

HomeStreet, Inc.  
Form 10-K  
March 09, 2017

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

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FORM 10-K

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(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, 2016

OR

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission file number: 001-35424

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HOMESTREET, INC.

(Exact name of registrant as specified in its charter)

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Washington 91-0186600  
(State or other jurisdiction of (I.R.S. Employer  
incorporation or organization) 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	Name of each exchange on which registered
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Common Stock, no par value	Nasdaq Stock Market LLC
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Securities registered pursuant to Section 12(g) of the Act:

None.

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

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Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes  No

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

Large accelerated filer  Accelerated filer

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

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 30, 2016, 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 \$413.1 million, based on a closing price of \$19.92 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 5% 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 7, 2017 was 26,836,773.6.

**DOCUMENTS INCORPORATED BY REFERENCE**

Certain information that will be contained in the definitive proxy statement for the registrant's annual meeting to be held in May 2017 is incorporated by reference into Part III of this Form 10-K.

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Unless we state otherwise or the content otherwise requires, references in this 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 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”). These statements relate to our future plans, objectives, expectations, intentions and financial performance, and assumptions that underlie these statements. 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 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 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. is a diversified financial services company founded in 1921 headquartered in Seattle, Washington and serving customers primarily in the western United States, including Hawaii. We are principally engaged in commercial lending, commercial and consumer retail banking and real estate lending. Our primary subsidiaries are HomeStreet Bank and HomeStreet Capital Corporation. HomeStreet Bank is a Washington state-chartered commercial bank that provides consumer, mortgage and commercial loans, deposit products and services, non-deposit investment products, private banking and cash management services. Our loan products include consumer loans, single family residential mortgages, loans secured by commercial real estate, construction loans for residential and commercial real estate projects, commercial business loans and agricultural loans. HomeStreet Capital Corporation, a Washington corporation, originates, sells and services multifamily mortgage loans under the Fannie Mae Delegated Underwriting and Servicing Program (“DUS”)<sup>1</sup> in conjunction with HomeStreet Bank. Doing business as HomeStreet Insurance Agency, we provide insurance products and services for consumers and businesses. We also offer single family home loans through our partial ownership of WMS Series LLC, an affiliated business arrangement with various owners of Windermere Real Estate Company franchises whose home loan businesses are known as Penrith Home Loans (some of which were formerly known as Windermere Mortgage Services).

Shares of our common stock are traded on the Nasdaq Global Select Market under the symbol “HMST.” We also have outstanding \$65 million in aggregate principal amount of 6.5% senior notes due 2026, of which \$64.8 million in aggregate principal amount is registered pursuant to Section 15(d) of the Securities Exchange Act of 1934, as amended.

At December 31, 2016, we had total assets of \$6.24 billion, net loans held for investment of \$3.82 billion, deposits of \$4.43 billion and shareholders’ equity of \$629.3 million.

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 earn noninterest income from the origination, sale and servicing of loans and from fees earned on deposit services and investment and insurance sales.

At December 31, 2016, we had a network of 55 retail deposit branches located in Washington State, Southern California, the Portland, Oregon area and the State of Hawaii, as well as 48 primary stand-alone home loan centers and five primary commercial lending centers. These offices are located within our retail deposit branch footprint as well as in Phoenix, Arizona; Northern California (including the San Francisco Bay Area); Eugene, Salem and Bend, Oregon; Eastern Washington; Boise and northern Idaho; and Salt Lake City, Utah. WMS Series LLC, doing business as Penrith Home Loans provides point-of-sale loan origination services at certain Windermere Real Estate offices in Washington and Oregon. We also have one stand-alone insurance agency office located in Spokane, Washington. 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.

**Commercial and Consumer Banking.** We provide diversified financial products and services to our commercial and consumer customers through retail deposit branches and commercial lending centers, ATMs, and online, mobile and telephone banking. These products and services include deposit products; residential, consumer, business and agricultural loans for our portfolio; non-deposit investment products; insurance products and cash management services. We originate construction loans, bridge loans and permanent loans for the Company's portfolio, primarily on single family residences, and on office, retail, industrial and multifamily properties. We also have a commercial

lending team specializing in U.S. Small Business Administration (“SBA”) lending. We intend to pool a portion of our permanent commercial real estate loans, primarily up to \$10 million in principal amount, to sell into the secondary market. We also originate multifamily real estate loans for Fannie Mae under the DUS Program, whereby loans are sold to or securitized by Fannie Mae, while we generally retain the servicing rights. This segment is also responsible for managing our investment securities portfolio.

**Mortgage Banking.** We originate single family residential mortgage loans for sale in the secondary markets. The majority of our mortgage loans are sold to or securitized by Fannie Mae, Freddie Mac or Ginnie Mae, while we retain the right to service these loans. We are a rated originator and servicer of jumbo nonconforming mortgage loans, allowing us to sell the loans we originate to other entities for inclusion in securities. Additionally, we purchase loans from WMS Series LLC through a correspondent arrangement. 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 ("MSR") portfolio. We hedge the loan funding and the interest rate risk associated with the secondary market loan sales and the retained single family mortgage servicing rights using a combination of risk management tools.

<sup>1</sup> DUS® is a registered trademark of Fannie Mae 4

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## Expansion Activities

Since 2013, we have been supplementing the organic growth of our operations, expertise and geographic footprint with strategic acquisitions. In 2013, we simultaneously acquired Fortune Bank ("Fortune") and Yakima National Bank ("YNB"). We also acquired two branches and certain related assets in the Seattle metropolitan area from another commercial bank. The Fortune merger increased our commercial business loan portfolio and added experienced commercial lending officers and managers, while the YNB merger and branch acquisitions grew our presence in Eastern Washington.

On March 1, 2015, we entered the retail banking market in Southern California with our acquisition by merger of Simplicity Bancorp, Inc. ("Simplicity") and its subsidiary, Simplicity Bank, acquiring seven retail deposit branches in the Los Angeles area. This provided our Southern California operations with a significant retail deposit customer base, reducing our reliance on time deposits and increasing our portfolios of commercial real estate and single family mortgage loans.

In early 2015, we further expanded into Orange County, California with the launch of our commercial real estate lending group HomeStreet Commercial Capital and a team specializing in SBA lending. Through HomeStreet Commercial Capital, we provide permanent financing for a range of commercial real estate property types including multifamily, industrial, retail, office, mobile home parks and self-storage facilities, generally with balances of less than \$10 million.

On December 11, 2015, we acquired a retail deposit branch and certain related assets in Dayton, Washington. This acquisition increased HomeStreet's network of retail deposit branches in Eastern Washington to six.

We continued to grow through acquisition in 2016. On February 1, 2016, we acquired Orange County Business Bank ("OCBB"), a California banking corporation in Irvine, California to complement our expansion of commercial and consumer banking activities into Southern California.

On August 12, 2016, we acquired substantially all of the bank's assets and liabilities and two branches from The Bank of Oswego. This acquisition expanded our presence in the Portland, Oregon area, increasing the number of retail branches in the metropolitan area to five. On November 10, 2016, we acquired two branches in Southern California, one in Granada Hills and one in Burbank, along with certain related deposits from another commercial bank, increasing our presence in Southern California to 14 retail locations as of December 31, 2016.

## Financing Activities

In order to fund our continued growth and maintain adequate capital resources to support future loan growth, we completed two securities offerings in 2016, raising aggregate gross proceeds of \$125 million. The proceeds from both offerings are intended to be used for general corporate purposes, including acquisitions and investment in the growth of HomeStreet Bank.

### 6.5% Senior Notes due 2026

In May 2016, we sold \$65 million in principal amount of our 6.5% senior notes due 2026 (the "Senior Notes") in an unregistered offering under Rule 144A to certain qualified institutional buyers and a concurrent offering under Regulation S to certain foreign purchasers. In August 2016, we exchanged all of the notes sold under Rule 144A for senior notes with substantially identical terms. Our net proceeds from this offering were approximately \$63.2 million.

At-the-Market Equity Offering

In December 2016, we offered and sold approximately \$60 million of our common stock from our shelf registration statement on Form S-3. The offering commenced on December 6, 2016 and was completed on December 8, 2016, raising a total of approximately \$58.7 million in net proceeds for HomeStreet.



## Recent Developments

### SEC Settlement Agreement

On January 19, 2017, the Securities and Exchange Commission (the “SEC”) issued an Order Instituting Cease-and-Desist Proceedings Pursuant to Section 21C of the Securities Exchange Act of 1934, Making Findings, and Imposing a Cease-And-Desist Order (the “Settlement Agreement”) for HomeStreet, Inc. on terms proposed by HomeStreet to the SEC on January 6, 2017 in an Offer of Settlement. The settlement relates primarily to certain allegations related to errors in HomeStreet’s fair value hedge accounting for certain commercial real estate loans, which was previously disclosed in our Quarterly Reports on Form 10-Q in the third quarter of 2014 as well as our Annual Report on Form 10-K for the year ended December 31, 2015. The Settlement Agreement relates to certain allegations that HomeStreet did not comply with Exchange Act requirements that all issuers make and keep books, records, and accounts in reasonable detail which accurately and fairly reflect the transactions and dispositions of the assets of the issuer, and further that HomeStreet had not complied with a separate requirement under the Exchange Act that issuers devise and maintain a system of internal accounting controls sufficient to provide reasonable assurances that transactions are recorded as necessary to permit preparation of financial statements in accordance with GAAP.

The Settlement Agreement also covers allegations by the SEC that HomeStreet violated Rule 21F-17(a) of the Exchange Act, which prohibits any person from taking an action to impede an individual from communicating directly with the Commission staff about a possible securities law violation, based on language in certain severance agreements (which has since been revised), and on certain alleged efforts to determine the identity of whistleblowers. The SEC stated in the Settlement Agreement that it was unaware of any instances where a current or former employee did not communicate with the Commission about potential securities law violations, however, pursuant to our undertaking in the Settlement Agreement, we have made certain changes to language in our severance agreements and have provided notice to certain former employees that nothing in those severance agreements is intended to violate Rule 21F-17. Additionally, the Company has not identified any instance of a current or former employee not communicating directly with the Commission about the hedge accounting errors as a consequence of the language in the settlement agreements.

In connection with the Settlement Agreement, HomeStreet paid the SEC a penalty of \$500,000 and agreed to cease and desist from committing any violations of those sections to which the allegations pertained, namely Section 13(b)(2)(A) and (B) of the Exchange Act, and Exchange Act Rule 21F-17, and to undertake the remediation noted above with respect to certain severance agreements.

HomeStreet neither admitted nor was required to admit to the allegations set forth in the Settlement Agreement, and the SEC did not allege any fraud in the Settlement Agreement, nor did it allege that HomeStreet acted with an intent to deceive investors, or that the violations had a material impact on HomeStreet’s financial statements.

### Business Strategy

During 2016, we made progress on our business strategy toward becoming a significant west coast regional bank serving consumers and businesses by expanding our Commercial and Consumer Banking segment and continuing to build Mortgage Banking market share in new and existing markets. In the Commercial and Consumer Banking segment, we expanded our operations through the addition of 11 retail deposit branches, including six de novo branches opened in new and existing markets and five branches obtained through acquisitions in our existing geographic footprint, increasing the density of commercial and retail deposits in connection with that expansion. In our Mortgage Banking segment, we continued to build on our heritage as a leading single family mortgage lender,

expanding opportunistically both within our existing market and into other parts of the western United States, including opening three new primary stand-alone home loan centers in new and existing markets and investing in the implementation of a new loan origination system expected to be fully installed during 2017.

We are pursuing the following strategies in our business segments:

**Commercial and Consumer Banking.** We believe there is a significant opportunity for a well-capitalized, community-focused bank that emphasizes responsive and personalized service to provide a full range of financial services to small- and middle-market commercial and consumer customers in markets that are not well served by existing community banks focused on that demographic, including Southern California. Our Commercial and Consumer Banking strategy involves organic growth and strategic acquisitions along with improvements in operations and productivity intended to drive cost efficiencies. On the consumer banking side, our acquisitions since our initial public offering in 2012 have added a total of 15 retail branches in Washington State, Oregon and Southern California to complement the 16 de novo openings we have had in the same time period. We have also expanded our commercial lending presence, acquired experienced commercial lending personnel and grew our commercial loan portfolio in part through acquisitions such as Fortune and OCBB. In addition to that acquisitive growth, on the commercial side, we have added two Orange County based commercial lending teams, HomeStreet Commercial Capital and our SBA lending team. We expect to continue to grow our commercial lending (including SBA lending), commercial real estate and residential construction lending in Southern California.

We are also in the process of growing our commercial and consumer banking business in the Portland, Oregon metropolitan area, and in 2016 we acquired substantially all of the banking operations, including two retail deposit branches from The Bank of Oswego in Lake Oswego, Oregon. We intend to continue to add de novo retail deposit branches in new and existing markets.

We plan to expand our commercial real estate business with a focus on multifamily mortgage origination, including through our Fannie Mae DUS 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 seller and servicer. We plan to continue supporting our DUS 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 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 may in the future sell those types of loans to other investors, such as life insurance companies.

We seek to meet the financial needs of our consumer and small business customers through our retail deposit branches by providing targeted banking products and services, investment services and products, and insurance products through our bank branches and through dedicated investment advisors, insurance agents and business banking officers. We intend to grow our network of retail deposit branches and in turn grow our core deposits and increase business deposits from new cash management and business lending customers, primarily focusing on high-growth areas of Puget Sound, Portland, Oregon, the Bay Area and Southern California, building loyalty with our customers and growing market share.

**Mortgage Banking.** We have leveraged our reputation for high quality service and reliable loan closing to increase our single family mortgage market share significantly over the last five years. In addition, we plan to continue to grow our business in the western U.S. through expanding in high growth markets and the targeted hiring of loan originators with successful track records and an emphasis on purchase mortgage transactions. We intend to continue to focus on conventional conforming and government insured or guaranteed single family mortgage origination. We also offer home equity and other portfolio loan products to complement secondary market lending, particularly for well-qualified borrowers with loan sizes greater than the conventional conforming limits.

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Our single family mortgage origination and servicing business is highly dependent upon compliance with underwriting and servicing guidelines of Fannie Mae, Freddie Mac, FHA, VA and Ginnie Mae as well as a myriad of federal and state consumer compliance regulations. However, our demonstrated expertise in these activities, together with our significant volume of lending in low- and moderate-income areas and direct community investment, contribute to our uninterrupted record of “Outstanding” Community Reinvestment Act (“CRA”) ratings since 1986. We believe our historically strong compliance culture represents a significant competitive advantage in today's market, especially in the face of increasing regulatory compliance requirements.

