detailed below.

In the first quarter of 2019, the Company successfully closed and settled two sales of the rights to service \$14.26 billion in total unpaid principal balance of single family mortgage loans serviced for Federal National Mortgage Association ("Fannie Mae"), Federal Home Loan Mortgage Corporation ("Freddie Mac") and Government National Mortgage Association ("Ginnie Mae"), representing approximately 71% of HomeStreet's total single family mortgage loans serviced for others portfolio as of December 31, 2018. These sales resulted in a \$919 thousand

**HOMESTREET, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 2 — DISCONTINUED OPERATIONS:** (cont.)

pre-tax loss from discontinued operations during the year ended December 31, 2019. The Company finalized the servicing transfer for these loans in 2019 and subserviced these loans through the transfer dates. These loans are excluded from the Company’s MSR portfolio at December 31, 2019.

On April 4, 2019 the Company entered into a definitive agreement related to the sale of the HLC based mortgage origination business assets and transfer of personnel to Homebridge Financial Services, Inc. — (“Homebridge”).

On June 24, 2019 the Company completed the sale with Homebridge. This sale included 47 stand-alone HLCs and the transfer of certain related mortgage personnel. These HLCs, along with certain other mortgage banking related assets and liabilities that were to be sold or abandoned within one year, are classified as discontinued operations in the accompanying Consolidated Statements of Financial Condition and Consolidated Statements of Operations. HLCs that were not sold were closed during the second quarter and none remained as of December 31, 2019. Certain remaining bank location-based components of the Company’s former Mortgage Banking segment, including MSRs on certain mortgage loans that were not part of the sales and right-of-use assets and lease liabilities where we did not obtain full landlord release have been classified as continuing operations based on management’s intent.

At the end of the second quarter 2019, we also entered into a non-binding letter of interest to sell our ownership interest in WMS LLC at which time related operations also met the criteria to be included in discontinued operations for all periods presented. The sales transaction was closed in November 2019, resulting in an immaterial loss on disposal.

The following table summarizes the calculation of the net loss on disposal of discontinued operations.

| <b>(in thousands)</b>                                      | <b>Year Ended<br/>December 31,<br/>2019</b> |
|--|---|
| Proceeds from asset sales . . . . .                        | \$ 186,692                                  |
| Book value of assets sold . . . . .                        | <u>181,243</u>                              |
| Gain on assets sold . . . . .                              | 5,449                                       |
| Transaction costs . . . . .                                | 8,770                                       |
| Compensation expense related to the transactions . . . . . | 4,636                                       |
| Facility and IT related costs . . . . .                    | <u>13,660</u>                               |
| Total costs . . . . .                                      | <u>27,066</u>                               |
| Net loss on disposal of discontinued operations . . . . .  | <u>\$ (21,617)</u>                          |

The carrying amount of major classes of assets and liabilities related to discontinued operations consisted of the following.

| <b>(in thousands)</b>                            | <b>December 31,<br/>2019</b> | <b>December 31,<br/>2018</b> |
|--|------------------------------|------------------------------|
| <b>ASSETS</b>                                    |                              |                              |
| Loans held-for-sale, at fair value . . . . .     | \$ 26,123                    | \$ 269,683                   |
| Mortgage serving rights . . . . .                | —                            | 177,121                      |
| Premises and equipment, net. . . . .             | —                            | 6,689                        |
| Other assets <sup>(1)</sup> . . . . .            | <u>2,505</u>                 | <u>23,541</u>                |
| Assets of discontinued operations . . . . .      | <u>\$ 28,628</u>             | <u>\$ 477,034</u>            |
| <b>LIABILITIES</b>                               |                              |                              |
| Deposits . . . . .                               | \$ —                         | \$ 162,850                   |
| Accrued expenses and other liabilities . . . . . | <u>2,603</u>                 | <u>4,271</u>                 |
| Liabilities of discontinued operations . . . . . | <u>\$ 2,603</u>              | <u>\$ 167,121</u>            |

(1) Includes \$227 thousand and \$15.5 million of derivative balances at December 31, 2019 and December 31, 2018, respectively.

**HOMESTREET, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 2 — DISCONTINUED OPERATIONS:** (cont.)

Statements of Operations of Discontinued Operations

| <u>(in thousands)</u>                                | <b>Year Ended December 31,</b> |                  |                  |
|--|--------------------------------|------------------|------------------|
|  | <b>2019</b>                    | <b>2018</b>      | <b>2017</b>      |
| Net interest income . . . . .                        | \$ 5,858                       | \$ 12,516        | \$ 19,897        |
| Noninterest income . . . . .                         | 63,713                         | 200,426          | 269,557          |
| Noninterest expense . . . . .                        | 97,856                         | 195,332          | 249,039          |
| (Loss) income before income taxes . . . . .          | (28,285)                       | 17,610           | 40,415           |
| Income tax (benefit) expense . . . . .               | (5,077)                        | 3,806            | 14,137           |
| (Loss) income from discontinued operations . . . . . | <u>\$ (23,208)</u>             | <u>\$ 13,804</u> | <u>\$ 26,278</u> |

Cash Flows from Discontinued Operations

| <u>(in thousands)</u>   | <b>Year Ended December 31,</b> |             |             |
|---|--------------------------------|-------------|-------------|
|   | <b>2019</b>                    | <b>2018</b> | <b>2017</b> |
| Net cash provided by operating activities . . . . .           | \$ 238,212                     | \$ 201,001  | \$ 111,682  |
| Net cash provided by (used in) investing activities . . . . . | 185,458                        | 64,849      | (4,369)     |

**NOTE 3 — BUSINESS COMBINATIONS:**

Recent Acquisition Activity

On March 25, 2019, the Company completed its acquisition of a branch and its related deposits and loans in San Diego County from Silvergate Bank, along with its business lending team. The application of the acquisition method of accounting resulted in goodwill of \$5.9 million.

On September 15, 2017, the Company completed its acquisition of one branch and its related deposits in San Diego County, from Opus Bank. The application of the acquisition method of accounting resulted in goodwill of \$389 thousand.

**NOTE 4 — REGULATORY CAPITAL REQUIREMENTS:**

The Company and Bank are subject to various regulatory capital requirements administered by the federal banking agencies. Failure to meet minimum capital requirements can initiate certain mandatory and possible additional discretionary actions by regulators that, if undertaken, could have a material effect on the Company's operations and financial statements. Under capital adequacy guidelines, we must meet specific capital guidelines that involve quantitative measures of our assets, liabilities, and certain off-balance sheet items as calculated under regulatory accounting practices. The Company and Bank's capital amounts and classifications are also subject to qualitative judgments by the regulators about risk components, asset risk weighting, and other factors.

Quantitative measures established by regulation to ensure capital adequacy require the Bank and the Company to maintain minimum amounts and ratios of Tier 1 leverage capital, common equity risk-based capital, Tier 1 risk-based capital and total risk-based capital (as defined in the regulations). The regulators also have the ability to impose elevated capital requirements in certain circumstances. At December 31, 2019 and 2018 the Bank's capital ratios meet the regulatory capital category of "well capitalized" as defined by the Rules.

**HOMESTREET, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 4 — REGULATORY CAPITAL REQUIREMENTS:** (cont.)

The Bank's and the Company's capital amounts and ratios under Basel III are included in the following tables:

| <b>HomeStreet Bank</b><br><b>(dollars in thousands)</b>            | <b>At December 31, 2019</b> |              |  |              |  |              |
|--|-----------------------------|--------------|--|--------------|--|--------------|
|  | <b>Actual</b>               |              | <b>For Minimum<br/>Capital Adequacy<br/>Purposes</b> |              | <b>To Be Categorized As<br/>"Well Capitalized"<br/>Under Prompt<br/>Corrective Action<br/>Provisions</b> |              |
|  | <b>Amount</b>               | <b>Ratio</b> | <b>Amount</b>  | <b>Ratio</b> | <b>Amount</b>  | <b>Ratio</b> |
| Tier 1 leverage capital<br>(to average assets) . . . . .           | \$ 712,596                  | 10.56%       | \$ 269,930   | 4.0%         | \$ 337,413   | 5.0%         |
| Common equity tier 1 capital<br>(to risk-weighted assets). . . . . | 712,596                     | 13.50        | 237,451  | 4.5          | 342,985  | 6.5          |
| Tier 1 risk-based capital<br>(to risk-weighted assets). . . . .    | 712,596                     | 13.50        | 316,602  | 6.0          | 422,136  | 8.0          |
| Total risk-based capital<br>(to risk-weighted assets). . . . .     | 758,303                     | 14.37        | 422,136  | 8.0          | 527,669  | 10.0         |

| <b>HomeStreet, Inc.</b><br><b>(dollars in thousands)</b>           | <b>At December 31, 2019</b> |              |  |              |  |              |
|--|-----------------------------|--------------|--|--------------|--|--------------|
|  | <b>Actual</b>               |              | <b>For Minimum<br/>Capital Adequacy<br/>Purposes</b> |              | <b>To Be Categorized As<br/>"Well Capitalized"<br/>Under Prompt<br/>Corrective Action<br/>Provisions</b> |              |
|  | <b>Amount</b>               | <b>Ratio</b> | <b>Amount</b>  | <b>Ratio</b> | <b>Amount</b>  | <b>Ratio</b> |
| Tier 1 leverage capital<br>(to average assets) . . . . .           | \$ 691,323                  | 10.16%       | \$ 272,253   | 4.0%         | \$ 340,316   | 5.0%         |
| Common equity tier 1 capital<br>(to risk-weighted assets). . . . . | 631,323                     | 11.43        | 248,523  | 4.5          | 358,977  | 6.5          |
| Tier 1 risk-based capital<br>(to risk-weighted assets). . . . .    | 691,323                     | 12.52        | 331,364  | 6.0          | 441,818  | 8.0          |
| Total risk-based capital<br>(to risk-weighted assets). . . . .     | 739,812                     | 13.40        | 441,818  | 8.0          | 552,273  | 10.0         |

| <b>HomeStreet Bank</b><br><b>(dollars in thousands)</b>            | <b>At December 31, 2018</b> |              |  |              |  |              |
|--|-----------------------------|--------------|--|--------------|--|--------------|
|  | <b>Actual</b>               |              | <b>For Minimum<br/>Capital Adequacy<br/>Purposes</b> |              | <b>To Be Categorized As<br/>"Well Capitalized"<br/>Under Prompt<br/>Corrective Action<br/>Provisions</b> |              |
|  | <b>Amount</b>               | <b>Ratio</b> | <b>Amount</b>  | <b>Ratio</b> | <b>Amount</b>  | <b>Ratio</b> |
| Tier 1 leverage capital<br>(to average assets) . . . . .           | \$ 707,710                  | 10.15%       | \$ 278,898   | 4.0%         | \$ 348,622   | 5.0%         |
| Common equity tier 1 capital<br>(to risk-weighted assets). . . . . | 707,710                     | 13.82        | 230,471  | 4.5          | 332,902  | 6.5          |
| Tier 1 risk-based capital<br>(to risk-weighted assets). . . . .    | 707,710                     | 13.82        | 307,295  | 6.0          | 409,726  | 8.0          |
| Total risk-based capital<br>(to risk-weighted assets). . . . .     | 753,742                     | 14.72        | 409,726  | 8.0          | 512,158  | 10.0         |

**HOMESTREET, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 4 — REGULATORY CAPITAL REQUIREMENTS: (cont.)**

| <b>HomeStreet, Inc.</b><br><b>(dollars in thousands)</b>            | <b>At December 31, 2018</b> |              |  |              |  |              |
|---|-----------------------------|--------------|--|--------------|--|--------------|
|   | <b>Actual</b>               |              | <b>For Minimum<br/>Capital Adequacy<br/>Purposes</b> |              | <b>To Be Categorized As<br/>“Well Capitalized”<br/>Under Prompt<br/>Corrective Action<br/>Provisions</b> |              |
|   | <b>Amount</b>               | <b>Ratio</b> | <b>Amount</b>  | <b>Ratio</b> | <b>Amount</b>  | <b>Ratio</b> |
| Tier 1 leverage capital<br>(to average assets) . . . . .            | \$ 667,301                  | 9.51%        | \$ 280,592   | 4.0%         | \$ 350,740   | 5.0%         |
| Common equity tier 1 capital<br>(to risk-weighted assets) . . . . . | 607,388                     | 11.26        | 242,832  | 4.5          | 350,757  | 6.5          |
| Tier 1 risk-based capital<br>(to risk-weighted assets) . . . . .    | 667,301                     | 12.37        | 323,776  | 6.0          | 431,701  | 8.0          |
| Total risk-based capital<br>(to risk-weighted assets) . . . . .     | 715,848                     | 13.27        | 431,701  | 8.0          | 539,626  | 10.0         |

At periodic intervals, the FDIC and the Washington State Department of Financial Institutions (“WDFI”) routinely examine the Bank’s financial statements as part of their legally prescribed oversight of the banking industry. Based on their examinations, these regulators can direct that the Bank’s financial statements be adjusted in accordance with their findings.

**NOTE 5 — INVESTMENT SECURITIES:**

The following tables set forth certain information regarding the amortized cost and fair values of our investment securities available for sale and held to maturity.

| <b>(in thousands)</b>                    | <b>At December 31, 2019</b> |                                       |  |                       |
|--|-----------------------------|---------------------------------------|--|-----------------------|
|  | <b>Amortized<br/>cost</b>   | <b>Gross<br/>unrealized<br/>gains</b> | <b>Gross<br/>unrealized<br/>losses</b> | <b>Fair<br/>value</b> |
| <b>AVAILABLE FOR SALE</b>                |                             |                                       |  |                       |
| Mortgage-backed securities:              |                             |                                       |  |                       |
| Residential . . . . .                    | \$ 93,283                   | \$ 120                                | \$ (1,708)                             | \$ 91,695             |
| Commercial . . . . .                     | 37,972                      | 411                                   | (358)                                  | 38,025                |
| Collateralized mortgage obligations:     |                             |                                       |  |                       |
| Residential . . . . .                    | 292,370                     | 935                                   | (1,687)                                | 291,618               |
| Commercial . . . . .                     | 156,693                     | 684                                   | (1,223)                                | 156,154               |
| Municipal bonds . . . . .                | 333,303                     | 8,997                                 | (982)                                  | 341,318               |
| Corporate debt securities . . . . .      | 18,391                      | 313                                   | (43)                                   | 18,661                |
| U.S. Treasury securities . . . . .       | 1,296                       | 11                                    | —                                      | 1,307                 |
|  | \$ 933,308                  | \$ 11,471                             | \$ (6,001)                             | \$ 938,778            |
| <b>HELD TO MATURITY</b>                  |                             |                                       |  |                       |
| Municipal bonds <sup>(1)</sup> . . . . . | 4,372                       | 129                                   | —                                      | 4,501                 |
|  | \$ 4,372                    | \$ 129                                | \$ —                                   | \$ 4,501              |

(1) In conjunction with adopting ASU 2017-12, in the first quarter of 2019, we transferred \$66.2 million in HTM securities to AFS.



**HOMESTREET, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 5 — INVESTMENT SECURITIES: (cont.)**

| (in thousands)                               | At December 31, 2018 |                              |                               |               |
|--|----------------------|------------------------------|-------------------------------|---------------|
|  | Amortized<br>cost    | Gross<br>unrealized<br>gains | Gross<br>unrealized<br>losses | Fair<br>value |
| <b>AVAILABLE FOR SALE</b>                    |                      |                              |                               |               |
| Mortgage-backed securities:                  |                      |                              |                               |               |
| Residential. . . . .                         | \$ 112,852           | \$ 19                        | \$ (4,910)                    | \$ 107,961    |
| Commercial. . . . .                          | 34,892               | 109                          | (487)                         | 34,514        |
| Collateralized mortgage obligations:         |                      |                              |                               |               |
| Residential. . . . .                         | 171,412              | 221                          | (4,889)                       | 166,744       |
| Commercial. . . . .                          | 118,555              | 140                          | (2,021)                       | 116,674       |
| Municipal bonds . . . . .                    | 393,463              | 1,526                        | (9,334)                       | 385,655       |
| Corporate debt securities . . . . .          | 21,177               | 1                            | (1,183)                       | 19,995        |
| U.S. Treasury securities. . . . .            | 11,211               | 6                            | (317)                         | 10,900        |
| Agency debentures . . . . .                  | 9,876                | —                            | (351)                         | 9,525         |
|  | \$ 873,438           | \$ 2,022                     | \$ (23,492)                   | \$ 851,968    |
| <b>HELD TO MATURITY</b>                      |                      |                              |                               |               |
| Mortgage-backed securities:                  |                      |                              |                               |               |
| Residential. . . . .                         | \$ 11,071            | \$ —                         | \$ (274)                      | \$ 10,797     |
| Commercial. . . . .                          | 17,307               | 30                           | (311)                         | 17,026        |
| Collateralized mortgage obligations. . . . . | 15,624               | 10                           | (65)                          | 15,569        |
| Municipal bonds . . . . .                    | 27,191               | 190                          | (319)                         | 27,062        |
| Corporate debt securities . . . . .          | 92                   | —                            | —                             | 92            |
|  | \$ 71,285            | \$ 230                       | \$ (969)                      | \$ 70,546     |

Mortgage-backed securities (“MBS”) and collateralized mortgage obligations (“CMO”) represent securities primarily issued by government sponsored enterprises (“GSEs”). Most of the MBS and CMO securities in our investment portfolio are guaranteed by Fannie Mae, Ginnie Mae or Freddie Mac. Municipal bonds are comprised of general obligation bonds (i.e., backed by the general credit of the issuer) and revenue bonds (i.e., backed by either collateral or revenues from the specific project being financed) issued by various municipal corporations. As of December 31, 2019 and 2018, all securities held, including municipal bonds and corporate debt securities, were rated investment grade based upon external ratings where available and, where not available, based upon internal ratings which correspond to ratings as defined by Standard and Poor’s Rating Services (“S&P”) or Moody’s Investors Services (“Moody’s”). As of December 31, 2019 and 2018, substantially all securities held had ratings available by external ratings agencies.

**HOMESTREET, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 5 — INVESTMENT SECURITIES: (cont.)**

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

| (in thousands)                       | At December 31, 2019          |                   |                               |                   |                               |                   |
|--------------------------------------|-------------------------------|-------------------|-------------------------------|-------------------|-------------------------------|-------------------|
|                                      | Less than 12 months           |                   | 12 months or more             |                   | Total                         |                   |
|                                      | Gross<br>unrealized<br>losses | Fair<br>value     | Gross<br>unrealized<br>losses | Fair<br>value     | Gross<br>unrealized<br>losses | Fair<br>value     |
| <b>AVAILABLE FOR SALE</b>            |                               |                   |                               |                   |                               |                   |
| Mortgage-backed securities:          |                               |                   |                               |                   |                               |                   |
| Residential. . . . .                 | \$ (409)                      | \$ 18,440         | \$ (1,299)                    | \$ 68,362         | \$ (1,708)                    | \$ 86,802         |
| Commercial. . . . .                  | (352)                         | 21,494            | (6)                           | 2,483             | (358)                         | 23,977            |
| Collateralized mortgage obligations: |                               |                   |                               |                   |                               |                   |
| Residential. . . . .                 | (965)                         | 171,708           | (722)                         | 29,264            | (1,687)                       | 200,972           |
| Commercial. . . . .                  | (680)                         | 67,160            | (543)                         | 41,605            | (1,223)                       | 108,765           |
| Municipal bonds . . . . .            | (334)                         | 39,127            | (648)                         | 45,869            | (982)                         | 84,996            |
| Corporate debt securities . . . .    | (5)                           | 3,689             | (38)                          | 1,743             | (43)                          | 5,432             |
|                                      | <u>\$ (2,745)</u>             | <u>\$ 321,618</u> | <u>\$ (3,256)</u>             | <u>\$ 189,326</u> | <u>\$ (6,001)</u>             | <u>\$ 510,944</u> |

There were no held to maturity securities in an unrealized loss position at December 31, 2019.

| (in thousands)                       | At December 31, 2018          |                   |                               |                   |                               |                   |
|--------------------------------------|-------------------------------|-------------------|-------------------------------|-------------------|-------------------------------|-------------------|
|                                      | Less than 12 months           |                   | 12 months or more             |                   | Total                         |                   |
|                                      | Gross<br>unrealized<br>losses | Fair<br>value     | Gross<br>unrealized<br>losses | Fair<br>value     | Gross<br>unrealized<br>losses | Fair<br>value     |
| <b>AVAILABLE FOR SALE</b>            |                               |                   |                               |                   |                               |                   |
| Mortgage-backed securities:          |                               |                   |                               |                   |                               |                   |
| Residential. . . . .                 | \$ (34)                       | \$ 1,269          | \$ (4,876)                    | \$ 104,822        | \$ (4,910)                    | \$ 106,091        |
| Commercial. . . . .                  | —                             | —                 | (487)                         | 18,938            | (487)                         | 18,938            |
| Collateralized mortgage obligations: |                               |                   |                               |                   |                               |                   |
| Residential. . . . .                 | (131)                         | 24,085            | (4,758)                       | 128,899           | (4,889)                       | 152,984           |
| Commercial. . . . .                  | (350)                         | 22,051            | (1,671)                       | 73,429            | (2,021)                       | 95,480            |
| Municipal bonds . . . . .            | (1,283)                       | 85,057            | (8,051)                       | 201,189           | (9,334)                       | 286,246           |
| Corporate debt securities . . . .    | (104)                         | 5,557             | (1,079)                       | 14,213            | (1,183)                       | 19,770            |
| U.S. Treasury securities. . . . .    | —                             | —                 | (317)                         | 9,598             | (317)                         | 9,598             |
| Agency debentures . . . . .          | —                             | —                 | (351)                         | 9,525             | (351)                         | 9,525             |
|                                      | <u>\$ (1,902)</u>             | <u>\$ 138,019</u> | <u>\$ (21,590)</u>            | <u>\$ 560,613</u> | <u>\$ (23,492)</u>            | <u>\$ 698,632</u> |

**HELD TO MATURITY**

|  |                 |                  |                 |                  |                 |                  |
|--|-----------------|------------------|-----------------|------------------|-----------------|------------------|
| Mortgage-backed securities:                  |                 |                  |                 |                  |                 |                  |
| Residential. . . . .                         | \$ (31)         | \$ 2,314         | \$ (243)        | \$ 6,197         | \$ (274)        | \$ 8,511         |
| Commercial. . . . .                          | (24)            | 2,800            | (287)           | 11,256           | (311)           | 14,056           |
| Collateralized mortgage obligations. . . . . |                 |                  |                 |                  |                 |                  |
|  | (65)            | 10,597           | —               | —                | (65)            | 10,597           |
| Municipal bonds . . . . .                    | (102)           | 7,210            | (217)           | 11,273           | (319)           | 18,483           |
|  | <u>\$ (222)</u> | <u>\$ 22,921</u> | <u>\$ (747)</u> | <u>\$ 28,726</u> | <u>\$ (969)</u> | <u>\$ 51,647</u> |

**HOMESTREET, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 5 — INVESTMENT SECURITIES: (cont.)**

The Company has evaluated securities available for sale that are in an unrealized loss position and has determined that the decline in value is temporary and is related to the change in market interest rates since purchase. The decline in value is not related to any issuer- or industry-specific credit event. The Company has not identified any expected credit losses on its debt securities as of December 31, 2019 and 2018. In addition, as of December 31, 2019 and 2018, the Company had not made a decision to sell any of its debt securities held, nor did the Company consider it more likely than not that it would be required to sell such securities before recovery of their amortized cost basis.

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

|                                      | At December 31, 2019 |                              |                                      |                              |                                       |                              |                    |                              |                   |                              |
|--------------------------------------|----------------------|------------------------------|--------------------------------------|------------------------------|---------------------------------------|------------------------------|--------------------|------------------------------|-------------------|------------------------------|
|                                      | Within one year      |                              | After one year<br>through five years |                              | After five years<br>through ten years |                              | After<br>ten years |                              | Total             |                              |
|                                      | Fair<br>Value        | Weighted<br>Average<br>Yield | Fair<br>Value                        | Weighted<br>Average<br>Yield | Fair<br>Value                         | Weighted<br>Average<br>Yield | Fair<br>Value      | Weighted<br>Average<br>Yield | Fair<br>Value     | Weighted<br>Average<br>Yield |
| <b>(dollars in thousands)</b>        |                      |                              |                                      |                              |                                       |                              |                    |                              |                   |                              |
| <b>AVAILABLE FOR SALE</b>            |                      |                              |                                      |                              |                                       |                              |                    |                              |                   |                              |
| Mortgage-backed securities:          |                      |                              |                                      |                              |                                       |                              |                    |                              |                   |                              |
| Residential . . . . .                | \$ —                 | —%                           | \$ 3                                 | 1.30%                        | \$ 5,428                              | 1.67%                        | \$ 86,264          | 2.10%                        | \$ 91,695         | 2.08%                        |
| Commercial . . . . .                 | —                    | —                            | 7,514                                | 2.73                         | 20,631                                | 2.50                         | 9,880              | 2.32                         | 38,025            | 2.49                         |
| Collateralized mortgage obligations: |                      |                              |                                      |                              |                                       |                              |                    |                              |                   |                              |
| Residential . . . . .                | —                    | —                            | —                                    | —                            | —                                     | —                            | 291,618            | 2.39                         | 291,618           | 2.39                         |
| Commercial . . . . .                 | —                    | —                            | 7,563                                | 2.20                         | 68,470                                | 2.41                         | 80,121             | 2.31                         | 156,154           | 2.35                         |
| Municipal bonds . . . . .            | 5,337                | 3.41                         | 555                                  | 3.90                         | 13,000                                | 3.01                         | 322,426            | 3.61                         | 341,318           | 3.59                         |
| Corporate debt securities . .        | 1,007                | 3.40                         | 7,544                                | 3.64                         | 10,022                                | 3.70                         | 88                 | 6.10                         | 18,661            | 3.67                         |
| U.S. Treasury securities . .         | 1,307                | 2.82                         | —                                    | —                            | —                                     | —                            | —                  | —                            | 1,307             | 2.82                         |
| Total available for sale . .         | <u>\$ 7,651</u>      | 3.31%                        | <u>\$ 23,179</u>                     | 2.87%                        | <u>\$ 117,551</u>                     | 2.57%                        | <u>\$ 790,397</u>  | 2.84%                        | <u>\$ 938,778</u> | 2.81%                        |
| <b>HELD TO MATURITY</b>              |                      |                              |                                      |                              |                                       |                              |                    |                              |                   |                              |
| Municipal bonds . . . . .            | \$ —                 | —%                           | \$ 1,787                             | 2.90%                        | \$ 2,714                              | 2.09%                        | \$ —               | —%                           | \$ 4,501          | 2.41%                        |
| Total held to maturity . . .         | <u>\$ —</u>          | —%                           | <u>\$ 1,787</u>                      | 2.90%                        | <u>\$ 2,714</u>                       | 2.09%                        | <u>\$ —</u>        | —%                           | <u>\$ 4,501</u>   | 2.41%                        |

**HOMESTREET, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 5 — INVESTMENT SECURITIES: (cont.)**

| (dollars in thousands)                        | At December 31, 2018 |                              |                                      |                              |                                       |                              |                    |                              |                   |                              |
|---|----------------------|------------------------------|--------------------------------------|------------------------------|---------------------------------------|------------------------------|--------------------|------------------------------|-------------------|------------------------------|
|   | Within one year      |                              | After one year<br>through five years |                              | After five years<br>through ten years |                              | After<br>ten years |                              | Total             |                              |
|   | Fair<br>Value        | Weighted<br>Average<br>Yield | Fair<br>Value                        | Weighted<br>Average<br>Yield | Fair<br>Value                         | Weighted<br>Average<br>Yield | Fair<br>Value      | Weighted<br>Average<br>Yield | Fair<br>Value     | Weighted<br>Average<br>Yield |
| <b>AVAILABLE FOR SALE</b>                     |                      |                              |                                      |                              |                                       |                              |                    |                              |                   |                              |
| Mortgage-backed securities:                   |                      |                              |                                      |                              |                                       |                              |                    |                              |                   |                              |
| Residential . . . . .                         | \$ —                 | —%                           | \$ —                                 | —%                           | \$ 7,094                              | 1.62%                        | \$ 100,867         | 2.05%                        | \$ 107,961        | 2.03%                        |
| Commercial . . . . .                          | —                    | —                            | 14,175                               | 2.20                         | 16,737                                | 2.99                         | 3,602              | 2.90                         | 34,514            | 2.66                         |
| Collateralized mortgage obligations:          |                      |                              |                                      |                              |                                       |                              |                    |                              |                   |                              |
| Residential . . . . .                         | —                    | —                            | —                                    | —                            | —                                     | —                            | 166,744            | 2.43                         | 166,744           | 2.43                         |
| Commercial . . . . .                          | —                    | —                            | 9,008                                | 2.42                         | 29,292                                | 2.88                         | 78,374             | 2.42                         | 116,674           | 2.53                         |
| Municipal bonds . . . . .                     | 5,670                | 2.12                         | 16,276                               | 2.24                         | 30,659                                | 2.89                         | 333,050            | 3.51                         | 385,655           | 3.39                         |
| Corporate debt securities . .                 | —                    | —                            | 3,949                                | 2.96                         | 13,608                                | 3.31                         | 2,438              | 3.65                         | 19,995            | 3.29                         |
| U.S. Treasury securities . .                  | —                    | —                            | 10,900                               | 1.87                         | —                                     | —                            | —                  | —                            | 10,900            | 1.87                         |
| Agency debentures . . . . .                   | —                    | —                            | —                                    | —                            | 9,525                                 | 2.23                         | —                  | —                            | 9,525             | 2.23                         |
| Total available for sale . .                  | <u>\$ 5,670</u>      | 2.12%                        | <u>\$ 54,308</u>                     | 2.24%                        | <u>\$ 106,915</u>                     | 2.81%                        | <u>\$ 685,075</u>  | 2.90%                        | <u>\$ 851,968</u> | 2.84%                        |
| <b>HELD TO MATURITY</b>                       |                      |                              |                                      |                              |                                       |                              |                    |                              |                   |                              |
| Mortgage-backed securities:                   |                      |                              |                                      |                              |                                       |                              |                    |                              |                   |                              |
| Residential . . . . .                         | \$ —                 | —%                           | \$ —                                 | —%                           | \$ —                                  | —%                           | \$ 10,797          | 2.82%                        | \$ 10,797         | 2.82%                        |
| Commercial . . . . .                          | —                    | —                            | 12,147                               | 2.51                         | 4,879                                 | 2.64                         | —                  | —                            | 17,026            | 2.55                         |
| Collateralized mortgage obligations . . . . . |                      |                              |                                      |                              |                                       |                              |                    |                              |                   |                              |
| Municipal bonds . . . . .                     | —                    | —                            | 7,205                                | 3.59                         | —                                     | —                            | 8,364              | 2.94                         | 15,569            | 3.24                         |
| Corporate debt securities . .                 | —                    | —                            | —                                    | —                            | —                                     | —                            | 92                 | 6.00                         | 92                | 6.00                         |
| Total held to maturity . . .                  | <u>\$ —</u>          | —%                           | <u>\$ 21,142</u>                     | 2.91%                        | <u>\$ 10,530</u>                      | 2.45%                        | <u>\$ 38,874</u>   | 3.07%                        | <u>\$ 70,546</u>  | 2.93%                        |

Sales of investment securities available for sale were as follows.

| (in thousands)         | Years Ended December 31, |           |            |
|------------------------|--------------------------|-----------|------------|
|                        | 2019                     | 2018      | 2017       |
| Proceeds . . . . .     | \$ 184,871               | \$ 46,081 | \$ 397,492 |
| Gross gains . . . . .  | 894                      | 310       | 1,214      |
| Gross losses . . . . . | (901)                    | (75)      | (725)      |

The following table summarizes the carrying value of securities pledged as collateral to secure public deposits, borrowings and other purposes as permitted or required by law.

| (in thousands)   | At<br>December 31,<br>2019 | At<br>December 31,<br>2018 |
|--|----------------------------|----------------------------|
| Federal Home Loan Bank to secure borrowings . . . . .                      | \$ —                       | \$ 63,179                  |
| Washington and California State to secure public deposits . . . . .        | 200,571                    | 126,565                    |
| Securities pledged to secure derivatives in a liability position . . . . . | —                          | 5,077                      |
| Other securities pledged . . . . .   | 4,332                      | 5,147                      |
| Total securities pledged as collateral . . . . .                           | <u>\$ 204,903</u>          | <u>\$ 199,968</u>          |

**HOMESTREET, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 5 — INVESTMENT SECURITIES:** (cont.)

The Company assesses the creditworthiness of the counterparties that hold the pledged collateral and has determined that these arrangements have little risk. There were no securities pledged under repurchase agreements at December 31, 2019 and 2018.

