UMPQUA HOLDINGS CORP
Form 10-K
February 21, 2019
United States
Securities and Exchange Commission
Washington, D.C. 20549

FORM 10-K
[X] Annual Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
for the fiscal year ended: December 31, 2018
[ ] 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: 001-34624

Umpqua Holdings Corporation
(Exact Name of Registrant as Specified in Its Charter)

| | |
|---|---|
| OREGON | 93-1261319 |
| (State or Other Jurisdiction of Incorporation or Organization) | (I.R.S. Employer Identification Number) |

One SW Columbia Street, Suite 1200
Portland, Oregon 97258
(Address of Principal Executive Offices)(Zip Code)

(503) 727-4100
(Registrant's Telephone Number, Including Area Code)

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

| Title of each class | Name of each exchange on which registered |
|---|---|
| Common Stock | The NASDAQ Global Select Market |

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

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

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of the Form 10-K or any amendment to the Form 10-K. [X]

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

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

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

The aggregate market value of the voting common stock held by non-affiliates of the registrant as of June 30, 2018, based on the closing price on that date of $22.59 per share, and 218,926,715 shares held was $4,945,554,492.

Indicate the number of shares outstanding of each of the registrant's classes of common stock, as of the latest practical date:
The number of shares of the Registrant's common stock (no par value) outstanding as of January 31, 2019 was 220,296,659.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Proxy Statement for the 2019 Annual Meeting of Shareholders of Umpqua Holdings Corporation ("Proxy Statement") are incorporated by reference in this Form 10-K in response to Part III, Items 10, 11, 12, 13 and 14.

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UMPQUA HOLDINGS CORPORATION
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PART I

ITEM 1. BUSINESS.

In this Annual Report on Form 10-K, we refer to Umpqua Holdings Corporation as the "Company," "Umpqua," "we," "us," "our," or similar references.

This Annual Report on Form 10-K contains certain forward-looking statements, within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934, which are intended to be covered by the safe harbor for "forward-looking statements" provided by the Private Securities Litigation Reform Act of 1995. These statements may include statements that expressly or implicitly predict future results, performance or events. Statements other than statements of historical fact are forward-looking statements. You can find many of these statements by looking for words such as "anticipates," "expects," "believes," "estimates," "intends" and "forecast" and words or phrases of similar meaning. We make forward-looking statements regarding projected sources of funds; Next Gen initiatives; investments in data, analytics and technology; our securities portfolio; loan sales; adequacy of our allowance for loan and lease losses and reserve for unfunded commitments; provision for loan and lease losses; impaired loans and future losses; performance of troubled debt restructurings; our commercial real estate portfolio, its collectability and subsequent charge-offs; resolution of non-accrual loans; litigation; dividends; junior subordinated debentures; mortgage servicing rights values; tax rates and the effect of accounting pronouncements. Forward-looking statements involve substantial risks and uncertainties, many of which are difficult to predict and are generally beyond our control. There are many factors that could cause actual results to differ materially from those contemplated by these forward-looking statements. Risks and uncertainties include those set forth in our filings with the Securities and Exchange Commission (the "SEC") and the following factors that might cause actual results to differ materially from those presented:

- our ability to successfully implement and sustain information technology product and system enhancements and operational initiatives;
- our ability to attract new deposits and loans and leases on acceptable terms;
- our ability to retain deposits and customer relationships during store consolidations;
- demand for financial services in our market areas;
- competitive market pricing factors;
- our ability to effectively develop and implement new technology;
- deterioration in economic conditions that could result in increased loan and lease losses, especially those risks associated with concentrations in real estate related loans;
- market interest rate volatility;
- prolonged low interest rate environments;
- compression of our net interest margin;
- stability and cost of funding sources
- continued availability of borrowings and other funding sources such as brokered and public deposits;
- changes in legal or regulatory requirements or the results of regulatory examinations that could increase expenses or restrict growth;
- our ability to recruit and retain key management and staff;
- availability of and competition for acquisition opportunities;
- risks associated with merger and acquisition integration;
- significant decline in the market value of the Company that could result in an impairment of goodwill;
- our ability to raise capital or incur debt on reasonable terms;
- regulatory limits on the Bank's ability to pay dividends to the Company;
- financial services reform and the impact legislation and implementing regulations on our business operations, including our compliance costs, interest expense, and revenue;

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- a breach or failure of our operational or security systems, or those of our third-party vendors, including as a result of cyberattacks; and
- competition, including from financial technology companies.

For a more detailed discussion of some of the risk factors, see the section entitled "Risk Factors" below. We do not intend to update any factors, except as required by SEC rules, or to publicly announce revisions to any of our forward-looking statements. Any forward-looking statement speaks only as of the date that such statement was made. You should consider any forward-looking statements in light of this explanation, and we caution you about relying on forward-looking statements.

Introduction

Umpqua Holdings Corporation, an Oregon corporation, was formed as a bank holding company in March 1999. At that time, we acquired 100% of the outstanding shares of South Umpqua Bank, an Oregon state-chartered bank formed in 1953. We became a financial holding company in March 2000 under the provisions of the Gramm-Leach-Bliley Act of 1999 ("GLB Act"). Umpqua has two principal operating subsidiaries, Umpqua Bank (the "Bank") and Umpqua Investments, Inc. ("Umpqua Investments").

We electronically file annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, proxy and information statements and other information with the SEC. You may obtain these reports and statements, and any amendments, from the SEC's website at www.sec.gov. You may obtain copies of these reports, and any amendments, through our website at www.umpquabank.com. These reports are available through our website as soon as reasonably practicable after they are filed electronically with the SEC.

General Background

Headquartered in Roseburg, Oregon, Umpqua Bank is considered one of the most innovative community banks in the United States, recognized nationally and internationally for its unique company culture and customer experience strategy, which we believe differentiate the Company from its competition. The Bank provides a broad range of banking, wealth management, mortgage and other financial services to corporate, institutional, and individual customers, and also has a wholly-owned subsidiary, Financial Pacific Leasing Inc., a commercial equipment leasing company.

Umpqua Investments is a registered broker-dealer and registered investment advisor with offices in Oregon, Washington, and California, and also offers products and services through Umpqua Bank stores. The firm is one of the oldest investment companies in the Northwest. Umpqua Investments offers a full range of investment products and services including: stocks, fixed income securities (municipal, corporate, and government bonds, CDs, and money market instruments), mutual funds, annuities, options, retirement planning, advisory account services, goals-based planning and insurance.