For a discussion of operating results of these lines of business, see "Business Segments" within Management's Discussion and Analysis of this Form 10-K.

## Market and Competition

We view our market as the major metropolitan areas in 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 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 most recent financial crisis. We believe this dislocation has left a void for a strong regional bank serving consumers and businesses with significant long-term opportunities to grow organically and through acquisitions.

We currently operate full service bank branches in the Puget Sound and eastern regions of Washington, the Portland, Oregon metropolitan area, the Hawaiian Islands, and Southern California. We also have primary stand-alone commercial and residential lending centers in the metropolitan areas of San Francisco, California; Phoenix, Arizona; and Salt Lake City, Utah. Over time, we expect to efficiently expand our full service bank branches, on a prudent and opportunistic basis, to areas currently being served only by stand-alone lending centers, and to further expand our geographic footprint into other large metropolitan areas in the western United States that share the same or substantially similar characteristics to our current markets.

The financial services industry is highly competitive. We compete with other banks, savings and loan associations, 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 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.

We believe we are well positioned to take advantage of changes in the single family mortgage origination and servicing industry that have helped to reduce the number of competitors. The mortgage industry is compliance-intensive and requires significant expertise and internal control systems to ensure mortgage loan origination and servicing providers meet all origination, processing, underwriting, servicing and disclosure requirements. We believe our compliance-centered culture affords us a competitive advantage even as a growing complexity of the regulatory landscape poses a barrier to entry for many of our would-be competitors. For example, the Truth in Lending Act-Real Estate Settlement Procedures Act "TILA-RESPA" Integrated Disclosure (commonly known as "TRID") requirements have substantially increased documentation requirements and responsibilities for the mortgage industry, further complicating work flow and increasing training costs, thereby increasing barriers to entry and costs of operations across the mortgage industry. These rules have added to the work involved in originating mortgage loans and added to processing costs for all mortgage originators. In some cases, these rules have lengthened the time needed to close loans. Increased costs and additional compliance burdens are causing some competitors to exit the industry. Mortgage lenders must make significant investments in experienced personnel and specialized systems to manage the compliance process, which creates a significant barrier to entry. In addition, lending in conventional and government guaranteed or insured mortgage products, including Federal Housing Administration ("FHA") and Department of Veterans' Affairs ("VA") loans, requires significantly higher capitalization than had previously been required for mortgage brokers and non-bank mortgage companies.

## Employees

As of December 31, 2016 we employed 2,552 full-time equivalent employees, compared to 2,139 full-time equivalent employees at December 31, 2015.

#### 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 report or any of our other securities filings. You may review a copy of our reports, including exhibits and schedules filed therewith, and obtain copies of such materials at the SEC's Public Reference Room at 100 F Street, NE, Washington, D.C. 20549. You may obtain information on the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0330. The SEC maintains a website (<http://www.sec.gov>) that contains reports, proxy and information statements and other information regarding registrants, such as HomeStreet, that file 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 annual report on 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 considered regularly 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 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. In December 2015 and again in December 2016, the Federal Reserve increased short-term interest rates. 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 and fiscal 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 to a bank holding company, the Company continues to be subject to capital requirements. See "Regulation and Supervision of HomeStreet Bank - Capital and Prompt Corrective Action Requirements - Capital Requirements."

Regulations and historical practice of the Federal Reserve have required bank holding companies to serve as a “source of strength” for their subsidiary banks. The Dodd-Frank Act codifies this requirement and extends 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 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 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.

#### 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. Effective on June 25, 2010, federal banking regulators adopted 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 HomeStreet's

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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 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.

#### Emerging Growth Company

We are an "Emerging Growth Company," as defined in the Jumpstart Our Business Startups Act (the "JOBS Act"), and are eligible to take advantage of certain exemptions from various reporting requirements that are applicable to other public companies that are not Emerging Growth Companies. These include, but are not limited to, not being required to comply with the auditor attestation requirements of Section 404 of the Sarbanes-Oxley Act of 2002, reduced disclosure obligations regarding executive compensation in our periodic reports and proxy statements, and exemptions from certain requirements under the Dodd-Frank Act, including the requirement to hold a non-binding advisory vote on executive compensation and the requirement to obtain shareholder approval of any golden parachute payments not previously approved. We currently take advantage of some or all of these reporting exemptions and intend to continue to do so until we no longer qualify as an Emerging Growth Company.

We will remain an Emerging Growth Company for up to five years from the end of the year of our initial public offering, or until (1) we have total annual gross revenues of at least \$1 billion, (2) we qualify as a large accelerated filer, or (3) we issue more than \$1 billion in nonconvertible debt in a three-year period. Based on these requirements, we expect to lose our status as an Emerging Growth Company no later than January 1, 2018.

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 if payment of such dividend would cause its net worth to be reduced below the net worth requirements, if any, imposed by the WDFI and dividends may not be paid in an amount greater than its retained earnings without the approval of the WDFI. These restrictions are 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 an application with the WDFI, which has the authority to disapprove the 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. Under the Dodd-Frank Act, the amount of federal deposit insurance coverage was permanently increased from \$100,000 to \$250,000, per depositor, for each account ownership category at each depository institution. This change made permanent the coverage increases that had been in effect since October 2008. 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. The minimum ratio of assets in the DIF to the total of estimated insured deposits was increased from 1.15% to 1.35%, and the FDIC is given until September 30, 2020 to meet the reserve ratio. In December 2010, the FDIC adopted a final rule setting the reserve ratio of the DIF at 2.0%. 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. The current rates were lowered effective July 1, 2016, since the reserve ratio reached 1.15% as of June 30, 2016. In the future, if the reserve

ratio reaches certain levels, these assessment rates will generally be further lowered. As of December 31, 2016, the Bank's assessment rate was 6 basis points on average assets less average tangible equity capital. In addition, all FDIC-insured institutions are 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 Financing Corporation rate is adjusted quarterly to reflect changes in assessment bases of the DIF. These assessments will continue until the Financing Corporation bonds mature in 2019. The annual rate for the first quarter of 2017 is 0.54 basis points.

## 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 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.

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.

Both the Company and the Bank were generally required to begin compliance with the Rules on January 1, 2015. The conservation buffer began being phased in beginning in 2016 and will take 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.



### 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.

### 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 current 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. In December 2014, the federal banking regulators, together with the SEC, the Federal Housing Finance Agency and the Department of Housing and Urban Development, published a final rule implementing this requirement. Generally, the final rule provides 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. Compliance with the final rule with respect to residential mortgage securitizations was required beginning in December 2015 and was required beginning in December 2016 for all other securitizations.

## Volcker Rule

In December 2013, the FDIC, the FRB and various other federal agencies issued final rules to implement certain provisions of the Dodd-Frank Act commonly known as the “Volcker Rule.” Subject to certain exceptions, the final rules generally prohibit banks and affiliated companies from engaging in short-term proprietary trading of certain securities, derivatives, commodity futures and options on those instruments, for their own account. The final rules also impose 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.

### 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. Currently, reserves must be maintained against transaction accounts (primarily negotiable order of withdrawal and regular checking accounts). The regulations generally required in 2016 that reserves be maintained as follows:

- Net transaction accounts up to \$15.2 million were exempt from reserve requirements.
- A reserve of 3.0% of the aggregate is required for transaction accounts over \$15.2 million up to \$110.2 million.
- A reserve of 10% is required for any transaction accounts over \$110.2 million.

In 2017, the regulations generally require that reserves be maintained as follows:

- Net transaction accounts up to \$15.5 million were exempt from reserve requirements.
- A reserve of 3.0% of the aggregate is required for transaction accounts over \$15.5 million up to \$115.1 million.
- A reserve of 10% is required for any transaction accounts over \$115.1 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”) and is a borrowing non-member financial institution with the Federal Home Loan Bank of San Francisco (“San Francisco FHLB”). As a member of the Des Moines FHLB, the Bank is required to own stock in the Des Moines FHLB. Separately, pursuant to a non-member lending agreement with the San Francisco FHLB that we entered into at the time of the Simplicity Acquisition, we are required to own stock of the San Francisco FHLB so long as we continue to be a borrower from the San Francisco FHLB. We currently own \$40.3 million of stock in the FHLB in the aggregate based on these obligations.

#### 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 “Outstanding” 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, the Bank may not declare or pay a cash dividend on its capital stock if this would cause its net worth to be reduced below the net worth requirements, if any, imposed by the WDFI. In addition, dividends on the Bank's capital stock 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 “- 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.

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 21st 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 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 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 imposes a variety of requirements on entities that service mortgage loans.

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 and the Federal Reserve has stated that it will monitor and report to Congress on the effectiveness of the exemption.

#### 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. In particular, the Trump administration and various members of Congress have expressed a desire to modify or repeal parts of the Dodd-Frank Act. 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 Annual Report on 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 are growing rapidly, and we may fail to manage our growth properly.

Since our initial public offering (“IPO”) in February 2012, we have pursued targeted and opportunistic growth which has included four whole-bank acquisitions along with seven branch acquisitions. These acquisitions represent both significant operational growth and a substantial geographic expansion of our commercial and consumer banking operations. Simultaneously with this growth of our banking operations through acquisition, we have also grown our mortgage origination operations opportunistically but quickly, opening new primary and satellite offices in Northern and Southern California starting in 2013, and further expanding our mortgage origination operations into Arizona beginning in the fourth quarter of 2014 and Central California in the second quarter of 2015, while also continuing to grow those operations in the Pacific Northwest. Beginning in 2015, we also started expanding our commercial lending activities, opening new primary offices in Salt Lake City, Utah and adding production personnel in Southern California focused on residential construction and SBA loans. At the time of our IPO, we had 20 retail branches and nine stand-alone lending centers. As of December 31, 2016 we have grown to a total of 55 retail branches, 53 primary stand-alone lending centers, including five primary commercial lending centers, and one stand-alone insurance office.

These activities reflect substantial growth in terms of total assets, total deposits, total loans and employees. We plan to continue both strategic and opportunistic growth, which can present substantial demands on management personnel, line employees, and other aspects of our operations, especially if growth occurs rapidly. We may face difficulties in managing that growth, and we may experience a variety of adverse consequences, including:

- Loss of or damage to key customer relationships;
- Distraction of management from ordinary course operations;
- Costs incurred in the process of vetting potential acquisition candidates which we may not recoup;
- Loss of key employees or significant numbers of employees;
- The potential of litigation from prior employers relating to the portability of their employees;
- Costs associated with opening new offices and systems expansion to accommodate our growth in employees;
- Increased costs related to hiring, training and providing initial compensation to new employees, which may not be recouped if those employees do not remain with us long enough to be profitable;
- Challenges in complying with legal and regulatory requirements in new jurisdictions;
  - Inadequacies in our computer systems, accounting policies and procedures, and management personnel (some of which may be difficult to detect until other problems become manifest);
- Challenges integrating different systems, practices, and customer relationships;
- An inability to attract and retain personnel whose experience and (in certain circumstances) business relationships promote the achievement of our strategic goals; and
- Increasing volatility in our operating results as we progress through these initiatives.

Because our business strategy includes growth in total assets, total deposits, total loans and employees, including through opportunistic acquisitions, if we fail to manage our growth properly, our financial condition and results of operations could be negatively affected.

Volatility in mortgage markets, changes in interest rates, operational costs and other factors beyond our control may adversely impact our ability to remain profitable.

We have sustained significant losses in the past, and we cannot guarantee that we will remain profitable or be able to maintain the level of profit we are currently experiencing. For example, in the fourth quarter of 2016, unexpected sharp increases in interest rates related to the results of the U.S. presidential election as well as asymmetrical changes in the values of mortgage servicing rights and certain derivative hedging instruments created an unforeseen and material adverse impact on our earnings for that quarter. Many factors affect our profitability, and our ability to remain profitable is threatened by a myriad of issues, including:

Increases in interest rates that may limit our ability to make loans, decrease our net interest income and noninterest income, increase the number of rate locks that become closed loans which may in turn increase our costs relative to our income, reduce demand for loans, diminish the value of our mortgage servicing rights, affect the value of our hedging instruments, increase the cost of deposits and otherwise negatively impact our financial situation;

Volatility in mortgage markets, which is driven by factors outside of our control such as interest rate changes, housing inventory and general economic conditions, may negatively impact our ability to originate loans and change the fair value of our existing loans and servicing rights;

Our hedging strategies to offset risks related to interest rate changes may not prove to be successful and may result in unanticipated losses for the Company;

Changes in regulations or interpretation of regulation through enforcement actions may negatively impact the Company or the Bank and may limit our ability to offer certain products or services or may increase our costs of compliance;

Increased costs from growth through acquisition could exceed the income growth anticipated from these opportunities, especially in the short term as these acquisitions are integrated into our business;

Increased costs for controls over data confidentiality, integrity, and availability due to growth or to strengthen the security profile of our computer systems and computer networks;

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;

Competition in the mortgage market industry may drive down the interest rates we are able to offer on our mortgages, which will negatively impact our net interest income; and

Changes in the cost structures and fees of government-sponsored enterprises to whom we sell many of these loans may compress our margins and reduce our net income and profitability.

These and other factors may limit our ability to generate revenue in excess of our costs, which in turn may result in a lower rate of profitability or even substantial losses for the Company.

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

We have completed four whole-bank acquisitions and acquired seven stand-alone branches in the past four years, all of which has required substantial resources and costs related to the acquisition process and subsequent integration. For example, we incurred \$4.6 million and \$10.7 million of acquisition related expenses, net of tax, in the fiscal years ended December 31, 2016 and 2015, respectively. We regularly evaluate merger and acquisition opportunities with other financial institutions and financial services companies. 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 as part of our ongoing strategy to grow our business and our market share.

Any future acquisition we may undertake may involve numerous 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 HomeStreet and HomeStreet Bank, including risks that arise after the transaction is completed. These risks include:

- Diversion of management's attention from normal daily operations of the business;
- Difficulties in integrating the operations, technologies, and personnel of the acquired companies;
- Difficulties in implementing, upgrading and maintaining our internal controls over financial reporting and our disclosure controls and procedures;
- Inability to maintain the key business relationships and the reputations of acquired businesses;
- Entry into markets in which we have limited or no prior experience and in which competitors have stronger market positions;

Potential responsibility for the liabilities of acquired businesses;  
Inability to maintain our internal standards, procedures and policies at the acquired companies or businesses; and  
Potential loss of key employees of the acquired companies.