Tax-exempt interest income on securities available for sale totaling \$10.2 million, \$8.5 million and \$8.8 million for the years ended December 31, 2019, 2018 and 2017, respectively, was recorded in the Company's consolidated statements of operations.

**NOTE 6 — LOANS AND CREDIT QUALITY:**

For a detailed discussion of loans and credit quality, including accounting policies and the methodology used to estimate the allowance for credit losses, see Note 1, *Summary of Significant Accounting Policies*.

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

Loans held for investment consist of the following:

| <b>(in thousands)</b>   | <b>At December 31,</b> |              |
|---|------------------------|--------------|
|   | <b>2019</b>            | <b>2018</b>  |
| Consumer loans  |                        |              |
| Single family <sup>(1)</sup> . . . . .                                    | \$ 1,070,332           | \$ 1,358,175 |
| Home equity and other . . . . .   | 532,926                | 570,923      |
| Total consumer loans . . . . .  | 1,603,258              | 1,929,098    |
| Commercial real estate loans  |                        |              |
| Non-owner occupied commercial real estate . . . . .                       | 894,896                | 701,928      |
| Multifamily . . . . .   | 996,498                | 908,015      |
| Construction/land development . . . . .                                   | 702,399                | 794,544      |
| Total commercial real estate loans . . . . .                              | 2,593,793              | 2,404,487    |
| Commercial and industrial loans   |                        |              |
| Owner occupied commercial real estate . . . . .                           | 478,172                | 429,158      |
| Commercial business . . . . .   | 414,880                | 331,004      |
| Total commercial and industrial loans . . . . .                           | 893,052                | 760,162      |
| Loans held for investment before deferred fees, costs and allowance . . . | 5,090,103              | 5,093,747    |
| Net deferred loan fees and costs . . . . .                                | 24,453                 | 23,094       |
|   | 5,114,556              | 5,116,841    |
| Allowance for loan losses . . . . .                                       | (41,772)               | (41,470)     |
| Total loans held for investment . . . . .                                 | \$ 5,072,784           | \$ 5,075,371 |

(1) Includes \$3.5 million and \$4.1 million at December 31, 2019 and December 31, 2018, respectively, of loans where a fair value option election was made at the time of origination and, therefore, are carried at fair value with changes recognized in the consolidated statements of operations.

**HOMESTREET, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 6 — LOANS AND CREDIT QUALITY:** (cont.)

Loans in the amount of \$2.01 billion and \$2.16 billion at December 31, 2019 and 2018, respectively, were pledged to secure borrowings from the FHLB as part of our liquidity management strategy. Additionally, loans totaling \$490.7 million and \$502.7 million at December 31, 2019 and 2018, respectively, were pledged to secure borrowings from the Federal Reserve Bank. The FHLB and Federal Reserve Bank do not have the right to sell or re-pledge these loans.

It is the Company's policy to make loans to officers, directors, and their associates in the ordinary course of business on substantially the same terms as those prevailing at the time for comparable transactions with other persons. There were no material loans outstanding to these related parties and their associates at December 31, 2019 and 2018.

**Credit Risk Concentrations**

Concentrations of credit risk arise when a number of customers are engaged in similar business activities or activities in the same geographic region, or when they have similar economic features that would cause their ability to meet contractual obligations to be similarly affected by changes in economic conditions. Loans held for investment are primarily secured by real estate located in the Pacific Northwest, California and Hawaii. At December 31, 2019, we had concentrations representing 10% or more of the total portfolio by state and property type for the loan classes of single family and multifamily within the states of Washington and California, which represented 10.7% and 12.2% of the total portfolio, respectively. At December 31, 2018 we had concentrations representing 10% or more of the total portfolio by state and property type for the loan classes of single family and multifamily within the states of Washington and California, which represented 13.1% and 10.2% of the total portfolio, respectively.

**Credit Quality**

Management considers the level of allowance for loan losses to be appropriate to cover credit losses inherent within the loans held for investment portfolio as of December 31, 2019. In addition to the allowance for loan losses, the Company maintains a separate allowance for losses related to unfunded loan commitments, and this amount is included in accounts payable and other liabilities on the consolidated statements of financial condition. Collectively, these allowances are referred to as the allowance for credit losses.

For further information on the policies that govern the determination of the allowance for loan losses levels, see Note 1, *Summary of Significant Accounting Policies*.

Activity in the allowance for credit losses was as follows.

| <u>(in thousands)</u>                        | <u>Years Ended December 31,</u> |                  |                  |
|--|---------------------------------|------------------|------------------|
|  | <u>2019</u>                     | <u>2018</u>      | <u>2017</u>      |
| Allowance for credit losses (roll-forward):  |                                 |                  |                  |
| Beginning balance . . . . .                  | \$ 42,913                       | \$ 39,116        | \$ 35,264        |
| Provision for credit losses . . . . .        | (500)                           | 3,000            | 750              |
| Recoveries, net of charge-offs . . . . .     | 424                             | 797              | 3,102            |
| Ending balance . . . . .                     | <u>\$ 42,837</u>                | <u>\$ 42,913</u> | <u>\$ 39,116</u> |
| Components:                                  |                                 |                  |                  |
| Allowance for loan losses . . . . .          | \$ 41,772                       | \$ 41,470        | \$ 37,847        |
| Allowance for unfunded commitments . . . . . | 1,065                           | 1,443            | 1,269            |
| Allowance for credit losses . . . . .        | <u>\$ 42,837</u>                | <u>\$ 42,913</u> | <u>\$ 39,116</u> |





**HOMESTREET, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 6 — LOANS AND CREDIT QUALITY:** (cont.)

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

| <u>(in thousands)</u>  | <u>At December 31, 2019</u>   |   |                  |   |   |                      |
|--|---|---|------------------|---|---|----------------------|
|  | <u>Allowance:<br/>collectively<br/>evaluated for<br/>impairment</u> | <u>Allowance:<br/>individually<br/>evaluated for<br/>impairment</u> | <u>Total</u>     | <u>Loans:<br/>collectively<br/>evaluated for<br/>impairment</u> | <u>Loans:<br/>individually<br/>evaluated for<br/>impairment</u> | <u>Total</u>         |
| Consumer loans   |   |   |                  |   |   |                      |
| Single family . . . . .                                      | \$ 6,333  | \$ 117  | \$ 6,450         | \$ 1,005,386  | \$ 61,503   | \$ 1,066,889         |
| Home equity and other . . . . .                              | 6,815   | 28  | 6,843            | 532,038   | 863   | 532,901              |
| Total consumer loans . . . . .                               | <u>13,148</u>   | <u>145</u>  | <u>13,293</u>    | <u>1,537,424</u>  | <u>62,366</u>   | <u>1,599,790</u>     |
| Commercial real estate loans                                 |   |   |                  |   |   |                      |
| Non-owner occupied<br>commercial real estate . . . . .       | 7,249   | —   | 7,249            | 894,896   | —   | 894,896              |
| Multifamily . . . . .  | 7,015   | —   | 7,015            | 996,498   | —   | 996,498              |
| Construction/land<br>development . . . . .                   | 8,679   | —   | 8,679            | 702,399   | —   | 702,399              |
| Total commercial real estate<br>loans . . . . .              | <u>22,943</u>   | <u>—</u>  | <u>22,943</u>    | <u>2,593,793</u>  | <u>—</u>  | <u>2,593,793</u>     |
| Commercial and industrial loans                              |   |   |                  |   |   |                      |
| Owner occupied commercial<br>real estate . . . . .           | 3,640   | —   | 3,640            | 475,281   | 2,891   | 478,172              |
| Commercial business . . . . .                                | 2,953   | 8   | 2,961            | 411,386   | 3,494   | 414,880              |
| Total commercial and<br>industrial loans . . . . .           | <u>6,593</u>  | <u>8</u>  | <u>6,601</u>     | <u>886,667</u>  | <u>6,385</u>  | <u>893,052</u>       |
| Total loans evaluated for<br>impairment . . . . .            | <u>42,684</u>   | <u>153</u>  | <u>42,837</u>    | <u>5,017,884</u>  | <u>68,751</u>   | <u>5,086,635</u>     |
| Loans held for investment<br>carried at fair value . . . . . | —   | —   | —                | —   | —   | 3,468 <sup>(1)</sup> |
| Total loans held for investment . .                          | <u>\$ 42,684</u>  | <u>\$ 153</u>   | <u>\$ 42,837</u> | <u>\$ 5,017,884</u>   | <u>\$ 68,751</u>  | <u>\$ 5,090,103</u>  |

**HOMESTREET, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 6 — LOANS AND CREDIT QUALITY:** (cont.)

| (in thousands)   | At December 31, 2018                                      |   |                  |   |   |                      |
|--|---|---|------------------|---|---|----------------------|
|  | Allowance:<br>collectively<br>evaluated for<br>impairment | Allowance:<br>individually<br>evaluated for<br>impairment | Total            | Loans:<br>collectively<br>evaluated for<br>impairment | Loans:<br>individually<br>evaluated for<br>impairment | Total                |
| Consumer loans   |   |   |                  |   |   |                      |
| Single family . . . . .                                      | \$ 8,151  | \$ 66   | \$ 8,217         | \$ 1,286,556  | \$ 67,575   | \$ 1,354,131         |
| Home equity and other . . . . .                              | 7,671   | 41  | 7,712            | 569,673   | 1,237   | 570,910              |
| Total consumer loans . . . . .                               | <u>15,822</u>   | <u>107</u>  | <u>15,929</u>    | <u>1,856,229</u>                                      | <u>68,812</u>   | <u>1,925,041</u>     |
| Commercial real estate loans                                 |   |   |                  |   |   |                      |
| Non-owner occupied<br>commercial real estate . . . . .       | 5,496   | —   | 5,496            | 701,928   | —   | 701,928              |
| Multifamily . . . . .  | 5,754   | —   | 5,754            | 907,523   | 492   | 908,015              |
| Construction/land<br>development . . . . .                   | 9,539   | —   | 9,539            | 793,818   | 726   | 794,544              |
| Total commercial real estate<br>loans . . . . .              | <u>20,789</u>   | <u>—</u>  | <u>20,789</u>    | <u>2,403,269</u>                                      | <u>1,218</u>  | <u>2,404,487</u>     |
| Commercial and industrial loans                              |   |   |                  |   |   |                      |
| Owner occupied commercial<br>real estate . . . . .           | 3,282   | —   | 3,282            | 427,938   | 1,220   | 429,158              |
| Commercial business . . . . .                                | 2,787   | 126   | 2,913            | 329,170   | 1,834   | 331,004              |
| Total commercial and<br>industrial loans . . . . .           | <u>6,069</u>  | <u>126</u>  | <u>6,195</u>     | <u>757,108</u>  | <u>3,054</u>  | <u>760,162</u>       |
| Total loans evaluated for<br>impairment . . . . .            | <u>42,680</u>   | <u>233</u>  | <u>42,913</u>    | <u>5,016,606</u>                                      | <u>73,084</u>   | <u>5,089,690</u>     |
| Loans held for investment<br>carried at fair value . . . . . | —   | —   | —                | —   | —   | 4,057 <sup>(1)</sup> |
| Total loans held for investment . .                          | <u>\$ 42,680</u>  | <u>\$ 233</u>   | <u>\$ 42,913</u> | <u>\$ 5,016,606</u>                                   | <u>\$ 73,084</u>                                      | <u>\$ 5,093,747</u>  |

(1) Comprised of single family loans where a fair value option election was made at the time of origination and, therefore, are carried at fair value with changes recognized in the consolidated statements of operations.

**HOMESTREET, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 6 — LOANS AND CREDIT QUALITY:** (cont.)

Impaired Loans

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

| <u>(in thousands)</u>                           | At December 31, 2019                  |   |                      |
|---|---------------------------------------|---|----------------------|
|   | Recorded<br>investment <sup>(1)</sup> | Unpaid<br>principal<br>balance <sup>(2)</sup> | Related<br>allowance |
| With no related allowance recorded:             |                                       |   |                      |
| Consumer loans                                  |                                       |   |                      |
| Single family <sup>(3)</sup> . . . . .          | \$ 60,009                             | \$ 60,448                                     | \$ —                 |
| Home equity and other . . . . .                 | 472                                   | 472   | —                    |
| Total consumer loans . . . . .                  | 60,481                                | 60,920  | —                    |
| Commercial and industrial loans . . . . .       |                                       |   |                      |
| Owner occupied commercial real estate . . . . . | 2,891                                 | 3,013   | —                    |
| Commercial business . . . . .                   | 2,954                                 | 3,267   | —                    |
| Total commercial and industrial loans . . . . . | 5,845                                 | 6,280   | —                    |
|   | \$ 66,326                             | \$ 67,200                                     | \$ —                 |
| With an allowance recorded:                     |                                       |   |                      |
| Consumer loans                                  |                                       |   |                      |
| Single family . . . . .                         | \$ 1,494                              | \$ 1,494                                      | \$ 117               |
| Home equity and other . . . . .                 | 391                                   | 391   | 28                   |
| Total consumer loans . . . . .                  | 1,885                                 | 1,885   | 145                  |
| Commercial and industrial loans                 |                                       |   |                      |
| Commercial business . . . . .                   | 540                                   | 919   | 8                    |
| Total commercial and industrial loans . . . . . | 540                                   | 919   | 8                    |
|   | \$ 2,425                              | \$ 2,804                                      | \$ 153               |
| Total:  |                                       |   |                      |
| Consumer loans                                  |                                       |   |                      |
| Single family <sup>(3)</sup> . . . . .          | \$ 61,503                             | \$ 61,942                                     | \$ 117               |
| Home equity and other . . . . .                 | 863                                   | 863   | 28                   |
| Total consumer loans . . . . .                  | 62,366                                | 62,805  | 145                  |
| Commercial and industrial loans                 |                                       |   |                      |
| Owner occupied commercial real estate . . . . . | 2,891                                 | 3,013   | —                    |
| Commercial business . . . . .                   | 3,494                                 | 4,186   | 8                    |
| Total commercial and industrial loans . . . . . | 6,385                                 | 7,199   | 8                    |
| Total impaired loans . . . . .                  | \$ 68,751                             | \$ 70,004                                     | \$ 153               |

- (1) Includes partial charge-offs and nonaccrual interest paid and purchase discounts and premiums.
- (2) Unpaid principal balance does not include partial charge-offs, purchase discounts and premiums or nonaccrual interest paid. Related allowance is calculated on net book balances not unpaid principal balances.
- (3) Includes \$59.8 million in single family performing TDRs.

**HOMESTREET, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 6 — LOANS AND CREDIT QUALITY:** (cont.)

| <b>(in thousands)</b>                           | <b>At December 31, 2018</b>              |   |                          |
|---|--|---|--------------------------|
|   | <b>Recorded investment<sup>(1)</sup></b> | <b>Unpaid principal balance<sup>(2)</sup></b> | <b>Related allowance</b> |
| <b>With no related allowance recorded:</b>      |  |   |                          |
| Consumer loans                                  |  |   |                          |
| Single family <sup>(3)</sup> . . . . .          | \$ 66,725                                | \$ 67,496                                     | \$ —                     |
| Home equity and other . . . . .                 | 743                                      | 769   | —                        |
| Total consumer loans . . . . .                  | 67,468                                   | 68,265  | —                        |
| Commercial real estate loans                    |  |   |                          |
| Multifamily . . . . .                           | 492                                      | 492   | —                        |
| Construction/land development . . . . .         | 726                                      | 726   | —                        |
| Total commercial real estate loans . . . . .    | 1,218                                    | 1,218   | —                        |
| Commercial and industrial loans                 |  |   |                          |
| Owner occupied commercial real estate . . . . . | 1,220                                    | 1,543   | —                        |
| Commercial business . . . . .                   | 1,331                                    | 2,087   | —                        |
| Total commercial and industrial loans . . . . . | 2,551                                    | 3,630   | —                        |
|   | \$ 71,237                                | \$ 73,113                                     | \$ —                     |
| <b>With an allowance recorded:</b>              |  |   |                          |
| Consumer loans                                  |  |   |                          |
| Single family . . . . .                         | \$ 850                                   | \$ 850  | \$ 66                    |
| Home equity and other . . . . .                 | 494                                      | 494   | 41                       |
| Total consumer loans . . . . .                  | 1,344                                    | 1,344   | 107                      |
| Commercial and industrial loans                 |  |   |                          |
| Commercial business . . . . .                   | 503                                      | 503   | 126                      |
| Total commercial and industrial loans . . . . . | 503                                      | 503   | 126                      |
|   | \$ 1,847                                 | \$ 1,847                                      | \$ 233                   |
| <b>Total:</b>                                   |  |   |                          |
| Consumer loans                                  |  |   |                          |
| Single family <sup>(3)</sup> . . . . .          | \$ 67,575                                | \$ 68,346                                     | \$ 66                    |
| Home equity and other . . . . .                 | 1,237                                    | 1,263   | 41                       |
| Total consumer loans . . . . .                  | 68,812                                   | 69,609  | 107                      |
| Commercial real estate loans                    |  |   |                          |
| Multifamily . . . . .                           | 492                                      | 492   | —                        |
| Construction/land development . . . . .         | 726                                      | 726   | —                        |
| Total commercial real estate loans . . . . .    | 1,218                                    | 1,218   | —                        |
| Commercial and industrial loans                 |  |   |                          |
| Owner occupied commercial real estate . . . . . | 1,220                                    | 1,543   | —                        |
| Commercial business . . . . .                   | 1,834                                    | 2,590   | 126                      |
| Total commercial and industrial loans . . . . . | 3,054                                    | 4,133   | 126                      |
| Total impaired loans . . . . .                  | \$ 73,084                                | \$ 74,960                                     | \$ 233                   |

- (1) Includes partial charge-offs and nonaccrual interest paid and purchase discounts and premiums.  
(2) Unpaid principal balance does not include partial charge-offs, purchase discounts and premiums or nonaccrual interest paid. Related allowance is calculated on net book balances not unpaid principal balances.  
(3) Includes \$65.8 million in single family performing TDRs.

**HOMESTREET, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 6 — LOANS AND CREDIT QUALITY:** (cont.)

The following table provides the average recorded investment and interest income recognized on impaired loans by portfolio and class.

| (in thousands)   | Year Ended<br>December 31, 2019   |                                  | Year Ended<br>December 31, 2018   |                                  | Year Ended<br>December 31, 2017   |                                  |
|--|-----------------------------------|----------------------------------|-----------------------------------|----------------------------------|-----------------------------------|----------------------------------|
|  | Average<br>Recorded<br>Investment | Interest<br>Income<br>Recognized | Average<br>Recorded<br>Investment | Interest<br>Income<br>Recognized | Average<br>Recorded<br>Investment | Interest<br>Income<br>Recognized |
| Consumer loans   |                                   |                                  |                                   |                                  |                                   |                                  |
| Single family . . . . .                                | \$ 66,845                         | \$ 2,701                         | \$ 69,022                         | \$ 2,636                         | \$ 80,519                         | \$ 2,963                         |
| Home equity and other . . . . .                        | 1,062                             | 59                               | 1,261                             | 78                               | 1,432                             | 80                               |
| Total consumer loans . . . . .                         | 67,907                            | 2,760                            | 70,283                            | 2,714                            | 81,951                            | 3,043                            |
| Commercial real estate loans                           |                                   |                                  |                                   |                                  |                                   |                                  |
| Non-owner occupied commercial<br>real estate . . . . . | 2                                 | —                                | —                                 | —                                | 686                               | —                                |
| Multifamily . . . . .                                  | 293                               | 14                               | 676                               | 25                               | 824                               | 25                               |
| Construction/land development . . . . .                | 1,351                             | —                                | 625                               | 24                               | 917                               | 73                               |
| Total commercial real estate<br>loans . . . . .        | 1,646                             | 14                               | 1,301                             | 49                               | 2,427                             | 98                               |
| Commercial and industrial loans                        |                                   |                                  |                                   |                                  |                                   |                                  |
| Owner occupied commercial<br>real estate . . . . .     | 2,927                             | 112                              | 1,912                             | 93                               | 2,922                             | 170                              |
| Commercial business . . . . .                          | 2,211                             | 37                               | 2,303                             | 104                              | 2,533                             | 144                              |
| Total commercial and industrial<br>loans . . . . .     | 5,138                             | 149                              | 4,215                             | 197                              | 5,455                             | 314                              |
|  | <u>\$ 74,691</u>                  | <u>\$ 2,923</u>                  | <u>\$ 75,799</u>                  | <u>\$ 2,960</u>                  | <u>\$ 89,833</u>                  | <u>\$ 3,455</u>                  |

Credit Quality Indicators

Management regularly reviews loans in the portfolio to assess credit quality indicators and to determine appropriate loan classification and grading in accordance with applicable bank regulations. The Company's risk rating methodology assigns risk ratings ranging from 1 to 10, where a higher rating represents higher risk. The Company differentiates its lending portfolios into homogeneous loans and non-homogeneous loans.

The 10 risk rating categories can be generally described by the following groupings for non-homogeneous loans:

*Pass.* We have five pass risk ratings which represent a level of credit quality that ranges from no well-defined deficiency or weakness to some noted weakness; however, the risk of default on any loan classified as pass is expected to be remote. The five pass risk ratings are described below:

*Minimal Risk.* A minimal risk loan, risk rated 1-Exceptional, is to a borrower of the highest quality. The borrower has an unquestioned ability to produce consistent profits and service all obligations and can absorb severe market disturbances with little or no difficulty.

*Low Risk.* A low risk loan, risk rated 2-Superior, is similar in characteristics to a minimal risk loan. Balance sheet and operations are slightly more prone to fluctuations within the business cycle; however, debt capacity and debt service coverage remains strong. The borrower will have a strong demonstrated ability to produce profits and absorb market disturbances.

*Modest Risk.* A modest risk loan, risk rated 3-Excellent, is a desirable loan with excellent sources of repayment and no currently identifiable risk associated with collection. The borrower exhibits a very strong capacity to repay the loan in accordance with the repayment agreement. The borrower may be susceptible to economic cycles, but will have cash reserves to weather these cycles.



**HOMESTREET, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 6 — LOANS AND CREDIT QUALITY:** (cont.)

*Average Risk.* An average risk loan, risk rated 4-Good, is an attractive loan with sound sources of repayment and no material collection or repayment weakness evident. The borrower has an acceptable capacity to pay in accordance with the agreement. The borrower is susceptible to economic cycles and more efficient competition, but should have modest reserves sufficient to survive all but the most severe downturns or major setbacks.

*Acceptable Risk.* An acceptable risk loan, risk rated 5-Acceptable, is a loan with lower than average, but still acceptable credit risk. These borrowers may have higher leverage, less certain but viable repayment sources, have limited financial reserves and may possess weaknesses that can be adequately mitigated through collateral, structural or credit enhancement. The borrower is susceptible to economic cycles and is less resilient to negative market forces or financial events. Reserves may be insufficient to survive a modest downturn.

*Watch.* A watch loan, risk rated 6-Watch, is still pass-rated, but represents the lowest level of acceptable risk due to an emerging risk element or declining performance trend. Watch ratings are expected to be temporary, with issues resolved or manifested to the extent that a higher or lower rating would be appropriate. The borrower should have a plausible plan, with reasonable certainty of success, to correct the problems in a short period of time. Borrowers rated watch are characterized by elements of uncertainty, such as:

- The borrower may be experiencing declining operating trends, strained cash flows or less-than anticipated performance. Cash flow should still be adequate to cover debt service, and the negative trends should be identified as being of a short-term or temporary nature.
- The borrower may have experienced a minor, unexpected covenant violation.
- Companies who may be experiencing tight working capital or have a cash cushion deficiency.
- A loan may also be a watch if financial information is late, there is a documentation deficiency, the borrower has experienced unexpected management turnover, or if they face industry issues that, when combined with performance factors create uncertainty in their future ability to perform.
- Delinquent payments, increasing and material overdraft activity, request for bulge and/or out- of-formula advances may be an indicator of inadequate working capital and may suggest a lower rating.
- Failure of the intended repayment source to materialize as expected, or renewal of a loan (other than cash/marketable security secured or lines of credit) without reduction are possible indicators of a watch or worse risk rating.