Along with its subsidiaries, the Company is subject to the regulations of state and federal agencies and undergoes regular examinations by these regulatory agencies.

Business Strategy

Umpqua Bank's primary objective is to become the leading community-oriented financial services organization throughout the Western United States. We intend to increase market share, grow our assets and increase profitability and shareholder value by differentiating ourselves from competitors through the following strategies:

Use Human Digital Banking Approach to Retain and Expand Customer Base. As consumer preferences evolve with technological changes, our strategy remains consistent: deliver an extraordinary experience across all customer touchpoints. As a result, we've developed our Human Digital banking approach, which uses technology to empower deeper, even more meaningful relationships with our customers. We believe this differentiates Umpqua and positions the Company well to adapt quickly as customer use of physical and digital channels evolves. We believe that by introducing this combination of personal and digital banking services through platforms like Umpqua Go-To, we're enhancing our ability to attract a broader range of customers and expand our value proposition across all channels.

Capitalize on Innovative Product Delivery System. Our philosophy has been to create a unique delivery model that transforms banking from a chore into an experience that's both relevant to customers and highly differentiated from other financial institutions. With this approach in mind, we maintain a bank store concept designed to reflect customer and community preferences and drive revenue growth by making the Bank's products and services more tangible and accessible.

Deliver on Strategic Initiative. The Company's 3-year (2018 - 2020) strategic initiative, "Umpqua Next Gen," is designed to modernize the company, diversify and increase revenue, and streamline expenses. Umpqua Next Gen builds on the customer-centric approach to banking, allowing us to differentiate ourselves in the marketplace and create a competitive advantage. This strategy is called Human Digital banking, an approach that helps the Company transform into an organization that uses technology, data and analytics to empower our associates to build deeper, more valuable, and more profitable customer relationships. During 2018, we launched our Go-To application, which puts customers in touch with their accounts as well as with their own financial advisor.

Focus on Customer Experience. At every level of the Company, from the Board of Directors to our newest associates, and across all customer service delivery channels, we are focused on delivering an extraordinary customer experience. It is an integral part of our culture, and we believe we are among the first banks to introduce a measurable quality service program. Under our Return on Quality or ROQ program, the performance of each sales associate and store is evaluated based on specific measurable factors, including reports by incognito "mystery shoppers" and customer surveys. Based on scores achieved, Umpqua's ROQ program rewards both individual sales associates and store teams with financial incentives. Through such programs, we are able to measure the quality of the experience provided to our customers and maintain employee focus on quality customer service.

Establish Strong Brand Awareness. As a financial services provider, we devote considerable resources to developing the "Umpqua Bank" brand. This is done through design strategy, marketing, merchandising, and delivery through our customer-facing channels, as well as through active public relations, social media and community-based events and initiatives. From Bank-branded bags of custom roasted coffee beans to educational seminars, in-store events and social giving campaigns, Umpqua's goal is to connect with our customers and communities in fresh and engaging ways. The unique look and feel of our stores and interactive displays help demonstrate our commitment to being an innovative, customer-friendly provider of financial products and services, and our active community engagement and investments stand out with commercial customers. Our brand activation approach is based on actions, not just advertising, and builds strong consumer awareness of our products and services.

Prudently Manage Capital. An important part of our strategy is to continue to manage capital prudently, and to employ excess capital in a thoughtful and opportunistic manner that improves shareholder returns and minimizes risk to capital. We accomplish this through organic growth, dividends, and nominal share repurchases. We also opportunistically pursue strategic acquisitions, which could include technology-driven enterprises or banks and financial services companies in markets where we see growth potential.

Marketing and Sales

Our goal of increasing our share of financial services in our market areas is driven by a technology, marketing, communications and sales strategy with the following key components:

Integrated Marketing and Communications. Our comprehensive marketing and communications strategy aims to strengthen the Umpqua Bank brand and generate public awareness through innovative marketing initiatives that stand out in our markets and our industry. The Bank has been recognized nationally for its use of new media and unique approach. From the Bank's Local Spotlight program, ice cream trucks and social giving platform, to interactive community activation initiatives, Umpqua is leveraging both traditional and emerging media channels in new ways to advance the brand and create meaningful connections with consumers.

Retail Store Concept. The physical environment continues to play a critical role both in creating awareness of our brand and franchise, as well as in successfully providing the right products and services to our customers. Using a more retailer-oriented approach, we encourage existing and potential customers to come in to our physical locations. To that end, we design our physical locations to display financial services and products in ways that are highly tactile and engaging. Unlike many financial institutions, we encourage all in our communities to visit our stores, where they are greeted by well-trained associates and encouraged to browse our products and services. Our "Next Gen" store model includes features like free wireless, free use of laptop computers, open rooms with refrigerated beverages and innovative product packaging.

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Growth Culture. We believe strongly that by investing in the growth of our associates, customers and communities, we will create more opportunity to provide our products and services and to create deeper customer relationships across all divisions, from retail to mortgage and wholesale. Although a successful marketing program will attract customers to visit, well-trained associates are critical to solving customer needs with the right products and services. Umpqua's culture has become well established throughout the organization due to a clear focus and ongoing training of our associates on all aspects of sales and service. We provide training through our in-house training to recognize and celebrate associates who demonstrate an exceptional commitment to our customers and deliver smart financial solutions our customers value. This service culture has become iconic in our industry, and is a key element in our ability to attract both talented associates and loyal customers.

Products and Services

We offer an array of traditional and digital financial products to meet the banking needs of our market area and target customers. To ensure the ongoing viability of our product offerings, we regularly examine the desirability and profitability of existing and potential new products. Other avenues through which customers can access our products include our Go-To app and redesigned web site.

Deposit Products. We offer deposit products, including non-interest bearing checking accounts, interest bearing checking and savings accounts, money market accounts and certificates of deposit. Interest-bearing accounts earn interest at rates established by management based on competitive market factors and management's desire to increase certain types or maturities of deposit liabilities. Our approach is to provide a streamlined customer experience that meets the customer's needs across all channels. This approach is designed to add value for the customer, increase products per household and generate related fee income.

Private Bank. Umpqua Private Bank serves high net worth individuals and nonprofits, providing investment services. The private bank is designed to augment Umpqua's existing high-touch customer experience, and works collaboratively with the Bank's affiliate Umpqua Investments to offer a comprehensive, integrated approach that meets clients' financial goals, including financial planning, trust services, and investments.