In addition, in certain cases our acquisition of a whole bank or a branch includes the acquisition of all or a substantial portion of the target bank or branch's assets and liabilities, including all or a substantial portion of its loan portfolio. There may be instances where we, under our normal operating procedures, may find after the acquisition that there may be additional losses or undisclosed liabilities with respect to the assets and liabilities of the target bank or branch, and, with respect to its loan portfolio, that the ability of a borrower to repay a loan may have become impaired, the quality of the value of the collateral securing a loan may fall below our standards, or the allowance for loan losses may not be adequate. One or more of these

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factors might cause us to have additional losses or liabilities, additional loan charge-offs or increases in allowances for loan losses.

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.

In addition, we may choose to issue additional common stock for future acquisitions, or we may instead choose to pay the consideration in cash or a combination of stock and cash. Any issuances of stock relating to an acquisition may have a dilutive effect on earnings per share, book value per share or the percentage ownership of current shareholders depending on the value of the assets or entity acquired. Alternatively, the use of cash as consideration in any such acquisitions could impact our capital position and may require us to raise additional capital.

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, a characteristic we expect to continue indefinitely. 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, and a degeneration in prevailing economic conditions may result in higher than expected loan delinquencies, foreclosures, problem loans, OREO, net charge-offs and provisions for credit and OREO losses. Although real estate prices are stable in the markets in which we operate, if market values decline, the collateral for our loans may provide less security and our ability to recover the principal, interest and costs due on defaulted loans by selling the underlying real estate will be diminished, leaving us more likely to suffer additional losses 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.

Worsening conditions in the real estate market 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 loan 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.

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 with fluctuations in interest rates, among other things, reflecting the changing expectations of mortgage prepayment activity. 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, as occurred in the fourth quarter of 2016, and we could incur a net valuation loss as a result of our hedging activities. As we continue to expand our single family mortgage operations and add more single family mortgage origination personnel, the volume of our single family loans held for sale and MSR's has continued to increase. The increase in volume in turn increases our exposure to the risks associated with the impact of interest rate fluctuations on single family loans held for sale and MSR's. Further, in times of significant financial disruption, as in 2008, hedging counterparties have been known to default on their obligations. Any such events or conditions may harm our results of operations.

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 operations in eight states, a substantial majority of our revenues are derived from operations in the Puget Sound region of Washington State, the Portland, Oregon metropolitan area and the Los Angeles and San Diego metropolitan areas in Southern California and 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 each has experienced disproportionately significant economic declines in the past decade. Economic declines or natural disasters that affect these areas in particular, or economic events that particularly or more significantly affect the Western United States, the Puget Sound region or Southern California, may have an unusually pronounced impact on our business and, 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.

We have previously had deficiencies in our internal controls over financial reporting, and those deficiencies or others that we have not discovered 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 assure 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 and effectively prevent fraud and to 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 control from time to time we have discovered deficiencies in our internal controls that have required remediation. 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. For example, our management determined that we had experienced a material weakness in our internal controls over financial reporting as of September 30, 2014 related to errors in the analysis of hedge effectiveness related to fair value hedge accounting for certain commercial real estate loans and related swap or derivative instruments, and also concluded that our internal controls over financial reporting were not effective as of December 31, 2014 because of a material weakness in our internal controls related to certain new back office systems, primarily relating to accounts payable processing and payroll processing. We also have discovered “significant deficiencies,” defined as a deficiency or combination of deficiencies in internal control over financial reporting that is less severe than a material weakness, yet important enough to merit attention by those responsible for oversight of the Company's financial reporting.

Management has in place a process to document and analyze all identified internal control deficiencies and implement remedial measures sufficient to resolve those deficiencies. To support our growth initiatives and to create operating efficiencies we have implemented, and will continue to implement, new systems and processes. If our project management processes are not sound and adequate resources are not deployed to these implementations, we may experience additional internal control lapses that could expose the company to operating losses. However, any failure to maintain effective controls or timely effect 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.

If our internal controls over financial reporting are subject to additional defects we have not identified, we may be unable to maintain adequate control over our assets, or we may experience material errors in recording our assets, liabilities and results of operations. Repeated or continuing deficiencies may cause investors to question the reliability of our internal controls or our financial statements, and may result in an erosion of confidence in our management or

result in penalties or other potential enforcement action by the Securities and Exchange Commission (the “SEC”). On January 19, 2017, we finalized a settlement agreement with the SEC and paid a fine of \$500,000 related to the previously disclosed SEC investigation into our fair value hedge accounting for certain commercial real estate loans and swaps. While the fair value hedge accounting error at issue in the settlement was disclosed by HomeStreet in November 2014 and neither the errors nor the amount of the settlement was ultimately material to our financial statements in any period, inquiries by the SEC took the time and attention of management for significant periods of time and may have had an adverse impact on investor confidence in us in the near term which may have had a negative impact on the value of our securities.

Our allowance for loan losses may prove inadequate or we may be negatively affected by credit risk exposures. Future additions to our allowance for loan 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 loan 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. The determination of the appropriate level of the allowance for loan losses inherently involves a high degree of subjectivity and judgment and requires us to make estimates of current credit risks and future trends, all of which may undergo material changes. 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.

In addition, as we have acquired new operations, we have added the loans previously held by the acquired companies or related to the acquired branches to our books. We expect that future acquisition we may make 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 loan losses, adversely affect our financial condition, results of operations and cash flows stemming from losses on those additional loans.

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 as 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. As we grow the expectation for the sophistication of our models will increase and we may need to hire additional personnel with sufficient expertise.

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. As we continue to grow, we are likely to become more dependent on these sources, which may include Federal Home Loan Bank advances, proceeds from the sale of loans, federal funds purchased and brokered certificates of deposit. 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. 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 including 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.

Our capital ratios are higher than regulatory minimums. We may choose to have a lower capital ratio in the future in order to take advantage of growth opportunities, including acquisition and organic loan growth, 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.

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

When we sell or securitize mortgage loans in the ordinary course of business, we are required to make certain representations and warranties to the purchaser about the mortgage loans and the manner in which they were originated. Our agreements require us to repurchase mortgage 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 mortgage 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.

If repurchase and indemnity demands increase on loans or MSR that we sell from our portfolios, our liquidity, results of operations and financial condition will be adversely affected.

If we breach any representations or warranties or fail to follow guidelines when originating an 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. As a result of the housing crisis, the FHA/HUD has stepped up enforcement initiatives. In addition to regular FHA/HUD audits, HUD's Inspector General has become active in enforcing FHA regulations with respect to individual loans and has partnered with the Department of Justice ("DOJ") in filing lawsuits against lenders for systemic violations. The penalties resulting from such lawsuits can be much more 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.

We may face risk of loss if we purchase loans from a seller that fails to satisfy its indemnification obligations.

We generally receive representations and warranties from the originators and sellers from whom we purchase loans and servicing rights such that if a loan defaults and there has been a breach of such representations and warranties, we

may be able to pursue a remedy against the seller of the loan for the unpaid principal and interest on the defaulted loan. However, if the originator and/or seller breaches such representations and warranties and does not have the financial capacity to pay the related damages, we may be subject to the risk of loss for such loan as the originator or seller may not be able to pay such damages or repurchase loans when called upon by us to do so. Currently, we only purchase loans from WMS Series LLC, an affiliated business arrangement with certain Windermere real estate brokerage franchise owners.

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

Changes in the fee structures by Fannie Mae, Freddie Mac or other third party loan purchasers, such as an increase in guarantee fees and other required fees and payments, may increase the costs of doing business with them and, in turn, increase the cost of mortgages to consumers and the cost of selling conforming loans to third party loan purchasers. Increases in those costs could in turn decrease our margin and negatively impact our profitability. Additionally, increased costs for premiums from mortgage

insurers, extensions of the period for which private mortgage insurance is required on a loan purchased by third party purchasers and other changes to mortgage insurance requirements could also increase our costs of completing a mortgage and our margins for home loan origination. 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 consumers. 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 myriad 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 also may expose us to environmental liabilities.

In the course of our business, it is necessary to foreclose and take title to 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, as the 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 ever 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 such as those in the fourth quarter of 2016 relating to the reaction to the U.S. presidential election resulted in an increased percentage of rate lock customer closing loans, which in turn increased our costs relative to income. Related and concomitant asymmetrical changes in the values of MSRs and certain derivative instruments used in related hedging transactions also adversely impacted our MSR-related risk management results in that period. Even expected increases in interest rates, such as those implemented in early 2014, may reduce our mortgage revenues by reducing the market for refinancings, which may negatively impact our noninterest income and, to a lesser extent, our net interest income, as well as demand for our residential loan products and the revenue realized on the sale of

loans. Market volatility in interest rates 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.

In addition, our securities portfolio 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.

A significant portion of our noninterest income is derived from originating residential mortgage loans and selling them into the secondary market. That business has benefited from a long period of historically low interest rates. To the extent interest rates rise, particularly if they rise substantially, we may experience a reduction in mortgage financing of new home purchases and refinancing. These factors have negatively affected our mortgage loan origination volume and our noninterest income in the past and may do so again in the future.

Our mortgage operations are impacted by changes in the housing market, including factors that impact housing affordability and availability.

Housing affordability is directly affected by both the level of mortgage interest rates and the inventory of houses available for sale. The housing market recovery has been aided by a protracted period of historically low mortgage interest rates that has made it easier for consumers to qualify for a mortgage and purchase a home, however, mortgage rates have now begun to rise again. Should mortgage rates substantially increase over current levels, it would become more difficult for many consumers to qualify for mortgage credit. This could have a dampening effect on home sales and on home values.

In addition, constraints on the number of houses available for sale in some of our largest markets are driving up home prices, which may also make it harder for our customer to qualify for a mortgage, adversely impact our ability to originate mortgages and, as a consequence, our results of operations. Any return to a recessionary economy could also result in financial stress on our borrowers that may result in volatility in home prices, increased foreclosures and significant write-downs of asset values, all of which would adversely affect our financial condition and results of operations.

The stock 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 or other strategic developments;
- Future securities offerings by us of debt or equity securities
- 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; or
- Trends relating to the economic markets generally.

The stock markets in general experience substantial price and trading fluctuations, and 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 is 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.

Current 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, and a substantial amount of our revenue and earnings comes from the net interest and noninterest income that we earn from our mortgage banking and commercial lending 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 disrupt or dampen the economic recovery, could dampen



consumer confidence, adversely impact the models we use to assess creditworthiness, and materially adversely affect our financial results and condition. If the economy worsens and unemployment rises, which also would likely result in a decrease in consumer and business confidence and spending, the demand for our credit products, including our mortgages, may fall, reducing our net interest and noninterest income and our earnings. Significant and unexpected market developments may also make it more challenging for us to properly forecast our expected financial results.

A change in federal monetary policy could adversely impact our mortgage banking revenues.

The Federal Reserve 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. The Federal Reserve Board's interest rate policies can also materially affect the value of financial instruments we hold, including debt securities, mortgage servicing rights, or MSR's and derivative instruments used to hedge against changes in the value of our MSR's. 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.

The Federal Reserve Board's monetary policies during the recession and subsequent economic recovery may have had the effect of supporting higher revenues than might otherwise be available. For instance, during a period beginning in November 2008 through October 2014, the Federal Reserve Board purchased certain mortgage-backed securities and United States Treasury securities under its quantitative easing programs in an effort to meet specific economic targets and bolster the U.S. economy. If the rebound in employment and real wages is not adequate to offset the termination of that program, or if the Federal Reserve begins selling off the securities it has accumulated, we may see a reduction in mortgage originations throughout the United States, and may see a corresponding rise in interest rates, which could reduce our mortgage origination revenues and in turn have a material adverse impact upon our business.

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

A substantial portion of our consolidated net revenues (net interest income plus noninterest income) are derived from originating and selling residential mortgages. Residential mortgage lending in general has experienced substantial volatility in recent periods. An increase in interest rates in the second quarter of 2013 resulted in a significant adverse impact on our business and financial results due primarily to a related decrease in volume of loan originations, especially refinancings. The Federal Reserve increased interest rates in December 2015 and again in December 2016. Interest rate changes in the fourth quarter of 2016 resulted in lower rate locks and higher closed loan volume. 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 mortgage 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 residential mortgage loans may be

influenced by changing national and regional economic trends, such as recessions or depressed real estate markets, as well as the difference between interest rates on existing residential mortgage loans relative to prevailing residential mortgage rates. Changes in prepayment rates are therefore difficult for us to predict. An increase in the general level of interest rates may adversely affect the ability of some borrowers to pay the interest and principal of their obligations. During periods of declining interest rates, many residential borrowers refinance their mortgage loans. The loan administration fee income (related to the residential mortgage loan servicing rights corresponding to a mortgage loan) decreases as mortgage loans are prepaid. Consequently, the fair value of portfolios of residential mortgage loan servicing rights tend to decrease during periods of declining interest rates, because greater prepayments can be expected and, as a result, the amount of loan administration income received also decreases.

## Regulatory-Related Risks

We are subject to extensive regulation that may restrict our activities, including declaring cash dividends or capital distributions, 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, and are subject to various laws and judicial and administrative decisions imposing requirements and restrictions on part or all of our operations. Our business is highly regulated, and the laws, rules and regulations to which we are subject have been evolving and changing frequently following the economic recession that began in 2008. Recent political shifts in the United States may result in additional significant changes in legislation and regulations that impact us, however, the direction and impact of those changes is not immediately known and some uncertainty may arise as a result. Changing conditions in the real estate and financial markets and the sometimes arduous and uncertain regulatory climate in which they operate also impact our business. Changes to the laws, rules and regulations that affect us are also sometimes retroactively applied. For instance, the Dodd-Frank Act significantly changed the laws as they apply to financial institutions and revised and expanded the rulemaking, supervisory and enforcement authority of federal banking regulators. Some of these changes were effective immediately, others are still being phased in gradually, and some still require additional regulatory rulemaking. As a result, a few of the regulations called for by the Dodd-Frank Act have not yet been completed or are not yet in effect, so not all of the precise contours of that law and its effects on us can be fully understood. In addition, the Trump administration and Republicans controlling Congress have announced that they intend to repeal or revise significant portions of Dodd-Frank and other regulation impacting financial institutions, however, the nature and extent of such repeals or revisions are not presently known. These circumstances lead to additional uncertainty regarding our regulatory environment and the cost and requirements for compliance. We are unable to predict whether U.S. federal, state or local authorities, or other pertinent bodies, will enact legislation, laws, rules, regulations, handbooks, guidelines or similar provisions that will affect our business or require changes in our practices in the future, and any such changes could adversely affect our cost of doing business and profitability.