*Special Mention.* A special mention loan, risk rated 7-Special Mention, has potential weaknesses that deserve management's close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the loans or the institutions credit position at some future date. They contain unfavorable characteristics and are generally undesirable. Loans in this category are currently protected but are potentially weak and constitute an undue and unwarranted credit risk, but not to the point of a substandard classification. A special mention loan has potential weaknesses, which if not checked or corrected, weaken the loan or inadequately protect the Company's position at some future date. Such weaknesses include:

- Performance is poor or significantly less than expected. There may be a temporary debt-servicing deficiency or inadequate working capital as evidenced by a cash cushion deficiency, but not to the extent that repayment is compromised. Material violation of financial covenants is common.
- Loans with unresolved material issues that significantly cloud the debt service outlook, even though a debt servicing deficiency does not currently exist.
- Modest underperformance or deviation from plan for real estate loans where absorption of rental/sales units is necessary to properly service the debt as structured. Depth of support for interest carry provided by owner/guarantors may mitigate and provide for improved rating.

**HOMESTREET, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 6 — LOANS AND CREDIT QUALITY:** (cont.)

- This rating may be assigned when a loan officer is unable to supervise the credit properly, an inadequate loan agreement, an inability to control collateral, failure to obtain proper documentation, or any other deviation from prudent lending practices.
- Unlike a substandard credit, there should be a reasonable expectation that these temporary issues will be corrected within the normal course of business, rather than liquidation of assets, and in a reasonable period of time.

*Substandard.* A substandard loan, risk rated 8-Substandard, is inadequately protected by the current sound worth and paying capacity of the borrower or of the collateral pledged, if any. Loans so classified must have a well-defined weakness or weaknesses that jeopardize the liquidation of the loan. They are characterized by the distinct possibility that the Company will sustain some loss if the deficiencies are not corrected. Loss potential, while existing in the aggregate amount of substandard loans, does not have to exist in individual loans classified substandard. Loans are classified as substandard when they have unsatisfactory characteristics causing unacceptable levels of risk. A substandard loan normally has one or more well-defined weaknesses that could jeopardize repayment of the loan. The likely need to liquidate assets to correct the problem, rather than repayment from successful operations is the key distinction between special mention and substandard. The following are examples of well-defined weaknesses:

- Cash flow deficiencies or trends are of a magnitude to jeopardize current and future payments with no immediate relief. A loss is not presently expected; however, the outlook is sufficiently uncertain to preclude ruling out the possibility.
- The borrower has been unable to adjust to prolonged and unfavorable industry or economic trends.
- Material underperformance or deviation from plan for real estate loans where absorption of rental/sales units is necessary to properly service the debt and risk is not mitigated by willingness and capacity of owner/guarantor to support interest payments.
- Management character or honesty has become suspect. This includes instances where the borrower has become uncooperative.
- Due to unprofitable or unsuccessful business operations, some form of restructuring of the business, including liquidation of assets, has become the primary source of loan repayment. Cash flow has deteriorated, or been diverted, to the point that sale of collateral is now the Company's primary source of repayment (unless this was the original source of repayment). If the collateral is under the Company's control and is cash or other liquid, highly marketable securities and properly margined, then a more appropriate rating might be special mention or watch.
- The borrower is involved in bankruptcy proceedings where collateral liquidation values are expected to fully protect the Company against loss.
- There is material, uncorrectable faulty documentation or materially suspect financial information.

*Doubtful.* Loans classified as doubtful, risk rated 9-Doubtful, have all the weaknesses inherent in one classified substandard with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently existing facts, conditions and values, highly questionable and improbable. The possibility of loss is extremely high, but because of certain important and reasonably specific pending factors, which may work towards strengthening of the loan, classification as a loss (and immediate charge-off) is deferred until more exact status may be determined. Pending factors include proposed merger, acquisition, liquidation procedures, capital injection, and perfection of liens on additional collateral and refinancing plans. In certain circumstances, a doubtful rating will be temporary, while the Company is awaiting an updated collateral valuation. In these cases, once the collateral is valued and appropriate margin applied, the remaining un-collateralized portion will be charged-off. The remaining balance, properly margined, may then be upgraded to substandard, however must remain on non-accrual.

**HOMESTREET, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 6 — LOANS AND CREDIT QUALITY:** (cont.)

*Loss.* Loans classified as loss, risk rated 10-Loss, are considered un-collectible and of such little value that the continuance as an active Company asset is not warranted. This rating does not mean that the loan has no recovery or salvage value, but rather that the loan should be charged-off now, even though partial or full recovery may be possible in the future.

Homogeneous loans maintain their original risk rating until they are greater than 30 days past due, and risk rating reclassification is based primarily on the past due status of the loan. The risk rating categories can be generally described by the following groupings for commercial and industrial homogeneous loans:

*Watch.* A homogeneous watch loan, risk rated 6, is 60-89 days past due from the required payment date at month-end.

*Special Mention.* A homogeneous special mention loan, risk rated 7, is less than 90 days past due from the required payment date at month-end.

*Substandard.* A homogeneous substandard loan, risk rated 8, is 90 or more days past due from the required payment date at month-end.

*Loss.* A homogeneous loss loan, risk rated 10, is 120 days or more past due from the required payment date for non-real estate secured closed-end loans or 180 days or more past due from the required payment date for open-end loans and all loans secured by real estate. These loans are generally charged-off in the month in which the applicable time period elapses.

The risk rating categories can be generally described by the following groupings for residential and home equity and other homogeneous loans:

*Watch.* A homogeneous retail watch loan, risk rated 6, is 60-89 days past due from the required payment date at month-end.

*Substandard.* A homogeneous retail substandard loan, risk rated 8, is 90-180 days past due from the required payment date at month-end.

*Loss.* A homogeneous retail loss loan, risk rated 10, becomes past due 180 cumulative days from the contractual due date. These loans are generally charged-off in the month in which the 180 day period elapses.

Residential and home equity loans modified in a troubled debt restructure are not considered homogeneous. The risk rating classification for such loans are based on the non-homogeneous definitions noted above.

**HOMESTREET, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 6 — LOANS AND CREDIT QUALITY:** (cont.)

The following tables summarize designated loan grades by loan portfolio and loan class.

| (in thousands)   | At December 31, 2019        |            |                    |             |              |
|--|-----------------------------|------------|--------------------|-------------|--------------|
|  | Pass                        | Watch      | Special<br>mention | Substandard | Total        |
| Consumer loans   |                             |            |                    |             |              |
| Single family . . . . .                                | \$ 1,053,648 <sup>(1)</sup> | \$ 2,518   | \$ 8,802           | \$ 5,364    | \$ 1,070,332 |
| Home equity and other . . . . .                        | 530,784                     | 318        | 664                | 1,160       | 532,926      |
| Total consumer loans . . . . .                         | 1,584,432                   | 2,836      | 9,466              | 6,524       | 1,603,258    |
| Commercial real estate loans                           |                             |            |                    |             |              |
| Non-owner occupied commercial<br>real estate . . . . . | 892,890                     | 2,006      | —                  | —           | 894,896      |
| Multifamily . . . . .                                  | 991,696                     | 4,802      | —                  | —           | 996,498      |
| Construction/land development . . . . .                | 669,751                     | 11,694     | 20,954             | —           | 702,399      |
| Total commercial real estate loans . .                 | 2,554,337                   | 18,502     | 20,954             | —           | 2,593,793    |
| Commercial and industrial loans                        |                             |            |                    |             |              |
| Owner occupied commercial real<br>estate . . . . .     | 422,434                     | 37,885     | 12,709             | 5,144       | 478,172      |
| Commercial business . . . . .                          | 351,911                     | 50,149     | 9,405              | 3,415       | 414,880      |
| Total commercial and industrial<br>loans . . . . .     | 774,345                     | 88,034     | 22,114             | 8,559       | 893,052      |
|  | \$ 4,913,114                | \$ 109,372 | \$ 52,534          | \$ 15,083   | \$ 5,090,103 |

(1) Includes \$3.5 million of loans where a fair value option election was made at the time of origination and, therefore, are carried at fair value with changes recognized in the consolidated statements of operations.

| (in thousands)   | At December 31, 2018        |           |                    |             |              |
|--|-----------------------------|-----------|--------------------|-------------|--------------|
|  | Pass                        | Watch     | Special<br>mention | Substandard | Total        |
| Consumer loans   |                             |           |                    |             |              |
| Single family . . . . .                                | \$ 1,338,025 <sup>(1)</sup> | \$ 2,882  | \$ 8,775           | \$ 8,493    | \$ 1,358,175 |
| Home equity and other . . . . .                        | 569,370                     | 95        | 510                | 948         | 570,923      |
| Total consumer loans . . . . .                         | 1,907,395                   | 2,977     | 9,285              | 9,441       | 1,929,098    |
| Commercial real estate loans                           |                             |           |                    |             |              |
| Non-owner occupied commercial<br>real estate . . . . . | 695,077                     | 1,426     | 5,425              | —           | 701,928      |
| Multifamily . . . . .                                  | 903,897                     | 3,626     | 492                | —           | 908,015      |
| Construction/land development . . . . .                | 767,113                     | 21,531    | 1,084              | 4,816       | 794,544      |
| Total commercial real estate loans . .                 | 2,366,087                   | 26,583    | 7,001              | 4,816       | 2,404,487    |
| Commercial and industrial loans                        |                             |           |                    |             |              |
| Owner occupied commercial real<br>estate . . . . .     | 392,273                     | 22,928    | 11,087             | 2,870       | 429,158      |
| Commercial business . . . . .                          | 299,225                     | 14,331    | 15,427             | 2,021       | 331,004      |
| Total commercial and industrial<br>loans . . . . .     | 691,498                     | 37,259    | 26,514             | 4,891       | 760,162      |
|  | \$ 4,964,980                | \$ 66,819 | \$ 42,800          | \$ 19,148   | \$ 5,093,747 |

(1) Includes \$4.1 million of loans of loans where a fair value option election was made at the time of origination and, therefore, are carried at fair value with changes recognized in the consolidated statements of operations.

**HOMESTREET, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 6 — LOANS AND CREDIT QUALITY:** (cont.)

As of December 31, 2019 and 2018, none of the Company's loans were rated Doubtful or Loss.

Nonaccrual and Past Due Loans

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

The following tables present an aging analysis of past due loans by loan portfolio and loan class.

| At December 31, 2019                                   |                          |                          |                                |                   |                             |                     |   |
|--|--------------------------|--------------------------|--------------------------------|-------------------|-----------------------------|---------------------|---|
| (in thousands)   | 30 – 59 days<br>past due | 60 – 89 days<br>past due | 90 days or<br>more past<br>due | Total<br>past due | Current                     | Total loans         | 90 days<br>or more<br>past due<br>and<br>accruing |
| Consumer loans   |                          |                          |                                |                   |                             |                     |   |
| Single family . . . . .                                | \$ 5,694                 | \$ 4,261                 | \$ 25,066                      | \$ 35,021         | \$ 1,035,311 <sup>(1)</sup> | \$ 1,070,332        | \$ 19,702 <sup>(2)</sup>                          |
| Home equity and other . . . . .                        | 837                      | 372                      | 1,160                          | 2,369             | 530,557                     | 532,926             | —   |
| Total consumer loans . . . . .                         | 6,531                    | 4,633                    | 26,226                         | 37,390            | 1,565,868                   | 1,603,258           | 19,702  |
| Commercial real estate loans                           |                          |                          |                                |                   |                             |                     |   |
| Non-owner occupied commercial<br>real estate . . . . . | —                        | —                        | —                              | —                 | 894,896                     | 894,896             | —   |
| Multifamily . . . . .                                  | —                        | —                        | —                              | —                 | 996,498                     | 996,498             | —   |
| Construction/land development . . . . .                | —                        | —                        | —                              | —                 | 702,399                     | 702,399             | —   |
| Total commercial real estate<br>loans . . . . .        | —                        | —                        | —                              | —                 | 2,593,793                   | 2,593,793           | —   |
| Commercial and industrial loans                        |                          |                          |                                |                   |                             |                     |   |
| Owner occupied commercial<br>real estate . . . . .     | —                        | —                        | 2,891                          | 2,891             | 475,281                     | 478,172             | —   |
| Commercial business . . . . .                          | 44                       | —                        | 3,446                          | 3,490             | 411,390                     | 414,880             | —   |
| Total commercial and<br>industrial loans . . . . .     | 44                       | —                        | 6,337                          | 6,381             | 886,671                     | 893,052             | —   |
|  | <u>\$ 6,575</u>          | <u>\$ 4,633</u>          | <u>\$ 32,563</u>               | <u>\$ 43,771</u>  | <u>\$ 5,046,332</u>         | <u>\$ 5,090,103</u> | <u>\$ 19,702</u>                                  |

**HOMESTREET, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 6 — LOANS AND CREDIT QUALITY: (cont.)**

| At December 31, 2018                                   |                          |                          |                                |                   |                             |                     |  |
|--|--------------------------|--------------------------|--------------------------------|-------------------|-----------------------------|---------------------|--|
| (in thousands)   | 30 – 59 days<br>past due | 60 – 89 days<br>past due | 90 days or<br>more past<br>due | Total past<br>due | Current                     | Total loans         | 90 days or<br>more past<br>due and<br>accruing |
| Consumer loans   |                          |                          |                                |                   |                             |                     |  |
| Single family . . . . .                                | \$ 9,725                 | \$ 3,653                 | \$ 47,609                      | \$ 60,987         | \$ 1,297,188 <sup>(1)</sup> | \$ 1,358,175        | \$ 39,116 <sup>(2)</sup>                       |
| Home equity and other . . . . .                        | 145                      | 100                      | 948                            | 1,193             | 569,730                     | 570,923             | —  |
| Total consumer loans . . . . .                         | 9,870                    | 3,753                    | 48,557                         | 62,180            | 1,866,918                   | 1,929,098           | 39,116   |
| Commercial real estate loans                           |                          |                          |                                |                   |                             |                     |  |
| Non-owner occupied commercial<br>real estate . . . . . | —                        | —                        | —                              | —                 | 701,928                     | 701,928             | —  |
| Multifamily . . . . .                                  | —                        | —                        | —                              | —                 | 908,015                     | 908,015             | —  |
| Construction/land development . . . . .                | —                        | —                        | 72                             | 72                | 794,472                     | 794,544             | —  |
| Total commercial real estate<br>loans . . . . .        | —                        | —                        | 72                             | 72                | 2,404,415                   | 2,404,487           | —  |
| Commercial and industrial loans                        |                          |                          |                                |                   |                             |                     |  |
| Owner occupied commercial<br>real estate . . . . .     | —                        | —                        | 374                            | 374               | 428,784                     | 429,158             | —  |
| Commercial business . . . . .                          | —                        | —                        | 1,732                          | 1,732             | 329,272                     | 331,004             | —  |
| Total commercial and<br>industrial loans . . . . .     | —                        | —                        | 2,106                          | 2,106             | 758,056                     | 760,162             | —  |
|  | <u>\$ 9,870</u>          | <u>\$ 3,753</u>          | <u>\$ 50,735</u>               | <u>\$ 64,358</u>  | <u>\$ 5,029,389</u>         | <u>\$ 5,093,747</u> | <u>\$ 39,116</u>                               |

- (1) Includes \$3.5 million and \$4.1 million of loans at December 31, 2019 and 2018 respectively, where a fair value option election was made at the time of origination and, therefore, are carried at fair value with changes recognized in the consolidated statements of operations.
- (2) FHA-insured and VA-guaranteed single family loans that are 90 days or more past due are maintained on accrual status if they are determined to have little to no risk of loss.

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

| At December 31, 2019                                |                             |                  |                     |
|---|-----------------------------|------------------|---------------------|
| (in thousands)                                      | Accrual                     | Nonaccrual       | Total               |
| Consumer loans                                      |                             |                  |                     |
| Single family . . . . .                             | \$ 1,064,968 <sup>(1)</sup> | \$ 5,364         | \$ 1,070,332        |
| Home equity and other . . . . .                     | 531,766                     | 1,160            | 532,926             |
| Total consumer loans . . . . .                      | 1,596,734                   | 6,524            | 1,603,258           |
| Commercial real estate loans                        |                             |                  |                     |
| Non-owner occupied commercial real estate . . . . . | 894,896                     | —                | 894,896             |
| Multifamily . . . . .                               | 996,498                     | —                | 996,498             |
| Construction/land development . . . . .             | 702,399                     | —                | 702,399             |
| Total commercial real estate loans . . . . .        | 2,593,793                   | —                | 2,593,793           |
| Commercial and industrial loans                     |                             |                  |                     |
| Owner occupied commercial real estate . . . . .     | 475,281                     | 2,891            | 478,172             |
| Commercial business . . . . .                       | 411,434                     | 3,446            | 414,880             |
| Total commercial and industrial loans . . . . .     | 886,715                     | 6,337            | 893,052             |
|   | <u>\$ 5,077,242</u>         | <u>\$ 12,861</u> | <u>\$ 5,090,103</u> |



**HOMESTREET, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 6 — LOANS AND CREDIT QUALITY:** (cont.)

| <b>(in thousands)</b>                               | <b>At December 31, 2018</b> |                   |                     |
|---|-----------------------------|-------------------|---------------------|
|   | <b>Accrual</b>              | <b>Nonaccrual</b> | <b>Total</b>        |
| Consumer loans                                      |                             |                   |                     |
| Single family . . . . .                             | \$ 1,349,682 <sup>(1)</sup> | \$ 8,493          | \$ 1,358,175        |
| Home equity and other . . . . .                     | <u>569,975</u>              | <u>948</u>        | <u>570,923</u>      |
| Total consumer loans . . . . .                      | 1,919,657                   | 9,441             | 1,929,098           |
| Commercial real estate loans                        |                             |                   |                     |
| Non-owner occupied commercial real estate . . . . . | 701,928                     | —                 | 701,928             |
| Multifamily . . . . .                               | 908,015                     | —                 | 908,015             |
| Construction/land development . . . . .             | <u>794,472</u>              | <u>72</u>         | <u>794,544</u>      |
| Total commercial real estate loans . . . . .        | 2,404,415                   | 72                | 2,404,487           |
| Commercial and industrial loans                     |                             |                   |                     |
| Owner occupied commercial real estate . . . . .     | 428,784                     | 374               | 429,158             |
| Commercial business . . . . .                       | <u>329,272</u>              | <u>1,732</u>      | <u>331,004</u>      |
| Total commercial and industrial loans . . . . .     | <u>758,056</u>              | <u>2,106</u>      | <u>760,162</u>      |
|   | <u>\$ 5,082,128</u>         | <u>\$ 11,619</u>  | <u>\$ 5,093,747</u> |

(1) Includes \$3.5 million and \$4.1 million of loans at December 31, 2019 and 2018, respectively, where a fair value option election was made at the time of origination and, therefore, are carried at fair value with changes recognized in the consolidated statements of operations.

**HOMESTREET, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 6 — LOANS AND CREDIT QUALITY:** (cont.)

The following tables present information about TDR activity during the periods presented.

| <u>(dollars in thousands)</u>         | <u>Year Ended December 31, 2019</u> |   |                                |                                |
|---------------------------------------|-------------------------------------|---|--------------------------------|--------------------------------|
|                                       | <u>Concession type</u>              | <u>Number of<br/>loan<br/>modifications</u> | <u>Recorded<br/>investment</u> | <u>Related<br/>charge-offs</u> |
| Consumer loans                        |                                     |   |                                |                                |
| Single family                         |                                     |   |                                |                                |
|                                       | Interest rate reduction             | 21  | \$ 3,925                       | \$ —                           |
|                                       | Payment restructure                 | 118   | 25,795                         | —                              |
| Home equity and other                 |                                     |   |                                |                                |
|                                       | Payment restructure                 | 1   | 116                            | —                              |
| Total consumer                        |                                     |   |                                |                                |
|                                       | Interest rate reduction             | 21  | 3,925                          | —                              |
|                                       | Payment restructure                 | 119   | 25,911                         | —                              |
|                                       |                                     | <u>140</u>                                  | <u>29,836</u>                  | <u>—</u>                       |
| Commercial real estate loans          |                                     |   |                                |                                |
| Construction/land development         |                                     |   |                                |                                |
|                                       | Payment restructure                 | 1   | 4,675                          | —                              |
| Total commercial real estate          |                                     |   |                                |                                |
|                                       | Payment restructure                 | 1   | 4,675                          | —                              |
|                                       |                                     | <u>1</u>                                    | <u>4,675</u>                   | <u>—</u>                       |
| Commercial and industrial loans       |                                     |   |                                |                                |
| Owner occupied commercial real estate |                                     |   |                                |                                |
|                                       | Payment restructure                 | 1   | 5,840                          | —                              |
| Commercial business                   |                                     |   |                                |                                |
|                                       | Payment restructure                 | 1   | 259                            | —                              |
| Total commercial and industrial       |                                     |   |                                |                                |
|                                       | Payment restructure                 | 2   | 6,099                          | —                              |
|                                       |                                     | <u>2</u>                                    | <u>6,099</u>                   | <u>—</u>                       |
| Total loans                           |                                     |   |                                |                                |
|                                       | Interest rate reduction             | 21  | 3,925                          | —                              |
|                                       | Payment restructure                 | 122   | 36,685                         | —                              |
|                                       |                                     | <u>143</u>                                  | <u>\$ 40,610</u>               | <u>\$ —</u>                    |

**HOMESTREET, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 6 — LOANS AND CREDIT QUALITY: (cont.)**

|  |                         | <b>Year Ended December 31, 2018</b>         |                                |                                |  |
|--|-------------------------|---|--------------------------------|--------------------------------|--|
| <b>(dollars in thousands)</b>          | <b>Concession type</b>  | <b>Number of<br/>loan<br/>modifications</b> | <b>Recorded<br/>investment</b> | <b>Related<br/>charge-offs</b> |  |
| <b>Consumer loans</b>                  |                         |   |                                |                                |  |
| Single family                          |                         |   |                                |                                |  |
|  | Interest rate reduction | 17  | \$ 3,174                       | \$ —                           |  |
|  | Payment restructure     | 153   | 31,626                         | —                              |  |
| <b>Total consumer</b>                  |                         |   |                                |                                |  |
|  | Interest rate reduction | 17  | 3,174                          | —                              |  |
|  | Payment restructure     | 153   | 31,626                         | —                              |  |
|  |                         | <u>170</u>                                  | <u>34,800</u>                  | <u>—</u>                       |  |
| <b>Commercial and industrial loans</b> |                         |   |                                |                                |  |
| Commercial business                    |                         |   |                                |                                |  |
|  | Payment restructure     | 2   | 267                            | —                              |  |
| <b>Total commercial and industrial</b> |                         |   |                                |                                |  |
|  | Payment restructure     | <u>2</u>                                    | <u>267</u>                     | <u>—</u>                       |  |
|  |                         | <u>2</u>                                    | <u>267</u>                     | <u>—</u>                       |  |
| <b>Total loans</b>                     |                         |   |                                |                                |  |
|  | Interest rate reduction | 17  | 3,174                          | —                              |  |
|  | Payment restructure     | 155   | 31,893                         | —                              |  |
|  |                         | <u>172</u>                                  | <u>\$ 35,067</u>               | <u>\$ —</u>                    |  |
|  |                         | <b>Year Ended December 31, 2017</b>         |                                |                                |  |
| <b>(dollars in thousands)</b>          | <b>Concession type</b>  | <b>Number of<br/>loan<br/>modifications</b> | <b>Recorded<br/>investment</b> | <b>Related<br/>charge-offs</b> |  |
| <b>Consumer loans</b>                  |                         |   |                                |                                |  |
| Single family                          |                         |   |                                |                                |  |
|  | Interest rate reduction | 56  | \$ 10,040                      | \$ —                           |  |
|  | Payment restructure     | 102   | 21,356                         | —                              |  |
| Home equity and other                  |                         |   |                                |                                |  |
|  | Payment restructure     | <u>2</u>                                    | <u>351</u>                     | <u>—</u>                       |  |
| <b>Total consumer</b>                  |                         |   |                                |                                |  |
|  | Interest rate reduction | 56  | 10,040                         | —                              |  |
|  | Payment restructure     | 104   | 21,707                         | —                              |  |
|  |                         | <u>160</u>                                  | <u>31,747</u>                  | <u>—</u>                       |  |
| <b>Commercial and industrial loans</b> |                         |   |                                |                                |  |
| Commercial business                    |                         |   |                                |                                |  |
|  | Payment restructure     | 1   | 18                             | —                              |  |
| <b>Total commercial and industrial</b> |                         |   |                                |                                |  |
|  | Payment restructure     | <u>1</u>                                    | <u>18</u>                      | <u>—</u>                       |  |
|  |                         | <u>1</u>                                    | <u>18</u>                      | <u>—</u>                       |  |
| <b>Total loans</b>                     |                         |   |                                |                                |  |
|  | Interest rate reduction | 56  | 10,040                         | —                              |  |
|  | Payment restructure     | 105   | 21,725                         | —                              |  |
|  |                         | <u>161</u>                                  | <u>\$ 31,765</u>               | <u>\$ —</u>                    |  |

**HOMESTREET, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 6 — LOANS AND CREDIT QUALITY:** (cont.)

The following table presents loans that were modified as TDRs within the previous 12 months and subsequently re-defaulted during the years ended December 31, 2019 and 2018, respectively. A TDR loan is considered re-defaulted when it becomes doubtful that the objectives of the modifications will be met, generally when a consumer loan TDR becomes 60 days or more past due on principal or interest payments or when a commercial loan TDR becomes 90 days or more past due on principal or interest payments.

| <b>(dollars in thousands)</b> | <b>Years Ended December 31,</b>                       |                            |   |                            |
|-------------------------------|---|----------------------------|---|----------------------------|
|                               | <b>2019</b>   |                            | <b>2018</b>   |                            |
|                               | <b>Number of loan relationships that re-defaulted</b> | <b>Recorded investment</b> | <b>Number of loan relationships that re-defaulted</b> | <b>Recorded investment</b> |
| Consumer loans                |   |                            |   |                            |
| Single family . . . . .       | 13  | \$ 3,059                   | 24  | \$ 4,723                   |
|                               | <u>13</u>   | <u>\$ 3,059</u>            | <u>24</u>   | <u>\$ 4,723</u>            |

**NOTE 7 — OTHER REAL ESTATE OWNED:**

Other real estate owned consisted of the following.

| <b>(in thousands)</b>         | <b>At December 31,</b> |               |
|-------------------------------|------------------------|---------------|
|                               | <b>2019</b>            | <b>2018</b>   |
| Single family . . . . .       | \$ 1,393               | \$ 455        |
| Valuation allowance . . . . . | —                      | —             |
|                               | <u>\$ 1,393</u>        | <u>\$ 455</u> |

Activity in other real estate owned was as follows.

| <b>(in thousands)</b>                 | <b>Years Ended December 31,</b> |               |
|---------------------------------------|---------------------------------|---------------|
|                                       | <b>2019</b>                     | <b>2018</b>   |
| Beginning balance . . . . .           | \$ 455                          | \$ 664        |
| Additions . . . . .                   | 1,933                           | 455           |
| Reductions related to sales . . . . . | (995)                           | (664)         |
| Ending balance . . . . .              | <u>\$ 1,393</u>                 | <u>\$ 455</u> |

Activity in the valuation allowance for other real estate owned was as follows.

| <b>(in thousands)</b>                      | <b>Year Ended December 31, 2017</b> |
|--|-------------------------------------|
| Beginning balance . . . . .                | \$ 3,095                            |
| Loss provisions . . . . .                  | 33                                  |
| (Charge-offs), net of recoveries . . . . . | (3,128)                             |
| Ending balance . . . . .                   | <u>\$ —</u>                         |

There was no activity or balance in the valuation allowance for other real estate owned for the years ended December 31, 2019 and 2018.

**HOMESTREET, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 7 — OTHER REAL ESTATE OWNED:** (cont.)

The components of the net cost of operation and sale of other real estate owned are as follows.

| <u>(in thousands)</u>  | <u>Years Ended December 31,</u> |                 |                 |
|--|---------------------------------|-----------------|-----------------|
|  | <u>2019</u>                     | <u>2018</u>     | <u>2017</u>     |
| Maintenance (reimbursements) costs . . . . .                             | \$ 29                           | \$ 33           | \$ (114)        |
| Loss provisions . . . . .  | —                               | —               | —               |
| Net gain on sales . . . . .  | (101)                           | (172)           | (416)           |
| Net benefit from operation and sale of other real estate owned . . . . . | <u>\$ (72)</u>                  | <u>\$ (139)</u> | <u>\$ (530)</u> |

At December 31, 2019, we had concentrations of 47% in California and 53% in Hawaii representing the balance of other real estate owned. At December 31, 2018, we had concentrations within the state of Oregon, primarily in Marion County, representing 100% of the total balance of other real estate owned. At December 31, 2017, we had concentrations within the state of Washington, primarily in Spokane County, representing 77% of the total balance of other real estate owned.