Wealth Management. In its combined role as a broker/dealer and a registered investment advisor, Umpqua Investments may provide comprehensive financial planning advice to its clients as well as investment services. This advice can include cash management, risk management (insurance planning/sales), investment planning (including investment advice and/or portfolio checkups), retirement planning (for employees and employers), or estate planning. The broker/dealer side of Umpqua Investments offers a full range of brokerage services including equity and fixed income products, mutual funds, annuities, options and life insurance products. At December 31, 2018, Umpqua Investments had 57 Series 7-licensed financial advisors serving clients at stand-alone retail brokerage offices, as well as "Investment Opportunity Centers" located in select Bank stores.

Commercial Loans and Leases and Commercial Real Estate Loans. We offer specialized loans for corporate and commercial customers, including accounts receivable and inventory financing, multifamily loans, equipment loans, commercial equipment leases, international trade, real estate construction loans and permanent financing and Small Business Administration ("SBA") program financing as well as capital markets and treasury management services. Additionally, we offer specially designed loan products for small businesses through our Small Business Division, and have a business banking division to increase lending to small and mid-sized businesses. Ongoing credit management activities continue to focus on commercial real estate loans given this is a significant portion of our loan portfolio. We are also engaged in initiatives that continue to diversify the loan portfolio including a strong focus on commercial and industrial loans in addition to financing owner-occupied properties.

Residential Real Estate Loans. Real estate loans are available for the construction, purchase, and refinancing of residential owner-occupied and rental properties. Borrowers can choose from a variety of fixed and adjustable rate options and terms. We sell most residential real estate loans that we originate into the secondary market. Servicing is retained on the majority of these loans. We also support the Home Affordable Refinance Program and Home Affordable Modification Program.

Consumer Loans. We provide loans to individual borrowers for a variety of purposes, including secured and unsecured personal loans, home equity and personal lines of credit and motor vehicle loans.

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Market Area and Competition

The geographic markets we serve are highly competitive for deposits, loans, leases and retail brokerage services. We compete with traditional banking institutions, as well as non-bank financial service providers, such as credit unions, brokerage firms and mortgage companies. In our primary market areas of Oregon, Washington, California, Idaho, and Nevada, major national banks generally hold dominant market share positions. By virtue of their larger capital bases, these institutions have significantly larger lending limits than we do, generally have more expansive branch networks, and can invest in technology on a larger scale than we can. Competition also includes other commercial banks that are community-focused.

As the industry becomes increasingly oriented toward technology-driven delivery systems, permitting transactions to be conducted on mobile devices and computers, non-bank institutions are able to attract funds and provide lending and other financial services even without offices located in our primary service area. Some insurance companies and brokerage firms compete for deposits by offering rates that are higher than may be appropriate for the Bank in relation to its asset and liability management objectives. However, we offer a wide array of deposit products and believe we can compete effectively through rate-driven product promotions. We also compete with full service investment firms for non-bank financial products and services offered by Umpqua Investments.

Credit unions present a significant competitive challenge for our banking services and products. As credit unions currently enjoy an exemption from income tax, they are able to offer higher deposit rates and lower loan rates than banks can on a comparable basis. Credit unions are also not currently subject to certain regulatory constraints, such as the Community Reinvestment Act ("CRA"), which, among other things, requires us to implement procedures to make and monitor loans throughout the communities we serve. Adhering to such regulatory requirements raises the costs associated with our lending activities, and reduces potential operating profits. Accordingly, we seek to compete by focusing on building customer relationships, providing superior service and offering a wide variety of commercial banking products, such as commercial real estate loans, inventory and accounts receivable financing, and SBA program loans for qualified businesses.

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The following tables presents the Bank's market share percentage for total deposits as of June 30, 2018, in each county where we have operations. The table also indicates the ranking by deposit size in each market. All information in the table was obtained from S&P Global, which compiles deposit data published by the Federal Deposit Insurance Corporation ("FDIC") as of June 30, 2018 and updates the information for any bank mergers and acquisitions completed subsequent to the reporting date.

| Oregon | | | | Washington | | | |
|---|---|---|---|---|---|---|---|
| County | Market Share | Market Rank | Number of Stores | County | Market Share | Market Rank | Number of Stores |
| Baker | 29.8 % | 1 | 1 | Adams | 21.4 % | 3 | 2 |
| Benton | 7.5 % | 6 | 2 | Asotin | 18.4 % | 2 | 1 |
| Clackamas | 3.0 % | 7 | 3 | Benton | 5.1 % | 8 | 2 |
| Columbia | 16.9 % | 3 | 1 | Clallam | 4.5 % | 8 | 2 |
| Coos | 39.5 % | 1 | 5 | Clark | 14.9 % | 3 | 8 |
| Curry | 45.1 % | 1 | 2 | Douglas | 10.9 % | 3 | 1 |
| Deschutes | 8.5 % | 6 | 5 | Franklin | 7.3 % | 7 | 1 |
| Douglas | 68.8 % | 1 | 8 | Grant | 7.9 % | 6 | 2 |
| Grant | 21.5 % | 3 | 1 | Grays Harbor | 7.9 % | 4 | 1 |
| Harney | 25.3 % | 2 | 1 | King | 1.6 % | 10 | 20 |
| Jackson | 18.4 % | 1 | 7 | Kitsap | 0.9 % | 15 | 1 |
| Josephine | 19.0 % | 2 | 4 | Kittitas | 16.5 % | 3 | 2 |
| Klamath | 31.4 % | 1 | 3 | Klickitat | 35.4 % | 1 | 2 |
| Lake | 30.6 % | 2 | 1 | Lewis | 13.3 % | 2 | 3 |
| Lane | 16.6 % | 2 | 6 | Okanogan | 22.4 % | 2 | 2 |
| Lincoln | 8.3 % | 6 | 2 | Pierce | 3.5 % | 8 | 8 |
| Linn | 14.9 % | 4 | 3 | Skamania | 66.5 % | 1 | 1 |
| Malheur | 20.5 % | 2 | 3 | Snohomish | 1.2 % | 19 | 1 |
| Marion | 6.4 % | 7 | 3 | Spokane | 18.3 % | 2 | 9 |
| Multnomah | 4.5 % | 6 | 14 | Thurston | 3.1 % | 10 | 4 |
| Polk | 6.7 % | 6 | 1 | Walla Walla | 3.3 % | 6 | 2 |
| Tillamook | 29.4 % | 2 | 1 | Whatcom | 3.1 % | 11 | 3 |
| Umatilla | 5.5 % | 6 | 2 | Whitman | 5.4 % | 8 | 1 |
| Union | 22.3 % | 2 | 2 | | | | |
| Wallowa | 24.5 % | 2 | 1 | | | | |
| Washington | 7.0 % | 5 | 6 | | | | |
| Yamhill | 2.7 % | 9 | 1 | | | | |