Changes in regulatory scrutiny of the industry could lead to new regulation of our industry that could in turn create higher costs of compliance, limit our ability to pursue business opportunities and increase our exposure to the judicial system and the plaintiff's bar. Examination findings by the regulatory agencies may also result in adverse consequences to the Company or the Bank. 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. Regulatory authorities have extensive discretion in their supervisory and enforcement activities, including the authority to restrict our operations, including acquisition activity, adversely reclassify our assets, determine the level of deposit premiums assessed, require us to increase our allowance for loan losses, require customer restitution and impose fines or other penalties.

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 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 or force us to discontinue businesses and expose us to additional costs, taxes, liabilities, 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. For instance, we may be limited in our ability to take actions that may be essential to preserve the value of the mortgage loans we service or hold for investment. Any restriction on our ability to foreclose on a loan, any requirement that we forego a portion of the amount otherwise due on a loan or any requirement that we modify any original loan terms may require us to advance principal, interest, tax and insurance payments, which would negatively impact our business, financial condition, liquidity and results of operations. Given the relatively high percentage of our business that derives from originating residential

mortgages, any such actions are likely to have a significant impact on our business, and the effects we experience will likely be disproportionately high in comparison to financial institutions whose residential mortgage lending is more attenuated.

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 with a significant mortgage banking operation, 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. These risks are enhanced because of our growth activities as we integrate operations from our acquisitions and expand our geographic markets. As 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.

Policies and regulations enacted by CFPB may negatively impact our residential mortgage loan business and 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 new 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. The 2014 regulations also require changes to certain loan servicing procedures and practices, which has 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.

On October 3, 2015, the CFPB's Final Integrated Disclosure Rule, commonly known as TRID, became effective. Among other things, TRID requires lenders to combine the initial Good Faith Estimate and Initial Truth in Lending

(“TIL”) 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 procedures changes and training and we have incurred and will continue to incur additional personnel costs in the near future related to compliance with TRID. Failure to comply with these new requirements may result in regulatory penalties for disclosure violations under the Real Estate Settlement Procedures Act (“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 recently adopted 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 will be subject to the disclosure requirements of the rule and expand the categories of information that financial institutions such as the Bank will be required to report with respect to such loans and such borrowers, including potentially sensitive customer information. Most of the rule's provisions are expected to become effective January 1, 2018. These changes may increase our compliance costs due to the

anticipated need for additional resources to meet the enhanced disclosure requirements, including additional personnel and training costs as well as informational systems to allow the Bank to properly capture and report the additional mandated information. The volume of new data that will be required to be reported under the updated rules will also cause the Bank to face an increased risk of errors in the 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 a security breach resulting in the disclosure of sensitive customer information in the event the HMDA reporting files were obtained by an unauthorized party.

While the full impact of CFPB's activities on our business is still unknown, and there is a potential for repeal or significant revision of new and proposed CFPB regulations under the Trump administration, any additional rule changes under the HMDA and other CFPB actions that may follow could increase our compliance costs and require changes in our business practices as a result of new regulations and requirements and could limit the products and services we are able to provide to customers.

Changes to regulatory requirements relating to customer information may increase our cost of doing business and create additional compliance risk.

In May 2016, the Financial Crimes Enforcement Network of the Department of Justice announced that beginning in May 2018, financial institutions would be required to identify the ultimate beneficial owners of all entity clients as part of their customer due diligence compliance. Meeting this new requirement will increase our overall compliance burden and require us to expend additional resources in the review of customers who are entities. In addition, there may be unforeseen challenges in obtaining beneficial ownership information about all of our entity customers, which increases the risk that we will not be in compliance with this new requirement.

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 is being phased in and will take full effect on January 1, 2019. This conservation buffer consists of common equity Tier 1 capital and will ultimately be required to be 2.0% above existing capital ratio requirements, which means that once the conservation buffer is fully phased in, in order to prevent certain regulatory restrictions, the common equity Tier 1 capital ratio requirement will be 7.0%, the Tier 1 risk-based ratio requirement will be 8.5% and the total risk-based capital ratio requirement will be 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 mortgage servicing rights and deferred tax assets. For more on these regulatory requirements and how they apply to the Company and the Bank, see "Regulation and Supervision of HomeStreet Bank - Capital and Prompt Corrective Action Requirements - Capital Requirements" in this Annual Report on Form 10-K. 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.

Any restructuring or replacement of Fannie Mae and Freddie Mac and changes in existing government-sponsored and federal mortgage programs could adversely affect our business.

We originate and purchase, sell and thereafter service single family and multifamily mortgages under the Fannie Mae, and to a lesser extent, the Freddie Mac single family purchase programs and the Fannie Mae multifamily DUS program. In 2008, Fannie Mae and Freddie Mac were placed into conservatorship, and since then Congress, various executive branch agencies and certain large private investors in Fannie Mae and Freddie Mac have offered a wide range of proposals aimed at restructuring these agencies.

We cannot be certain whether or how Fannie Mae and Freddie Mac ultimately will be restructured or replaced, if or when additional reform of the housing finance market will be implemented or what the future role of the U.S. government will be in the mortgage market, and, accordingly, we will not be able to determine the impact that any such reform may have on us until a



definitive reform plan is adopted. However, any restructuring or replacement of Fannie Mae and Freddie Mac that restricts the current loan purchase programs of those entities may have a material adverse effect on our business and results of operations. Moreover, we have recorded on our balance sheet an intangible asset (mortgage servicing rights, or MSR) relating to our right to service single and multifamily loans sold to Fannie Mae and Freddie Mac. We valued our MSR at \$226.1 million at December 31, 2016. Changes in the policies and operations of Fannie Mae and Freddie Mac or any replacement for or successor to those entities that adversely affect our single family residential loan and DUS mortgage servicing assets may require us to record impairment charges to the value of these assets, and significant impairment charges could be material and adversely affect our business.

In addition, our ability to generate income through mortgage sales to institutional investors depends in part on programs sponsored by Fannie Mae, Freddie Mac and Ginnie Mae, which facilitate the issuance of mortgage-backed securities in the secondary market. Any significant revision or reduction in the operation of those programs could have a material adverse effect on our loan origination and mortgage sales as well as our results of operations. Also, any significant adverse change in the level of activity in the secondary market or the underwriting criteria of these entities could negatively impact our results of business, operations and cash flows.

Changes in accounting standards may require us to increase our Allowance for Loan Losses and could materially impact our financial statements.

From time to time, the Financial Accounting Standards Board (the "FASB") and the SEC change the financial accounting and reporting standards that govern the preparation of our financial statements. These changes can materially impact how we record and report our financial condition and results of operations. For example, in June 2016, the FASB issued ASU 2016-13, Financial Instruments - Credit Losses (Topic 326) which changes, among other things, the way companies must record expected credit losses on financial instruments that are not accounted for at fair value through net income, including loans held for investment, available for sale and held-to-maturity debt securities, trade and other receivables, net investment in leases and other commitments to extend credit held by a reporting entity at each reporting date, and require that financial assets measured at amortized cost be presented at the net amount expected to be collected, through an allowance for credit losses that is deducted from the amortized cost basis and eliminate the probable initial recognition in current GAAP and reflect the current estimate of all expected credit losses based upon historical experience, current conditions, and reasonable and supportable forecasts that affect the collectability of the financial assets.

For purchased financial assets with a more-than-insignificant amount of credit deterioration since origination ("PCD assets") that are measured at amortized cost, an allowance for expected credit losses will be recorded as an adjustment to the cost basis of the asset. Subsequent changes in estimated cash flows would be recorded as an adjustment to the allowance and through the statement of income. Credit losses relating to available-for-sale debt securities will be recorded through an allowance for credit losses rather than as a direct write-down to the security's cost basis. The amendments in this ASU will be effective for us beginning on January 1, 2020. For most debt securities, the transition approach requires a cumulative-effect adjustment to the statement of financial position as of the beginning of the first reporting period the guidance is effective. For other-than-temporarily impaired debt securities and PCD assets, the guidance will be applied prospectively. We are currently evaluating the provisions of this ASU to determine the impact and developing appropriate systems to prepare for compliance with this new standard, however, we expect the new standard could have a material impact on the Company's consolidated financial statements.

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, as well as by our policy of retaining a significant portion of our earnings to support the Bank's operations. New capital rules impose more stringent capital requirements to maintain "well capitalized" status which may additionally impact the Bank's ability to pay dividends to the Company. See "Management's Discussion and Analysis of Financial Condition and Results of Operations - Capital Management" as well as "Regulation and Supervision of HomeStreet Bank - Capital and Prompt Corrective Action Requirements" in Item 1 of 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 debts, fund the Company's operations and acquisition plans and pay dividends to the Company's shareholders. While the Company has paid special dividends in some prior quarters, we have not adopted a dividend policy and our board of directors has elected to retain capital for growth rather than to declare a dividend in each of the last eight quarters. As such, our dividends are not regular and are subject to restriction due to cash flow limitations, capital requirements, capital and strategic needs and other factors.

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 on technology to provide financial services. 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 will be subject to heightened regulatory requirements if we exceed \$10 billion in assets.

We anticipate that our total assets could exceed \$10 billion in the next several years, based on our historic organic and acquisition growth rates. The Dodd-Frank Act and its implementing regulations impose various additional requirements on bank holding companies with \$10 billion or more in total assets, including compliance with portions of the Federal Reserve's enhanced prudential oversight requirements and annual stress testing requirements. In addition, banks with \$10 billion or more in total assets are primarily examined by the CFPB with respect to various federal consumer financial protection laws and regulations. Currently, our bank is subject to regulations adopted by the CFPB, but the FDIC is primarily responsible for examining our bank's compliance with consumer protection laws and those CFPB regulations. As a relatively new agency with evolving regulations and practices, there is uncertainty as to how the CFPB's examination and regulatory authority might impact our business.

Compliance with these requirements may necessitate that we hire additional compliance or other personnel, design and implement additional internal controls, or incur other significant expenses, any of which could have a material adverse effect on our business, financial condition or results of operations. Compliance with the annual stress testing requirements, part of which must be publicly disclosed, may also be misinterpreted by the market generally or our customers and, as a result, may adversely affect our stock price or our ability to retain our customers or effectively compete for new business opportunities. To ensure compliance with these heightened requirements when effective, our regulators may require us to fully comply with these requirements or take actions to prepare for compliance even before our or the Bank's total assets equal or exceed \$10 billion. As a result, we may incur compliance-related costs before we might otherwise be required, including if we do not continue to grow at the rate we expect or at all. Our regulators may also consider our preparation for compliance with these regulatory requirements when examining our operations generally or considering any request for regulatory approval we may make, even requests for approvals on unrelated matters.



## 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 are heavily reliant 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 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 implement 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 physical and electronic break-ins, denial of service and other cyber-attacks or security breaches.

We maintain insurance coverage related to business interruptions and breaches of our security systems. However, 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, 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 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 breakdowns or failures of their own systems or capacity constraints. Specifically, we receive core systems processing, essential web hosting and other Internet

systems and deposit and other processing services from third-party service providers. Such third parties may also be target of cyber-attacks, computer viruses, malicious code, unauthorized access, hackers or information security breaches that could compromise the confidential or proprietary information of HomeStreet and our customers. To date none of our third party vendors or service providers has notified us of any security breach in their systems.

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 be materially increased. 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 payment of 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.

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 classified board of directors so that only approximately one third of our board of directors is 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 Mortgage Lending as well as Commercial and Consumer Banking activities in leased and owned locations in Washington, California, Oregon, Hawaii, Idaho, Arizona, Colorado and Utah. We currently lease space for 146 primary and satellite office locations. Of these, we lease 73 Mortgage Banking locations, 55 Commercial and Consumer Banking locations, 10 combined-use Mortgage Banking and Commercial and Consumer Banking location and three combined-use Mortgage Banking and loan fulfillment center locations. We also operate four leased facilities for the purpose of administrative and other functions in addition to the principal offices: a loan fulfillment center and a call center and operations support facility, both located in Federal Way, Washington; and loan fulfillment centers in Pleasanton, California and Vancouver, Washington. We own several properties where our Commercial and Consumer Banking retail deposit branches are or will be located, including properties in Selah, Washington; Edmonds, Washington; Kennewick, Washington; Dayton, Washington; Tacoma, Washington, Granada Hills, California, and an owned building on ground lease in Issaquah, Washington. Furthermore, in January of 2017, we purchased under a separately formed, wholly owned entity the above referenced operations center in Federal Way. The Federal Way lease mentioned above will remain in place. 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

Our common stock is traded on the NASDAQ Global Select Market under the symbol "HMST." The following table sets forth, for the periods indicated, the high and low reported sales prices per share of the common stock as reported on the NASDAQ Global Select Market, our principal trading market.

	High	Low	Special Cash Dividends Declared	
For the Year Ended December 31, 2016				
First quarter ended March 31	\$22.79	\$18.58	\$	—
Second quarter ended June 30	22.97	18.74	—	
Third quarter ended September 30	27.21	19.07	—	
Fourth quarter ended December 31	33.70	24.03	—	
For the Year Ended December 31, 2015				
First quarter ended March 31	\$18.81	\$16.70	\$	—
Second quarter ended June 30	24.43	18.24	—	
Third quarter ended September 30	24.36	20.39	—	
Fourth quarter ended December 31	23.56	20.05	—	

As of March 7, 2017, there were 2,547 shareholders of record of our common stock.

## Dividend Policy

We have not adopted a formal dividend policy and did not pay any dividends in 2016 or 2015. The amount and timing of any future dividends have not been determined. The payment of dividends will depend upon a number of factors, including regulatory capital requirements, the Company's and the Bank's liquidity, financial condition and results of operations, strategic growth plans, tax considerations, statutory and regulatory limitations and general economic conditions. Our ability to pay dividends to shareholders is significantly dependent on the Bank's ability to pay dividends to the Company, which is 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. New capital rules implemented on January 1, 2015 have imposed more stringent requirements on the ability of the Bank to maintain "well-capitalized" status and to pay dividends to the Company. See "Regulation and Supervision of HomeStreet Bank - Capital and Prompt Corrective Action Requirements - Capital Requirements."

For the foregoing reasons, there can be no assurance that we will pay any further special dividends in any future period.

## Sales of Unregistered Securities

There were no sales of unregistered securities in the fourth quarter of 2016.

## Stock Repurchases in the Fourth Quarter

Not applicable.

#### 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, 2016 under the HomeStreet, Inc. 2014 Equity Incentive Plan (the “2014 Plan”).