**NOTE 8 — PREMISES AND EQUIPMENT, NET:**

Premises and equipment consisted of the following.

| <u>(in thousands)</u>                    | <u>At December 31,</u>         |                                |
|--|--------------------------------|--------------------------------|
|  | <u>2019</u>                    | <u>2018</u>                    |
| Furniture and equipment . . . . .        | \$ 56,849                      | \$ 70,692                      |
| Leasehold improvements . . . . .         | 46,088                         | 52,596                         |
| Land and buildings . . . . .             | 34,558                         | 34,552                         |
|  | <u>137,495</u>                 | <u>157,840</u>                 |
| Less: accumulated depreciation . . . . . | (60,522)                       | (63,039)                       |
|  | <u>\$ 76,973<sup>(1)</sup></u> | <u>\$ 94,801<sup>(1)</sup></u> |

(1) Includes zero and \$6.7 million of premises and equipment related to discontinued operations as of December 31, 2019 and 2018.

Depreciation expense for the years ended December 31, 2019, 2018, and 2017, was \$10.8 million, \$13.9 million, and \$13.5 million, respectively. Includes both continuing and discontinued operations.

**NOTE 9 — DEPOSITS:**

Deposit balances, including stated rates, were as follows.

| <u>(in thousands)</u>  | <u>At December 31,</u> |                     |
|--|------------------------|---------------------|
|  | <u>2019</u>            | <u>2018</u>         |
| Noninterest-bearing accounts <sup>(1)</sup> . . . . .  | \$ 907,918             | \$ 914,154          |
| NOW accounts, 0.00% to 1.19% at December 31, 2019 and 0.00% to 1.44%<br>at December 31, 2018 . . . . .                         | 373,832                | 376,137             |
| Statement savings accounts, due on demand, 0.05% to 1.13% at December 31,<br>2019 and 2018 . . . . .                           | 219,182                | 245,795             |
| Money market accounts, due on demand, 0.00% to 2.42% at December 31,<br>2019 and 0.00% to 2.40% at December 31, 2018 . . . . . | 2,224,494              | 1,935,516           |
| Certificates of deposit, 0.10% to 3.06% at December 31, 2019 and 0.10% to<br>3.80% at December 31, 2018 . . . . .              | 1,614,533              | 1,579,806           |
|  | <u>\$ 5,339,959</u>    | <u>\$ 5,051,408</u> |

(1) Includes zero and \$162.8 million in servicing deposits related to discontinued operations at December 31, 2019 and 2018, respectively. These deposits were transferred to the MSR buyers concurrent with the transfer of the loan servicing.

**HOMESTREET, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 9 — DEPOSITS:** (cont.)

There were \$330.4 million and \$191.8 million in public funds included in deposits at December 31, 2019 and 2018, respectively.

Interest expense on deposits was as follows.

| <u>(in thousands)</u>                | <u>Years Ended December 31,</u> |                  |                  |
|--------------------------------------|---------------------------------|------------------|------------------|
|                                      | <u>2019</u>                     | <u>2018</u>      | <u>2017</u>      |
| NOW accounts . . . . .               | \$ 1,507                        | \$ 1,678         | \$ 1,964         |
| Statement savings accounts . . . . . | 525                             | 816              | 1,007            |
| Money market accounts . . . . .      | 27,259                          | 17,199           | 8,604            |
| Certificates of deposit . . . . .    | 41,189                          | 22,302           | 12,337           |
|                                      | <u>\$ 70,480<sup>(1)</sup></u>  | <u>\$ 41,995</u> | <u>\$ 23,912</u> |

(1) Includes \$91 thousand in interest expense on deposits related to discontinued operations for the year ended December 31, 2019.

The weighted-average interest rates on certificates of deposit at December 31, 2019, 2018 and 2017 were 2.24%, 1.87% and 1.12% respectively.

Certificates of deposit outstanding mature as follows.

| <u>(in thousands)</u>         | <u>At<br/>December 31,<br/>2019</u> |
|-------------------------------|-------------------------------------|
| Within one year . . . . .     | \$ 1,282,411                        |
| One to two years . . . . .    | 240,121                             |
| Two to three years . . . . .  | 62,417                              |
| Three to four years . . . . . | 13,938                              |
| Four to five years . . . . .  | 15,517                              |
| Thereafter . . . . .          | 129                                 |
|                               | <u>\$ 1,614,533</u>                 |

The aggregate amount of time deposits in denominations of more than \$250 thousand at December 31, 2019 and 2018 was \$222.9 million and \$85.3 million, respectively. There were \$266.5 million and \$786.1 million of brokered deposits at December 31, 2019 and 2018, respectively.

**NOTE 10 — FEDERAL HOME LOAN BANK AND OTHER BORROWINGS:**

Federal Home Loan Bank

The Company borrows funds through advances from the Des Moines FHLB. FHLB advances totaled \$346.6 million and \$932.6 million as of December 31, 2019, and 2018, respectively.

Weighted-average interest rates on the advances were 1.86%, 2.63%, and 1.58% at December 31, 2019, 2018 and 2017, respectively. The advances may be collateralized by stock in the FHLB, pledged securities, and unencumbered qualifying loans. The Company has an available line of credit with the FHLB equal to 45.0% of assets, subject to collateralization requirements. Based on the amount of qualifying collateral available, borrowing capacity from the FHLB was \$943.3 million as of December 31, 2019. The FHLB is not contractually bound to continue to offer credit to the Company, and the Company's access to credit from this agency for future borrowings may be discontinued at any time.



**HOMESTREET, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 10 — FEDERAL HOME LOAN BANK AND OTHER BORROWINGS:** (cont.)

FHLB advances outstanding by contractual maturities were as follows.

| (dollars in thousands)    | At December 31, 2019    |                                   |
|---------------------------|-------------------------|-----------------------------------|
|                           | Advances<br>outstanding | Weighted-average<br>interest rate |
| 2020.....                 | \$ 341,000              | 1.80%                             |
| 2021.....                 | —                       | —                                 |
| 2022.....                 | —                       | —                                 |
| 2023.....                 | —                       | —                                 |
| 2024 and thereafter ..... | 5,590                   | 5.31                              |
|                           | \$ 346,590              | 1.86%                             |

The Company, as a member of the FHLB, is required to own shares of FHLB stock. This requirement is based upon the amount of either the eligible collateral or advances outstanding from the FHLB. As of December 31, 2019 and 2018, the Company held \$22.4 million and \$45.5 million respectively, of FHLB stock. FHLB stock is carried at par value and is restricted to transactions between the FHLB and its member institutions. FHLB stock can only be purchased or redeemed at par value. Both cash and dividends received on FHLB stock are reported in earnings.

Management periodically evaluates FHLB stock for other-than-temporary impairment. Management’s determination of whether these investments are impaired is based on its assessment of ultimate recoverability of par value rather than recognizing temporary declines in value. The determination of whether the decline affects the ultimate recoverability is influenced by criteria such as: (1) the significance of the decline in net assets of the FHLB as compared to the capital stock amount for the FHLB and the length of time this situation has persisted; (2) commitments by the FHLB to make payments required by law or regulation and the level of such payments in relation to the operating performance of the FHLB; (3) the impact of legislative and regulatory changes on institutions and, accordingly, on the customer base of the FHLB; and (4) the liquidity position of the FHLB. Based on this evaluation, the Company determined there is no other-than-temporary impairment of the FHLB stock investment as of December 31, 2019, or 2018.

Federal Reserve Bank of San Francisco

The Company may also borrow on a collateralized basis from the Federal Reserve Bank of San Francisco (“FRBSF”). At December 31, 2019 and 2018, there were no outstanding borrowings from the FRBSF. Based on the amount of qualifying collateral available, borrowing capacity from the FRBSF was \$267.1 million at December 31, 2019. The FRBSF is not contractually bound to offer credit to the Company, and the Company’s access to credit from this agency for future borrowings may be discontinued at any time.

Federal Funds Purchased and Securities Sold Under Agreements to Repurchase

Federal funds transactions involve lending reserve balances on a short-term basis. Securities borrowed or purchased under agreements to resell are collateralized lending transactions utilized to accommodate customer transactions, earn interest rate spreads, and obtain securities for settlement and for collateral. At December 31, 2019 and 2018, we had a \$125.0 million and a \$19.0 million balance of federal funds purchased and securities sold under agreements to repurchase.

**NOTE 11 — LONG-TERM DEBT:**

At December 31, 2019 and 2018, the Company had long-term debt balance of \$125.7 million and \$125.5 million respectively, consisting of senior notes issued during 2016 and junior subordinated debentures issued in prior years.

In 2016, the Company closed on \$65.0 million in aggregate principal amount of its 6.50% Senior Notes due 2026 (the “Senior Notes”) at an offering price of 100% plus accrued interest, which represented \$63.8 million of long-term debt balance at December 31, 2019.

**HOMESTREET, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 11 — LONG-TERM DEBT:** (cont.)

The Company raised capital by issuing trust preferred securities during the period from 2005 through 2007, resulting in a debt balance of \$61.9 million that remains outstanding at December 31, 2019. In connection with the issuance of trust preferred securities, HomeStreet, Inc. issued to HomeStreet Statutory Trust Junior Subordinated Deferrable Interest Debentures. The sole assets of the HomeStreet Statutory Trust are the Subordinated Debt Securities I, II, III, and IV.

The Subordinated Debt Securities are as follows:

| (dollars in thousands)               | HomeStreet Statutory |                    |                    |                    |
|--------------------------------------|----------------------|--------------------|--------------------|--------------------|
|                                      | I                    | II                 | III                | IV                 |
| Date issued . . . . .                | June 2005            | September 2005     | February 2006      | March 2007         |
| Amount . . . . .                     | \$5,155              | \$20,619           | \$20,619           | \$15,464           |
| Interest rate . . . . .              | 3 MO LIBOR + 1.70%   | 3 MO LIBOR + 1.50% | 3 MO LIBOR + 1.37% | 3 MO LIBOR + 1.68% |
| Maturity date. . . . .               | June 2035            | December 2035      | March 2036         | June 2037          |
| Call option <sup>(1)</sup> . . . . . | Quarterly            | Quarterly          | Quarterly          | Quarterly          |

(1) Call options are exercisable at par and are callable, without penalty on a quarterly basis, starting five years after issuance.

**NOTE 12 — DERIVATIVES AND HEDGING ACTIVITIES:**

To reduce the risk of significant interest rate fluctuations on the value of certain assets and liabilities, such as certain mortgage loans held for sale or MSR, the Company utilizes derivatives, such as forward sale commitments, futures, option contracts, interest rate swaps and interest rate swaptions as risk management instruments in its hedging strategy. Derivative transactions are measured in terms of notional amount, which is not recorded in the consolidated statements of financial condition. The notional amount is generally not exchanged and is used as the basis for interest and other contractual payments.

The use of derivatives as interest rate risk management instruments helps minimize significant, unplanned fluctuations in earnings, fair value of assets and liabilities, and cash flows caused by interest rate volatility. This approach involves mitigating the repricing characteristics of certain assets or liabilities so that changes in interest rates do not have a significant adverse effect on net interest margin and cash flows. As a result of interest rate fluctuations, hedged assets and liabilities will gain or lose market value. In a fair value hedging strategy, the effect of this gain or loss will generally be offset by the gain or loss on the derivatives linked to hedged assets or liabilities. In a cash flow hedging strategy, management manages the variability of cash payments due to interest rate fluctuations by the effective use of derivatives linked to hedged assets and liabilities.

We held no derivatives designated as a fair value, cash flow or foreign currency hedge instrument at December 31, 2019 or 2018. Derivatives are reported at their respective fair values in the other assets or accounts payable and other liabilities line items on the consolidated statements of financial condition, with changes in fair value reflected in current period earnings.

As permitted under U.S. GAAP, the Company nets derivative assets and liabilities when a legally enforceable master netting agreement exists between the Company and the derivative counterparty, which are documented under industry standard master agreements and credit support annexes. The Company's master netting agreements provide that following an uncured payment default or other event of default the non-defaulting party may promptly terminate all transactions between the parties and determine a net amount due to be paid to, or by, the defaulting party. An event of default may also occur under a credit support annex if a party fails to make a collateral delivery (which remains uncured following applicable notice and grace periods). The Company's right of offset requires that master netting agreements are legally enforceable and that the exercise of rights by the non-defaulting party under these agreements will not be stayed, or avoided under applicable law upon an event of default including bankruptcy, insolvency or similar proceeding.

**HOMESTREET, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 12 — DERIVATIVES AND HEDGING ACTIVITIES:** (cont.)

The collateral used under the Company’s master netting agreements is typically cash, but securities may be used under agreements with certain counterparties. Receivables related to cash collateral that has been paid to counterparties is included in other assets on the Company’s consolidated statements of financial condition. Any securities pledged to counterparties as collateral remain on the consolidated statement of financial condition. Refer to Note 5, *Investment Securities* for further information on securities collateral pledged. At December 31, 2019, the Company held \$15.2 million collateral received from counterparties under derivative transactions. In 2018 we did not hold any collateral received from counterparties under derivative transactions.

In addition, the Company periodically enters into certain commercial loan interest rate swap agreements in order to provide commercial loan customers the ability to convert from variable to fixed interest rates. Under these agreements, the Company enters into a variable-rate loan agreement with a customer in addition to a swap agreement. This swap agreement effectively converts the customer’s variable rate loan into a fixed rate. The Company then enters into a corresponding swap agreement with a third-party in order to offset its exposure on the variable and fixed components of the customer loan agreement. As the interest rate swap agreements with the customers and third parties are not designated as hedges under the Derivatives and Hedging topic of the FASB ASC 815, the instruments are marked to market in earnings. The notional amount of open interest rate swap agreements at December 31, 2019 and 2018 were \$144.1 million and \$2.6 million, respectively. During the years ended December 31, 2019 and 2018 there were \$121 thousand and \$5 thousand mark-to-market losses recorded to “Other” noninterest income in our consolidated statements of operations. The Company had no similar activity in the year ended December 31, 2017.

The Company’s derivative activities are monitored by the asset/liability management committee. The treasury function, which includes asset/liability management, is responsible for hedging strategies developed through analysis of data from financial models and other internal and industry sources. The resulting hedging strategies are incorporated into the overall risk management strategies.

For further information on the policies that govern derivative and hedging activities, see Note 1, *Summary of Significant Accounting Policies*.

The notional amounts and fair values for derivatives consist of the following.

| <b>(in thousands)</b>   | <b>At December 31, 2019</b> |                               |                   |
|---|-----------------------------|-------------------------------|-------------------|
|   | <b>Notional amount</b>      | <b>Fair value derivatives</b> |                   |
|   |                             | <b>Asset</b>                  | <b>Liability</b>  |
| Forward sale commitments . . . . .  | \$ 651,838                  | \$ 830                        | \$ (492)          |
| Interest rate lock and purchase loan commitments . . . . .                                | 124,379                     | 2,281                         | (58)              |
| Interest rate swaps . . . . .   | 688,516                     | 27,097                        | (10,889)          |
| Eurodollar futures . . . . .  | 2,232,000                   | 3                             | —                 |
| Total derivatives before netting . . . . .  | <u>\$ 3,696,733</u>         | 30,211                        | (11,439)          |
| Netting adjustment/Cash collateral <sup>(1)</sup> . . . . .                               |                             | <u>(21,414)</u>               | <u>9,101</u>      |
| Carrying value on consolidated statements of financial condition <sup>(2)</sup> . . . . . |                             | <u>\$ 8,797</u>               | <u>\$ (2,338)</u> |

**HOMESTREET, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 12 — DERIVATIVES AND HEDGING ACTIVITIES: (cont.)**

| <b>(in thousands)</b>   | <b>At December 31, 2018</b> |                               |                  |
|---|-----------------------------|-------------------------------|------------------|
|   | <b>Notional<br/>amount</b>  | <b>Fair value derivatives</b> |                  |
|   |                             | <b>Asset</b>                  | <b>Liability</b> |
| Forward sale commitments . . . . .  | \$ 1,334,947                | \$ 3,025                      | \$ (5,340)       |
| Interest rate swaptions . . . . .   | 34,000                      | 203                           | —                |
| Interest rate lock and purchase loan commitments . . . . .                          | 390,558                     | 10,289                        | (5)              |
| Interest rate swaps . . . . .   | 803,652                     | 14,566                        | (11,549)         |
| Eurodollar futures . . . . .  | 3,135,000                   | —                             | (110)            |
| Total derivatives before netting . . . . .  | \$ 5,698,157                | 28,083                        | (17,004)         |
| Netting adjustment/Cash collateral <sup>(1)</sup> . . . . .                         |                             | (8,329)                       | 12,517           |
| Carrying value on consolidated statements of financial condition <sup>(2)</sup> . . |                             | \$ 19,754                     | \$ (4,487)       |

(1) Includes net cash collateral received of \$12.3 million and net cash collateral paid of \$4.2 million at December 31, 2019 and 2018, respectively, as part of netting adjustments.

(2) Includes both continuing and discontinued operations.

The following tables present gross and net information about derivative instruments.

| <b>(in thousands)</b>            | <b>At December 31, 2019</b> |  |                           |  |                       |
|----------------------------------|-----------------------------|--|---------------------------|--|-----------------------|
|                                  | <b>Gross<br/>fair value</b> | <b>Netting<br/>adjustments/Cash<br/>collateral<sup>(1)</sup></b> | <b>Carrying<br/>value</b> | <b>Securities<br/>not offset in<br/>consolidated<br/>balance sheet<br/>(disclosure-only<br/>netting)</b> | <b>Net<br/>amount</b> |
|                                  |                             |  |                           |  |                       |
| Derivative assets . . . . .      | \$ 30,211                   | \$ (21,414)  | \$ 8,797                  | \$ —   | \$ 8,797              |
| Derivative liabilities . . . . . | (11,439)                    | 9,101  | (2,338)                   | —  | (2,338)               |

| <b>(in thousands)</b>            | <b>At December 31, 2018</b> |  |                           |  |                       |
|----------------------------------|-----------------------------|--|---------------------------|--|-----------------------|
|                                  | <b>Gross<br/>fair value</b> | <b>Netting<br/>adjustments/Cash<br/>collateral<sup>(1)</sup></b> | <b>Carrying<br/>value</b> | <b>Securities<br/>not offset in<br/>consolidated<br/>balance sheet<br/>(disclosure-only<br/>netting)</b> | <b>Net<br/>amount</b> |
|                                  |                             |  |                           |  |                       |
| Derivative assets . . . . .      | \$ 28,083                   | \$ (8,329)   | \$ 19,754                 | \$ —   | \$ 19,754             |
| Derivative liabilities . . . . . | (17,004)                    | 12,517   | (4,487)                   | 3,223  | (1,264)               |

(1) Includes net cash collateral received of \$12.3 million and net cash collateral paid of \$4.2 million at December 31, 2019 and 2018, respectively, as part of netting adjustments.

Free-standing derivatives are used for fair value interest rate risk management purposes and do not qualify for hedge accounting treatment, referred to as economic hedges. Economic hedges are used to hedge against adverse changes in fair value of single family mortgage servicing rights (“single family MSR”), interest rate lock commitments (“IRLCs”) for single family mortgage loans that the Company intends to sell, and single family mortgage loans held for sale.

Free-standing derivatives used as economic hedges for single family MSR typically include positions in interest rate futures, options on 10-year treasury contracts, forward sales commitments on mortgage-backed securities, and interest rate swap and swaption contracts. The single family MSR and the free-standing derivatives are carried at fair value with changes in fair value included in mortgage servicing income.

**HOMESTREET, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 12 — DERIVATIVES AND HEDGING ACTIVITIES:** (cont.)

The free-standing derivatives used as economic hedges for IRLCs and single family mortgage loans held for sale are forward sales commitments on mortgage-backed securities and option contracts. IRLCs, single family mortgage loans held for sale, and the free-standing derivatives (“economic hedges”) are carried at fair value with changes in fair value included in net gain on mortgage loan origination and sale activities.

The following table presents the net gain (loss) recognized on derivatives, including economic hedge derivatives, within the respective line items in the statement of operations for the periods indicated.

| <b>(in thousands)</b>  | <b>Years Ended December 31,</b> |                    |                    |
|--|---------------------------------|--------------------|--------------------|
|  | <b>2019</b>                     | <b>2018</b>        | <b>2017</b>        |
| Recognized in noninterest income: <sup>(1)</sup>                                 |                                 |                    |                    |
| Net (loss) gain on loan origination and sale activities <sup>(2)</sup> . . . . . | \$ (19,394)                     | \$ 7,790           | \$ (28,549)        |
| Loan servicing income (loss) <sup>(3)</sup> . . . . .                            | 14,435                          | (40,474)           | 9,732              |
| Other <sup>(4)</sup> . . . . .   | 121                             | 3                  | —                  |
|  | <u>\$ (4,838)</u>               | <u>\$ (32,681)</u> | <u>\$ (18,817)</u> |

- (1) Includes both continuing and discontinued operations.
- (2) Comprised of IRLCs and forward contracts used as an economic hedge of IRLCs and single family mortgage loans held for sale.
- (3) Comprised of interest rate swaps, interest rate swaptions and futures and forward contracts used as an economic hedge of single family MSR.
- (4) Comprised of interest rate swaps used as an economic hedge of loans held for investment.

**NOTE 13 — MORTGAGE BANKING OPERATIONS:**

Loans held for sale consisted of the following.

| <b>(in thousands)</b>                  | <b>At December 31,</b> |                   |
|--|------------------------|-------------------|
|  | <b>2019</b>            | <b>2018</b>       |
| Commercial . . . . .                   | \$ 128,841             | \$ 25,139         |
| Single family <sup>(1)</sup> . . . . . | 105,458                | 321,868           |
| Total loans held for sale . . . . .    | <u>\$ 234,299</u>      | <u>\$ 347,007</u> |

- (1) Includes loans from discontinued operations of \$26.1 million and \$269.7 million at December 31, 2019 and 2018, respectively.

Loans sold proceeds consisted of the following.

| <b>(in thousands)</b>                     | <b>Years Ended December 31,</b> |                     |                     |
|---|---------------------------------|---------------------|---------------------|
|   | <b>2019</b>                     | <b>2018</b>         | <b>2017</b>         |
| Commercial . . . . .                      | \$ 843,864                      | \$ 591,121          | \$ 695,624          |
| Single family <sup>(1)</sup> . . . . .    | 3,925,302                       | 6,300,838           | 7,508,949           |
| Total loans sold <sup>(2)</sup> . . . . . | <u>\$ 4,769,166</u>             | <u>\$ 6,891,959</u> | <u>\$ 8,204,573</u> |

- (1) Includes both continuing and discontinued operations.
- (2) Includes loans originated as held for investment.

**HOMESTREET, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 13 — MORTGAGE BANKING OPERATIONS: (cont.)**

Gain on loan origination and sale activities, including the effects of derivative risk management instruments, consisted of the following.

| <u>(in thousands)</u>   | <b>Years Ended December 31,</b> |                   |                   |
|---|---------------------------------|-------------------|-------------------|
|   | <b>2019</b>                     | <b>2018</b>       | <b>2017</b>       |
| Commercial . . . . .  | \$ 17,492                       | \$ 11,776         | \$ 20,027         |
| Single family <sup>(1)</sup> . . . . .                                      | 86,686                          | 174,473           | 235,849           |
| Total gain on loan origination and sale activities <sup>(2)</sup> . . . . . | <u>\$ 104,178</u>               | <u>\$ 186,249</u> | <u>\$ 255,876</u> |

- (1) Includes \$60.1 million, \$174.4 million and \$235.9 million from discontinued operations for the years ended 2019, 2018 and 2017, respectively.
- (2) Includes loans originated as held for investment.

The Company's portfolio of loans serviced for others is primarily comprised of loans held in U.S. government and agency MBS issued by Fannie Mae, Freddie Mac and Ginnie Mae. Loans serviced for others are not included in the consolidated statements of financial condition as they are not assets of the Company.

The composition of loans serviced for others that contribute to loan servicing income is presented below at the unpaid principal balance.

| <u>(in thousands)</u>                     | <b>At December 31,</b> |                      |
|---|------------------------|----------------------|
|   | <b>2019</b>            | <b>2018</b>          |
| Commercial . . . . .                      | \$ 1,618,876           | \$ 1,542,477         |
| Single family <sup>(1)(2)</sup> . . . . . | 7,023,441              | 20,151,735           |
| Total loans serviced for others . . . . . | <u>\$ 8,642,317</u>    | <u>\$ 21,694,212</u> |

- (1) Includes both continuing and discontinued operations at December 31, 2018.
- (2) On March 29, 2019, the Company closed and settled two sales of the rights to service \$14.26 billion in total unpaid principal balance of single family mortgage loans representing approximately 71% of single family mortgage loans serviced for others portfolio as of December 31, 2018.

The Company has made representations and warranties that the loans sold meet certain requirements. The Company may be required to repurchase mortgage loans or indemnify loan purchasers due to defects in the origination process of the loan, such as documentation errors, underwriting errors and judgments, appraisal errors, early payment defaults and fraud. For further information on the Company's mortgage repurchase liability, see Note 14, *Commitments, Guarantees and Contingencies*.

The following is a summary of changes in the Company's liability for estimated mortgage repurchase losses.

| <u>(in thousands)</u>                                  | <b>Years Ended December 31,</b> |                 |
|--|---------------------------------|-----------------|
|  | <b>2019</b>                     | <b>2018</b>     |
| Balance, beginning of period . . . . .                 | \$ 3,120                        | \$ 3,015        |
| Additions, net of adjustments <sup>(1)</sup> . . . . . | 226                             | 1,930           |
| Realized losses <sup>(2)</sup> . . . . .               | (475)                           | (1,825)         |
| Balance, end of period . . . . .                       | <u>\$ 2,871</u>                 | <u>\$ 3,120</u> |

- (1) Includes additions for new loan sales and changes in estimated probable future repurchase losses on previously sold loans.
- (2) Includes principal losses and accrued interest on repurchased loans, "make-whole" settlements, settlements with claimants and certain related expenses.



**HOMESTREET, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 13 — MORTGAGE BANKING OPERATIONS:** (cont.)

The Company has agreements with investors to advance scheduled principal and interest amounts on delinquent loans.

Advances are also made to fund the foreclosure and collection costs of delinquent loans prior to the recovery of reimbursable amounts from investors or borrowers. Advances of \$2.5 million and \$2.5 million were recorded in other assets as of December 31, 2019 and 2018, respectively.

When the Company has the unilateral right to repurchase Ginnie Mae pool loans it has previously sold (generally loans that are more than 90 days past due), the Company then records the loan on its consolidated statement of financial condition. At December 31, 2019 and 2018, delinquent or defaulted mortgage loans currently in Ginnie Mae pools that the Company has recognized on its consolidated statements of financial condition totaled \$9.4 million and \$37.7 million, respectively, with a corresponding amount recorded within accounts payable and other liabilities on the consolidated statements of financial condition. The recognition of previously sold loans does not impact the accounting for the previously recognized MSR.

Revenue from mortgage servicing, including the effects of derivative risk management instruments, consisted of the following.

| <b>(in thousands)</b>  | <b>Years Ended December 31,</b> |             |             |
|--|---------------------------------|-------------|-------------|
|  | <b>2019</b>                     | <b>2018</b> | <b>2017</b> |
| <b>Servicing income, net:</b>  |                                 |             |             |
| Servicing fees and other. . . . .  | \$ 37,558                       | \$ 68,938   | \$ 66,192   |
| Changes in fair value of single family MSRs due to modeled amortization <sup>(1)</sup> . . . . .             | (20,670)                        | (34,705)    | (35,451)    |
| Amortization of multifamily and SBA MSRs . . . . .   | (5,219)                         | (4,383)     | (3,932)     |
|  | 11,669                          | 29,850      | 26,809      |
| <b>Risk management, single family MSRs:</b>  |                                 |             |             |
| Changes in fair value of MSRs due to changes in market inputs and/or assumptions <sup>(2)(3)</sup> . . . . . | (16,224)                        | 39,348      | (1,157)     |
| Net gain (loss) from derivatives economically hedging MSR . . .  | 14,435                          | (40,474)    | 9,732       |
|  | (1,789)                         | (1,126)     | 8,575       |
| Loan servicing income <sup>(4)</sup> . . . . .   | \$ 9,880                        | \$ 28,724   | \$ 35,384   |

- (1) Represents changes due to collection/realization of expected cash flows and curtailments.
- (2) Principally reflects changes in market inputs, which include current market interest rates and prepayment model updates, both of which affect future prepayment speed and cash flow projections.
- (3) Includes pre-tax loss of \$919 thousand and pre-tax gain of \$573 thousand, net of transaction costs and prepayment reserves, resulting from the sales of single family MSR for year ended December 31, 2019 and December 31, 2018, respectively.
- (4) Includes \$3.0 million, \$25.1 million and \$32.1 million from discontinued operations for the years ended December 31, 2019, 2018 and 2017, respectively.