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California

| County | Market Share | Market Rank | Number of Stores |
|---|---|---|---|
| Amador | 4.8 % | 7 | 1 |
| Butte | 2.6 % | 10 | 1 |
| Calaveras | 25.7 % | 2 | 3 |
| Colusa | 43.9 % | 1 | 2 |
| Contra Costa | 0.4 % | 17 | 3 |
| El Dorado | 5.8 % | 6 | 3 |
| Glenn | 28.7 % | 2 | 2 |
| Humboldt | 25.0 % | 1 | 5 |
| Lake | 19.9 % | 2 | 2 |
| Los Angeles | 0.1 % | 63 | 3 |
| Marin | 1.6 % | 12 | 3 |
| Mendocino | 4.2 % | 6 | 1 |
| Napa | 9.1 % | 4 | 5 |
| Orange | 0.6 % | 28 | 1 |
| Placer | 4.1 % | 6 | 6 |
| Sacramento | 0.8 % | 14 | 5 |
| San Diego | 0.2 % | 30 | 2 |
| San Francisco | 0.2 % | 17 | 3 |
| San Joaquin | 0.6 % | 17 | 1 |
| San Luis Obispo | 0.5 % | 11 | 1 |
| Santa Clara | 0.0 % | 38 | 1 |
| Shasta | 2.0 % | 8 | 1 |
| Solano | 3.3 % | 8 | 3 |
| Sonoma | 3.7 % | 9 | 8 |
| Stanislaus | 0.9 % | 15 | 2 |
| Sutter | 10.7 % | 5 | 2 |
| Tehama | 15.0 % | 2 | 2 |
| Trinity | 37.4 % | 2 | 1 |
| Tuolumne | 13.5 % | 4 | 2 |
| Ventura | 0.2 % | 22 | 1 |
| Yolo | 2.2 % | 10 | 1 |
| Yuba | 23.0 % | 3 | 2 |

Idaho

| County | Market Share | Market Rank | Number of Stores |
|---|---|---|---|
| Ada | 0.4 % | 17 | 2 |
| Benewah | 20.3 % | 3 | 1 |
| Idaho | 43.4 % | 1 | 1 |
| Kootenai | 2.3 % | 9 | 2 |
| Latah | 24.3 % | 2 | 2 |
| Nez Perce | 16.2 % | 3 | 1 |
| Valley | 26.5 % | 3 | 2 |

Nevada

| | | | |
|---|---|---|---|
| Washoe | 3.4 % | 7 | 4 |

Lending and Credit Functions

The Bank makes both secured and unsecured loans to individuals and businesses. At December 31, 2018, commercial real estate, commercial, residential, and consumer and other represented approximately 50.4%, 23.1%, 23.6%, and 2.9%, respectively, of the total loan and lease portfolio.

Inter-agency guidelines adopted by federal bank regulators mandate that financial institutions establish real estate lending policies with maximum allowable real estate loan-to-value limits, subject to an allowable amount of non-conforming loans as a percentage of capital. We have adopted as loan policy loan-to-value limits that range from 5% to 10% less than the federal guidelines for each category; however, policy exceptions are permitted for real estate loan customers with strong financial credentials.

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Loans and Leases
We manage asset quality and control credit risk through diversification of the loan and lease portfolio and the application of policies designed to promote sound underwriting and loan and lease monitoring practices. The Bank's Credit Quality Group is charged with monitoring asset quality, establishing credit policies and procedures and enforcing the consistent application of these policies and procedures across the Bank. The provision for loan and lease losses charged to earnings is based upon management's judgment of the amount necessary to maintain the allowance at a level adequate to absorb probable incurred losses. The amount of provision charged is dependent upon many factors, including loan and lease growth, net charge-offs, changes in the composition of the loan and lease portfolio, delinquencies, management's assessment of loan and lease portfolio quality, general economic conditions that can impact the value of collateral, and other trends. The evaluation of these factors is performed through an analysis of the adequacy of the allowance for loan and lease losses. Reviews of non-performing, past due loans and leases and larger credits, designed to identify potential charges to the allowance for loan and lease losses, and to determine the adequacy of the allowance, are conducted on a quarterly basis. These reviews consider such factors as the financial strength of borrowers, the value of the applicable collateral, loan and lease loss experience, estimated loan and lease losses, growth in the loan and lease portfolio, prevailing economic conditions and other factors.
Employees
As of December 31, 2018, we had a total of 3,928 full-time equivalent employees. None of the employees are subject to a collective bargaining agreement and management believes its relations with employees to be good. Information regarding employment agreements with our executive officers is contained in Item 11 below, which item is incorporated by reference to our proxy statement for the 2019 annual meeting of shareholders.
Government Policies
The operations of our subsidiaries are affected by state and federal legislative and regulatory changes and by policies of various regulatory authorities, including, domestic monetary policies of the Board of Governors of the Federal Reserve System ("Federal Reserve"), United States fiscal policy, and capital adequacy and liquidity constraints imposed by federal and state regulatory agencies.
Supervision and Regulation
General.  We are extensively regulated under federal and state law. These laws and regulations are generally intended to protect depositors and customers, not shareholders. To the extent that the following information describes statutory or regulatory provisions, it is qualified in its entirety by reference to the particular statute or regulation. Any change in applicable laws or regulations may have a material effect on our business and prospects. We cannot accurately predict the nature or the extent of the effects on our business and earnings that fiscal or monetary policies, or new federal or state legislation or regulation may have in the future. Umpqua is subject to the disclosure and other requirements of the Securities Act of 1933, as amended, and the Securities Exchange Act of 1934, as amended, and rules promulgated thereunder and administered by the Securities and Exchange Commission. As a listed company on NASDAQ, Umpqua is subject to NASDAQ rules for listed companies.
The Federal Reserve and the FDIC have adopted non-capital safety and soundness standards for financial institutions. These standards cover internal controls, information and internal audit systems, loan documentation, credit underwriting, interest rate exposure, asset growth, compensation, fees and benefits, and standards for asset quality, earnings and stock valuation. An institution that fails to meet these standards must develop a plan acceptable to the agency, specifying the steps that it will take to meet the standards. Failure to submit or implement such a plan may subject the institution to regulatory sanctions.
Holding Company Regulation.  We are a registered financial holding company under the GLB Act, and are subject to the supervision of, and regulation by the Federal Reserve. As a financial holding company, we are examined by and file reports with the Federal Reserve. The Federal Reserve expects a bank holding company to serve as a source of financial and managerial strength to its subsidiary bank and, under appropriate circumstances, to commit resources to support the subsidiary bank.
Financial holding companies are bank holding companies that satisfy certain criteria and are permitted to engage in activities that traditional bank holding companies are not. The qualifications and permitted activities of financial holdings companies are described below under "Regulatory Structure of the Financial Services Industry."