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Plan Category	(a) Number of Securities to be Issued Upon Exercise of Outstanding Options, Warrants and Rights	(b) Weighted Average Exercise Price of Outstanding Options, Warrants, and Rights	(c) Number of Securities Remaining Available for Future Issuance Under Equity Compensation Plans (Excluding Securities Reflected in Column (a))
Plans approved by shareholders	570,041	(1) \$ 12.46	(2) 505,648 (3)
Plans not approved by shareholders <sup>(4)</sup>	10,800	(4) \$ 1.07	N/A
Total	580,841	\$ 12.00	(2) 505,648

(1) Consists of 257,747 shares subject to option grants awarded pursuant to the HomeStreet, Inc. 2010 Equity Incentive Plan (the "2010 Plan"), 116,043 shares subject to Restricted Stock Units awarded under the 2014 Plan and 196,251 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.

(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. 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.

(4) Consists of retention equity awards granted in 2010 outside of the 2010 Plan but subject to its terms and conditions.

### 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 February 10, 2012 (the date our common stock commenced trading on the NASDAQ Global Select Market) through December 31, 2016 of the cumulative total return for our common stock, the KBW Bank Index (BKX) and the Russell 2000 Index (RUT). The graph assumes that \$100 was invested at the market close on February 10, 2012 in the common stock of HomeStreet, Inc., the KBW Bank Index and the Russell 2000 Index and data for HomeStreet, Inc., the KBW Bank Index and the Russell 2000 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 report.

The following table sets forth selected historical consolidated financial and other data for us at and for each of the periods ended as described below. The selected historical consolidated financial data as of December 31, 2016 and 2015 and for each of the years ended December 31, 2016, 2015 and 2014 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, 2014, 2013 and 2012 and for each of the years ended December 31, 2014, 2013 and 2012 have been derived from our audited consolidated financial statements for those years, which are not included in this Form 10-K. 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,				
	2016	2015	2014	2013	2012
Income statement data (for the period ended):					
Net interest income	\$ 180,049	\$ 148,338	\$ 98,669	\$ 74,444	\$ 60,743
Provision (reversal of provision) for credit losses	4,100	6,100	(1,000)	900	11,500
Noninterest income	359,150	281,237	185,657	190,745	238,020
Noninterest expense	444,322	366,568	252,011	229,495	183,591
Income before income taxes	90,777	56,907	33,315	34,794	103,672
Income tax expense	32,626	15,588	11,056	10,985	21,546
Net income	\$58,151	\$ 41,319	\$ 22,259	\$ 23,809	\$ 82,126
Basic income per share <sup>(1)</sup>	\$2.36	\$ 1.98	\$ 1.50	\$ 1.65	\$ 6.17
Diluted income per share <sup>(1)</sup>	\$2.34	\$ 1.96	\$ 1.49	\$ 1.61	\$ 5.98
Common shares outstanding <sup>(1)</sup>	26,800,183	22,076,534	14,856,611	14,799,991	14,382,638
Weighted average number of shares outstanding:					
Basic <sup>(1)</sup>	24,615,990	20,818,045	14,800,689	14,412,059	13,312,939
Diluted <sup>(1)</sup>	24,843,683	21,059,201	14,961,081	14,798,168	13,739,398
Book value per share <sup>(1)</sup>	\$23.48	\$ 21.08	\$ 20.34	\$ 17.97	\$ 18.34
Dividends per share	\$—	\$—	\$0.11	\$ 0.33	\$—
Financial position (at year end):					
Cash and cash equivalents	\$53,932	\$ 32,684	\$ 30,502	\$ 33,908	\$ 25,285
Investment securities	1,043,851	572,164	455,332	498,816	416,517
Loans held for sale	714,559	650,163	621,235	279,941	620,799
Loans held for investment, net	3,819,027	3,192,720	2,099,129	1,871,813	1,308,974
Mortgage servicing rights	245,860	171,255	123,324	162,463	95,493
Other real estate owned	5,243	7,531	9,448	12,911	23,941
Total assets	6,243,700	4,894,495	3,535,090	3,066,054	2,631,230
Deposits	4,429,701	3,231,953	2,445,430	2,210,821	1,976,835
Federal Home Loan Bank advances	868,379	1,018,159	597,590	446,590	259,090

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Federal funds purchased and securities sold under agreements to repurchase	—	—	50,000	—	—
Total shareholders' equity	\$629,284	\$465,275	\$302,238	\$265,926	\$263,762

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## Summary Financial Data (continued)

(dollars in thousands, except share data)	At or for the Years Ended December 31,					2012
	2016	2015	2014	2013	2012	
Financial position (averages):						
Investment securities	\$834,671	\$523,756	\$459,060	\$515,000		\$410,819
Loans held for investment	3,668,263	2,834,511	1,890,537	1,496,146		1,303,010
Total interest-earning assets	5,307,118	4,150,089	2,869,414	2,422,136		2,167,363
Total interest-bearing deposits	3,145,137	2,499,538	1,883,622	1,661,568		1,644,859
Federal Home Loan Bank advances	942,593	795,368	431,623	293,871		93,325
Total interest-bearing liabilities	4,189,582	3,368,160	2,386,537	2,020,613		1,817,847
Shareholders' equity	566,148	442,105	289,420	249,081		211,329
Financial performance:						
Return on average shareholders' equity <sup>(2)</sup>	10.27	% 9.35	% 7.69	% 9.56	%	38.86 %
Return on average total assets	1.01	% 0.91	% 0.69	% 0.88	%	3.42 %
Net interest margin <sup>(3)</sup>	3.45	% 3.63	% 3.51	% 3.17	% <sup>(4)</sup>	2.89 %
Efficiency ratio <sup>(5)</sup>	82.40	% 85.33	% 88.63	% 86.54	%	61.45 %
Asset quality:						
Allowance for credit losses	\$35,264	\$30,659	\$22,524	\$24,089		\$27,751
Allowance for loan losses/total loans <sup>(6)</sup>	0.88	% 0.91	% 1.04	% 1.26	%	2.06 %
Allowance for loan losses/nonaccrual loans	165.52	% 170.54	% 137.51	% 93.00	%	92.20 %
Total nonaccrual loans <sup>(7)/(8)</sup>	\$20,542	\$17,168	\$16,014	\$25,707		\$29,892
Nonaccrual loans/total loans	0.53	% 0.53	% 0.75	% 1.36	%	2.24 %
Other real estate owned	\$5,243	\$7,531	\$9,448	\$12,911		\$23,941
Total nonperforming assets	\$25,785	\$24,699	\$25,462	\$38,618		\$53,833
Nonperforming assets/total assets	0.41	% 0.50	% 0.72	% 1.26	%	2.05 %
Net (recoveries) charge-offs	\$(505)	\$(2,035)	\$565	\$4,562		\$26,549
Regulatory capital ratios for the Bank:						
Basel III - Tier 1 leverage capital (to average assets)	10.26	% 9.46	% NA	NA		NA
Basel III - Tier 1 common equity risk-based capital (to risk-weighted assets)	13.92	% 13.04	% NA	NA		NA
Basel III - Tier 1 risk-based capital (to risk-weighted assets)	13.92	% 13.04	% NA	NA		NA
Basel III - Total risk-based capital (to risk-weighted assets)	14.69	% 13.92	% NA	NA		NA
Basel I - Tier 1 leverage capital (to average assets)	NA	NA	9.38	% 9.96	%	11.78 %
Basel I - Tier 1 risk-based capital (to risk-weighted assets)	NA	NA	13.10	% 14.12	%	18.05 %
Basel I - Total risk-based capital (to risk-weighted assets)	NA	NA	14.03	% 15.28	%	19.31 %
Regulatory capital ratios for the Company:						
Basel III - Tier 1 leverage capital (to average assets)	9.78	% 9.95	% NA	NA		NA
Basel III - Tier 1 common equity risk-based capital (to risk-weighted assets)	10.54	% 10.52	% NA	NA		NA
Basel III - Tier 1 risk-based capital (to risk-weighted assets)	11.66	% 11.94	% NA	NA		NA
	12.34	% 12.70	% NA	NA		NA

Basel III - Total risk-based capital (to risk-weighted assets)

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(in thousands)	At or for the Years Ended December 31,				
	2016	2015	2014	2013	2012
<b>SUPPLEMENTAL DATA:</b>					
Loans serviced for others					
Single family	\$ 19,488,456	\$ 15,347,811	\$ 11,216,208	\$ 11,795,621	\$ 8,870,688
Multifamily	1,108,040	924,367	752,640	720,429	727,118
Other	69,323	79,513	82,354	95,673	53,235
Total loans serviced for others	\$ 20,665,819	\$ 16,351,691	\$ 12,051,202	\$ 12,611,723	\$ 9,651,041
Loan origination activity					
Single family	\$ 9,214,463	\$ 7,440,612	\$ 4,697,767	\$ 4,852,879	\$ 4,901,073
Other	2,560,549	1,540,455	967,500	603,271	255,435
Total loan origination activity	\$ 11,775,012	\$ 8,981,067	\$ 5,665,267	\$ 5,456,150	\$ 5,156,508

- (1) Share and per share data shown after giving effect to the 2-for-1 forward stock splits effective March 6, 2012 and November 5, 2012.
- (2) Net earnings available to common shareholders divided by average shareholders' equity.
- (3) Net interest income divided by total average interest-earning assets on a tax equivalent basis.  
Net interest margin for the year ended December 31, 2013 included \$1.4 million in interest expense related to the correction of the cumulative effect of an error in prior years, resulting from the under accrual of interest due on the trust preferred securities for which the Company had deferred the payment of interest. Excluding the impact of the prior period interest expense correction, the net interest margin was 3.23% for the year ended December 31, 2013.
- (4) Noninterest expense divided by total revenue (net interest income and noninterest income).
- (5) Includes loans acquired with bank acquisitions. Excluding acquired loans, allowance for loan losses /total loans was 1.00%, 1.10% and 1.10% at December 31, 2016, 2015 and 2014, respectively.
- (6) 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.
- (7) Includes \$1.9 million and \$1.2 million of nonperforming loans at December 31, 2016 and 2015, respectively, which are guaranteed by the Small Business Administration ("SBA").
- (8)

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 the words "anticipate," "believe," "could," "estimate," "expect," "intend," "may," "plan," "potential," "should," "will" and "would" and similar expressions (or their variations) (collectively, "forward-looking 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 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.

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 annual report on Form 10-K.

Executive Summary

HomeStreet is a diversified financial services company founded in 1921 headquartered in Seattle, Washington and serving customers primarily in the western United States, including Hawaii. HomeStreet, Inc. is a bank holding company that has elected to be treated as a financial holding company whose operating subsidiaries are principally engaged in commercial and consumer banking, real estate lending, including mortgage origination and servicing. Our primary subsidiaries are HomeStreet Bank and HomeStreet Capital Corporation.

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

HomeStreet Capital Corporation, a Washington corporation, originates, sells and services multifamily mortgage loans under the Fannie Mae Delegated Underwriting and Servicing Program ("DUS®")<sup>1</sup> in conjunction with HomeStreet Bank. HomeStreet Inc. does business as HomeStreet Insurance, providing insurance products and services for consumers and businesses. We also have a partial ownership in an affiliated business arrangement with WMS Series LLC, doing business as Penrith Home Loans formerly known as Windermere Mortgage Services).

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 investment and insurance sales.

In 2016, we continued to execute our strategy of diversifying earnings by expanding the commercial and consumer banking business; growing our mortgage banking market share in existing and new markets; growing and improving the quality of our deposits; and bolstering our processing, compliance and risk management capabilities. We continue to expand our retail deposit branch network, primarily focusing on high-growth areas of Puget Sound and Southern California, in order to build convenience and market share. We are continuing to expand into markets that are relatively new to us, including opening three de novo branches in the San Diego area, and adding four new branches in Los Angeles and Orange County, two de novo and two acquired from Boston Private Bank & Trust ("Boston Private") in Southern California. As of December 31, 2016 we had 14 retail branches in Southern California. We have also increased stand-alone lending centers in both our existing retail deposit markets as well as Northern California; Salt Lake City, Utah; Phoenix, Arizona; Boise, Idaho; and Denver, Colorado.

As part of our organic growth in commercial real estate lending, in 2015 we launched a new division of the Bank called HomeStreet Commercial Capital, which originates permanent commercial real estate loans, primarily up to \$10 million in size, a

<sup>1</sup> DUS® is a registered trademark of Fannie Mae 43

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portion of which we intend to sell into the secondary market. At the same time, we added another team specializing in originating U.S. Small Business Administration ("SBA") loans. Both of these groups are located in Orange County, California.

In addition to the two branches acquired from Boston Private Bank & Trust, our acquisitions in 2016 have included Orange County Business Bank ("OCBB"), which we merged into HomeStreet Bank, and two retail bank branches and all related deposits and loans from The Bank of Oswego in Lake Oswego, Oregon which expanded our presence in the Portland metropolitan area.

#### Management's Overview of 2016 Financial Performance

At December 31, 2016, we had total assets of \$6.24 billion, net loans held for investment of \$3.82 billion, deposits of \$4.43 billion and shareholders' equity of \$629.3 million. Through the OCBB merger and the four branch acquisitions completed in 2016, we added \$234.1 million of assets, \$166.1 million of loans and \$279.1 million of deposits.

In 2016, we also used security offerings at the holding company to augment capital at the Bank and support strategic growth through issuing \$65.0 million in principal amount of 6.50% senior unsecured notes in May for net proceeds of \$63.2 million and issuing approximately 2.0 million shares of our common stock in a separate equity offering in December with net proceeds of \$58.6 million.

Results for 2016 reflect the continued expansion of our commercial and consumer business and growth of our mortgage banking business. During 2016, we have increased our lending capacity by adding loan origination and operations personnel in all of our lending lines of business. We added four primary lending centers and 11 retail deposit branches to bring our total home loan centers to 48, our total commercial lending centers to five and our total retail deposit branches to 55. We also have one stand-alone insurance office.

#### Consolidated Financial Performance

(in thousands, except per share data and ratios)	At or for the Years Ended December 31,			
	2016	2015	2014	
Selected statement of operations data				
Total net revenue <sup>(1)</sup>	\$539,199	\$429,575	\$284,326	
Total noninterest expense	444,322	366,568	252,011	
Provision (reversal of provision) for credit losses	4,100	6,100	(1,000 )	
Income tax expense	32,626	15,588	11,056	
Net income	\$58,151	\$41,319	\$22,259	
Financial performance				
Diluted income per share	\$2.34	\$1.96	\$1.49	
Return on average common shareholders' equity	10.27	% 9.35	% 7.69	%
Return on average assets	1.01	% 0.91	% 0.69	%
Net interest margin	3.45	% 3.63	% 3.51	%

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

#### Commercial and Consumer Banking Segment Results

Commercial and Consumer Banking segment net income increased 70.9% to \$30.8 million for the year ended December 31, 2016 from \$18.0 million in 2015, primarily due to higher net interest income from higher average balances of interest-earning assets, partially offset by higher noninterest expense, which were the combined result of merger and acquisition activities and organic growth. Included in net income for the years ended December 31, 2016 and 2015 were acquisition related expenses, net of tax of \$4.6 million and \$10.7 million, respectively. For the year ended December 31, 2015, acquisition related expenses were partially offset by a bargain purchase gain of \$7.7 million.