The fair value of MSRs is determined based on the price that would be received to sell the MSRs in an orderly transaction between market participants at the measurement date. The Company determines fair value using a valuation model that calculates the net present value of estimated future cash flows. Estimates of future cash flows include contractual servicing fees, ancillary income and costs of servicing, the timing of which are impacted by assumptions, primarily expected prepayment speeds and discount rates, which relate to the underlying performance of the loans.

**HOMESTREET, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 13 — MORTGAGE BANKING OPERATIONS:** (cont.)

The initial fair value measurement of MSR is adjusted up or down depending on whether the underlying loan pool interest rate is at a premium, discount or par. Key economic assumptions used in measuring the initial fair value of capitalized single family MSR were as follows.

| (rates per annum) <sup>(1)</sup>                          | Years Ended December 31, |        |        |
|---|--------------------------|--------|--------|
|   | 2019                     | 2018   | 2017   |
| Constant prepayment rate (“CPR”) <sup>(2)</sup> . . . . . | 18.23%                   | 15.86% | 13.36% |
| Discount rate <sup>(3)</sup> . . . . .                    | 9.31%                    | 10.29% | 10.27% |

- (1) Weighted average rates for sales during the period for sales of loans with similar characteristics.
- (2) Represents the expected lifetime average.
- (3) Discount rate is based on market observations.

Key economic assumptions and the sensitivity of the current fair value for single family MSR to immediate adverse changes in those assumptions were as follows.

| (dollars in thousands)   | At<br>December 31,<br>2019 |
|--|----------------------------|
| Fair value of single family MSR . . . . .  | \$ 68,109                  |
| Expected weighted-average life (in years) . . . . .                                | 4.69                       |
| Constant prepayment rate <sup>(1)</sup> . . . . .                                  | 17.67%                     |
| Impact on fair value of 25 basis points adverse change in interest rates . . . . . | \$ (4,838)                 |
| Impact on fair value of 50 basis points adverse change in interest rates . . . . . | \$ (9,330)                 |
| Discount rate . . . . .  | 9.20%                      |
| Impact on fair value of 100 basis points increase . . . . .                        | \$ (2,098)                 |
| Impact on fair value of 200 basis points increase . . . . .                        | \$ (4,059)                 |

- (1) Represents the expected lifetime average.

These sensitivities are hypothetical and subject to key assumptions of the underlying valuation model. As the table above demonstrates, the Company’s methodology for estimating the fair value of MSR is highly sensitive to changes in key assumptions. For example, actual prepayment experience may differ and any difference may have a material effect on MSR fair value. Changes in fair value resulting from changes in assumptions generally cannot be extrapolated because the relationship of the change in assumption to the change in fair value may not be linear. Also, in this table, the effect of a variation in a particular assumption on the fair value of the MSR is calculated without changing any other assumption; in reality, changes in one factor may be associated with changes in another (for example, decreases in market interest rates may provide an incentive to refinance; however, this may also indicate a slowing economy and an increase in the unemployment rate, which reduces the number of borrowers who qualify for refinancing), which may magnify or counteract the sensitivities. Thus, any measurement of MSR fair value is limited by the conditions existing and assumptions made as of a particular point in time. Those assumptions may not be appropriate if they are applied to a different point in time.

In March 2019, the Company successfully closed and settled two sales of the rights to service an aggregate of \$14.26 billion in total unpaid principal balance of single family mortgage loans serviced for Fannie Mae, Ginnie Mae and Freddie Mac representing 71% of HomeStreet’s total single family mortgage loans serviced for others portfolio as of December 31, 2018. These sales resulted in a \$919 thousand pre-tax loss from discontinued operations for the year ended December 31, 2019, respectively. For more information, see Note. 2, *Discontinued Operations*.

**HOMESTREET, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 13 — MORTGAGE BANKING OPERATIONS: (cont.)**

The changes in single family MSR measured at fair value are as follows.

| <b>(in thousands)</b>   | <b>Years Ended December 31,</b> |                   |                   |
|---|---------------------------------|-------------------|-------------------|
|   | <b>2019</b>                     | <b>2018</b>       | <b>2017</b>       |
| Beginning balance . . . . .   | \$ 252,168                      | \$ 258,560        | \$ 226,113        |
| Additions and amortization:   |                                 |                   |                   |
| Originations . . . . .  | 28,774                          | 55,608            | 68,499            |
| Purchases . . . . .   | 14                              | —                 | 565               |
| Sale of single family MSRs . . . . .  | (176,944)                       | (66,902)          | —                 |
| Changes due to modeled amortization <sup>(1)</sup> . . . . .  | (20,670)                        | (34,705)          | (35,451)          |
| Net additions and amortization . . . . .  | (168,826)                       | (45,999)          | 33,613            |
| Changes in fair value of MSRs due to changes in market inputs and/or model updates <sup>(2)</sup> . . . . . | (15,233)                        | 39,607            | (1,166)           |
| Ending balance . . . . .  | <u>\$ 68,109</u>                | <u>\$ 252,168</u> | <u>\$ 258,560</u> |

(1) Represents changes due to collection/realization of expected cash flows and curtailments.

(2) Principally reflects changes in market inputs, which include current market interest rates and prepayment model updates, both of which affect future prepayment speed and cash flow projections.

MSRs resulting from the sale of multifamily loans are recorded at fair value and subsequently carried at the lower of amortized cost or fair value. Multifamily MSRs are amortized in proportion to, and over, the estimated period the net servicing income will be collected.

The changes in multifamily MSR measured at the lower of amortized cost or fair value were as follows.

| <b>(in thousands)</b>       | <b>Years Ended December 31,</b> |                  |                  |
|-----------------------------|---------------------------------|------------------|------------------|
|                             | <b>2019</b>                     | <b>2018</b>      | <b>2017</b>      |
| Beginning balance . . . . . | \$ 28,328                       | \$ 26,093        | \$ 19,747        |
| Origination . . . . .       | 5,832                           | 6,268            | 9,915            |
| Amortization . . . . .      | (4,666)                         | (4,033)          | (3,569)          |
| Ending balance . . . . .    | <u>\$ 29,494</u>                | <u>\$ 28,328</u> | <u>\$ 26,093</u> |

At December 31, 2019, the expected weighted-average life of the Company's multifamily MSRs was 10.48.

Projected amortization expense for the gross carrying value of multifamily MSRs is estimated as follows.

| <b>(in thousands)</b>                       | <b>At<br/>December 31,<br/>2019</b> |
|---|-------------------------------------|
| 2020 . . . . .                              | \$ 4,193                            |
| 2021 . . . . .                              | 4,080                               |
| 2022 . . . . .                              | 3,861                               |
| 2023 . . . . .                              | 3,644                               |
| 2024 . . . . .                              | 3,373                               |
| 2025 and thereafter . . . . .               | 10,343                              |
| Carrying value of multifamily MSR . . . . . | <u>\$ 29,494</u>                    |

The projected amortization expense of multifamily MSRs is an estimate and subject to key assumptions of the underlying valuation model. The amortization expense for future periods was calculated by applying the same quantitative factors, such as actual MSR prepayment experience and discount rates, which were used to determine amortization expense. These factors are inherently subject to significant fluctuations, primarily due to the effect that changes in interest rates may have on expected loan prepayment experience. Accordingly, any projection of MSR amortization in future periods is limited by the conditions that existed at the time the calculations were performed and may not be indicative of actual amortization expense that will be recorded in future periods.

**HOMESTREET, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 14 — COMMITMENTS, GUARANTEES AND CONTINGENCIES:**

Commitments

Commitments to extend credit are agreements to lend to customers in accordance with predetermined contractual provisions. These commitments may be for specific periods or contain termination clauses and may require the payment of a fee by the borrower. The total amount of unused commitments do not necessarily represent future credit exposure or cash requirements in that commitments may expire without being drawn upon.

The Company makes certain unfunded loan commitments as part of its lending activities that have not been recognized in the Company's financial statements. These include commitments to extend credit made as part of the Company's lending activities on loans the Company intends to hold in its loans held for investment portfolio. The aggregate amount of these unrecognized unfunded loan commitments existing at December 31, 2019 and 2018 was \$52.8 million and \$33.8 million, respectively.

In the ordinary course of business, the Company extends secured and unsecured open-end loans to meet the financing needs of its customers. These commitments include unused consumer portfolio lines of \$485.1 million and \$462.0 million as of December 31, 2019 and 2018, respectively, and commercial portfolio lines of \$722.2 million and \$852.9 million at December 31, 2019 and 2018, respectively. Within the commercial portfolio, undistributed construction loan proceeds, where the Company has an obligation to advance funds for construction progress payments, were \$435.2 million and \$607.2 million at December 31, 2019 and 2018, respectively. The total amounts of unused commitments do not necessarily represent future credit exposure or cash requirements in that commitments may expire without being drawn upon. The Company has recorded an allowance for credit losses on loan commitments, included in accounts payable and other liabilities on the consolidated statements of financial condition, of \$1.1 million and \$1.4 million at December 31, 2019 and 2018, respectively.

The Company is in certain agreements to invest in qualifying small businesses and small enterprises, as well as low income housing tax credit partnerships and a tax exempt bond partnership that have not been recognized in the Company's financial statements. At December 31, 2019 and 2018 we had \$23.5 million and 23.9 million, respectively, of future commitments to invest in these enterprises.

Guarantees

In the ordinary course of business, the Company sells loans through the Fannie Mae Multifamily Delegated Underwriting and Servicing Program ("DUS"<sup>®</sup>) that are subject to a credit loss sharing arrangement. The Company services the loans for Fannie Mae and shares in the risk of loss with Fannie Mae under the terms of the DUS contracts. Under the DUS program, the Company and Fannie Mae share losses on a pro rata basis, where the Company is responsible for losses incurred up to one-third of principal balance on each loan with two-thirds of the loss covered by Fannie Mae. For loans that have been sold through this program, a liability is recorded for this loss sharing arrangement under the accounting guidance for guarantees. As of December 31, 2019 and 2018, the total unpaid principal balance of loans sold under this program was \$1.55 billion and \$1.46 billion, respectively. The Company's reserve liability related to this arrangement totaled \$2.8 million and \$2.5 million at December 31, 2019 and 2018, respectively. There were no actual losses incurred under this arrangement during the years ended December 31, 2019, 2018 and 2017.

Mortgage repurchase liability

In the ordinary course of business, the Company sells residential mortgage loans to GSEs and other entities. In addition, the Company pools FHA-insured and VA-guaranteed mortgage loans into Ginnie Mae, Fannie Mae and Freddie Mac guaranteed mortgage-backed securities. The Company has made representations and warranties that the loans sold meet certain requirements. The Company may be required to repurchase mortgage loans or indemnify loan purchasers due to defects in the origination process of the loan, such as documentation errors, underwriting errors and judgments, early payment defaults and fraud.

**HOMESTREET, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 14 — COMMITMENTS, GUARANTEES AND CONTINGENCIES: (cont.)**

These obligations expose the Company to mark-to-market and credit losses on the repurchased mortgage loans after accounting for any mortgage insurance that we may receive. Generally, the maximum amount of future payments the Company would be required to make for breaches of these representations and warranties would be equal to the unpaid principal balance of such loans that are deemed to have defects that were sold to purchasers plus, in certain circumstances, accrued and unpaid interest on such loans and certain expenses.

The Company does not typically receive repurchase requests from the FHA or VA. As an originator of FHA-insured or VA-guaranteed loans, the Company is responsible for obtaining the insurance with FHA or the guarantee with the VA. If loans are later found not to meet the requirements of FHA or VA, through required internal quality control reviews or through agency audits, the Company may be required to indemnify FHA or VA against losses. The loans remain in Ginnie Mae pools unless and until they are repurchased by the Company. In general, once an FHA or VA loan becomes 90 days past due, the Company repurchases the FHA or VA residential mortgage loan to minimize the cost of interest advances on the loan. If the loan is cured through borrower efforts or through loss mitigation activities, the loan may be resold into another Ginnie Mae pool. The Company's liability for mortgage loan repurchase losses incorporates probable losses associated with such indemnification.

The total unpaid principal balance of loans sold on a servicing-retained basis that were subject to the terms and conditions of these representations and warranties totaled \$7.10 billion and \$20.24 billion as of December 31, 2019 and 2018, respectively. At December 31, 2019 and 2018, the Company had recorded a mortgage repurchase liability for loans sold on a servicing-retained and servicing-released basis, included in accounts payable and other liabilities on the consolidated statements of financial condition, of \$2.9 million and \$3.1 million, respectively.

Contingencies

In the normal course of business, the Company may have various legal claims and other similar contingent matters outstanding for which a loss may be realized. For these claims, the Company establishes a liability for contingent losses when it is probable that a loss has been incurred and the amount of loss can be reasonably estimated. For claims determined to be reasonably possible but not probable of resulting in a loss, there may be a range of possible losses in excess of the established liability. At December 31, 2019, we reviewed our legal claims and determined that there were no material claims that were considered to be probable or reasonably possible of resulting in a material loss. As a result, the Company did not have any material amounts reserved for legal claims as of December 31, 2019.

**NOTE 15 — INCOME TAXES:**

On December 22, 2017, The President of the United States signed into law H.R. 1, commonly referred to as the Tax Cuts and Jobs Act ("Tax Reform Act"). The Tax Reform Act reduces the U.S. federal corporate income tax rate from 35% to 21% and makes many other changes to the U.S. tax code. In the year of enactment, we were required to revalue our deferred tax assets and liabilities at the new statutory tax rate. As a result of this revaluation, we recognized a one-time, non-cash, \$4.9 million deferred income tax benefit in our 2018 year-end provision and a \$23.3 million benefit in our 2017 year-end provision.

Income tax expense (benefit) from continuing operations consisted of following:

| <u>(in thousands)</u>   | <u>Years Ended December 31,</u> |                 |                    |
|---|---------------------------------|-----------------|--------------------|
|   | <u>2019</u>                     | <u>2018</u>     | <u>2017</u>        |
| Current expense (benefit)   |                                 |                 |                    |
| Federal . . . . .   | \$ 32,738                       | \$ (11,205)     | \$ (13,508)        |
| State and local . . . . .   | 5,153                           | (54)            | (1,216)            |
| Deferred (benefit) expense  |                                 |                 |                    |
| Federal . . . . .   | (28,313)                        | 14,215          | 17,637             |
| Revaluation of deferred items . . . . .                           | —                               | (4,899)         | (23,325)           |
| State and local . . . . .   | (4,292)                         | 1,489           | 528                |
| Tax credit investment amortization . . . . .                      | 2,702                           | 2,486           | 2,990              |
| Total income tax expense (benefit) from continuing operations . . | <u>\$ 7,988</u>                 | <u>\$ 2,032</u> | <u>\$ (16,894)</u> |

**HOMESTREET, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 15 — INCOME TAXES: (cont.)**

Income tax expense (benefit) from continuing operations differed from amounts computed at the federal income tax statutory rate as follows:

| <u>(in thousands)</u>   | <u>Years Ended December 31,</u> |                 |                    |
|---|---------------------------------|-----------------|--------------------|
|   | <u>2019</u>                     | <u>2018</u>     | <u>2017</u>        |
| Income taxes at statutory rate . . . . .  | \$ 8,933                        | \$ 6,400        | \$ 9,852           |
| State income tax expense, net of federal tax benefit . . . . .                        | 1,078                           | 686             | 376                |
| Tax-exempt interest . . . . .   | (1,388)                         | (1,626)         | (2,855)            |
| Tax credits . . . . .   | (2,490)                         | (2,922)         | (2,041)            |
| Amortization of and pass-through losses from low income housing investments . . . . . | 2,237                           | 2,648           | 1,716              |
| Change in state rate . . . . .  | (252)                           | 220             | (714)              |
| Return to provision . . . . .   | (161)                           | 1,238           | (278)              |
| Impact from Federal Rate Change . . . . .   | —                               | (4,899)         | (23,326)           |
| Uncertain tax positions . . . . .   | —                               | (42)            | 76                 |
| Other, net . . . . .  | 31                              | 329             | 300                |
| Total income tax expense (benefit) from continuing operations . . . . .               | <u>\$ 7,988</u>                 | <u>\$ 2,032</u> | <u>\$ (16,894)</u> |

Deferred income taxes reflect the net tax effect of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and those amounts used for tax return purposes. The following is a summary of the Company's significant portions of deferred tax assets and liabilities:

| <u>(in thousands)</u>   | <u>At December 31,</u> |                    |
|---|------------------------|--------------------|
|   | <u>2019</u>            | <u>2018</u>        |
| Deferred tax assets:  |                        |                    |
| Provision for loan losses . . . . .                                   | \$ 12,731              | \$ 12,959          |
| Federal and state net operating loss carryforwards . . . . .          | 1,361                  | 2,407              |
| Accrued liabilities . . . . .   | 2,653                  | 2,319              |
| Other investments . . . . .   | 231                    | 37                 |
| Lease liabilities . . . . .   | 25,806                 | 2,386              |
| Unrealized loss on investment available for sale securities . . . . . | —                      | 4,498              |
| Tax credits . . . . .   | 27                     | 1,399              |
| Stock-based compensation . . . . .                                    | 785                    | 1,247              |
| Loan valuation . . . . .  | 712                    | 1,187              |
| Other, net . . . . .  | 1,237                  | 1,422              |
|   | <u>45,543</u>          | <u>29,861</u>      |
| Deferred tax liabilities:   |                        |                    |
| Mortgage servicing rights . . . . .                                   | (20,946)               | (57,452)           |
| FHLB dividends . . . . .  | (133)                  | (272)              |
| Deferred loan fees and costs . . . . .                                | (12,048)               | (10,718)           |
| Lease right-of-use assets . . . . .                                   | (25,406)               | —                  |
| Unrealized gain on investment securities available for sale . . . . . | (1,159)                | —                  |
| Premises and equipment . . . . .                                      | (4,588)                | (6,997)            |
| Intangibles . . . . .   | (885)                  | (1,133)            |
| Other, net . . . . .  | (167)                  | (25)               |
|   | <u>(65,332)</u>        | <u>(76,597)</u>    |
| Net deferred tax liability . . . . .                                  | <u>\$ (19,789)</u>     | <u>\$ (46,736)</u> |



**HOMESTREET, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 15 — INCOME TAXES: (cont.)**

The Company currently has a net deferred tax liability. This net deferred tax liability is included in accounts payable and other liabilities on the consolidated statements of financial condition.

Management assesses the available positive and negative evidence to estimate if sufficient future taxable income will be generated to utilize the existing deferred tax assets. As of December 31, 2019, management determined that sufficient evidence exists to support the future utilization of all of the Company's deferred tax assets.

Utilization of the federal and state net operating loss and tax credit carryforwards may be subject to an annual limitation due to the "change in ownership" provisions of the Internal Revenue Code of 1986, as amended. Specifically, the Company is subject to annual limitations on the amounts of net operating loss and credit carryover that the Company can use from its pre-IPO period, or from the pre-acquisition periods of the companies that it has acquired in prior years. At December 31, 2019 and 2018, the Company has federal net operating loss carryforwards totaling \$3.4 million and \$5.9 million, respectively, which are from tax years prior to 2018. As such, they can be carryforward for a period of 20 years and will begin to expire between 2029 and 2036. The Tax Reform Act repeals the corporate alternative minimum tax rules and makes any unused minimum tax credit partially refundable in tax years 2019 – 2020, and fully refundable in the tax year 2021. As of December 31, 2019, the Company had \$825 thousand of minimum tax credit carryforwards. The Company also has state net operating loss carryforwards as of December 31, 2019 and 2018 of \$12.2 million and \$18.3 million, respectively, that will expire at various dates from 2020 to 2036.

Retained earnings at December 31, 2019 and 2018 include approximately \$12.7 million in tax basis bad debt reserves for which no income tax liability has been recorded. This represents the balance of bad debt reserves created for tax purposes as of December 31, 1987. These amounts are subject to recapture (i.e., included in taxable income) in certain events, such as in the event HomeStreet Bank ceases to be a bank. In the event of recapture, the Company will incur both federal and state tax liabilities on this pre-1988 bad debt reserve balance at the then prevailing corporate tax rates.

The Company had no recorded unrecognized tax position as of December 31, 2019. During 2018, we settled our only unrecognized tax position and released the reserve. We periodically evaluate our exposure associated with filing positions to determine if any new positions need to be recorded, and concluded no new positions were created during the year.

A reconciliation of our unrecognized tax positions, excluding accrued interest and penalties, for the years ended December 31, 2019, 2018 and 2017 is as follows:

| (in thousands)  | Years Ended December 31, |        |        |
|---|--------------------------|--------|--------|
|   | 2019                     | 2018   | 2017   |
| Balance, beginning of year . . . . .                    | \$ —                     | \$ 495 | \$ 419 |
| Increases related to prior year tax positions . . . . . | —                        | —      | 76     |
| Settlements . . . . .                                   | —                        | (495)  | —      |
| Balance, end of year . . . . .                          | \$ —                     | \$ —   | \$ 495 |

We are currently under examination, or subject to examination, by various U.S. federal and state taxing authorities. The Company is no longer subject to federal income tax examinations for tax years prior to 2015 or state income tax examination for tax years prior to 2015, generally.

**NOTE 16 — REVENUE:**

On January 1, 2018, the Company adopted ASU No. 2014-09 *Revenue from Contracts with Customers* ("Topic 606"). We elected to implement Topic 606 using the modified retrospective application, with the cumulative effect recorded as an adjustment to retained earnings at January 1, 2018. Due to immateriality, we had no cumulative effect to record. Since net interest income on financial assets and liabilities is excluded from this guidance, a significant majority of our revenues are not subject to the new guidance.

**HOMESTREET, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 16 — REVENUE: (cont.)**

Our revenue streams that fall within the scope of Topic 606 are presented within noninterest income and are, in general, recognized as revenue as we satisfy our obligation to the customer. Most of the Company's contracts that fall within the scope of this guidance are contracts with customers that are cancelable by either party without penalty and are short-term in nature. These revenues include depositor and other retail and business banking fees, commission income, credit card fees and sales of other real estate owned. For the year ended December 31, 2019, in scope revenue streams were approximately 2.44% of our total revenues. As this standard is immaterial to our consolidated financial statements, the Company has omitted certain disclosures in ASU 2014-09, including the disaggregation of revenue table. Noninterest revenue streams within scope are discussed below.

*Depositor and other retail and business banking fees*

Depositor and other retail banking fees consist of monthly service fees, check orders, and other deposit account related fees. The Company's performance obligation for these fees is generally satisfied, and the related revenue recognized, over the period in which the service is provided.

*Commission Income*

Commission income primarily consists of revenue received on insurance policies and monthly investment management fees earned where the Company has acted as an intermediary between customers and the insurance carriers or investment advisers.

Under Topic 606, the commissions received at the inception of the policy should be deferred and recognized over the course of the policy. The Company's performance obligation for commissions is generally satisfied, and the related revenue generally recognized, over the course of the policy or over the period in which the services are provided, generally monthly.

*Credit Card Fees*

The Company offers credit cards to its customers through a third party and earns a fee on each transaction and a fee for each new account activation on a net basis. Revenue is recognized on a one-month lag when cash is received for these fees which does not vary materially from recognizing revenue over the period the services are performed.

*Sale of Real Estate Owned*

A gain or loss, the difference between the cost basis of the property and its sale price, on other real estate owned is recognized when the performance obligation is met, which is at the time the property title is transferred to the buyer.

**NOTE 17 — 401(k) SAVINGS PLAN:**

The Company maintains a 401(k) Savings Plan for the benefit of its employees. Substantially all of the Company's employees are eligible to participate in the HomeStreet, Inc. 401(k) Savings Plan (the "Plan"). The Plan provides for payment of retirement benefits to employees pursuant to the provisions of the plan and in conformity with Section 401(k) of the Internal Revenue Code. Employees may elect to have a portion of their salary contributed to the Plan. New employees are automatically enrolled in the Plan at a 3.0% deferral rate unless they elect otherwise. Participants receive a vested employer matching contribution equal to 100% of the first 3.0% of eligible compensation deferred by the participant and 50% of the next 2.0% of eligible compensation deferred by the participant.

Salaries and related costs for the years ended December 31, 2019, 2018, and 2017, included employer contributions of \$5.5 million, \$7.5 million and \$8.5 million, respectively.

**HOMESTREET, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 18 — SHARE-BASED COMPENSATION PLANS:**

For the year ended December 31, 2019, the Company recognized a net reversal of compensation cost of \$434 thousand. The net reversal of expense related to Performance Share Units (“PSUs”) that did not meet their performance metrics. For the years ended December 31, 2018 and 2017, the Company recognized \$3.0 million, and \$2.5 million of compensation cost, respectively, for share-based compensation awards.

2014 Equity Incentive Plan

In May 2014, the shareholders approved the Company’s 2014 Equity Incentive Plan (the “2014 EIP”). Under the 2014 EIP, all of the Company’s officers, employees, directors and/or consultants are eligible to receive awards. Awards which may be granted under the 2014 EIP include incentive stock options, non-qualified stock options, stock appreciation rights, restricted stock awards, restricted stock units, unrestricted stock, performance share awards and performance compensation awards. The maximum amount of HomeStreet, Inc. common stock available for grant under the 2014 EIP is 900,000 shares, which includes shares of common stock that were still available for issuance under the 2010 Plan and the 2011 Plan.

*Nonqualified Stock Options*

The Company grants nonqualified options to key senior management personnel. A summary of changes in nonqualified stock options granted for the year ended December 31, 2019 is as follows:

|   | <u>Number</u>   | <u>Weighted<br/>Average<br/>Exercise Price</u> | <u>Weighted<br/>Average<br/>Remaining<br/>Contractual<br/>Term</u> | <u>Aggregate<br/>Intrinsic Value<sup>(2)</sup><br/>(in thousands)</u> |
|---|-----------------|--|--|---|
| Options outstanding at December 31, 2018 . .  | 263,925         | \$ 11.91                                       | 3.2 years  | \$ 2,459  |
| Exercised . . . . .   | <u>(30,924)</u> | 7.53   | 0.0 years  | 651   |
| Options outstanding at December 31, 2019 . .  | <u>233,001</u>  | 12.49  | 2.2 years  | 5,011   |
| Options that are exercisable and expected to<br>be exercisable <sup>(1)</sup> . . . . . | 233,001         | 12.49  | 2.2 years  | 5,011   |
| Options exercisable . . . . .   | 233,001         | \$ 12.49                                       | 2.2 years  | \$ 5,011  |

(1) Adjusted for estimated forfeitures.

(2) Intrinsic value is the amount by which fair value of the underlying stock exceeds the exercise price.

Under this plan, 30,924 options have been exercised during the year ended December 31, 2019, resulting in cash received and related income tax benefits totaling \$326 thousand. As of December 31, 2019, there were no unrecognized compensation costs related to stock options. Compensation costs are recognized over the requisite service period, which typically is the vesting period.

As observable market prices are generally not available for estimating the fair value of stock options, an option-pricing model is utilized to estimate fair value. There were no options granted during the years ended December 31, 2019, 2018 and 2017.

**HOMESTREET, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 18 — SHARE-BASED COMPENSATION PLANS: (cont.)**

*Restricted Shares*

The Company grants restricted shares to key senior management personnel and directors. A summary of the status of restricted shares follows.

|  | <b>Number</b> | <b>Weighted<br/>Average<br/>Grant Date<br/>Fair Value</b> |
|--|---------------|---|
| Restricted shares outstanding at December 31, 2018 . . . . . | 292,217       | \$ 26.42  |
| Granted . . . . .  | 129,987       | 27.92   |
| Cancelled or forfeited . . . . .                             | (85,783)      | 23.34   |
| Vested . . . . .   | (67,715)      | 25.63   |
| Restricted shares outstanding at December 31, 2019 . . . . . | 268,706       | \$ 28.32  |

At December 31, 2019, there was \$3.2 million of total unrecognized compensation cost related to nonvested restricted shares. Unrecognized compensation cost is generally expected to be recognized over a weighted average period of 1.9 years.

Certain restricted stock awards granted to senior management during the years ended December 31, 2019, 2018 and 2017, contain both service conditions and performance conditions. Restricted stock units (“RSUs”) are stock awards with a pro-rata three year vesting, and the fair market value of the awards are determined at the grant date based on the Company’s stock price. PSUs are stock awards where the number of shares ultimately received by the employee depends on the Company’s performance against specified targets and vest over a three-year period. Prior to 2019, the fair value of each PSU is determined on the grant date, based on the Company’s stock price, and assumes that performance targets will be achieved.