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Federal and State Bank Regulation. Umpqua Bank, as a state chartered bank with deposits insured by the FDIC, is primarily subject to the supervision and regulation of the Oregon Department of Consumer and Business Services Division of Financial Regulation ("DCBS"), the Washington Department of Financial Institutions ("DFI"), the California Department of Business Oversight ("DBO"), the Idaho Department of Finance Banking Section, the Nevada Division of Financial Institutions, the FDIC and the Consumer Financial Protection Bureau ("CFPB"). These agencies may prohibit the Bank from engaging in what they believe constitute unsafe or unsound banking practices. Our primary state regulator, DCBS, regularly examines the Bank or participates in joint examinations with the FDIC.
Community Reinvestment Act and Fair Lending Laws. Umpqua Bank has a responsibility under the CRA, as implemented by FDIC regulations, to help meet the credit needs of its communities, including low and moderate-income neighborhoods. The CRA does not establish specific lending requirements or programs for financial institutions nor does it limit an institution's discretion to develop the types of products and services that it believes are best suited to its particular community, consistent with the CRA. In connection with its examination, the FDIC assesses Umpqua Bank's record of compliance with the CRA. In addition, the Equal Credit Opportunity Act and the Fair Housing Act prohibit discrimination in lending practices on the basis of characteristics specified in those statutes. These factors are also considered in evaluating mergers, acquisitions and applications to open a branch or new facility. Umpqua Bank's failure to comply with the provisions of the CRA could, at a minimum, result in regulatory restrictions on its activities and the activities of Umpqua potentially resulting in the suspension of any growth of the Bank through acquisitions or opening de novo branches until the rating is improved. Umpqua Bank's failure to comply with the Equal Credit Opportunity Act and the Fair Housing Act could result in enforcement actions against it by the FDIC, as well as other federal regulatory agencies, including the CFPB and the Department of Justice. As of the most recent CRA examination, the Bank's CRA rating was "Satisfactory".

Transactions with Affiliates and Insiders. Banks are also subject to certain restrictions imposed by the Federal Reserve Act on extensions of credit to executive officers, directors, principal shareholders or any related interest of such persons. Extensions of credit must be made on substantially the same terms, including interest rates and collateral, and follow credit underwriting procedures that are not less stringent than, those prevailing at the time for comparable transactions with persons not affiliated with the bank, and must not involve more than the normal risk of repayment or present other unfavorable features. Banks are also subject to certain lending limits and restrictions on overdrafts to such persons. A violation of these restrictions may result in the assessment of substantial civil monetary penalties on the affected bank or any officer, director, employee, agent or other person participating in the conduct of the affairs of that bank, the imposition of a cease and desist order, and other regulatory sanctions.
The Federal Reserve Act and related Regulation W limit the amount of certain loan and investment transactions between the Bank and its affiliates, require certain levels of collateral for such loans, and limit the amount of advances to third parties that may be collateralized by the securities of Umpqua or its subsidiaries. Regulation W requires that certain transactions between the Bank and its affiliates be on terms substantially the same, or at least as favorable to the Bank, as those prevailing at the time for comparable transactions with or involving nonaffiliated companies or, in the absence of comparable transactions, on terms and under circumstances, including credit standards, that in good faith would be offered to or would apply to nonaffiliated companies. Umpqua and its subsidiaries have adopted an Affiliate Transactions Policy and have entered into various affiliate agreements in compliance with Regulation W.
Financial Privacy. Federal law and certain state laws currently contain client privacy protection provisions. These provisions limit the ability of banks and other financial institutions to disclose non-public information about consumers to affiliated companies and non-affiliated third parties. These rules require disclosure of privacy policies to clients and, in some circumstances, allow consumers to prevent disclosure of certain personal information to affiliates or non-affiliated third parties by means of opt out or opt in authorizations. Pursuant to the Gramm-Leach-Bliley Act and certain state laws, companies are required to notify clients of security breaches resulting in unauthorized access to their personal information. In connection with the regulations governing the privacy of consumer financial information, the federal banking agencies have also adopted guidelines for establishing information security standards and programs to protect such information.

Federal Deposit Insurance. Substantially all deposits with Umpqua Bank are insured up to applicable limits by the Deposit Insurance Fund ("DIF") of the FDIC and are subject to deposit insurance assessments to maintain the DIF. The standard maximum federal deposit insurance amount is $250,000 per qualified account.

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The FDIC may terminate the deposit insurance of any insured depository institution if it determines that the institution has engaged in or is engaging in unsafe and unsound banking practices, is in an unsafe or unsound condition or has violated any applicable law, regulation or order or any condition imposed in writing by, or pursuant to, any written agreement with the FDIC. The termination of deposit insurance for the Bank would have a material adverse effect on our financial condition and results of operations.

Dividends. Under the Oregon Bank Act and the Federal Deposit Insurance Corporation Improvement Act of 1991 ("FDICIA"), the Bank is subject to restrictions on the payment of cash dividends to its parent company. A bank may not pay cash dividends if that payment would reduce the amount of its capital below that necessary to meet minimum applicable regulatory capital requirements. In addition, under the Oregon Bank Act, the amount of the dividend paid by the Bank may not be greater than net unreserved retained earnings, after first deducting to the extent not already charged against earnings or reflected in a reserve, all bad debts, which are debts on which interest is unpaid and past due at least six months unless the debt is fully secured and in the process of collection; all other assets charged-off as required by Oregon bank regulators or a state or federal examiner; and all accrued expenses, interest and taxes of the Bank. In addition, state and federal regulatory authorities are authorized to prohibit banks and holding companies from paying dividends that would constitute an unsafe or unsound banking practice. The Federal Reserve has issued a policy statement on the payment of cash dividends by bank holding companies, which expresses the Federal Reserve's view that a bank holding company should pay cash dividends only to the extent that its net income for the past year is sufficient to cover both the cash dividends and a rate of earnings retention that is consistent with the holding company's capital needs, asset quality, and overall financial condition.