Commercial and Consumer Banking segment net interest income was \$154.0 million for the year ended December 31, 2016, an increase of \$34.0 million, or 28.3%, from \$120.0 million for the year ended December 31, 2015, reflecting higher average balances of loans held for investment as a result of organic growth and acquisitions.

The Company recorded a \$4.1 million of provision for credit losses for the year ended December 31, 2016 compared to a \$6.1 million provision for credit losses for the year ended December 31, 2015. The reduction in credit loss provision in the year was due in part to a continuing decline in historical loss rates as a result of net recoveries for the past two years and continued improvements in portfolio performance which was reflected in the qualitative reserves. In 2015, one-time model adjustments contributed to an increase in provision expense.

Net recoveries were \$505 thousand in 2016 compared to net recoveries of \$2.0 million in 2015. Overall, the allowance for loan losses (which excludes the allowance for unfunded commitments) represented 0.88% of loans held for investment at December 31, 2016 compared to 0.91% at December 31, 2015, which primarily reflected the improved credit quality of the Company's loan portfolio. Excluding acquired loans, the allowance for loan losses was 1.00% of loans held for investment at December 31, 2016 compared to 1.10% at December 31, 2015. Nonperforming assets were \$25.8 million, or 0.41% of total assets at December 31, 2016, compared to \$24.7 million, or 0.50% of total assets at December 31, 2015.

Commercial and Consumer Banking segment noninterest expense of \$138.4 million for the year ended December 31, 2016 increased \$15.8 million, or 12.9%, from \$122.6 million for the year ended December 31, 2015, primarily due to the continued organic growth of our commercial real estate and commercial business lending units and the expansion of our branch banking network and merger and acquisition costs. We added 11 retail deposit branches, six de novo and five from acquisitions, and increased the segment's headcount by 20.5% during the year. During the year ended December 31, 2016, the commercial and consumer banking segment further expanded its network into California through the acquisition of Orange County Business Bank and the acquisition of two branches from Boston Private.

#### Mortgage Banking Segment Results

Mortgage Banking segment net income was \$27.4 million for the year ended December 31, 2016, compared to net income of \$23.3 million for the year ended December 31, 2015. The 17.4% increase in net income is primarily due to a higher gain on single family mortgage loan origination and sale activities due to higher interest rate lock commitments, partially offset by higher noninterest expense resulting from higher closed loan volume, continued growth and expansion of our mortgage banking segment and increased costs from new regulatory disclosure requirements for the mortgage industry and lower risk management results.

Mortgage Banking noninterest income of \$323.5 million for the year ended December 31, 2016 increased \$71.6 million, or 28.43%, from \$251.9 million for the year ended December 31, 2015, primarily due to a 24.4% increase in single family mortgage interest rate lock commitments. Increased interest rate lock commitments reflected growth in the overall segment loan origination capacity through the addition of mortgage production personnel, expansion of our network of mortgage loan centers and higher refinance volumes. We increased our mortgage production personnel by 12.7% at December 31, 2016 compared to December 31, 2015.

Mortgage Banking noninterest expense of \$305.9 million for the year ended December 31, 2016 increased \$62.0 million, or 25.40%, from \$244.0 million for the year ended December 31, 2015, primarily due to increased commissions, salary, insurance, and benefit costs on higher closed loan volume, the continued expansion of personnel and offices, and increased costs resulting from new regulatory disclosure requirements for the mortgage industry. We added 13 home loan centers and increased the segment's headcount by 18.5% during 2016.



## 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 remain above current “well-capitalized” regulatory minimums. Under the Basel III standards, the Bank's Tier 1 leverage and total risk-based capital ratios at December 31, 2016 were 10.26% and 14.69% and at December 31, 2015 were 9.46% and 13.92%, respectively. The Company's Tier 1 leverage and total risk-based capital ratios were 9.78% and 12.34% at December 31, 2016, and 9.95% and 12.70% at December 31, 2015, 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.

## Recent Developments

For details of recent developments, please see "2016 Expansion Growth", "Capital Raising Activities" and "Recent Developments" within Part 1, Item I Business section 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 loan 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, in light of 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"). Once a third-party appraisal is six months old, or 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, we perform an internal collateral valuation to assess whether a change in collateral value requires an additional adjustment to carrying value. A collateral valuation is a restricted-use 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 classes. Loans are designated into loan classes based on loans pooled by 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 quality rating ("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 buckets using two-year analysis periods for commercial segments and one-year analysis periods for consumer segments, 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:

- ending 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 and process;
- 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.

Qualitative 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 qualitative 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 5—Loans and Credit Quality in the notes to the financial statements of this Form 10-K.

#### Fair Value of Financial Instruments, Single Family MSR's and OREO

A portion of our assets are carried at fair value, including single family mortgage servicing rights ("MSR's"), 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 under 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, 2016, 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 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.

In addition to the recurring fair value measurements, from time to time the Company may have certain nonrecurring fair value measurements. These fair value measurements usually result from the application of lower of cost or fair value accounting or impairment of individual assets. As of December 31, 2016 and 2015, the Company's Level 3 nonrecurring fair value measurements were based on the appraised value of collateral used as the basis for the valuation of collateral dependent loans held for investment and OREO.

Real estate valuations are overseen by our appraisal department, which is independent of our lending and credit administration functions. The appraisal department maintains the appraisal policy and recommends changes to the policy subject to approval by the Credit Committee of the Company's Board of Directors and Company's Loan Committee (the "Loan Committee"), established by the Credit Committee of the Company's Board of Directors and comprised of certain of the Company's management. Appraisals are prepared by independent third-party appraisers and our internal appraisers. Appraisals are reviewed either by our in-house appraisal staff or by independent and qualified third-party appraisers.

For further information on the fair value of financial instruments, single family MSR's and OREO, see Note 1–Summary of Significant Accounting Policies, Note 12–Mortgage Banking Operations and Note 17–Fair Value Measurements in the notes to the financial statements of this Form 10-K.

## Income Taxes

In establishing an income tax provision, we must make judgments and interpretations about the application of inherently complex tax laws. We must also make estimates about when in the future certain items will affect taxable income. Our interpretations may be subject to review during examination by taxing authorities and disputes may arise over the respective tax positions. We monitor tax authorities and revise our estimates of accrued income taxes due to changes in income tax laws and their interpretation by the courts and regulatory authorities on a quarterly basis. Revisions of our estimate of accrued income taxes also may result from our own income tax planning and strategies and from the resolution of income tax controversies. Such revisions in our estimates may be material to our operating results for any given reporting period.

Income taxes are accounted for using the asset and liability method, which requires the recognition of deferred tax assets and liabilities for the expected future tax consequences of events that have been included in the financial statements. Under this method, a deferred tax asset or liability is determined based on the differences between the tax basis of assets and liabilities and their reported amounts in the financial statements. The effect of a change in tax rates on deferred tax assets and liabilities is recognized in income in the period that includes the enactment date.

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 such determination, management 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 management 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 Company recognizes potential interest and penalties related to unrecognized tax benefits as income tax expense in the consolidated statements of operations. Accrued interest and penalties are included within the related tax liability line in the consolidated statements of financial condition. For further information regarding income taxes, see Note 14—Income Taxes to the financial statements of this Form 10-K.

#### Business Combinations

The Simplicity and Orange County Business Bank acquisitions, as well as the branch acquisitions were accounted for under the acquisition method of accounting pursuant to ASC 805, Business Combinations. The assets and liabilities, both tangible and intangible, were recorded at their estimated fair values as of acquisition date. Management made significant estimates and exercised significant judgment in estimating the fair values and accounting for such acquired assets and assumed liabilities, and in certain instances received "bargain purchase gains" or "goodwill" in these transactions. The valuation of acquired loans, mortgage servicing rights, premises and equipment, core deposit intangibles, deferred taxes, deposits, Federal Home Loan Bank advances and any contingent liabilities that arise as a result of the transaction are considered preliminary and such fair value estimates are subject to adjustment when additional information relative to the closing date fair values becomes available and such information is considered final or up to one year after the acquisition date or, whichever is earlier.

Management used valuation models to estimate the fair value for certain assets and liabilities. These models incorporate inputs such as forward yield curves, loan prepayment expectations, expected credit loss assumptions, market volatilities, and pricing spreads utilizing market-based inputs where 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 that could be realized in an actual sale or transfer of the asset or liability in a current market exchange.

#### 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.





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(in thousands)	Years Ended December 31,									
	2016			2015			2014			
	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	\$39,962	\$254	0.63 %	\$36,134	\$67	0.18 %	\$31,137	\$58	0.18 %	
Investment securities	834,671	21,611	2.57	523,756	14,270	2.72	459,060	12,945	2.82	
Loans held for sale	764,222	28,581	3.76	755,688	29,165	3.86	488,680	18,569	3.80	
Loans held for investment	3,668,263	162,219	4.40	2,834,511	123,680	4.36	1,890,537	81,659	4.32	
<b>Total interest-earning assets</b>	<b>5,307,118</b>	<b>212,665</b>	<b>4.00</b>	<b>4,150,089</b>	<b>167,182</b>	<b>4.03</b>	<b>2,869,414</b>	<b>113,231</b>	<b>3.95</b>	
Noninterest-earning assets <sup>(2)</sup>	470,021			410,404			335,037			
<b>Total assets</b>	<b>\$5,777,139</b>			<b>\$4,560,493</b>			<b>\$3,204,451</b>			
<b>Liabilities and shareholders' equity:</b>										
<b>Deposits:</b>										
Interest-bearing demand accounts	\$450,838	1,950	0.43 %	\$317,510	\$1,492	0.46 %	\$270,634	\$939	0.35 %	
Savings accounts	299,502	1,029	0.34	284,309	1,053	0.38	173,678	937	0.54	
Money market accounts	1,370,256	7,344	0.53	1,122,321	4,930	0.44	980,045	4,361	0.45	
Certificate accounts	1,024,541	9,086	0.88	775,398	4,501	0.58	459,265	3,244	0.71	
<b>Total interest-bearing deposits</b>	<b>3,145,137</b>	<b>19,409</b>	<b>0.61</b>	<b>2,499,538</b>	<b>11,976</b>	<b>0.48</b>	<b>1,883,622</b>	<b>9,481</b>	<b>0.50</b>	
Federal Home Loan Bank advances	942,593	6,030	0.64	795,368	3,669	0.46	431,623	1,990	0.46	
Federal funds purchased and securities sold under agreements to repurchase	803	6	0.40	11,397	29	0.31	8,977	22	0.25	
Long-term debt	101,049	4,043	3.73	61,857	1,104	1.78	62,315	1,121	1.80	
<b>Total interest-bearing liabilities</b>	<b>4,189,582</b>	<b>29,488</b>	<b>0.70</b>	<b>3,368,160</b>	<b>16,778</b>	<b>0.50</b>	<b>2,386,537</b>	<b>12,614</b>	<b>0.53</b>	
Noninterest-bearing liabilities	1,021,409			750,228			528,494			
<b>Total liabilities</b>	<b>5,210,991</b>			<b>4,118,388</b>			<b>2,915,031</b>			
Shareholders' equity	566,148			442,105			289,420			
<b>Total liabilities and shareholders' equity</b>	<b>\$5,777,139</b>			<b>\$4,560,493</b>			<b>\$3,204,451</b>			
Net interest income <sup>(3)</sup>		\$183,177			\$150,404			\$100,617		
Net interest spread			3.30 %			3.53 %			3.42 %	

Impact of noninterest-bearing sources	0.15 %	0.10 %	0.09 %
Net interest margin	3.45 %	3.63 %	3.51 %

(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) \$3.1 million, \$2.1 million and \$1.9 million for the years ended December 31, 2016, 2015 and 2014, respectively.

The estimated federal statutory tax rate was 35% for the periods presented.

#### 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 \$1.8 million, \$2.5 million and \$2.8 million for the years ended December 31, 2016, 2015 and 2014, 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), (3) changes attributable to changes in rate and volume (change in rate multiplied by change in volume), which were allocated in proportion to the percentage change in average volume and average rate and included in the relevant column and (4) the net change.

(in thousands)	Years Ended December 31,					
	2016 vs. 2015			2015 vs. 2014		
	Increase (Decrease) Due to		Total Change	Increase (Decrease) Due to		Total Change
	Rate	Volume		Rate	Volume	
<b>Assets:</b>						
<b>Interest-earning assets</b>						
Cash and cash equivalents	\$180	\$7	\$187	\$—	\$9	\$9
Investment securities	(1,128)	8,469	7,341	(499)	1,824	1,325
Loans held for sale	(914)	329	(585)	451	10,146	10,597
Loans held for investment	2,191	36,348	38,539	1,247	40,774	42,021
<b>Total interest-earning assets</b>	<b>329</b>	<b>45,153</b>	<b>45,482</b>	<b>1,199</b>	<b>52,753</b>	<b>53,952</b>
<b>Liabilities:</b>						
<b>Deposits</b>						
Interest-bearing demand accounts	(161)	619	458	391	163	554
Savings accounts	(81)	57	(24)	(481)	597	116
Money market accounts	1,325	1,089	2,414	(64)	633	569
Certificate accounts	3,130	1,454	4,584	(942)	2,199	1,257
<b>Total interest-bearing deposits</b>	<b>4,213</b>	<b>3,219</b>	<b>7,432</b>	<b>(1,096)</b>	<b>3,592</b>	<b>2,496</b>
Federal Home Loan Bank advances	1,682	679	2,361	2	1,677	1,679
Securities sold under agreements to repurchase	10	(32)	(22)	1	6	7
Long-term debt	2,242	697	2,939	(9)	(8)	(17)
<b>Total interest-bearing liabilities</b>	<b>8,147</b>	<b>4,563</b>	<b>12,710</b>	<b>(1,102)</b>	<b>5,267</b>	<b>4,165</b>
<b>Total changes in net interest income</b>	<b>\$(7,818)</b>	<b>\$40,590</b>	<b>\$32,772</b>	<b>\$2,301</b>	<b>\$47,486</b>	<b>\$49,787</b>

## Net Income

### Comparison of 2016 to 2015

For the year ended December 31, 2016, net income was \$58.2 million, an increase of \$16.8 million, or 40.7%, from \$41.3 million for the year ended December 31, 2015. Included in net income for the year ended December 31, 2016 were merger-related costs (net of tax) of \$4.6 million. Such merger-related costs (net of tax) relating to prior acquisitions totaled \$10.7 million which were offset by bargain purchase gains of \$7.7 million during 2015.