For PSUs granted in 2019, grants must meet a performance goal related to relative total shareholder return (“TSR”) over a three-year performance cycle. The performance goal over the respective performance cycles for the total shareholder return performance shares (“TSR performance shares”) granted during 2019 is the Company’s three-year total shareholder return relative to the three-year total shareholder return of companies in a performance peer group. The fair value price at the date of grant for the TSR performance shares is determined using a Monte Carlo simulation technique. In calculating the fair value of the award, the risk-free interest rate is based on the yield of a Treasury Note with a term commensurate with the remaining term of the TSR performance shares. The remaining term is based on the remainder of the performance cycle as of the date of grant. The expected volatility is based on historical daily stock price returns. For the TSR performance shares, it was assumed that there would be no forfeitures, based on the vesting term and the number of grantees.

Over the performance period, the number of shares of stock that will be issued is adjusted upward or downward based upon the probability of achievement of performance targets. The ultimate number of shares issued and the related compensation cost recognized as expense will be based on a comparison of the final performance metrics to the specified targets. Compensation cost is recognized over the requisite three-year service period on a straight-line basis and adjusted for changes in the probability that the performance targets will be achieved.

**HOMESTREET, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 18 — SHARE-BASED COMPENSATION PLANS: (cont.)**

The assumptions used for performance share units granted in 2019 are set forth in the table below:

|   | <b>2019</b> |
|---|-------------|
| Volatility of common stock <sup>(1)</sup> .....           | 29.4%       |
| Average volatility of peer companies <sup>(1)</sup> ..... | 24.5%       |
| Average correlation coefficient of peer companies .....   | 0.7272%     |
| Risk-free interest rate <sup>(2)</sup> .....              | 2.3%        |
| Expected term in years .....                              | 2.69 years  |
| Dividend yield .....                                      | —%          |

- (1) Expected volatilities are based on the daily closing price of our stock based on historical experience over a period which approximates the expected term of the performance share units.
- (2) The risk-free interest rate is based on U.S. Treasury securities for the expected term of the performance share units.

**NOTE 19 — FAIR VALUE MEASUREMENT:**

The term “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. A fair value measurement assumes that the transaction to sell the asset or transfer the liability occurs in the principal market for the asset or liability or, in the absence of a principal market, the most advantageous market for the asset or liability. The Company’s approach is to maximize the use of observable inputs and minimize the use of unobservable inputs when developing fair value measurements.

Fair Value Hierarchy

A three-level valuation hierarchy has been established under ASC 820 for disclosure of fair value measurements. The valuation hierarchy is based on the observability of inputs to the valuation of an asset or liability as of the measurement date. A financial instrument’s categorization within the valuation hierarchy is based on the lowest level of input that is significant to the fair value measurement. The levels are defined as follows:

- Level 1 — Quoted prices (unadjusted) in active markets for identical assets or liabilities that the reporting entity can access at the measurement date. An active market for the asset or liability is a market in which transactions for the asset or liability take place with sufficient frequency and volume to provide pricing information on an ongoing basis.
- Level 2 — Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly. This includes quoted prices for similar assets and liabilities in active markets and inputs that are observable for the asset or liability for substantially the full term of the financial instrument.
- Level 3 — Unobservable inputs for the asset or liability. These inputs reflect the Company’s assumptions of what market participants would use in pricing the asset or liability.

The Company’s policy regarding transfers between levels of the fair value hierarchy is that all transfers are assumed to occur at the end of the reporting period.

Valuation Processes

The Company has various processes and controls in place to ensure that fair value measurements are reasonably estimated. The Finance Committee of the Board provides oversight and approves the Company’s Asset/Liability Management Policy (“ALMP”). The Company’s ALMP governs, among other things, the application and control of the valuation models used to measure fair value. On a quarterly basis, the Company’s Asset/Liability Management Committee (“ALCO”) and the Finance Committee of the Board review significant modeling variables used to measure the fair value of the Company’s financial instruments, including the significant inputs used in the valuation

**HOMESTREET, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 19 — FAIR VALUE MEASUREMENT:** (cont.)

of single family MSRs. Additionally, ALCO periodically obtains an independent review of the MSR valuation process and procedures, including a review of the model architecture and the valuation assumptions. The Company obtains an MSR valuation from an independent valuation firm monthly to assist with the validation of the fair value estimate and the reasonableness of the assumptions used in measuring fair value.

The Company's real estate valuations are overseen by the Company's appraisal department, which is independent of the Company's lending and credit administration functions. The appraisal department maintains the Company's appraisal policy and recommends changes to the policy subject to approval by the Company's Loan Committee and the Credit Committee of the Board. The Company's appraisals are prepared by independent third-party appraisers and the Company's internal appraisers. Single family appraisals are generally reviewed by the Company's single family loan underwriters. Single family appraisals with unusual, higher risk or complex characteristics, as well as commercial real estate appraisals, are reviewed by the Company's appraisal department.

We obtain pricing from third party service providers for determining the fair value of a substantial portion of our investment securities available for sale. We have processes in place to evaluate such third party pricing services to ensure information obtained and valuation techniques used are appropriate. For fair value measurements obtained from third party services, we monitor and review the results to ensure the values are reasonable and in line with market experience for similar classes of securities. While the inputs used by the pricing vendor in determining fair value are not provided, and therefore unavailable for our review, we do perform certain procedures to validate the values received, including comparisons to other sources of valuation (if available), comparisons to other independent market data and a variance analysis of prices by Company personnel that are not responsible for the performance of the investment securities.

Estimation of Fair Value

Fair value is based on quoted market prices, when available. In cases where a quoted price for an asset or liability is not available, the Company uses valuation models to estimate fair value. These models incorporate inputs such as forward yield curves, loan prepayment assumptions, expected loss assumptions, market volatilities, and pricing spreads utilizing market-based inputs where readily available. The Company believes its valuation methods are appropriate and consistent with those that would be used by other market participants. However, imprecision in estimating unobservable inputs and other factors may result in these fair value measurements not reflecting the amount realized in an actual sale or transfer of the asset or liability in a current market exchange.

The following table summarizes the fair value measurement methodologies, including significant inputs and assumptions, and classification of the Company's assets and liabilities valued at fair value on a recurring basis.

| <u>Asset/Liability class</u>             | <u>Valuation methodology, inputs and assumptions</u>   | <u>Classification</u>  |
|--|--|--|
| Investment securities                    |  |  |
| Investment securities available for sale | Observable market prices of identical or similar securities are used where available.<br><br>If market prices are not readily available, value is based on discounted cash flows using the following significant inputs: <ul style="list-style-type: none"> <li>• Expected prepayment speeds</li> <li>• Estimated credit losses</li> <li>• Market liquidity adjustments</li> </ul> | Level 2 recurring fair value measurement.<br><br>Level 3 recurring fair value measurement. |



**HOMESTREET, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 19 — FAIR VALUE MEASUREMENT: (cont.)**

| <u>Asset/Liability class</u>  | <u>Valuation methodology, inputs and assumptions</u>   | <u>Classification</u>   |
|---|--|---|
| Loans held for sale   |  |   |
| Single family loans, excluding loans transferred from held for investment | <p>Fair value is based on observable market data, including:</p> <ul style="list-style-type: none"> <li>• Quoted market prices, where available</li> <li>• Dealer quotes for similar loans</li> <li>• Forward sale commitments</li> </ul> <p>When not derived from observable market inputs, fair value is based on discounted cash flows, which considers the following inputs:</p> <ul style="list-style-type: none"> <li>• Benchmark yield curve</li> <li>• Estimated discount spread to the benchmark yield curve</li> <li>• Expected prepayment speeds</li> </ul> | <p>Level 2 recurring fair value measurement.</p> <p>Estimated fair value classified as Level 3.</p> |
| Mortgage servicing rights   |  |   |
| Single family MSR   | For information on how the Company measures the fair value of its single family MSRs, including key economic assumptions and the sensitivity of fair value to changes in those assumptions, see Note 13, <i>Mortgage Banking Operations</i> .  | Level 3 recurring fair value measurement.   |
| Derivatives   |  |   |
| Eurodollar futures  | Fair value is based on closing exchange prices.  | Level 1 recurring fair value measurement.   |
| Interest rate swaps Interest rate swaptions Forward sale commitments      | <p>Fair value is based on quoted prices for identical or similar instruments when available. When quoted prices are not available, fair value is based on internally developed modeling techniques, which require the use of multiple observable market inputs, including:</p> <ul style="list-style-type: none"> <li>• Forward interest rates</li> <li>• Interest rate volatilities</li> </ul>  | Level 2 recurring fair value measurement.   |
| Interest rate lock and purchase loan commitments                          | <p>The fair value considers several factors including:</p> <ul style="list-style-type: none"> <li>• Fair value of the underlying loan based on quoted prices in the secondary market, when available.</li> <li>• Value of servicing</li> <li>• Fall-out factor</li> </ul>  | Level 3 recurring fair value measurement.   |

**HOMESTREET, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 19 — FAIR VALUE MEASUREMENT:** (cont.)

The following tables present the levels of the fair value hierarchy for the Company's assets and liabilities measured at fair value on a recurring basis.

| <u>(in thousands)</u>                                      | <u>Fair Value at<br/>December 31,<br/>2019</u> | <u>Level 1</u> | <u>Level 2</u>      | <u>Level 3</u>   |
|--|--|----------------|---------------------|------------------|
| <b>Assets:</b>   |  |                |                     |                  |
| Investment securities available for sale                   |  |                |                     |                  |
| Mortgage backed securities:                                |  |                |                     |                  |
| Residential. . . . .                                       | \$ 91,695                                      | \$ —           | \$ 89,831           | \$ 1,864         |
| Commercial. . . . .  | 38,025   | —              | 38,025              | —                |
| Collateralized mortgage obligations:                       |  |                |                     |                  |
| Residential. . . . .                                       | 291,618  | —              | 291,618             | —                |
| Commercial. . . . .  | 156,154  | —              | 156,154             | —                |
| Municipal bonds . . . . .                                  | 341,318  | —              | 341,318             | —                |
| Corporate debt securities . . . . .                        | 18,661   | —              | 18,573              | 88               |
| U.S. Treasury securities. . . . .                          | 1,307  | —              | 1,307               | —                |
| Single family loans held for sale <sup>(1)</sup> . . . . . | 105,458  | —              | 105,458             | —                |
| Single family loans held for investment . . . . .          | 3,468  | —              | —                   | 3,468            |
| Single family mortgage servicing rights. . . . .           | 68,109   | —              | —                   | 68,109           |
| Derivatives <sup>(1)</sup>                                 |  |                |                     |                  |
| Eurodollar futures . . . . .                               | 3  | 3              | —                   | —                |
| Forward sale commitments . . . . .                         | 830  | —              | 830                 | —                |
| Interest rate lock and purchase loan                       |  |                |                     |                  |
| commitments. . . . .                                       | 2,281  | —              | —                   | 2,281            |
| Interest rate swaps. . . . .                               | 27,097   | —              | 27,097              | —                |
| Total assets . . . . .                                     | <u>\$ 1,146,024</u>                            | <u>\$ 3</u>    | <u>\$ 1,070,211</u> | <u>\$ 75,810</u> |
| <b>Liabilities:</b>  |  |                |                     |                  |
| Derivatives <sup>(1)</sup>                                 |  |                |                     |                  |
| Forward sale commitments . . . . .                         | 492  | —              | 492                 | —                |
| Interest rate lock and purchase loan                       |  |                |                     |                  |
| commitments. . . . .                                       | 58   | —              | —                   | 58               |
| Interest rate swaps. . . . .                               | 10,889   | —              | 10,889              | —                |
| Total liabilities. . . . .                                 | <u>\$ 11,439</u>                               | <u>\$ —</u>    | <u>\$ 11,381</u>    | <u>\$ 58</u>     |

(1) Includes both continuing and discontinued operations.

**HOMESTREET, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 19 — FAIR VALUE MEASUREMENT:** (cont.)

| <u>(in thousands)</u>  | <u>Fair Value at<br/>December 31,<br/>2018</u> | <u>Level 1</u> | <u>Level 2</u>      | <u>Level 3</u>    |
|--|--|----------------|---------------------|-------------------|
| Assets:  |  |                |                     |                   |
| Investment securities available for sale                     |  |                |                     |                   |
| Mortgage backed securities:                                  |  |                |                     |                   |
| Residential. . . . .   | \$ 107,961                                     | \$ —           | \$ 107,961          | \$ —              |
| Commercial. . . . .  | 34,514   | —              | 34,514              | —                 |
| Collateralized mortgage obligations:                         |  |                |                     |                   |
| Residential. . . . .   | 166,744  | —              | 166,744             | —                 |
| Commercial. . . . .  | 116,674  | —              | 116,674             | —                 |
| Municipal bonds . . . . .                                    | 385,655  | —              | 385,655             | —                 |
| Corporate debt securities . . . . .                          | 19,995   | —              | 19,995              | —                 |
| U.S. Treasury securities. . . . .                            | 10,900   | —              | 10,900              | —                 |
| Agency debentures . . . . .                                  | 9,525  | —              | 9,525               | —                 |
| Single family loans held for sale <sup>(1)</sup> . . . . .   | 321,868  | —              | 319,177             | 2,691             |
| Single family loans held for investment . . . . .            | 4,057  | —              | —                   | 4,057             |
| Single family mortgage servicing rights. . . . .             | 252,168  | —              | —                   | 252,168           |
| Derivatives <sup>(1)</sup>                                   |  |                |                     |                   |
| Forward sale commitments . . . . .                           | 3,025  | —              | 3,025               | —                 |
| Interest rate swaptions. . . . .                             | 203  | —              | 203                 | —                 |
| Interest rate lock and purchase loan<br>commitments. . . . . | 10,289   | —              | —                   | 10,289            |
| Interest rate swaps. . . . .                                 | 14,566   | —              | 14,566              | —                 |
| Total assets . . . . .                                       | <u>\$ 1,458,144</u>                            | <u>\$ —</u>    | <u>\$ 1,188,939</u> | <u>\$ 269,205</u> |
| Liabilities:   |  |                |                     |                   |
| Derivatives <sup>(1)</sup>                                   |  |                |                     |                   |
| Eurodollar futures . . . . .                                 | \$ 110   | \$ 110         | \$ —                | \$ —              |
| Forward sale commitments . . . . .                           | 5,340  | —              | 5,340               | —                 |
| Interest rate lock and purchase loan<br>commitments. . . . . | 5  | —              | —                   | 5                 |
| Interest rate swaps. . . . .                                 | 11,550   | —              | 11,550              | —                 |
| Total liabilities. . . . .                                   | <u>\$ 17,005</u>                               | <u>\$ 110</u>  | <u>\$ 16,890</u>    | <u>\$ 5</u>       |

(1) Includes both continuing and discontinued operations.

There were no transfers between levels of the fair value hierarchy during the years ended December 31, 2019 and 2018.

Level 3 Recurring Fair Value Measurements

The Company's level 3 recurring fair value measurements consist of investment securities available for sale, single family mortgage servicing rights, single family loans held for investment where fair value option was elected, certain single family loans held for sale, and interest rate lock and purchase loan commitments, which are accounted for as derivatives. For information regarding fair value changes and activity for single family MSRs during the years ended December 31, 2019 and 2018, see Note 13, *Mortgage Banking Operations*.

**HOMESTREET, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 19 — FAIR VALUE MEASUREMENT:** (cont.)

The fair value of IRLCs considers several factors including the fair value in the secondary market of the underlying loan resulting from the exercise of the commitment, the expected net future cash flows related to the associated servicing of the loan (referred to as the value of servicing) and the probability that the commitment will not be converted into a funded loan (referred to as a fall-out factor). The fair value of IRLCs on loans held for sale, while based on interest rates observable in the market, is highly dependent on the ultimate closing of the loans. The significance of the fall-out factor to the fair value measurement of an individual IRLC is generally highest at the time that the rate lock is initiated and declines as closing procedures are performed and the underlying loan gets closer to funding. The fall-out factor applied is based on historical experience. The value of servicing is impacted by a variety of factors, including prepayment assumptions, discount rates, delinquency rates, contractually specified servicing fees, servicing costs, and underlying portfolio characteristics. Because these inputs are not observable in market trades, the fall-out factor and value of servicing are considered to be level 3 inputs. The fair value of IRLCs decreases in value upon an increase in the fall-out factor and increases in value upon an increase in the value of servicing. Changes in the fall-out factor and value of servicing do not increase or decrease based on movements in other significant unobservable inputs.

The Company recognizes unrealized gains and losses from the time that an IRLC is initiated until the gain or loss is realized at the time the loan closes, which generally occurs within 30-90 days. For IRLCs that fall out, any unrealized gain or loss is reversed, which generally occurs at the end of the commitment period. The gains and losses recognized on IRLC derivatives generally correlates to volume of single family interest rate lock commitments made during the reporting period (after adjusting for estimated fallout) while the amount of unrealized gains and losses realized at settlement generally correlates to the volume of single family closed loans during the reporting period.

The Company uses the discounted cash flow model to estimate the fair value of certain loans that have been transferred from held for sale to held for investment and single family loans held for sale when the fair value of the loans is not derived using observable market inputs. The key assumption in the valuation model is the implied spread to benchmark interest rate curve. The implied spread is not directly observable in the market and is derived from third party pricing which is based on market information from comparable loan pools. The fair value estimate of these certain single family loans that have been transferred from held for sale to held for investment and these certain single family loans held for sale is sensitive to changes in the benchmark interest rate which might result in a significantly higher or lower fair value measurement.

The Company transferred certain loans from held for sale to held for investment. These loans were originated as held for sale loans where the Company had elected fair value option. The Company determined these loans to be level 3 recurring assets as the valuation technique included a significant unobservable input. The total amount of held for investment loans where fair value option election was made was \$3.5 million and \$4.1 million at December 31, 2019 and December 31, 2018, respectively.

The following information presents significant Level 3 unobservable inputs used to measure fair value of certain investment securities available for sale.

| (dollars in thousands)   | Fair Value | Valuation<br>Technique | At December 31, 2019                                  |       |       | Weighted<br>Average |
|--|------------|------------------------|---|-------|-------|---------------------|
|  |            |                        | Significant<br>Unobservable Input                     | Low   | High  |                     |
| Investment securities<br>available for sale <sup>(1)</sup> . . . | \$ 1,952   | Income approach        | Implied spread to<br>benchmark interest<br>rate curve | 2.00% | 2.00% | 2.00%               |

(1) In conjunction with adopting ASU 2017-12 in the first quarter of 2019, we transferred \$66.2 million HTM securities to AFS, therefore we did not have a similar balance at December 31, 2018.

**HOMESTREET, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 19 — FAIR VALUE MEASUREMENT:** (cont.)

The following information presents significant Level 3 unobservable inputs used to measure fair value of single family loans held for investment where fair value option was elected.

| (dollars in thousands)                                 | At December 31, 2019 |                     |   |       |       |                  |
|--|----------------------|---------------------|---|-------|-------|------------------|
|  | Fair Value           | Valuation Technique | Significant Unobservable Input                  | Low   | High  | Weighted Average |
| Loans held for investment, fair value option . . . . . | \$ 3,468             | Income approach     | Implied spread to benchmark interest rate curve | 4.56% | 6.87% | 5.63%            |

| (dollars in thousands)                                 | At December 31, 2018 |                     |   |       |       |                  |
|--|----------------------|---------------------|---|-------|-------|------------------|
|  | Fair Value           | Valuation Technique | Significant Unobservable Input                  | Low   | High  | Weighted Average |
| Loans held for investment, fair value option . . . . . | \$ 4,057             | Income approach     | Implied spread to benchmark interest rate curve | 3.34% | 5.15% | 4.20%            |

The following information presents significant Level 3 unobservable inputs used to measure fair value of certain single family loans held for sale where fair value option was elected. We had no loans held for sale with fair value option at December 31, 2019.

| (dollars in thousands)                       | At December 31, 2018 |                     |   |       |       |                  |
|--|----------------------|---------------------|---|-------|-------|------------------|
|  | Fair Value           | Valuation Technique | Significant Unobservable Input                  | Low   | High  | Weighted Average |
| Loans held for sale, fair value option . . . | \$ 2,691             | Income approach     | Implied spread to benchmark interest rate curve | 4.26% | 4.96% | 4.40%            |
|  |                      |                     | Market price movement from comparable bond      | 0.71% | 1.09% | 0.90%            |

The following information presents significant Level 3 unobservable inputs used to measure fair value of interest rate lock and purchase loan commitments.

| (dollars in thousands)   | At December 31, 2019 |                     |                                |       |        |                  |
|--|----------------------|---------------------|--------------------------------|-------|--------|------------------|
|  | Fair Value           | Valuation Technique | Significant Unobservable Input | Low   | High   | Weighted Average |
| Interest rate lock and purchase loan commitments, net <sup>(1)</sup> . . | \$ 2,223             | Income approach     | Fall out factor                | —%    | 59.69% | 12.20%           |
|  |                      |                     | Value of servicing             | 0.55% | 1.77%  | 1.14%            |

(1) Includes both continuing and discontinued operations.

| (dollars in thousands)   | At December 31, 2018 |                     |                                |       |        |                  |
|--|----------------------|---------------------|--------------------------------|-------|--------|------------------|
|  | Fair Value           | Valuation Technique | Significant Unobservable Input | Low   | High   | Weighted Average |
| Interest rate lock and purchase loan commitments, net <sup>(1)</sup> . . | \$ 10,284            | Income approach     | Fall out factor                | —%    | 67.92% | 19.84%           |
|  |                      |                     | Value of servicing             | 0.54% | 1.64%  | 0.93%            |

(1) Includes both continuing and discontinued operations.

**HOMESTREET, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 19 — FAIR VALUE MEASUREMENT:** (cont.)

The following table presents fair value changes and activity for Level 3 investment securities available for sale.

| <u>(in thousands)</u>  | Year Ended December 31, 2019 |           |           |               |                             |                   |
|--|------------------------------|-----------|-----------|---------------|-----------------------------|-------------------|
|  | Beginning<br>balance         | Additions | Transfers | Payoffs/Sales | Change in<br>mark to market | Ending<br>balance |
| Investment securities<br>available for sale <sup>(1)</sup> . . . | —                            | \$ —      | \$ 2,379  | \$ (160)      | \$ (267)                    | \$ 1,952          |

(1) In conjunction with adopting ASU 2017-12 in the first quarter of 2019, we transferred \$66.2 million of HTM securities to AFS, therefore we did not have any similar activity for the year ended December 31, 2018.

The following table presents fair value changes and activity for Level 3 loans held for sale and loans held for investment.

| <u>(in thousands)</u>                  | Year Ended December 31, 2019 |           |           |               |                             |                   |
|--|------------------------------|-----------|-----------|---------------|-----------------------------|-------------------|
|  | Beginning<br>balance         | Additions | Transfers | Payoffs/Sales | Change in<br>mark to market | Ending<br>balance |
| Loans held for sale . . . . .          | \$ 2,691                     | \$ 5,859  | \$ 1,630  | \$ (10,060)   | \$ (120)                    | \$ —              |
| Loans held for<br>investment . . . . . | 4,057                        | 2,043     | (1,630)   | (980)         | (22)                        | 3,468             |

| <u>(in thousands)</u>                  | Year Ended December 31, 2018 |           |           |               |                             |                   |
|--|------------------------------|-----------|-----------|---------------|-----------------------------|-------------------|
|  | Beginning<br>balance         | Additions | Transfers | Payoffs/Sales | Change in<br>mark to market | Ending<br>balance |
| Loans held for sale . . .              | \$ 1,336                     | \$ 3,434  | \$ —      | \$ (1,998)    | \$ (81)                     | \$ 2,691          |
| Loans held for<br>investment . . . . . | 5,477                        | 487       | —         | (1,672)       | (235)                       | 4,057             |

The following table presents fair value changes and activity for Level 3 interest rate lock and purchase loan commitments.

| <u>(in thousands)</u>                     | Years Ended December 31, |           |
|---|--------------------------|-----------|
|   | 2019                     | 2018      |
| Beginning balance, net . . . . .          | \$ 10,284                | \$ 12,925 |
| Total realized/unrealized gains . . . . . | 36,487                   | 91,251    |
| Settlements . . . . .                     | (44,548)                 | (93,892)  |
| Ending balance, net . . . . .             | \$ 2,223                 | \$ 10,284 |

Nonrecurring Fair Value Measurements

Certain assets held by the Company are not included in the tables above, but are measured at fair value on a nonrecurring basis. These assets include certain loans held for investment and other real estate owned that are carried at the lower of cost or fair value of the underlying collateral, less the estimated cost to sell. The estimated fair values of real estate collateral are generally based on internal evaluations and appraisals of such collateral, which use the market approach and income approach methodologies. All impaired loans are subject to an internal evaluation completed quarterly by management as part of the allowance process.



**HOMESTREET, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 19 — FAIR VALUE MEASUREMENT:** (cont.)

The fair value of commercial properties are generally based on third-party appraisals that consider recent sales of comparable properties, including their income-generating characteristics, adjusted (generally based on unobservable inputs) to reflect the general assumptions that a market participant would make when analyzing the property for purchase. The Company uses a fair value of collateral technique to apply adjustments to the appraisal value of certain commercial loans held for investment that are collateralized by real estate.

The Company uses a fair value of collateral technique to apply adjustments to the stated value of certain commercial loans held for investment that are not collateralized by real estate and to the appraisal value of OREO. During the years ended December 31, 2019 and 2018 the Company didn't apply any adjustments to the appraisal value of OREO.

Residential properties are generally based on unadjusted third-party appraisals. Factors considered in determining the fair value include geographic sales trends, the value of comparable surrounding properties as well as the condition of the property.

These adjustments include management assumptions that are based on the type of collateral dependent loan and may increase or decrease an appraised value. Management adjustments vary significantly depending on the location, physical characteristics and income producing potential of each individual property. The quality and volume of market information available at the time of the appraisal can vary from period-to-period and cause significant changes to the nature and magnitude of the unobservable inputs used. Given these variations, changes in these unobservable inputs are generally not a reliable indicator for how fair value will increase or decrease from period to period.

The following tables present assets that had changes in their recorded fair value during the years ended December 31, 2019 and 2018 and what we still held at the end of the respective reporting period.

| <b>Year Ended December 31, 2019</b>                |   |                |                |                 |                                 |
|--|---|----------------|----------------|-----------------|---------------------------------|
| <b>(in thousands)</b>                              | <b>Fair Value of<br/>Assets Held at<br/>December 31,<br/>2019</b> | <b>Level 1</b> | <b>Level 2</b> | <b>Level 3</b>  | <b>Total Gains<br/>(Losses)</b> |
| Loans held for investment <sup>(1)</sup> . . . . . | \$ 266  | \$ —           | \$ —           | \$ 266          | \$ 316                          |
| Total . . . . .                                    | <u>\$ 266</u>   | <u>\$ —</u>    | <u>\$ —</u>    | <u>\$ 266</u>   | <u>\$ 316</u>                   |
| <b>Year Ended December 31, 2018</b>                |   |                |                |                 |                                 |
| <b>(in thousands)</b>                              | <b>Fair Value of<br/>Assets Held at<br/>December 31,<br/>2018</b> | <b>Level 1</b> | <b>Level 2</b> | <b>Level 3</b>  | <b>Total Gains<br/>(Losses)</b> |
| Loans held for investment <sup>(1)</sup> . . . . . | \$ 1,607  | \$ —           | \$ —           | \$ 1,607        | \$ (257)                        |
| Total . . . . .                                    | <u>\$ 1,607</u>   | <u>\$ —</u>    | <u>\$ —</u>    | <u>\$ 1,607</u> | <u>\$ (257)</u>                 |

(1) Represents the carrying value of loans for which adjustments are based on the fair value of the collateral.