Capital Adequacy. The federal and state bank regulatory agencies use capital adequacy guidelines in their examination and regulation of holding companies and banks. If capital falls below the minimum levels established by these guidelines, a holding company or a bank may be denied approval to acquire or establish additional banks or non-bank businesses or to open new facilities.

The FDIC and Federal Reserve have adopted risk-based capital guidelines for holding companies and banks. The risk-based capital guidelines are designed to make regulatory capital requirements more sensitive to differences in risk profile among holding companies and banks, to account for off-balance sheet exposure and to minimize disincentives for holding liquid assets. Assets and off-balance sheet items are assigned to broad risk categories, each with appropriate weightings. The resulting capital ratios represent capital as a percentage of total risk-weighted assets and off-balance sheet items. The capital adequacy guidelines limit the degree to which a holding company or bank may leverage its equity capital.

On July 2, 2013, federal banking regulators approved final rules that revised the regulatory capital rules to incorporate certain revisions by the Basel Committee on Banking Supervision to the Basel capital framework ("Basel III"). The phase-in period for the final rules began for the Company on January 1, 2015, originally full compliance with the final rules' requirements was to be phased in on January 1, 2019. On November 21, 2017, the federal banking regulators finalized a halt in the phase-in of certain provisions of the rule for certain banks including Umpqua.

The final rules, among other things, include a new common equity Tier 1 capital ("CET1") to risk-weighted assets ratio, including a capital conservation buffer. The required CET1 ratio was to gradually increase from 4.5% on January 1, 2015 to 7.0% on January 1, 2019. The final rules would also have raised the minimum ratio of Tier 1 capital to risk-weighted assets from 6.0%, the minimum as of December 31, 2018, to 8.5% on January 1, 2019, as well as require a minimum leverage ratio of 4.0%. Under the final rules, as Umpqua grew above $15.0 billion in assets as a result of an acquisition, the combined trust preferred security debt issuances were phased out of Tier 1 and into Tier 2 capital.

The final rules had provided for a number of adjustments to and deductions from the new CET1. Deductions included, for example, the requirement that mortgage servicing rights, certain deferred tax assets not dependent upon future taxable income and significant investments in non-consolidated financial entities be deducted from CET1 to the extent that any one such category exceeds 10% of CET1 or all such categories in the aggregate exceed 15% of CET1. Effective on January 1, 2018, the full transition to the Basel III treatment has been halted.

Under Basel III, the effects of certain accumulated other comprehensive items are not excluded; however, the Company and the Bank, have made a one-time permanent election to continue to exclude these items in order to avoid significant variations in the level of capital depending upon the impact of interest rate fluctuations on the fair value of the Company's securities portfolio.

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FDICIA requires federal banking regulators to take "prompt corrective action" with respect to a capital-deficient institution, including requiring a capital restoration plan and restricting certain growth activities of the institution. Umpqua could be required to guarantee any such capital restoration plan required of the Bank if the Bank became undercapitalized. Pursuant to FDICIA, regulations were adopted defining five capital levels: well capitalized, adequately capitalized, undercapitalized, severely undercapitalized and critically undercapitalized. Under the regulations, the Bank is considered "well capitalized" as of December 31, 2018.

Federal and State Regulation of Broker-Dealers. Umpqua Investments is regulated by the Financial Industry Regulatory Authority ("FINRA"), as well as the SEC, and has customer funds, excluding decline in value of securities, insured through the Securities Investors Protection Corporation ("SIPC") as well as third party insurers. FINRA and the SEC perform regular examinations of Umpqua Investments that include reviews of policies, procedures, recordkeeping, trade practices, and customer protection as well as other inquiries.

Effects of Government Monetary Policy. Our earnings and growth are affected not only by general economic conditions, but also by the fiscal and monetary policies of the federal government, particularly the Federal Reserve. The Federal Reserve implements national monetary policy for such purposes as curbing inflation and combating recession, through its open market operations in U.S. Government securities, control of the discount rate applicable to borrowings from the Federal Reserve, and establishment of reserve requirements against certain deposits. These activities influence growth of bank loans, investments and deposits, and also affect interest rates charged on loans or paid on deposits. The nature and impact of future changes in monetary policies and their impact on us cannot be predicted with certainty.

Regulation of the Financial Services Industry. Federal laws and regulations governing banking and financial services underwent significant changes in recent years and we believe will continue to undergo significant changes in the future. From time to time, legislation is introduced in the United States Congress that contains proposals for altering the structure, regulation, and competitive relationships of the nation's financial institutions. If enacted into law, these proposals could increase or decrease the cost of doing business, limit or expand permissible activities, or affect the competitive balance among banks, savings associations, and other financial institutions. Whether or in what form any such legislation may be adopted or the extent to which our business might be affected thereby cannot be predicted.

The GLB Act, enacted in November 1999, repealed sections of the Banking Act of 1933, commonly referred to as the Glass-Steagall Act, that prohibited banks from engaging in securities activities, and prohibited securities firms from engaging in banking. The GLB Act created a new form of holding company, known as a financial holding company, that is permitted to acquire subsidiaries that are engaged in banking, securities underwriting and dealing, and insurance underwriting.

To qualify as a financial holding company, the bank holding company must be deemed to be well-capitalized and well-managed, as those terms are used by the Federal Reserve. In addition, each subsidiary bank of a bank holding company must also be well-capitalized and well-managed and be rated at least "satisfactory" under the CRA. A bank holding company that does not qualify, or has not chosen, to become a financial holding company must limit its activities to traditional banking activities and those non-banking activities the Federal Reserve has deemed to be permissible because they are closely related to the business of banking.