### Comparison of 2015 to 2014

For the year ended December 31, 2015, net income was \$41.3 million, an increase of \$19.1 million, or 85.6%, compared to net income of \$22.3 million in 2014. Included in net income for the year ended December 31, 2015 were merger-related costs (net of tax) of \$10.7 million offset by bargain purchase gains of \$7.7 million. Such merger-related costs (net of tax) relating to prior acquisitions totaled \$2.0 million during 2014.

## Net Interest Income

### Comparison of 2016 to 2015

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 of Des Moines and the Federal Home Loan Bank of San Francisco ("FHLB").

Net interest income on a tax equivalent basis for the year ended December 31, 2016 increased \$32.8 million, or 21.8%, from December 31, 2015 as a result of growth in average interest earning assets, partially offset by a lower net interest margin. The net interest margin decreased to 3.45% for the year ended December 31, 2016 from 3.63% for the year ended December 31, 2015. The decrease in the net interest margin from the year ended December 31, 2015 was due primarily to shifts in asset mix from growth in lower yielding investment securities and loans held for sale and to higher costs of funds primarily related to our long-term debt issuance in 2016, money market products and FHLB borrowings.

Total average interest-earning assets increased by \$1.16 billion, or 28% in 2016 compared to 2015 primarily as a result of growth in average loans held for investment, both organically and through acquisition activity. Additionally, our average balance of investment securities grew from prior periods as part of the strategic growth of the Company.

Total interest income on a tax equivalent basis in 2016 increased \$45.5 million, or 27.2%, from 2015 resulting from higher average balances of loans held for investment, which increased \$833.8 million, or 29.4%, from 2015.

Total interest expense in 2016 increased \$12.7 million, or 75.8%, from 2015 primarily resulting from higher average balances of interest-bearing deposits and FHLB advances and interest paid on our \$65.0 million in senior debt issued in May 2016.

### Comparison of 2015 to 2014

Net interest income on a tax equivalent basis for the year ended December 31, 2015 increased \$49.8 million, or 49.5%, from December 31, 2014. The net interest margin improved to 3.63% for the year ended December 31, 2015 from 3.51% for the year ended December 31, 2014. The increase in the net interest margin from the year ended December 31, 2014 primarily resulted from higher average balances of higher yielding assets, coupled with a lower cost of interest-bearing funds.

Total average interest-earning assets increased by \$1.28 billion, or 44.63% in 2015 compared to 2014 primarily as a result of growth in average loans held for investment, both from originations and from the March 2015 merger with Simplicity. Additionally, the growth in our average loans held for investment resulted from increased commercial portfolio lending as we continued to grow our Commercial and Consumer Banking segment. Total average interest-bearing deposit balances increased from 2014 primarily due to growth in certificates of deposit accounts, mostly from the Simplicity merger.

Total interest income on a tax equivalent basis in 2015 increased \$54.0 million, or 47.6%, from 2014 resulting from higher average balances of loans held for investment, which increased \$944.0 million, or 49.9%, from 2014.

Total interest expense in 2015 increased \$4.2 million, or 33.0%, from 2014 primarily resulting from higher average balances of interest-bearing deposits and FHLB advances, partially offset by a 3 basis point reduction in the cost of such funds.

#### 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 improved since December 31, 2015 as illustrated by the credit trends below.

#### Comparison of 2016 to 2015

The Company recorded a \$4.1 million provision for credit losses of for the year ended December 31, 2016 compared to a \$6.1 million provision for credit losses for the year ended December 31, 2015. The reduction in credit loss provision in the year was due in part to a continuing decline in historical loss rates as a result of net recoveries for the past two years and continued improvements in portfolio performance which was reflected in the qualitative reserves. In 2015, one-time model adjustments contributed to an increase in provision expense.

Nonaccrual loans were \$20.5 million at December 31, 2016, an increase of \$3.4 million, or 19.7%, from \$17.2 million at December 31, 2015. Nonaccrual loans as a percentage of total loans remained steady at 0.53% at both December 31, 2016 and December 31, 2015. Net loan loss recoveries were \$505 thousand in 2016 compared to net loan loss recoveries of \$2.0 million in 2015. Overall, the allowance for credit losses, which includes the reserve for unfunded commitments, was \$35.3 million, or 0.92% of loans held for investment at December 31, 2016, compared to \$30.7 million, or 0.95% of loans held for investment at December 31, 2015.

#### Comparison of 2015 to 2014

The Company recorded a \$6.1 million provision for credit losses for the year ended December 31, 2015 compared to a \$1.0 million reversal of provision for credit losses for the year ended December 31, 2014. The additional credit loss provision in the year was due in part to overall growth in loans held for investment, and in part to an extension in the modeled loan loss emergence period for commercial loans and higher qualitative reserves for construction loans. These factors were partially offset by the favorable impact of net loan loss recoveries during the year.

Nonaccrual loans were \$17.2 million at December 31, 2015, an increase of \$1.2 million, or 7.2%, from \$16.0 million at December 31, 2014. Nonaccrual loans as a percentage of total loans decreased to 0.53% at December 31, 2015 from 0.75% at December 31, 2014. Net recoveries were \$2.0 million in 2015 compared to net charge-offs of \$565 thousand in 2014. Overall, the allowance for credit losses, which includes the reserve for unfunded commitments, was \$30.7 million, or 0.95% of loans held for investment at December 31, 2015, compared to \$22.5 million, or 1.06% of loans held for investment at December 31, 2014.

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 consisted of the following.

(in thousands)	Years Ended December 31,		Percent Change	2015	Dollar Change	Percent Change	2014
	2016	Dollar Change					
Noninterest income							
Gain on mortgage loan origination and sale activities <sup>(1)</sup>	\$307,313	\$70,925	30 %	\$236,388	\$92,266	64 %	\$144,122 <sup>(2)</sup>
Mortgage servicing income	35,940	11,509	47	24,431	(9,661 )	(28 )	34,092 <sup>(3)</sup>
Income from WMS Series LLC	2,333	709	44	1,624	1,523	1,508	101
Loss on debt extinguishment	—	—	NM	—	573	NM	(573 )
Depositor and other retail banking fees	6,790	909	15	5,881	2,309	65	3,572
Insurance agency commissions	1,619	(63 )	(4 )	1,682	529	46	1,153
Gain on sale of investment securities available for sale	2,539	133	6	2,406	48	2	2,358
Bargain purchase gain	—	(7,726 )	NM	7,726	7,726	NM	—
Other	2,616	1,517	138	1,099	267	32	832
Total noninterest income	\$359,150	\$77,913	28 %	\$281,237	\$95,580	51 %	\$185,657

NM = not meaningful

(1) Single family and multifamily mortgage banking activities.

(2) Includes \$4.6 million in pre-tax gain resulting from the sale of loans that were originally held for investment during 2014.

(3) Includes pre-tax income of \$4.7 million, net of transaction costs, resulting from the sale of single family MSRs during 2014.

## Comparison of 2016 to 2015

Our noninterest income is heavily dependent upon our single family mortgage banking activities, which are comprised of mortgage origination and sale as well as mortgage servicing activities. The level of our mortgage banking activity fluctuates and is highly sensitive to changes in mortgage interest rates, as well as to general economic conditions such as employment trends and housing supply and affordability. The increase in noninterest income in 2016 compared to 2015 was primarily the result of higher gain on mortgage loan origination and sale activities mostly due to increased single family mortgage interest rate lock commitments and higher mortgage servicing income. Included in noninterest income for 2015 was a bargain purchase gain of \$7.7 million from the Simplicity merger and our acquisition of a branch in Dayton, Washington. No similar bargain purchase gains occurred in 2016.

## Comparison of 2015 to 2014

The increase in noninterest income in 2015 compared to 2014 was primarily the result of higher gain on mortgage loan origination and sale activities mostly due to increased single family mortgage interest rate lock commitments. As noted above, noninterest income for 2015 includes a bargain purchase gain of \$7.7 million from the Simplicity merger and the Dayton branch acquisition. Included in noninterest income for 2014 were a \$4.7 million pre-tax net increase in mortgage servicing income resulting from the sale of MSRs and a \$4.6 million pre-tax gain on single family mortgage origination and sale activities from the sale of loans that were originally held for investment.





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

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

(in thousands)	Years Ended December 31,				2015	Dollar Change	Percent Change	2014
	2016	Dollar Change	Percent Change					
Single family held for sale:								
Servicing value and secondary market gains <sup>(1)</sup>	\$260,477	\$54,964	27 %	\$205,513	\$96,450	88 %	\$109,063	
Loan origination and administrative fees	29,966	7,745	35	22,221	(3,351 )	(13 )	25,572	
Total single family held for sale	290,443	62,709	28	227,734	93,099	69	134,635	
Multifamily DUS	11,397	4,272	60	7,125	2,402	51	4,723	
Other <sup>(3)</sup>	5,473	3,944	258	1,529	(3,235 )	(68 )	4,764 <sup>(2)</sup>	
Gain on mortgage loan origination and sale activities	\$307,313	\$70,925	30 %	\$236,388	\$92,266	64 %	\$144,122	

NM = not meaningful

Comprised of gains and losses on interest rate lock commitments (which considers the value of servicing), single (1)family loans held for sale, forward sale commitments used to economically hedge secondary market activities, and changes in the Company's repurchase liability for loans that have been sold.

(2)Includes \$4.6 million in pre-tax gain resulting from the sale of loans that were originally held for investment.

(3)Includes multifamily loans from sources other than DUS.

Single family production volumes related to loans designated for sale consisted of the following.

(in thousands)	For The Years Ended December 31,				2015	Dollar Change	Percent Change	2014
	2016	Dollar Change	Percent Change					
Single family mortgage closed loan volume <sup>(1)</sup>	\$8,997,347	\$1,784,912	25 %	\$7,212,435	\$2,811,818	64 %	\$4,400,617	
Single family mortgage interest rate lock commitments <sup>(1)</sup>	\$8,620,976	\$1,689,868	24 %	\$6,931,108	\$2,586,860	60 %	\$4,344,248	

(1)Includes loans originated by WMS Series LLC and purchased by HomeStreet Bank.

#### Comparison of 2016 to 2015

The increase in gain on mortgage loan origination and sale activities in 2016 compared to 2015 predominantly reflected higher single family mortgage interest rate lock commitments as a result of the expansion of our mortgage lending network, higher loan production per loan producer and higher refinance volumes. Mortgage production personnel grew by 12.7% at December 31, 2016 compared to December 31, 2015.

#### Comparison of 2015 to 2014

The increase in gain on mortgage loan origination and sale activities in 2015 compared to 2014 predominantly reflected higher single family mortgage interest rate lock commitments as a result of the expansion of our mortgage lending network, higher loan production per loan producer and higher refinance volumes. Mortgage production personnel grew by 14.6% during 2015 compared to 2014.



Management records a liability for estimated mortgage repurchase losses, which has 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 13, Commitments, Guarantees and Contingencies to the financial statements in this Form 10-K.

(in thousands)	Years Ended December 31,		
	2016	2015	2014
Effect of changes to the mortgage repurchase liability recorded in gain on mortgage loan origination and sale activities:			
New loan sales <sup>(1)</sup>	\$ (3,574)	\$ (2,764)	\$ (1,570)
Other changes in estimated repurchase losses <sup>(2)</sup>	2,032	—	140
	\$ (1,542)	\$ (2,764)	\$ (1,430)

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

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

Mortgage servicing income consisted of the following.

(in thousands)	Years Ended December 31,							
	2016	Dollar Change	Percent Change	2015	Dollar Change	Percent Change	2014	
Servicing income, net:								
Servicing fees and other	\$56,535	\$14,338	34 %	\$42,197	\$4,379	12 %	\$37,818	
Changes in fair value of MSR due to modeled amortization <sup>(1)</sup>	(33,305 )	733	(2 )	(34,038 )	(7,926 )	30	(26,112 )	
Amortization of multifamily MSRs	(2,635 )	(643 )	32	(1,992 )	(280 )	16	(1,712 )	
	20,595	14,428	234	6,167	(3,827 )	(38 )	9,994	
Risk management:								
Changes in fair value of MSR due to changes in market inputs and/or model updates <sup>(2)</sup>	20,025	13,470	205	6,555	22,184	(142)	(15,629 ) <sup>(3)</sup>	
Net (loss) gain from derivatives economically hedging MSRs	(4,680 )	(16,389 )	(140)	11,709	(28,018 )	(71 )	39,727	
	15,345	(2,919 )	(16 )	18,264	(5,834 )	(24 )	24,098	
Mortgage servicing income	\$35,940	\$11,509	47 %	\$24,431	\$ (9,661)	(28 )%	\$34,092	
NM = not meaningful								

(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 income of \$4.7 million, net of brokerage fees and prepayment reserves, resulting from the sale of single family MSRs during 2014.

#### Comparison of 2016 to 2015

The increase in mortgage servicing income in 2016 compared to 2015 was primarily due to higher servicing income, net, offset by lower risk management results. The higher servicing income was primarily attributed to higher servicing

fees on higher average balances of loans serviced for others and lower modeled amortization. Mortgage servicing fees collected in 2016 increased compared to 2015 primarily as a result of higher average balances of loans serviced for others during the year. Our loans serviced for others portfolio was \$20.67 billion at December 31, 2016 compared to \$16.35 billion at December 31, 2015.

MSR risk management results represent changes in the fair value of single family MSRs 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 on prepayment speeds. MSRs typically decrease in value when interest

rates decline because declining interest rates tend to increase mortgage prepayment speeds and therefore reduce 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. The lower risk management results in 2016 were mainly due to adverse results during the fourth quarter driven by the unexpected and significant increases in long-term Treasury rates beginning in November 2016 following the U.S. presidential election, coinciding with an increase in short-term interest rates by the Federal Reserve in December 2016. The unexpected and sustained increase in interest rates during the quarter resulted in asymmetrical changes in valuation between hedging derivatives and servicing valuations. This market dislocation in the fourth quarter reduced the value of our hedging derivatives to a greater extent than value of our mortgage servicing rights increased, resulting in lower risk management results.

#### Comparison of 2015 to 2014

The decrease in mortgage servicing income in 2015 compared to 2014 was primarily due to MSR risk management results. The lower net gain from our MSR risk management activities for 2015 was primarily attributable to a pre-tax gain of \$4.7 million included in 2014, resulting from the sale of single family MSRs, as well as an increased benefit due to changes in model assumptions in 2014 than in 2015, to better align observed borrower prepayment behavior with modeled borrower prepayment behavior.