**HOMESTREET, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 19 — FAIR VALUE MEASUREMENT: (cont.)**

Fair Value of Financial Instruments

The following presents the carrying value, estimated fair value and the levels of the fair value hierarchy for the Company's financial instruments other than assets and liabilities measured at fair value on a recurring basis.

| <u>(in thousands)</u>  | <u>At December 31, 2019</u> |                   |                |                |                |
|--|-----------------------------|-------------------|----------------|----------------|----------------|
|  | <u>Carrying Value</u>       | <u>Fair Value</u> | <u>Level 1</u> | <u>Level 2</u> | <u>Level 3</u> |
| Assets:  |                             |                   |                |                |                |
| Cash and cash equivalents. . . . .   | \$ 57,880                   | \$ 57,880         | \$ 57,880      | \$ —           | \$ —           |
| Federal funds sold and securities purchased under agreements to resell . . .     |                             |                   |                |                |                |
| Investment securities held to maturity . . . .                                   | 4,372                       | 4,501             | —              | 4,501          | —              |
| Loans held for investment. . . . .   | 5,069,316                   | 5,139,078         | —              | —              | 5,139,078      |
| Loans held for sale – multifamily and other . . . . .                            | 128,841                     | 130,720           | —              | 130,720        | —              |
| Mortgage servicing rights – multifamily . .                                      | 29,494                      | 32,738            | —              | —              | 32,738         |
| Federal Home Loan Bank stock . . . . .   | 22,399                      | 22,399            | —              | 22,399         | —              |
| Liabilities:   |                             |                   |                |                |                |
| Time deposits . . . . .  | \$ 1,614,533                | \$ 1,622,879      | \$ —           | \$1,622,879    | \$ —           |
| Federal Home Loan Bank advances . . . . .  | 346,590                     | 347,949           | —              | 347,949        | —              |
| Federal funds purchased and securities sold under agreements to repurchase . . . | 125,000                     | 125,101           | 125,101        | —              | —              |
| Long-term debt . . . . .   | 125,650                     | 115,011           | —              | 115,011        | —              |

| <u>(in thousands)</u>  | <u>At December 31, 2018</u> |                   |                |                |                |
|--|-----------------------------|-------------------|----------------|----------------|----------------|
|  | <u>Carrying Value</u>       | <u>Fair Value</u> | <u>Level 1</u> | <u>Level 2</u> | <u>Level 3</u> |
| Assets:  |                             |                   |                |                |                |
| Cash and cash equivalents. . . . .   | \$ 57,982                   | \$ 57,982         | \$ 57,982      | \$ —           | \$ —           |
| Investment securities held to maturity . . . .                                   | 71,285                      | 70,546            | —              | 70,546         | —              |
| Loans held for investment. . . . .   | 5,071,314                   | 5,099,960         | —              | —              | 5,099,960      |
| Loans held for sale – multifamily and other . . . . .                            | 25,139                      | 25,139            | —              | 25,139         | —              |
| Mortgage servicing rights – multifamily . .                                      | 28,328                      | 31,168            | —              | —              | 31,168         |
| Federal Home Loan Bank stock . . . . .   | 45,497                      | 45,497            | —              | 45,497         | —              |
| Liabilities:   |                             |                   |                |                |                |
| Time deposits . . . . .  | \$ 1,579,806                | \$ 1,575,139      | \$ —           | \$1,575,139    | \$ —           |
| Federal Home Loan Bank advances . . . . .  | 932,590                     | 935,021           | —              | 935,021        | —              |
| Federal funds purchased and securities sold under agreements to repurchase . . . | 19,000                      | 19,021            | 19,021         | —              | —              |
| Long-term debt . . . . .   | 125,462                     | 112,475           | —              | 112,475        | —              |

**HOMESTREET, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 20 — EARNINGS PER SHARE:**

The following table summarizes the calculation of earnings per share.

| <b>(in thousands, except share and per share data)</b>                           | <b>Years Ended December 31,</b> |                   |                   |
|--|---------------------------------|-------------------|-------------------|
|  | <b>2019</b>                     | <b>2018</b>       | <b>2017</b>       |
| EPS numerator:   |                                 |                   |                   |
| Income from continuing operations . . . . .                                      | \$ 40,720                       | \$ 26,223         | \$ 42,668         |
| Undistributed stock dividends share repurchase . . . . .                         | (505)                           | —                 | —                 |
| Allocated undistributed earnings in share repurchase . . . . .                   | (145)                           | —                 | —                 |
| Income from continuing operations available to common shareholders. . . . .      | 40,070                          | 26,223            | 42,668            |
| (Loss) income from discontinued operations . . . . .                             | (23,208)                        | 13,804            | 26,278            |
| Net income available to common shareholders. . . . .                             | <u>\$ 16,862</u>                | <u>\$ 40,027</u>  | <u>\$ 68,946</u>  |
| EPS denominator:   |                                 |                   |                   |
| Weighted average shares:   |                                 |                   |                   |
| Basic weighted-average number of common shares outstanding . . . . .             | 25,573,488                      | 26,970,916        | 26,864,657        |
| Dilutive effect of outstanding common stock equivalents <sup>(1)</sup> . . . . . | 197,295                         | 197,219           | 227,362           |
| Diluted weighted-average number of common stock outstanding . . . . .            | <u>25,770,783</u>               | <u>27,168,135</u> | <u>27,092,019</u> |
| Basic earnings per share:  |                                 |                   |                   |
| Income from continuing operations . . . . .                                      | \$ 1.57                         | \$ 0.97           | \$ 1.59           |
| (Loss) income from discontinued operations . . . . .                             | (0.91)                          | 0.51              | 0.98              |
| Basic earnings per share . . . . .   | <u>\$ 0.66</u>                  | <u>\$ 1.48</u>    | <u>\$ 2.57</u>    |
| Diluted earnings per share:  |                                 |                   |                   |
| Income from continuing operations . . . . .                                      | \$ 1.55                         | \$ 0.97           | \$ 1.57           |
| (Loss) income from discontinued operations . . . . .                             | (0.90)                          | 0.51              | 0.97              |
| Diluted earnings per share . . . . .   | <u>\$ 0.65</u>                  | <u>\$ 1.47</u>    | <u>\$ 2.54</u>    |

(1) Excluded from the computation of diluted earnings per share (due to their antidilutive effect) for the years ended December 31, 2019, 2018 and 2017 were certain stock options and unvested restricted stock issued to key senior management personnel and directors of the Company. The aggregate number of common stock equivalents related to such options and unvested restricted shares, which could potentially be dilutive in future periods, was 263, zero and 3,224 at December 31, 2019, 2018 and 2017, respectively.

**NOTE 21 — LEASES:**

On January 1, 2019, we adopted new FASB guidance on the accounting for leases. We applied the modified retrospective method of adoption and therefore, results for reporting periods beginning after January 1, 2019 are presented under the new guidance while prior periods have not been adjusted.

We have operating and finance leases for corporate offices, commercial lending centers, retail deposit branches and certain equipment. Our leases have remaining lease terms of up to 21 years some of which include options which are reasonably certain to be exercised. Leases with an initial term of less than a year are not included in the Statement of Financial Condition.

The Company, as sublessor, subleases certain office and retail space in which the terms of the subleases end by December 2027. Under all of our executed sublease arrangements, the sublessees are obligated to pay the Company sublease payments of \$6.3 million in 2020, \$5.1 million in 2021, \$3.9 million in 2022, \$2.4 million in 2023, \$901 thousand in 2024 and \$989 thousand thereafter.

In the year ended December 31, 2019, we incurred \$5.0 million in impairment charges on lease right-of-use assets.

**HOMESTREET, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 21 — LEASES:** (cont.)

The components of lease expense were as follows.

| <b>(in thousands)</b>                     | <b>Year Ended<br/>December 31,<br/>2019</b> |
|---|---|
| Operating lease cost .....                | \$ 14,538                                   |
| Short-term leases .....                   | 28  |
| Finance lease cost:                       |   |
| Amortization of right-of-use assets ..... | 2,030                                       |
| Interest on lease liabilities .....       | 340   |
| Variable lease costs .....                | 6,627                                       |
| Sublease income .....                     | (4,378)                                     |
| Total lease costs .....                   | \$ 19,185                                   |

Supplemental cash flow information related to leases was as follows.

| <b>(in thousands)</b>   | <b>Year Ended<br/>December 31,<br/>2019</b> |
|---|---|
| Cash paid for amounts included in the measurement of lease liabilities: |   |
| Operating cash flows from operating leases .....                        | \$ 17,054                                   |
| Operating cash flows from finance leases .....                          | 340   |
| Financing cash flows from finance leases .....                          | 1,694                                       |

Supplemental balance sheet information related to leases was as follows.

| <b>(in thousands, except lease term and discount rate)</b> | <b>December 31,<br/>2019</b> |
|--|------------------------------|
| Operating lease right-of-use assets .....                  | \$ 86,789                    |
| Operating lease liabilities .....                          | 104,579                      |
| Finance lease right-of-use assets .....                    | \$ 8,084                     |
| Finance lease liabilities .....                            | 8,513                        |
| Weighted Average Remaining lease term in years             |                              |
| Operating leases .....                                     | 11.87                        |
| Finance leases .....                                       | 15.46                        |
| Weighted Average Discount Rate                             |                              |
| Operating leases .....                                     | 3.48%                        |
| Finance leases .....                                       | 2.63%                        |

Maturities of lease liabilities were as follows.

|                             | <b>Operating<br/>Leases</b> | <b>Finance<br/>Leases</b> |
|-----------------------------|-----------------------------|---------------------------|
| Year ended December 31,     |                             |                           |
| 2020 .....                  | \$ 15,149                   | \$ 1,519                  |
| 2021 .....                  | 13,912                      | 1,297                     |
| 2022 .....                  | 12,399                      | 590                       |
| 2023 .....                  | 10,637                      | 473                       |
| 2024 .....                  | 10,205                      | 400                       |
| 2025 and thereafter .....   | 65,616                      | 7,238                     |
| Total lease payments .....  | 127,918                     | 11,517                    |
| Less imputed interest ..... | 23,339                      | 3,004                     |
| Total .....                 | \$ 104,579                  | \$ 8,513                  |

**HOMESTREET, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 21 — LEASES:** (cont.)

Leases (Topic 840) Disclosures

*Operating Leases*

Prior to 2019, under the previous lease standard, we had non-cancelable operating leases for office space. Generally, the office leases contain five-year renewal and space options. As of December 31, 2018, these leases had contractual terms expiring through 2035. Total rent expense under non-cancellable operating leases totaled \$27.7 million for the year ended December 31, 2018.

Minimum rental payments for all non-cancelable leases were as follows.

| <b>(in thousands)</b>        | <b>At<br/>December 31,<br/>2018</b> |
|------------------------------|-------------------------------------|
| 2019 .....                   | \$ 22,770                           |
| 2020 .....                   | 20,671                              |
| 2021 .....                   | 18,825                              |
| 2022 .....                   | 16,418                              |
| 2023 .....                   | 13,274                              |
| 2024 and thereafter .....    | 40,717                              |
| Total minimum payments ..... | <u>\$ 132,675</u>                   |

**NOTE 22 — ACCUMULATED OTHER COMPREHENSIVE INCOME (LOSS):**

The following table shows changes in accumulated other comprehensive income (loss) from unrealized gain (loss) on available-for-sale securities, net of tax.

| <b>(in thousands)</b>  | <b>Years Ended December 31,</b> |                    |                   |
|--|---------------------------------|--------------------|-------------------|
|  | <b>2019</b>                     | <b>2018</b>        | <b>2017</b>       |
| Beginning balance .....  | \$ (15,439)                     | \$ (7,122)         | \$ (10,412)       |
| Cumulative effect of adoption of new accounting standards <sup>(1)</sup> ..... | (2,080)                         | —                  | —                 |
| Other comprehensive income (loss) before reclassifications .....               | 21,834                          | (8,132)            | 3,607             |
| Amounts reclassified from accumulated other comprehensive income (loss) .....  | 6                               | (185)              | (317)             |
| Net current-period other comprehensive income (loss) .....                     | <u>21,840</u>                   | <u>(8,317)</u>     | <u>3,290</u>      |
| Ending balance .....   | <u>\$ 4,321</u>                 | <u>\$ (15,439)</u> | <u>\$ (7,122)</u> |

(1) Reflects the January 1, 2019 adoption of ASU 2018-02 and ASU 2017-12. For additional information see Note 1, *Summary of Significant Accounting Policies*.

The following table shows the affected line items in the consolidated statements of operations from reclassifications of unrealized gain (loss) on available-for-sale securities from accumulated other comprehensive income (loss).

| <b>Affected Line Item in the Consolidated Statements of Operations</b> | <b>Amount Reclassified from Accumulated<br/>Other Comprehensive Income (Loss)</b> |               |               |
|--|---|---------------|---------------|
|  | <b>Years Ended December 31,</b>   |               |               |
|  | <b>2019</b>   | <b>2018</b>   | <b>2017</b>   |
| <b>(in thousands)</b>  |   |               |               |
| (Loss) gain on sale of investment securities available for sale .....  | \$ (8)  | \$ 234        | \$ 489        |
| Income tax (benefit) expense .....                                     | (2)   | 49            | 172           |
| Total, net of tax .....  | <u>\$ (6)</u>   | <u>\$ 185</u> | <u>\$ 317</u> |

**HOMESTREET, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 23 — PARENT COMPANY FINANCIAL STATEMENTS:**

Condensed financial information for HomeStreet, Inc. is as follows.

| <b>Condensed Statements of Financial Condition</b><br><b>(in thousands)</b> | <b>At December 31,</b> |                   |
|---|------------------------|-------------------|
|   | <b>2019</b>            | <b>2018</b>       |
| <b>Assets:</b>  |                        |                   |
| Cash and cash equivalents . . . . .   | \$ 16,638              | \$ 12,399         |
| Other assets . . . . .  | 4,370                  | 5,375             |
| Investment in stock of subsidiaries . . . . .                               | 785,821                | 848,333           |
| <b>Total assets . . . . .</b>   | <b>\$ 806,829</b>      | <b>\$ 866,107</b> |
| <b>Liabilities:</b>   |                        |                   |
| Other liabilities . . . . .   | \$ 1,456               | \$ 1,125          |
| Long-term debt . . . . .  | 125,650                | 125,462           |
| <b>Total liabilities . . . . .</b>  | <b>127,106</b>         | <b>126,587</b>    |
| <b>Shareholders' Equity:</b>  |                        |                   |
| Preferred stock, no par value . . . . .                                     | —                      | —                 |
| Common stock, no par value . . . . .  | 511                    | 511               |
| Additional paid-in capital . . . . .  | 300,218                | 342,439           |
| Retained earnings . . . . .   | 374,673                | 412,009           |
| Accumulated other comprehensive income (loss) . . . . .                     | 4,321                  | (15,439)          |
| <b>Total stockholder's equity . . . . .</b>                                 | <b>679,723</b>         | <b>739,520</b>    |
| <b>Total liabilities and stockholder's equity . . . . .</b>                 | <b>\$ 806,829</b>      | <b>\$ 866,107</b> |

| <b>Condensed Statements of Operations</b><br><b>(in thousands)</b>                     | <b>Years Ended December 31,</b> |                  |                  |
|--|---------------------------------|------------------|------------------|
|  | <b>2019</b>                     | <b>2018</b>      | <b>2017</b>      |
| Net interest expense . . . . .   | \$ (4,821)                      | \$ (4,856)       | \$ (4,625)       |
| Noninterest income . . . . .   | 2,293                           | 2,193            | 1,904            |
| (Loss) income before income tax benefit and equity in income of subsidiaries . . . . . | (2,528)                         | (2,663)          | (2,721)          |
| Dividend from subsidiaries to parent . . . . .   | 110,000                         | 9,523            | 4,000            |
|  | 107,472                         | 6,860            | 1,279            |
| Noninterest expense . . . . .  | (8,437)                         | (10,368)         | (6,681)          |
| Income (loss) before income tax benefit . . . . .                                      | 99,035                          | (3,508)          | (5,402)          |
| Income tax expense (benefit) . . . . .   | 2,623                           | (385)            | 3,381            |
| (Loss) income from subsidiaries . . . . .  | (84,146)                        | 43,920           | 70,967           |
| <b>Net income . . . . .</b>  | <b>\$ 17,512</b>                | <b>\$ 40,027</b> | <b>\$ 68,946</b> |
| Other comprehensive income (loss) . . . . .  | 21,840                          | (8,317)          | 3,290            |
| <b>Comprehensive income . . . . .</b>  | <b>\$ 39,352</b>                | <b>\$ 31,710</b> | <b>\$ 72,236</b> |



**HOMESTREET, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 23 — PARENT COMPANY FINANCIAL STATEMENTS: (cont.)**

| <b>Condensed Statements of Cash Flows</b><br><b>(in thousands)</b>    | <b>Years Ended December 31,</b> |                  |                  |
|---|---------------------------------|------------------|------------------|
|   | <b>2019</b>                     | <b>2018</b>      | <b>2017</b>      |
| Net cash provided by (used in) operating activities . . . . .         | \$ 101,628                      | \$ (3,198)       | \$ (3,395)       |
| Cash flows from investing activities:                                 |                                 |                  |                  |
| Net purchases of and proceeds from investment securities . . . . .    | 1,049                           | 1,541            | 2,546            |
| Net payments for investments in and advances to subsidiaries. . . . . | —                               | (113)            | 2,685            |
| Net cash provided by investing activities . . . . .                   | 1,049                           | 1,428            | 5,231            |
| Cash flows from financing activities:                                 |                                 |                  |                  |
| Proceeds from issuance of common stock . . . . .                      | 105                             | 68               | 11               |
| Payment to repurchase common stock . . . . .                          | (98,543)                        |                  |                  |
| Other, net. . . . .   | —                               | —                | (6)              |
| Net cash (used in) provided by financing activities . . . . .         | (98,438)                        | 68               | 5                |
| Increase (decrease) in cash and cash equivalents . . . . .            | 4,239                           | (1,702)          | 1,841            |
| Cash and cash equivalents at beginning of year . . . . .              | 12,399                          | 14,101           | 12,260           |
| Cash and cash equivalents at end of year . . . . .                    | <u>\$ 16,638</u>                | <u>\$ 12,399</u> | <u>\$ 14,101</u> |

**NOTE 24 — UNAUDITED QUARTERLY FINANCIAL DATA:**

Our supplemental quarterly consolidated financial information is as follows.

| <b>(in thousands, except share data)</b>  | <b>Quarter Ended</b>     |                           |                          |                          |                          |                           |                          |                          |
|---|--------------------------|---------------------------|--------------------------|--------------------------|--------------------------|---------------------------|--------------------------|--------------------------|
|   | <b>Dec. 31,<br/>2019</b> | <b>Sept. 30,<br/>2019</b> | <b>June 30,<br/>2019</b> | <b>Mar. 31,<br/>2019</b> | <b>Dec. 31,<br/>2018</b> | <b>Sept. 30,<br/>2018</b> | <b>June 30,<br/>2018</b> | <b>Mar. 31,<br/>2018</b> |
| Interest income . . . . .   | \$ 66,767                | \$ 70,077                 | \$ 72,079                | \$ 68,683                | \$ 68,253                | \$ 64,280                 | \$ 61,818                | \$ 57,111                |
| Interest expense . . . . .  | 21,255                   | 22,943                    | 22,892                   | 21,126                   | 19,343                   | 16,420                    | 14,073                   | 11,663                   |
| Net interest income . . . . .   | 45,512                   | 47,134                    | 49,187                   | 47,557                   | 48,910                   | 47,860                    | 47,745                   | 45,448                   |
| (Reversal) provision for credit losses . . . . .  | (2,000)                  | —                         | —                        | 1,500                    | 500                      | 750                       | 1,000                    | 750                      |
| Net interest income after<br>provision for credit losses . . . . .                        | 47,512                   | 47,134                    | 49,187                   | 46,057                   | 48,410                   | 47,110                    | 46,745                   | 44,698                   |
| Noninterest income . . . . .  | 21,931                   | 24,580                    | 19,829                   | 8,092                    | 10,382                   | 10,650                    | 8,405                    | 7,096                    |
| Noninterest expense . . . . .   | 53,215                   | 55,721                    | 58,832                   | 47,846                   | 47,892                   | 47,914                    | 49,964                   | 49,471                   |
| Net income from continuing<br>operations before income tax<br>expense (benefit) . . . . . | 16,228                   | 15,993                    | 10,184                   | 6,303                    | 10,900                   | 9,846                     | 5,186                    | 2,323                    |
| Income tax expense (benefit) from<br>continuing operations . . . . .                      | 3,123                    | 2,328                     | 1,292                    | 1,245                    | (1,309)                  | 1,757                     | 1,015                    | 569                      |
| Income from continuing operations . . . . .   | \$ 13,105                | \$ 13,665                 | \$ 8,892                 | \$ 5,058                 | \$ 12,209                | \$ 8,089                  | \$ 4,171                 | \$ 1,754                 |
| (Loss) income from discontinued<br>operations before income taxes . . . . .               | \$ (3,357)               | \$ 190                    | \$ (16,678)              | \$ (8,440)               | \$ 3,959                 | \$ 4,561                  | \$ 3,641                 | \$ 5,449                 |
| Income tax (benefit) expense from<br>discontinued operations . . . . .                    | (1,240)                  | 28                        | (2,198)                  | (1,667)                  | 941                      | 815                       | 713                      | 1,337                    |
| (Loss) income from discontinued<br>operations . . . . .                                   | \$ (2,117)               | \$ 162                    | \$ (14,480)              | \$ (6,773)               | \$ 3,018                 | \$ 3,746                  | \$ 2,928                 | \$ 4,112                 |
| NET INCOME (LOSS). . . . .  | <u>\$ 10,988</u>         | <u>\$ 13,827</u>          | <u>\$ (5,588)</u>        | <u>\$ (1,715)</u>        | <u>\$ 15,227</u>         | <u>\$ 11,835</u>          | <u>\$ 7,099</u>          | <u>\$ 5,866</u>          |
| Basic earnings per common share:  |                          |                           |                          |                          |                          |                           |                          |                          |
| Income from continuing operations . . . . .   | 0.54                     | 0.55                      | 0.32                     | 0.19                     | 0.45                     | 0.30                      | 0.15                     | 0.07                     |
| (Loss) income from discontinued<br>operations . . . . .                                   | \$ (0.09)                | \$ 0.01                   | \$ (0.54)                | \$ (0.25)                | \$ 0.11                  | \$ 0.14                   | \$ 0.11                  | \$ 0.15                  |
| Basic earnings per share . . . . .  | <u>\$ 0.45</u>           | <u>\$ 0.55</u>            | <u>\$ (0.22)</u>         | <u>\$ (0.06)</u>         | <u>\$ 0.56</u>           | <u>\$ 0.44</u>            | <u>\$ 0.26</u>           | <u>\$ 0.22</u>           |
| Diluted earnings per common share:  |                          |                           |                          |                          |                          |                           |                          |                          |
| Income from continuing operations . . . . .   | \$ 0.54                  | \$ 0.54                   | \$ 0.32                  | \$ 0.19                  | \$ 0.45                  | \$ 0.30                   | \$ 0.15                  | \$ 0.06                  |
| (Loss) income from discontinued<br>operations . . . . .                                   | \$ (0.09)                | \$ 0.01                   | \$ (0.54)                | \$ (0.25)                | \$ 0.11                  | \$ 0.14                   | \$ 0.11                  | \$ 0.15                  |
| Diluted earnings per share . . . . .  | <u>\$ 0.45</u>           | <u>\$ 0.55</u>            | <u>\$ (0.22)</u>         | <u>\$ (0.06)</u>         | <u>\$ 0.56</u>           | <u>\$ 0.44</u>            | <u>\$ 0.26</u>           | <u>\$ 0.22</u>           |

**HOMESTREET, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 25 — RESTRUCTURING:**

In 2019, we took steps to restructure our corporate operations in order to improve productivity and reduce total corporate expenses in light of a substantial reduction in the size and complexity of our Company and a lower growth plan going forward. Throughout 2019, we began executing this restructuring plan which included:

- Simplifying the organizational structure by reducing management levels and management redundancy
- Consolidating similar functions currently residing in multiple organizations
- Renegotiating, where possible, our technology contracts
- Identifying and eliminating redundant or unnecessary systems and services
- Rationalizing staffing appropriate to recognize the significant changes in work volumes and company direction
- Eliminate excess occupancy costs consistent with reduced personnel

The costs incurred include severance, retention, facility related charges and consulting fees. These restructuring activities and related costs will continue through 2020.

Also in 2019, in connection with the Board of Directors approved plan of exit or disposal of our stand-alone home loan-center based mortgage origination business and related mortgage servicing, the Company restructured certain aspects of its infrastructure and back office operations, which resulted in certain indirect severance and other employee related costs and impairment charges related to certain facilities and information systems. Cost directly related to the plan of exit or disposal are not included in restructuring, but rather are characterized as gain loss on disposal; for further information, see *Note 2, Discontinued Operations*.

In 2017, in response to changing market conditions and forecasts, we implemented restructuring plans in the Company's former Mortgage Banking segment to reduce operating costs and improve efficiency. In June 2018, the Company implemented additional restructuring in the legacy Mortgage Banking segment to further reduce operating costs and improve profitability.

Restructuring charges primarily consist of facility-related costs and severance costs and are included in the occupancy and the salaries and related costs line items on our consolidated statement of operations in the applicable periods for continuing operations and in income (loss) from discontinued operations for the applicable periods for discontinued operations.

The following table summarizes the restructuring charges, the restructuring costs paid or settled during the years ended December 31, 2019, 2018 and 2017, and the Company's net remaining liability balance at December 31, 2019, 2018 and 2017 for both continuing and discontinued operations.

| <b>(in thousands)</b>                     | <b>Facility-related costs</b> | <b>Personnel-related costs</b> | <b>Other restructuring costs</b> | <b>Total</b>    |
|---|-------------------------------|--------------------------------|----------------------------------|-----------------|
| Balance, December 31, 2016 . . . . .      | \$ —                          | \$ —                           | \$ —                             | \$ —            |
| Restructuring charges . . . . .           | 3,072                         | 648                            | —                                | 3,720           |
| Costs paid or otherwise settled . . . . . | <u>(1,686)</u>                | <u>(648)</u>                   | <u>—</u>                         | <u>(2,334)</u>  |
| Balance, December 31, 2017 . . . . .      | 1,386                         | —                              | —                                | 1,386           |
| Restructuring charges . . . . .           | 5,762                         | 456                            | —                                | 6,218           |
| Costs paid or otherwise settled . . . . . | <u>(5,544)</u>                | <u>(456)</u>                   | <u>—</u>                         | <u>(6,000)</u>  |
| Balance, December 31, 2018 . . . . .      | 1,604                         | —                              | —                                | 1,604           |
| Restructuring charges . . . . .           | 1,373                         | 1,836                          | 1,302                            | 4,511           |
| Costs paid or otherwise settled . . . . . | <u>(1,742)</u>                | <u>(1,326)</u>                 | <u>(1,143)</u>                   | <u>(4,211)</u>  |
| Balance, December 31, 2019 . . . . .      | <u>\$ 1,235</u>               | <u>\$ 510</u>                  | <u>\$ 159</u>                    | <u>\$ 1,904</u> |

**HOMESTREET, INC. AND SUBSIDIARIES**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**NOTE 26 — SUBSEQUENT EVENTS:**

The Company has evaluated the events that have occurred subsequent to the year ended December 31, 2019 and has included all material events that would require recognition in the 2019 consolidated financial statements, disclosure in the notes to the consolidated financial statements or below.

The Board of Directors approved an addition to our share repurchase program for up to \$25 million of our common stock in January 2020, and our regulators have confirmed no objections to that repurchase. In February the Board increased the authorization by an additional \$10 million conditional on the non-objection of our regulators. Assuming no objections from our regulators for the additional repurchase authorization, we expect to commence repurchases in the first or second quarter of 2020. This authorization is in addition to the 3.4 million shares of common stock that the Company repurchased in 2019 and early 2020.

In January 2020, HomeStreet's Board of Directors approved a new dividend policy that contemplates the payment of quarterly cash dividends on our common stock when, if and in an amount declared by the Board after taking into consideration, among other things, earnings, regulatory capital levels, the overall payout ratio and expected asset growth. The first dividend declared under this policy was a cash dividend of \$0.15 per share for the first quarter of 2020, which was paid on February 21, 2020 to shareholders of record as of the close of business on February 5, 2020. The dividend rate to be paid will be reassessed each quarter by the Board of Directors in accordance with the dividend policy.

## **ITEM 9 CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE**

No disclosure required pursuant to Item 304 of Regulation S-K.

### **ITEM 9A CONTROLS AND PROCEDURES**

#### **Evaluation of Disclosure Controls and Procedures**

The Company's management conducted an evaluation, under the supervision and with the participation of its Chief Executive Officer ("CEO") and Chief Financial Officer ("CFO"), of the effectiveness of the design and operation of the Company's disclosure controls and procedures (as defined in Rule 13a-15(e) of the Exchange Act) at December 31, 2019. The Company's disclosure controls and procedures are designed to ensure that information required to be disclosed by the Company in the reports that it files or submits under the Exchange Act is recorded, processed, summarized, and reported within the time periods specified in the rules and forms of the SEC, and that such information is accumulated and communicated to the Company's management, including its CEO and CFO, as appropriate, to allow timely decisions regarding required disclosure. Based upon the evaluation, the CEO and CFO concluded that the Company's disclosure controls and procedures were effective at December 31, 2019.