The Riegle-Neal Interstate Banking and Branching Efficiency Act of 1994 ("Riegle-Neal Act") permits interstate banking and branching, which allows banks to expand nationwide through acquisition, consolidation or merger. Under this law, an adequately capitalized bank holding company may acquire banks in any state or merge banks across state lines if permitted by state law. Further, banks may establish and operate branches in any state subject to the restrictions of applicable state law. Under Oregon law, an out-of-state bank or bank holding company may merge with or acquire an Oregon state chartered bank or bank holding company upon receipt of approval from the Director of the DCBS. The Bank now has the ability to open additional de novo branches in the states of Oregon, California, Washington, Idaho, and Nevada.

Section 613 of the Dodd-Frank Act eliminated interstate branching restrictions that were implemented as part of the Riegle-Neal Act, and removed many restrictions on de novo interstate branching by national and state-chartered banks. The FDIC and the Office of the Comptroller of the Currency now have authority to approve applications by insured state nonmember banks and national banks, respectively, to establish de novo branches in states other than the bank's home state if "the law of the State in which the branch is located, or is to be located, would permit establishment of the branch, if the bank were a State bank chartered by such State." The enactment of this Section 613 may significantly increase interstate banking by community banks in western states, where barriers to entry were previously high.

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Anti-Terrorism Legislation. The Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act ("USA Patriot Act") prohibits banks from providing correspondent accounts directly to foreign shell banks, as well as imposes due diligence requirements on banks opening and holding accounts for foreign financial institutions or wealthy foreign individuals. Banks are also required to have effective compliance processes in place relating to anti-money laundering ("AML") compliance, as well as compliance with the Bank Secrecy Act.

Sarbanes-Oxley Act of 2002. The Sarbanes-Oxley Act of 2002 addresses public company corporate governance, auditing, accounting, executive compensation and enhanced and timely disclosure of corporate information.

The Dodd-Frank Wall Street Reform and Consumer Protection Act. On July 21, 2010, the Dodd-Frank Act was signed, which was a sweeping overhaul of financial industry regulation. The Dodd-Frank Act created the Financial Stability Oversight Council and permanently raised the FDIC deposit insurance coverage to $250,000. In addition, the Dodd-Frank Act added additional requirements on Bank and their regulators, including additional interchange fee limits, mortgage limit requirements, and say-on-pay executive compensation requirements.

Stress Testing and Capital Planning. Umpqua was subject to the annual Dodd-Frank Act capital stress testing ("DFAST") requirements of the Federal Reserve and the FDIC. As part of the DFAST process, Umpqua was required to submit the results of the company-run stress tests to the FDIC, and Umpqua disclosed certain results from stress testing exercises. However, in May 2018, the Economic Growth, Regulatory Relief, and Consumer Protection Act, modified provisions of the Dodd-Frank Act that impacted Umpqua, which includes raising the total asset threshold from $10 billion to $250 billion at which bank holding companies are required to conduct annual company-run stress tests. Although the Corporation will continue to monitor and stress test its capital consistent with the safety and soundness expectations of the federal regulators, the Company will no longer conduct company run DFAST capital stress-testing as a result of the legislative amendments.

CFPB Regulation and Supervision. The Dodd-Frank Act gives the CFPB authority to examine Umpqua and Umpqua Bank for compliance with a broad range of federal consumer financial laws and regulations, including the laws and regulations that relate to credit card, deposit, mortgage and other consumer financial products and services the Bank offers. In addition, the Dodd-Frank Act gives the CFPB broad authority to take corrective action against Umpqua and Umpqua Bank as it deems appropriate. The CFPB is authorized to issue regulations and take enforcement actions to prevent and remedy acts and practices relating to consumer financial products and services that it deems to be unfair, deceptive or abusive. The agency also has authority to impose new disclosure requirements for any consumer financial product or service.

In addition, the CFPB's regulations require lenders to conduct a reasonable and good faith determination at or before consummation of a residential mortgage loan that the borrower will have a reasonable ability to repay the loan. The regulations also define criteria for making Qualified Mortgages which entitle the lender and any assignee to either a conclusive or rebuttable presumption of compliance with the ability to repay rule. The mortgage servicing rules include new standards for notices to consumers, loss mitigation procedures, and consumer requests for information.

Joint Agency Guidance on Incentive Compensation. Federal banking regulators joint agency guidance applies to executive and non-executive incentive compensation plans administered by banks. The guidance says that incentive compensation programs must:

- Provide employees incentives that appropriately balance risk and reward.
- Be compatible with effective controls and risk- management; and
- Be supported by strong corporate governance, including active and effective oversight by the board;

The Federal Reserve reviews, as part of the regular, risk-focused examination process, the incentive compensation arrangements of the Company and other banking organizations. The findings of the supervisory initiatives are included in reports of examination and any deficiencies will be incorporated into the Company's supervisory ratings, which can affect the Company's ability to make acquisitions and take other actions.

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ITEM 1A.   RISK FACTORS.

In addition to the other information set forth in this report, you should carefully consider the risk factors discussed below. These factors could adversely affect our business, financial condition, liquidity, results of operations and capital position, and the value of, and return on, an investment in the Company. These factors could cause our actual results to differ materially from our historical results or the results contemplated by the forward-looking statements contained in this report. An investment in the Company involves risk, including the possibility that the value of the investment could fall substantially and that dividends on the investment could be reduced or eliminated.

Difficult or volatile market conditions or weak economic conditions may adversely affect our business.

Our business and financial performance are vulnerable to weak economic conditions, primarily in the United States and especially in the western United States. A deterioration in economic conditions in our primary market areas could result in the following consequences, any of which could materially and adversely affect our business: increased loan delinquencies; problem assets and foreclosures; significant write-downs of asset values; volatile financial markets; lower demand for our products and services; reduced low cost or noninterest bearing deposits; intangible asset impairment; and collateral for loans made by us, especially real estate, may decline in value, in turn reducing customers' borrowing power, and reducing the value of assets and collateral associated with our existing loans.

Additional issues surrounding weakening economic conditions and volatile markets that could adversely impact us include:

- Increased regulation of our industry, and resulting increased costs associated with regulatory compliance and potential limits on our ability to pursue business opportunities.
- Our ability to assess the creditworthiness of our customers may be impaired if the models and approaches we use to select, manage, and underwrite our customers become less predictive of future performance.
- The process we use to estimate losses inherent in our loan portfolio requires difficult, subjective, and complex judgments, including forecasts of economic conditions and how these economic predictions might impair the ability of our borrowers to repay their loans, which process may no longer be capable of accurate estimation and may, in turn, impact its reliability.
- Downward pressure on our stock price.

The majority of our assets are loans, which if not repaid would result in losses to the Bank.