Mortgage servicing fees collected in 2015 increased compared to 2014 primarily as a result of higher average balances of loans serviced for others during the year. Our loans serviced for others portfolio was \$16.35 billion at December 31, 2015 compared to \$12.05 billion at December 31, 2014. The lower balance at December 31, 2014 was the result of the June 2014 sale of the rights to service \$2.96 billion of single family mortgage loans.

#### Income from WMS Series LLC

##### Comparison of 2016 to 2015

Income from WMS Series LLC increased by \$709 thousand in 2016 to \$2.3 million compared to \$1.6 million in 2015 primarily due to a 15.1% increase in interest rate lock commitments and a 10.9% increase in closed loan volume, which were \$647.3 million and \$684.1 million, respectively, in 2016 compared to \$562.2 million and \$616.9 million, respectively, for the same period in 2015.

##### Comparison of 2015 to 2014

Income from WMS Series LLC increased by \$1.5 million in 2015 to \$1.6 million compared to \$101 thousand in 2014 primarily due to a 23.5% increase in interest rate lock commitments and a 25.6% increase in closed loan volume, which were \$562.2 million and \$616.9 million, respectively, in 2015 compared to \$455.2 million and \$491.3 million, respectively, for the same period in 2014.

Depositor and other retail banking fees for 2016 increased from 2015 primarily due to an increase in the number of transaction accounts as we grew our retail deposit branch network both organically and through acquisition. The following table presents the composition of depositor and other retail banking fees for the periods indicated.

(in thousands)	Years Ended December 31,		
	2016	2015	2014

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	Dollar	Percent		Dollar	Percent		Dollar	Percent
	Change	Change		Change	Change		Change	Change
Fees:								
Monthly maintenance and deposit-related fees	\$2,952	\$ 295	11 %	\$2,657	\$ 1,025	63 %	\$1,632	
Debit Card/ATM fees	3,621	476	15	3,145	1,247	66	1,898	
Other fees	217	138	175	79	37	88	42	
Total depositor and other retail banking fees	\$6,790	\$ 909	15 %	\$5,881	\$ 2,309	65 %	\$3,572	

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## Noninterest Expense

Noninterest expense consisted of the following.

(in thousands)	Years Ended December 31,						
	2016	Dollar Change	Percent Change	2015	Dollar Change	Percent Change	2014
Noninterest expense							
Salaries and related costs	\$303,354	\$62,767	26 %	\$240,587	\$77,200	47 %	\$163,387
General and administrative	63,206	6,385	11	56,821	15,083	36	41,738
Amortization of core deposit intangibles	2,166	242	13	1,924	829	76	1,095
Legal	1,867	(940 )	(33 )	2,807	736	36	2,071
Consulting	4,958	(2,257 )	(31 )	7,215	3,991	124	3,224
Federal Deposit Insurance Corporation assessments	3,414	841	33	2,573	257	11	2,316
Occupancy	30,530	5,603	22	24,927	6,329	34	18,598
Information services	33,063	4,009	14	29,054	9,002	45	20,052
Net cost of operation and sale of other real estate owned	1,764	1,104	167	660	1,130	(240)	(470 )
Total noninterest expense	\$444,322	\$77,754	21 %	\$366,568	\$114,557	45 %	\$252,011

The following table shows the acquisition-related expenses impacting the components of noninterest expense.

(in thousands)	Years Ended December 31,		
	2016	2015	2014
Noninterest expense			
Salaries and related costs	\$4,128	\$7,672	\$482
General and administrative	633	1,463	606
Legal	132	830	493
Consulting	1,500	5,703	1,179
Occupancy	180	382	15
Information services	563	514	281
Total noninterest expense	\$7,136	\$16,564	\$3,056

## Comparison of 2016 to 2015

The increase in noninterest expense in 2016 compared to 2015 was primarily due to increased commissions on higher closed loan volume, as well as other costs related to the growth in offices and personnel in connection with our expansion of our commercial and consumer and mortgage banking businesses, both organically and through acquisition-related activities.

Included in noninterest expense in 2016 was \$7.1 million of acquisition-related costs compared to \$16.6 million in 2015 primarily related to the Simplicity merger.

Salaries and related costs increased primarily due to a 19.3% increase in full-time equivalent employees at December 31, 2016 compared to December 31, 2015 and higher commission and incentive expense, as single family



mortgage closed loan volumes increased 24.7%, from 2015.

General and administrative and Information services costs increased primarily due to increased headcount and continued growth of our mortgage banking business and expansion of our commercial and consumer business.

Comparison of 2015 to 2014

The increase in noninterest expense in 2015 compared to 2014 was primarily due to increased salaries and related costs, general

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and administrative costs, and information services costs, primarily a result of the integration of the operations and personnel of Simplicity as well as organic growth in personnel in connection with our continued expansion of our commercial and consumer and mortgage banking businesses.

Included in noninterest expense in 2015 was \$16.6 million of acquisition-related costs primarily related to Simplicity. Such acquisition-related costs from prior acquisitions totaled \$3.1 million in 2014.

Salaries and related costs increased primarily due to a 32.8% increase in full-time equivalent employees at December 31, 2015 compared to December 31, 2014 and higher commission and incentive expense, as single family mortgage closed loan volumes increased 63.9%, from 2014.

General and administrative and Information services costs increased primarily due to increased headcount and continued growth of our mortgage banking business and expansion of our commercial and consumer business.

#### Income Tax Expense

##### Comparison of 2016 to 2015

For the year ended December 31, 2016, income tax expense was \$32.6 million with an effective tax rate of 35.9% (inclusive of discrete items) compared to income tax expense of \$15.6 million and an effective tax rate of 27.4% (inclusive of discrete items) for the year ended December 31, 2015.

The Company's effective income tax rate for the year ended December 31, 2016 differs from the Federal statutory tax rate of 35% primarily due to the impact of state income taxes, tax-exempt interest income and low income housing tax credit investments.

##### Comparison of 2015 to 2014

The Company's income tax expense for 2015 was \$15.6 million, representing an effective tax rate of 27.4%. In 2014, the Company's tax expense was \$11.1 million, representing an effective tax rate of 33.2%. The Company's effective income tax rate for the year ended December 31, 2015 was significantly less than the Federal statutory tax rate of 35% primarily due to the impact of state income taxes, tax-exempt interest income, low income housing tax credit investments, the Simplicity transaction, 2014 tax return true-up adjustments, and a deferred tax consequence previously reflected in equity.

Our discrete items for the year ended December 31, 2015 resulted in a net reduction of approximately 7.0% to the effective tax rate, largely due to bargain purchase gain from the Simplicity acquisition and the recognition of a deferred tax consequence previously recorded in equity.

#### Capital Expenditures

##### Comparison of 2016 to 2015

During 2016, our net expenditures for property and equipment were \$24.5 million, compared to net expenditures of \$20.6 million during 2015, as we continued the expansion of our commercial and consumer and mortgage banking businesses.

##### Comparison of 2015 to 2014

During 2015, our net expenditures for property and equipment were \$20.6 million, compared to net expenditures of \$19.9 million during 2014, as we continued the expansion of our commercial and consumer and mortgage banking businesses.

Review of Financial Condition – Comparison of December 31, 2016 to December 31, 2015

Total assets were \$6.24 billion at December 31, 2016 and \$4.89 billion at December 31, 2015. The OCBB merger added \$189.2 million of acquired assets and \$8.4 million of goodwill to our balance sheet in 2016. Additionally, in 2016, through the acquisition of two branches from The Bank of Oswego and two branches from Boston Private, we added \$41.6 million and \$3.2 million of assets, respectively.

Cash and cash equivalents were \$53.9 million at December 31, 2016 compared to \$32.7 million at December 31, 2015, an increase of \$21.2 million, or 65.0%.

Investment securities were \$1.04 billion at December 31, 2016 compared to \$572.2 million at December 31, 2015, an increase of \$471.7 million, or 82.4%, primarily due to the temporary deployment of excess capital from the 2016 debt and equity issuances and from the execution of our strategic growth and diversification.

We primarily hold investment securities for liquidity purposes, while also creating a relatively stable source of interest income. We designated substantially all securities as available for sale. We held securities having a carrying value of \$49.9 million at December 31, 2016, 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,			
	2016		2015	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
Investment securities available for sale:				
Mortgage-backed securities:				
Residential	\$181,158	\$177,074	\$69,342	\$68,101
Commercial	25,896	25,536	18,142	17,851
Municipal bonds	473,153	467,673	168,722	171,869
Collateralized mortgage obligations:				
Residential	194,982	191,201	86,167	84,497
Commercial	71,870	70,764	80,190	79,133
Corporate debt securities	52,045	51,122	81,280	78,736
U.S. Treasury securities	10,882	10,620	41,047	40,964
Total investment securities available for sale	\$1,009,986	\$993,990	\$544,890	\$541,151

Mortgage-backed securities ("MBS") and collateralized mortgage obligations ("CMO") represent securities issued by government sponsored entities. Each 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 municipalities. As of December 31, 2016 and 2015, 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, 2016 and 2015, substantially all securities held by the Company had ratings available by external ratings agencies.

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 4, Investment Securities to the financial statements of this Form 10-K.

Each of the MBS and CMO securities in our investment portfolio are guaranteed by Fannie Mae, Ginnie Mae or Freddie Mac. 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 premium or accretion of discount relating to such instruments, thereby changing the net yield on such securities. At December 31, 2016, the aggregate net premium associated with our MBS portfolio was \$10.1 million, or 4.5%, of the aggregate unpaid principal balance, compared with \$6.9 million or 6.3% at December 31, 2015. The aggregate net premium associated

with our CMO portfolio as of December 31, 2016 was \$4.8 million, or 1.8%, of the aggregate unpaid principal balance, compared with \$4.6 million, or 2.8%, at December 31, 2015. 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, which may result from credit deterioration of the issuer, changes in market interest rates relative to the rate of the instrument or changes in prepayment speeds. 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 has been impaired 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, 2016 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, 2016 were considered other than temporary.

Loans held for sale were \$714.6 million at December 31, 2016 compared to \$650.2 million at December 31, 2015, an increase of \$64.4 million, or 9.9%. Loans held for sale include single family and multifamily residential loans, typically sold within 30 days of closing the loan.

Loans held for investment, net increased \$626.3 million, or 19.6%, from December 31, 2015. Our single family loan portfolio decreased \$119.4 million from 2015. Our multifamily loan portfolio increased \$247.7 million from 2015, primarily as a result of the growth of our commercial and consumer banking segment, both organically and through acquisitions. Our construction loans, including commercial construction and residential construction, increased \$53.2 million from 2015, primarily from new originations in our commercial real estate and residential construction lending 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.

	At December 31,		2015		2014		2013		2012		
(in thousands)	Amount	Percent	Amount	Percent	Amount	Percent	Amount	Percent	Amount	Percent	
Consumer loans:											
Single family	\$1,083,822	28.2 %	\$1,203,180	37.3 %	\$896,665	42.2 %	\$904,913	47.7 %	\$673,865	50.3 %	
Home equity and other	359,874	9.3	256,373	8.0	135,598	6.4	135,650	7.1	136,746	10.2	
	1,443,696	37.5	1,459,553	45.3	1,032,263	48.6	1,040,563	54.8	810,611	60.5	
Commercial loans:											
Commercial real estate <sup>(2)</sup>	871,563	22.7	600,703	18.6	523,464	24.6	477,642	25.1	361,879	27.0	
Multifamily	674,219	17.5	426,557	13.2	55,088	2.6	79,216	4.2	17,012	1.3	
Construction/land development	636,320	16.5	583,160	18.1	367,934	17.3	130,465	6.9	71,033	5.3	
Commercial business	223,653	5.8	154,262	4.8	147,449	6.9	171,054	9.0	79,576	5.9	
	2,405,755	62.5	1,764,682	54.7	1,093,935	51.4	858,377	45.2	529,500	39.5	
	3,849,451	100.0%	3,224,235	100.0%	2,126,198	100.0%	1,898,940	100.0%	1,340,111	100.0%	
Net deferred loan fees and costs	3,577		(2,237)		(5,048)		(3,219)		(3,576)		
	3,853,028		3,221,998		2,121,150		1,895,721		1,336,535		

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Allowance for loan losses	(34,001 )	(29,278 )	(22,021 )	(23,908 )	(27,561 )
	\$3,819,027	\$3,192,720	\$2,099,129	\$1,871,813	\$1,308,974

Includes \$18.0 million and \$21.5 million of loans at December 31, 2016 and 2015 respectively, where a fair value (1) 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.

December 31, 2016, 2015 and 2014 balances comprised of \$282.9 million, \$154.9 million and \$143.8 million of (2) owner-occupied loans, respectively, and \$588.7 million, \$445.8 million and \$379.6 million of non-owner-occupied loans, respectively.

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

(in thousands)	At December 31,			
	2016 Amount	Percent	2015 Amount	Percent
Adjustable-rate loans:				
Single family	\$657,837	17.1 %	\$686,927	21.3 %
Commercial	701,694	18.3	450,424	14.0
Multifamily	655,271	17.0	417,217	12.9
Construction/land development, net <sup>(1)</sup>	355,111	9.2	334,235	10.4
Commercial business	143,960	3.7	87,970	2.7
Home equity and other	51,837	1.3	59,605	1.8
Total adjustable-rate loans	2,565,710	66.6	2,036,378	63.2
Fixed-rate loans:				
Single family	425,985	11.1	516,253	16.0
Commercial	169,869	4.4	150,280	4.7
Multifamily	18,949	0.5	9,339	0.3
Construction/land development, net <sup>(1)</sup>	281,209	7.3	248,925	7.7
Commercial business	79,693	2.1	66,292	2.1
Home equity and other	308,036	8.0	196,768	6.1
Total fixed-rate loans	1,283,741	33.4	1,187,857	36.8
Total loans held for investment	3,849,451	100.0%	3,224,235	100.0%
Less:				
Net deferred loan fees and costs	3,577		(2,237 )	
Allowance for loan losses	(34,001 )		(29,278 )	
Loans held for investment, net	\$3,819,027		\$3,192,720	

(1) Construction/land development is presented net of the undisbursed portion of the loan commitment.



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

(in thousands)	December 31, 2016			Total	Loans due after one year by rate characteristic	
	Within one year	After one year through five years	After five years		Fixed-rate	Adjustable-rate
Consumer:						
Single family	\$7,327	\$4,878	\$1,071,618	\$1,083,823	\$418,923	\$657,573
Home equity and other	7,156	27,879	324,838	359,873	304,328	48,390
Total consumer	14,483	32,757	1,396,456	1,443,696	723,251	