#### **Management's Report on Internal Control Over Financial Reporting**

Management is responsible for establishing and maintaining adequate internal control over financial reporting (as defined in Rule 13a-15(f) of the Exchange Act) for the Company. The Company's internal control over financial reporting is a process designed under the supervision of the Company's CEO and CFO to provide reasonable assurance regarding the reliability of financial reporting and the preparation of the Company's financial statements for external purposes in accordance with U.S. GAAP. Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions or that the degree of compliance with the policies or procedures may deteriorate. Management has made a comprehensive review, evaluation, and assessment of the Company's internal control over financial reporting at December 31, 2019. In making its assessment of internal control over financial reporting, management utilized the framework issued in 2013 by the Committee of Sponsoring Organizations of the Treadway Commission ("COSO") in *Internal Control — Integrated Framework*. Based on that assessment, management concluded that, at December 31, 2019, the Company's internal control over financial reporting was effective.

Deloitte & Touche LLP, the independent registered public accounting firm that audited our consolidated financial statements at, and for, the year ended December 31, 2019, has issued an audit report on the effectiveness of the Company's internal control over financial reporting at December 31, 2019, which report is included below in this Item 9A.

#### **Changes in Internal Control Over Financial Reporting**

As required by Rule 13a-15(d), our management, including our CEO and CFO, also conducted an evaluation of our internal control over financial reporting to determine whether any changes occurred during the quarter ended December 31, 2019 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

During the quarter ended March 31, 2019, as disclosed in our financial statements in Part III, Item 8 of this Annual Report on Form 10-K, the Company sold a significant portion of its single family mortgage servicing rights. The Company's Board of Directors also authorized the exit or disposal of the Company's home loan center-based origination business which resulted in elimination of segment reporting in the first quarter of 2019. Subsequent to the quarter ended March 31, 2019, the Company executed a definitive agreement with Homebridge Financial Services, Inc. to sell the assets of up to 50 stand-alone, satellite, and fulfillment offices. The Company completed the sale of assets related to 47 offices, including the sublease or assignment of leases of such offices, to Homebridge Financial Services, Inc. during the quarter ended June 30, 2019 and closed all remaining mortgage offices.

In connection with the adoption of the resolution to exit or dispose of the home loan center-based mortgage business, the sales of single family mortgage servicing rights and entering into a definitive agreement for the sale of assets to Homebridge, the Company adopted discontinued operations accounting for the legacy Mortgage Banking segment. Certain back office infrastructure and operations were also restructured as part of these activities. The combined initiatives were determined to have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting process. We will continue to closely monitor internal control over financial reporting until these initiatives are concluded.

## REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the shareholders and Board of Directors of HomeStreet, Inc.

### Opinion on Internal Control over Financial Reporting

We have audited the internal control over financial reporting of HomeStreet, Inc. and subsidiaries (the “Company”) as of December 31, 2019, based on criteria established in *Internal Control — Integrated Framework (2013)* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Because management’s assessment and our audit were conducted to meet the reporting requirements of Section 112 of the Federal Deposit Insurance Corporation Improvement Act (FDICIA), management’s assessment and our audit of the Company’s internal control over financial reporting included controls over the preparation of the schedules equivalent to the basic financial statements in accordance with the instructions for the Consolidated Reports of Condition and Income for Schedules RC, RI, and RI-A. In our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2019, based on criteria established in *Internal Control — Integrated Framework (2013)* issued by COSO.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States) (PCAOB), the consolidated financial statements as of and for the year ended December 31, 2019, of the Company and our report dated March 6, 2020, expressed an unqualified opinion on those financial statements and included an emphasis of matter paragraph regarding discontinued operations.

### Basis for Opinion

The Company’s management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management’s Report on Internal Control Over Financial Reporting. Our responsibility is to express an opinion on the Company’s internal control over financial reporting based on our audit. We are a public accounting firm registered with the PCAOB and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audit in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

### Definition and Limitations of Internal Control over Financial Reporting

A company’s internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company’s internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company’s assets that could have a material effect on the financial statements. Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

/s/ Deloitte & Touche LLP

Seattle, Washington

March 6, 2020



**ITEM 9B OTHER INFORMATION**

None.

## PART III

### ITEM 10 DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE

We have adopted a Code of Business Conduct and Ethics that applies to all of our directors, officers and employees, including our principal executive officer and principal financial officer. The Code of Business Conduct and Ethics is posted on our website at <http://ir.homestreet.com>.

We intend to satisfy the disclosure requirement under Item 5.05 of Form 8-K regarding an amendment to, or waiver from, a provision of this Code of Business Conduct and Ethics by posting such information on our corporate website, at the address and location specified above and, to the extent required by the listing standards of the Nasdaq Global Select Market, by filing a Current Report on Form 8-K with the SEC, disclosing such information.

The information required by this item with respect to our directors, our executive officers, our Audit Committee and its members, and audit committee financial expert will be set forth in our definitive proxy statement for the 2020 annual meeting of stockholders (the “2020 Proxy Statement”) under the captions “Election of Directors” and “Executive Officers,” which information is incorporated herein by reference. The information required by this item with respect to compliance with Section 16(a) of the Exchange Act will be set forth in our 2020 Proxy Statement under the caption “Principal Shareholders — Delinquent Section 16(a) Reports,” which information is incorporated herein by reference.

Our 2020 Proxy Statement is expected to be filed not later than 120 days after the end of our fiscal year ended December 31, 2019.

### ITEM 11 EXECUTIVE COMPENSATION

The information required by this item will be set forth in the 2020 Proxy Statement under the captions “Executive Compensation” and “Corporate Governance — Human Resources and Corporate Governance Committee Interlocks and Insider Participation,” which information is incorporated herein by reference.

### ITEM 12 SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS

#### Equity Compensation Plan Information

The following table gives information about our common stock that may be issued upon the exercise of options, warrants and rights under all of our existing equity compensation plans as of December 31, 2019 under the HomeStreet, Inc. 2014 Equity Incentive Plan (the “2014 Plan”).

| Plan Category   | (a)<br>Number of<br>Securities to be<br>Issued Upon<br>Exercise of<br>Outstanding<br>Options,<br>Warrants and<br>Rights | (b)<br>Weighted<br>Average Exercise<br>Price of<br>Outstanding<br>Options,<br>Warrants, and<br>Rights | (c)<br>Number of<br>Securities<br>Remaining<br>Available for<br>Future Issuance<br>Under Equity<br>Compensation<br>Plans (Excluding<br>Securities Reflected<br>in Column (a)) |
|---|---|---|---|
| Plans approved by shareholders . . . . .                    | 582,754 <sup>(1)</sup>  | \$ 12.49 <sup>(2)</sup>   | 938,581 <sup>(3)</sup>  |
| Plans not approved by shareholders <sup>(4)</sup> . . . . . | — <sup>(4)</sup>  | —   | N/A   |
| Total . . . . .   | 582,754   | \$ 12.49 <sup>(2)</sup>   | 938,581   |

(1) Consists of 233,001 shares subject to option grants awarded pursuant to the HomeStreet, Inc. 2010 Equity Incentive Plan (the “2010 Plan”), 121,991 shares subject to Restricted Stock Units awarded under the 2014 Plan and 227,762 shares issuable under Performance Share Units awarded under the 2014 Plan, assuming maximum performance goals are met under such awards, resulting in the issuance of the maximum number of shares allowed under those awards. The 2010 Plan was terminated when the 2014 Plan was approved by our shareholders on May 29, 2014. While the terms of the 2010 Plan remain in effect for any awards issued under that plan that are still outstanding, new awards may not be granted under the 2010 Plan.

- (2) Shares issued on vesting of Restricted Stock Units and Performance Share Units under the 2014 Plan are done without payment by the participant of any additional consideration and therefore have been excluded from this calculation. The weighted average exercise price reflects only the exercise price of the options issued under the 2010 Plan that are still outstanding as of the date of this table.
- (3) Consists of shares remaining available for issuance under the 2014 Plan.
- (4) The Company previously issued option awards as retention grants in 2010 that were outside of the 2010 Plan but subject to the terms of that plan. All remaining retention grants were exercised during 2019 and as of December 31, 2019, there were no awards outstanding that were granted outside of shareholder approved plans.

Except as disclosed above, the information required by this item will be set forth in the 2020 Proxy Statement under the caption “Principal Shareholders” which information is incorporated herein by reference.

### **ITEM 13 CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS AND DIRECTOR INDEPENDENCE**

The information required by this item will be set forth in the 2020 Proxy Statement under the caption “Certain Relationships and Related Transactions,” which information is incorporated herein by reference.

### **ITEM 14 PRINCIPAL ACCOUNTANT FEES AND SERVICES**

The information required by this item will be set forth in the 2020 Proxy Statement under the caption “Advisory (Non-Binding) Ratification of Appointment of Independent Registered Public Accounting Firm,” which information is incorporated herein by reference.

## PART IV

### ITEM 15 EXHIBITS AND FINANCIAL STATEMENT SCHEDULES

(a) Financial Statements and Financial Statement Schedules

(i) Financial Statements

The following consolidated financial statements of the registrant and its subsidiaries are included in Part II Item 8:

Report of Independent Registered Public Accounting Firm

Consolidated Statements of Financial Condition as of December 31, 2019 and 2018

Consolidated Statements of Operations for the three years ended December 31, 2019

Consolidated Statements of Comprehensive Income for the three years ended December 31, 2019

Consolidated Statements of Shareholders' Equity for the three years ended December 31, 2019

Consolidated Statements of Cash Flows for the three years ended December 31, 2019

Notes to Consolidated Financial Statements

(ii) Financial Statement Schedules

II — Valuation and Qualifying Accounts

All financial statement schedules for the Company have been included in the consolidated financial statements or the related footnotes, or are either inapplicable or not required.

(iii) Exhibits

### EXHIBIT INDEX

| <b>Exhibit Number</b> | <b>Description</b>   |
|-----------------------|--|
| 3.1 <sup>(1)</sup>    | Amended and Restated Bylaws of HomeStreet, Inc.  |
| 3.2 <sup>(1)</sup>    | Restated Articles of Incorporation of HomeStreet, Inc.   |
| 4.1 <sup>(2)</sup>    | Form of Common Stock Certificate   |
| 4.2 <sup>(3)††</sup>  | Indenture dated as of May 20, 2016 between HomeStreet, Inc. and Wells Fargo Bank, National Association, as Trustee   |
| 4.3                   | Description of Securities  |
| 10.1 <sup>*(4)</sup>  | HomeStreet, Inc. 2010 Equity Incentive Plan  |
| 10.2 <sup>*(5)</sup>  | Amended and Restated HomeStreet, Inc. 2014 Equity Incentive Plan   |
| 10.3 <sup>*(5)</sup>  | Standard Form of Restricted Stock Unit Agreement under the 2014 Plan   |
| 10.4 <sup>*(6)</sup>  | Standard Form of Performance Share Unit Agreement under the 2014 Plan  |
| 10.5 <sup>*(7)</sup>  | Amended and Restated HomeStreet, Inc. 401(k) Savings Plan, as of January 1, 2015   |
| 10.6 <sup>*(7)</sup>  | Amendment to the HomeStreet, Inc. 401(k) Savings Plan effective as of January 1, 2016  |
| 10.7 <sup>*(4)</sup>  | HomeStreet, Inc. Directors' Deferred Compensation Plan, effective May 19, 1999, as amended and restated December 19, 2008, executed by HomeStreet, Inc. and HomeStreet Bank                                    |
| 10.8 <sup>*(4)</sup>  | HomeStreet, Inc. Executive Deferred Compensation Plan, effective February 1, 2004, as amended and restated December 19, 2008, executed by HomeStreet, Inc., HomeStreet Bank and HomeStreet Capital Corporation |
| 10.9 <sup>*(4)</sup>  | Form of HomeStreet, Inc. Award Agreement for Nonqualified Stock Options and Standard Terms and Conditions for Nonqualified Stock Options, granted October 22, 2010 and November 29, 2010                       |

| Exhibit<br>Number      | Description  |
|------------------------|--|
| 10.10 <sup>*(8)</sup>  | Employment Agreement between HomeStreet, Inc., HomeStreet Bank, and Mark Mason, dated January 25, 2018   |
| 10.11 <sup>*(8)</sup>  | Amended and Restated Employment Agreement between HomeStreet, Inc., HomeStreet Bank, and William Endresen, dated February 26, 2018   |
| 10.12 <sup>*(9)</sup>  | Employment Agreement between HomeStreet, Inc., HomeStreet Bank, and Mark R. Ruh, dated September 11, 2017  |
| 10.13 <sup>*(8)</sup>  | Employment Agreement between HomeStreet, Inc., HomeStreet Bank, and Godfrey Evans, dated January 25, 2018  |
| 10.14 <sup>(4)</sup>   | Form of Officer Indemnification Agreement for HomeStreet, Inc.   |
| 10.15 <sup>(4)</sup>   | Form of Director Indemnification Agreement for HomeStreet, Inc.  |
| 10.16 <sup>(4)</sup>   | Form of 2011 Director and Officer Indemnification for HomeStreet, Inc.   |
| 10.17 <sup>(10)†</sup> | Office Lease, dated March 5, 1992, between Continental, Inc. and One Union Square Venture (“Office Lease”), as amended by Supplemental Lease Agreement dated August 25, 1992, Second Amendment to Lease dated May 6, 1998, Third Amendment to Lease dated June 17, 1998, Fourth Amendment to Lease dated February 15, 2000, Fifth Amendment to Lease dated July 30, 2001, Sixth Amendment to Lease dated March 5, 2002, Seventh Amendment to Lease dated May 19, 2004, Eighth Amendment to Lease dated August 31, 2004, Ninth Amendment to Lease dated April 19, 2006, Tenth Amendment to Lease dated July 20, 2006, Eleventh Amendment to Lease dated December 27, 2006, Twelfth Amendment to Lease dated October 1, 2007, Thirteenth Amendment to Lease dated January 26, 2010, Fourteenth Amendment to Lease dated January 19, 2012, Fifteenth Amendment to Lease dated May 24, 2012, Sixteenth Amendment to Lease dated September 12, 2012, Seventeenth Amendment to Lease dated November 8, 2012, Eighteenth Amendment to Lease dated May 3, 2013, Nineteenth Amendment to Lease dated May 28, 2013 and Twentieth Amendment to Lease dated June 19, 2013. |
| 10.18 <sup>(11)</sup>  | Twenty-First Amendment to Office Lease dated December 24, 2014.  |
| 10.19 <sup>(7)</sup>   | Advances, Security and Deposit Agreement, dated as of June 1, 2015, between HomeStreet Bank and the Federal Home Loan Bank of Des Moines   |
| 10.20 <sup>(10)</sup>  | Letter Agreement, dated January 15, 2013, by HomeStreet Bank to Federal Reserve Bank of San Francisco  |
| 10.21 <sup>(4)</sup>   | Master Custodial Agreement for Custody of Single Family MBS Pool Mortgage Loans, dated October 2009, between HomeStreet Bank, Federal National Mortgage Association, and U.S. Bank, N.A.   |
| 10.22 <sup>(12)†</sup> | Master Agreement ML 02783 between HomeStreet Bank and Fannie Mae, dated March 15, 2010, amended by Letter Agreement dated March 15, 2011   |
| 10.23 <sup>(4)</sup>   | Master Agreement, dated as of June 17, 2010, between HomeStreet Bank and Freddie Mac   |
| 10.24 <sup>(4)</sup>   | Cash Pledge Agreement, dated as of June 1, 2010, between HomeStreet Bank and Federal Home Loan Mortgage Corporation  |
| 10.27 <sup>(13)*</sup> | HomeStreet Bank 2017 Performance-Based Award Incentive Compensation Plan   |
| 10.28 <sup>(12)</sup>  | Master Agreement between HomeStreet Bank and Government National Mortgage Association effective January 3, 2011  |
| 10.30 <sup>(15)</sup>  | Purchase and Assumption Agreement dated as of April 4, 2019 by and between Homebridge Financial Services, Inc., and HomeStreet Bank  |
| 10.31 <sup>(16)</sup>  | Amendment No. 1 to Purchase and Assumption Agreement dated as of April 10, 2019 by and between Homebridge Financial Services, Inc., and HomeStreet Bank  |
| 10.32 <sup>(14)†</sup> | Agreement for the Bulk Purchase and Sale of Mortgage Servicing Rights dated June 29, 2018 between HomeStreet Bank and Matrix Financial Services Corporation  |
| 10.33 <sup>(17)</sup>  | Purchase Agreement dated July 10, 2019 among HomeStreet, Inc., Blue Lion Opportunity Master Fund, L.P., Roaring Blue Lion Capital Management, L.P., Roaring Blue Lion, LLC, BLOF II LP, Charles W. Griege, Jr. and Ronald K. Tanemura  |
| 21                     | Subsidiaries of HomeStreet, Inc.   |

| Exhibit Number     | Description   |
|--------------------|---|
| 23.1               | Consent of Deloitte & Touche LLP  |
| 24.1               | Powers of Attorney. Contained in the signature page of this Annual Report on Form 10-K and incorporated herein by reference.  |
| 31.1               | Certification of Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. Filed herewith.   |
| 31.2               | Certification of Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. Filed herewith.   |
| 32 <sup>(18)</sup> | Certifications of Chief Executive Officer and Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. Furnished herewith.   |
| 101                | The following financial information included in the Company's Annual Report on Form 10-K for the year ended December 31, 2019, formatted in Inline XBRL (eXtensible Business Reporting Language) and contained in Exhibit 101: (i) the Consolidated Statements of Financial Condition as of December 31, 2019 and December 31, 2018; (ii) the Consolidated Statements of Operations for the three years ended December 31, 2019, (iii) the Consolidated Statements of Comprehensive Income for the three years ended December 31, 2019; (iv) the Consolidated Statements of Shareholders' Equity for the three years ended December 31, 2019, (v) the Consolidated Statements of Cash Flows for the three years ended December 31, 2019, and (vi) the Notes to Consolidated Financial Statements. |
| 104                | The cover page from the Company's Annual Report on Form 10-K for the year ended December 31, 2019, formatted in Inline XBRL and contained in Exhibit 101.   |
| (1)                | Filed as an exhibit to HomeStreet, Inc.'s Current Report on Form 8-K (SEC File No. 001-35424) filed on July 31, 2019, and incorporated herein by reference.   |
| (2)                | Filed as an exhibit to HomeStreet, Inc.'s Amendment No. 5 to Registration Statement on Form S-1 (SEC File No. 333-173980) filed on August 9, 2011, and incorporated herein by reference.  |
| (3)                | Filed as an exhibit to HomeStreet, Inc.'s Current Report on Form 8-K (SEC File No. 001-35424) filed on May 20, 2016, and incorporated herein by reference.  |
| (4)                | Filed as an exhibit to HomeStreet, Inc.'s Amendment No. 1 to Registration Statement on Form S-1 (SEC File No. 333-173980) filed on May 19, 2011, and incorporated herein by reference.  |
| (5)                | Amended in the fourth quarter of 2018 to make administrative revisions that were not material and did not require shareholder approval. An updated version was filed as an exhibit to HomeStreet's Annual Report on Form 10-K (SEC File No. 001-35424) filed on March 6, 2019, and incorporated herein by reference.  |
| (6)                | Amended in the second quarter of 2019 to make administrative revisions that were not material and did not require shareholder approval. Updated revisions are filed herewith.   |
| (7)                | Filed as an exhibit to HomeStreet, Inc.'s Annual Report on Form 10-K (SEC File No. 001-35424) filed on March 11, 2016, and incorporated herein by reference.  |
| (8)                | Filed as an exhibit to HomeStreet, Inc.'s Annual Report on Form 10-K (SEC File No. 001-35424) filed on March 6, 2018 and incorporated herein by reference   |
| (9)                | Filed as an exhibit to HomeStreet, Inc.'s current Report on Form 8-K (SEC File No. 001-35424) filed on September 12, 2017, and incorporated herein by reference.  |
| (10)               | Filed as an exhibit to HomeStreet, Inc.'s Annual Report on Form 10-K (SEC File No. 001-35424) filed on March 17, 2014, and incorporated herein by reference.  |
| (11)               | Filed as an exhibit to HomeStreet, Inc.'s Annual Report on Form 10-K (SEC File No. 001-35424) filed on March 25, 2015, and incorporated herein by reference.  |
| (12)               | Filed as an exhibit to HomeStreet, Inc.'s Amendment No. 2 to Registration Statement on Form S-1 (SEC File No. 333-173980) filed on June 21, 2011, and incorporated herein by reference.   |
| (13)               | Filed as an exhibit to HomeStreet's Annual Report on Form 10-K (SEC File No. 001-35424) filed on March 6, 2019, and incorporated herein by reference.   |
| (14)               | Filed as an exhibit to HomeStreet Inc.'s Quarterly Report on Form 10-Q (SEC File No. 001-35424) filed on August 3, 2018, and incorporated herein by reference.  |
| (15)               | Filed as an exhibit to HomeStreet Inc.'s Current Report on Form 8-K (SEC File No. 001-35424) filed on April 4, 2019, and incorporated herein by reference.  |
| (16)               | Filed as an exhibit to HomeStreet Inc.'s Current Report on Form 8-K (SEC File No. 001-35424) filed on April 12, 2019, and incorporated herein by reference.   |
| (17)               | Filed as an exhibit to HomeStreet Inc.'s Current Report on Form 8-K (SEC File No. 001-35424) filed on July 11, 2019, and incorporated herein by reference   |



- (18) This exhibit shall not be deemed “filed” for purposes of Section 18 of the Securities Exchange Act of 1934, or otherwise subject to the liability of that Section. Such exhibit shall not be deemed incorporated into any filing under the Securities Act of 1933 or the Securities Exchange Act of 1934.
- † Certain portions of this exhibit constitute confidential information and have been redacted in accordance with Regulation S-K, Item 601(b)(10).
- †† Instruments with respect to any other long-term debt of HomeStreet, Inc. and its consolidated subsidiaries are omitted pursuant to Item 601(b)(4)(iii) of Regulation S-K since the total amount of securities authorized thereunder does not exceed 10 percent of the total assets of HomeStreet, Inc. and its subsidiaries on a consolidated basis. HomeStreet, Inc. hereby agrees to furnish a copy of any such instrument to the Securities and Exchange Commission upon request.
- \* Management contract or compensation plan or arrangement.

**ITEM 16 Form 10-K Summary**

None.

## SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this Report to be signed on its behalf by the undersigned, thereunto duly authorized, in the City of Seattle, State of Washington, on March 6, 2020.

### HomeStreet, Inc.

By: /s/ Mark K. Mason

Mark K. Mason

President and Chief Executive Officer

### HomeStreet, Inc.

By: /s/ Mark R. Ruh

Mark R. Ruh

Executive Vice President,

Chief Financial Officer and Principal Accounting Officer

## POWERS OF ATTORNEY

KNOW BY ALL PERSONS BY THESE PRESENTS, that each person whose signature appears below constitutes and appoints Mark K. Mason and Mark R. Ruh, and each of them his “or her” attorney-in-fact, with the power of substitution, for him “or her” in any and all capacities, to sign any amendment to this Report on Form 10-K and to file the same, with exhibits thereto and other documents in connection therewith, with the Securities and Exchange Commission, hereby ratifying and confirming all that said attorney-in-fact, or his “or her” substitute or substitutes, may do or cause to be done by virtue hereof.

Pursuant to the requirements of the Securities Exchange Act of 1934, this Report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

| <u>Signature</u>   | <u>Title</u>  | <u>Date</u>   |
|--|---|---------------|
| <u>/s/ Mark K. Mason</u><br>Mark K. Mason, Chairman              | Chairman of the Board, President and Chief Executive Officer (Principal Executive Officer)                                      | March 6, 2020 |
| <u>/s/ David A. Ederer</u><br>David A. Ederer, Chairman Emeritus | Chairman Emeritus of the Board  | March 6, 2020 |
| <u>/s/ Mark R. Ruh</u><br>Mark R. Ruh                            | Executive Vice President, Chief Financial Officer and Principal Accounting Officer (Principal Financial and Accounting Officer) | March 6, 2020 |
| <u>/s/ Donald R. Voss</u><br>Donald R. Voss                      | Lead Independent Director   | March 6, 2020 |
| <u>/s/ Scott M. Boggs</u><br>Scott M. Boggs                      | Director  | March 6, 2020 |
| <u>/s/ Sandra A. Cavanaugh</u><br>Sandra A. Cavanaugh            | Director  | March 6, 2020 |
| <u>/s/ Mark R. Patterson</u><br>Mark R. Patterson                | Director  | March 6, 2020 |

| <u>Signature</u>  | <u>Title</u> | <u>Date</u>   |
|---|--------------|---------------|
| <u>/s/ James R. Mitchell Jr.</u><br>James R. Mitchell Jr. | Director     | March 6, 2020 |
| <u>/s/ Thomas E. King</u><br>Thomas E. King               | Director     | March 6, 2020 |
| <u>/s/ George W. Kirk</u><br>George W. Kirk               | Director     | March 6, 2020 |
| <u>/s/ Nancy D. Pellegrino</u><br>Nancy D. Pellegrino     | Director     | March 6, 2020 |
| <u>/s/ Douglas I. Smith</u><br>Douglas I. Smith           | Director     | March 6, 2020 |

## Board of Directors<sup>1</sup>

Mark K. Mason, Chairman  
Donald R. Voss, Lead Independent Director  
David A. Ederer, Chairman Emeritus<sup>2</sup>  
Scott M. Boggs  
Sandra A. Cavanaugh  
Thomas E. King<sup>2</sup>

George “Judd” Kirk<sup>2</sup>  
James R. Mitchell, Jr.  
Mark R. Patterson  
Nancy D. Pellegrino  
Douglas I. Smith

## Executive Officers

Mark K. Mason  
Chairman, President  
and Chief Executive Officer<sup>3,4</sup>

Mark R. Ruh  
Executive Vice President  
and Chief Financial Officer<sup>3,4,5</sup>

William D. Endresen  
Executive Vice President,  
Commercial Real Estate and  
Commercial Capital President<sup>4</sup>

Godfrey B. Evans  
Executive Vice President, General Counsel,  
Chief Administrative Officer and Corporate Secretary<sup>3,4</sup>

Erik Hand  
Executive Vice President,  
Residential Lending Director<sup>4</sup>

Troy Harper  
Executive Vice President,  
Chief Information Officer<sup>3,4</sup>

Jay C. Iseman  
Executive Vice President,  
Chief Credit Officer<sup>3,4</sup>

Paulette Lemon  
Executive Vice President,  
Retail Banking Director<sup>4</sup>

Edward C. Schultz  
Executive Vice President,  
Director of Commercial Banking<sup>4</sup>

Jeff Todhunter  
Executive Vice President,  
Residential Construction Lending Director<sup>4</sup>

Darrell S. van Amen  
Executive Vice President,  
Chief Investment Officer and Treasurer<sup>3,4</sup>

Mary L. Vincent  
Executive Vice President,  
Chief Risk Officer<sup>3,4</sup>

<sup>1</sup> Members of the Board of HomeStreet, Inc. are also members of the Board of HomeStreet Bank.

<sup>2</sup> Mr. Ederer, Mr. King and Mr. Kirk will not stand for reelection at the Annual Meeting.

<sup>3</sup> HomeStreet, Inc.

<sup>4</sup> HomeStreet Bank

<sup>5</sup> Mr. Ruh has tendered his resignation from the Company effective June 5, 2020 and is expected to step down from the position of EVP, CFO effective with the assumption of that role by John Michel on May 4, 2020.

## General Corporate and Shareholders' Information

**Home Office**  
601 Union Street, Suite 2000  
Seattle, WA 98101  
206.623.3050

**Stock Transfer Agent**  
Broadridge Financial Solutions  
51 Mercedes Way  
Edgewood, NY 11717  
720.414.6867  
E-mail: [shareholder@broadridge.com](mailto:shareholder@broadridge.com)  
Shareholder portal:  
<http://shareholder.broadridge.com/hmst>

### Annual Meeting: May 21, 2020

As part of our precautions regarding the COVID-19 outbreak, we are planning for the possibility that the Annual Meeting may be held solely by means of remote communications. If we take this step, we will announce the decision to do so in advance, and details on how to participate will be posted on our website and filed with the Securities and Exchange Commission as additional proxy materials.

**Independent Accountants**  
Deloitte, LLP  
Seattle, WA



**Home Office**

601 Union Street, Suite 2000  
Seattle, WA 98101

206.623.3050  
800.654.1075  
[ir.homestreet.com](http://ir.homestreet.com)

**Investor Relations**

[ir@homestreet.com](mailto:ir@homestreet.com)  
206.389.6303