The Bank, like other lenders, is subject to credit risk, which is the risk of losing principal or interest due to borrowers' failure to repay loans in accordance with their terms. Underwriting and documentation controls cannot mitigate all credit risk. A downturn in the economy or the real estate market in our market areas or a rapid increase in interest rates could have a negative effect on collateral values and borrowers' ability to repay. To the extent loans are not paid timely by borrowers, the loans are placed on non-accrual status, thereby reducing interest income. Further, under these circumstances, an additional provision for loan and lease losses or unfunded commitments may be required.

Deterioration in the real estate market or other segments of our loan portfolio would lead to additional losses, which could have a material adverse effect on our business, financial condition and results of operations.

As of December 31, 2018, approximately 75% of our total loan portfolio is secured by real estate, the majority of which is commercial real estate. Our success depends in part on economic conditions in the western United States and adverse changes in markets where our real estate collateral is located could adversely affect our business. Increases in delinquency rates or declines in real estate market values would require increased net charge-offs and increases in the allowance for loan and lease losses, which could have a material adverse effect on our business, financial condition and results of operations and prospects.

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Deposit are an important source of funds for our continued growth and profitability.

Our business strategy calls for continued growth. Our ability to continue to grow depends in part on our ability to successfully attract deposits to fund loan growth. Core deposits are a low cost and stable source of funding and a significant source of funds for our lending activities. Our inability to retain or attract such funds could adversely affect our liquidity. If we are forced to seek other sources of funds, such as additional brokered deposits or borrowings from the FHLB, the interest expense associated with these other funding sources may be higher than the rates we are currently paying on our deposits, which would adversely impact our net income.

A rapid change in interest rates, or maintenance of rates at historically high or low levels for an extended period, could make it difficult to improve or maintain our current interest income spread and could result in reduced earnings.

Our earnings are largely derived from net interest income, which is interest income and fees earned on loans and investments, less interest paid on deposits and other borrowings. Interest rates are highly sensitive to many factors that are beyond the control of our management, including general economic conditions and the policies of various governmental and regulatory authorities. The actions of the Federal Reserve influence the rates of interest that we charge on loans and that we pay on borrowings and interest-bearing deposits. We cannot predict the nature or timing of future changes in monetary, tax and other policies or the effects that they may have on our activities and financial results.

As interest rates change, net interest income is affected. With fixed rate assets (such as fixed rate loans and most investment securities) and liabilities (such as certificates of deposit), the effect on net interest income depends on the cash flows associated with the maturity of the asset or liability. Asset/liability management policies may not be successfully implemented and from time to time our risk position is not balanced. An unanticipated rapid decrease or increase in interest rates could have an adverse effect on the spreads between the interest rates earned on assets and the rates of interest paid on liabilities, and therefore on the level of net interest income. For instance, any rapid increase in interest rates in the future could result in interest expense increasing faster than interest income because of fixed rate loans and longer-term investments. Historically low rates for an extended period of time result in reduced returns from the investment and loan portfolios. The current low interest rate environment could affect consumer and business behavior in ways that are adverse to us and negatively impact our ability to increase our net interest income. Further, substantially higher interest rates generally reduce loan demand and may result in slower loan growth than previously experienced.

While interest rates recently rose off historic lows set in July 2016, both shorter-term and longer-term interest rates remain below historical averages, as well as the yield curve, which has been relatively flat compared to recent years. A flat yield curve combined with low interest rates generally leads to lower revenue and reduced margins because it tends to limit our ability to increase the spread between asset yields and funding costs. Sustained periods of time with a flat yield curve coupled with low interest rates could have a material adverse effect on our earnings and our net interest margin. Although the Federal Reserve's recent decision to raise short-term interest rates may reduce prepayment risk, debt service requirements for some of our borrowers will increase, which may adversely affect those borrowers' ability to pay as contractually obligated. This could result in additional delinquencies or charge-offs and negatively impact our results of operations.

Changes in interest rates could reduce the value of mortgage servicing rights ("MSR").

We acquire MSR when we keep servicing rights after we sell originated residential mortgage loans. We sell the majority of our originated residential mortgage loans with servicing retained. We measure MSR at fair value. Fair value is the present value of estimated future net servicing income, calculated based on a number of variables, including assumptions about the likelihood of prepayment by borrowers. Changes in interest rates can affect prepayment assumptions and consequently MSR fair value. When interest rates fall, borrowers are usually more likely to prepay their mortgage loans by refinancing them at a lower rate. As the likelihood of prepayment increases, MSR fair value can decrease, which reduces earnings in the period in which the decrease occurs.

A low interest rate environment increases our exposure to prepayment risk in our mortgage portfolio and the mortgage-backed securities in our investment portfolio. Increased prepayments, refinancing or other factors that impact loan balances could reduce expected revenue associated with mortgage assets and could also lead to a reduction in the value of our mortgage servicing rights, which could have a negative impact on our financial results.

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Our mortgage banking revenue can fluctuate significantly.

We earn revenue from fees received for originating, selling and servicing mortgage loans. Generally, if interest rates rise, the demand for mortgage loans tends to fall, reducing the revenue we receive from originations and sales of mortgage loans. At the same time, mortgage banking revenue can increase through increases in fair value of MSR. When interest rates decline, originations tend to increase and the value of MSR tends to decline, also with some offsetting revenue effect. The negative effect on revenue from a decrease in the fair value of residential MSR is immediate, but any offsetting revenue benefit from more originations and the MSR relating to new loans accrues over time. It is also possible that even if interest rates were to fall, mortgage originations may also fall or any increase in mortgage originations may not be enough to offset the decrease in the MSR value caused by the lower rates.

We depend upon programs administered by Fannie Mae, Freddie Mac and Ginnie Mae.

Our ability to generate revenues in our home lending group depends on programs administered by government-sponsored entities that play an important role in the residential mortgage industry. During 2018, 63% of mortgage loans were originated for sale to, or through programs sponsored by Fannie Mae, Freddie Mac or Ginnie Mae. We service loans on behalf of Fannie Mae and Freddie Mac, as well as loans that have been securitized pursuant to securitization programs sponsored by Fannie Mae, Freddie Mac and Ginnie Mae. A majority of our mortgage servicing rights and loans serviced through subservicing agreements relate to these servicing activities. These entities establish the base service fee to compensate us for servicing loans as well as the assessment of fines and penalties that may be imposed upon us for failing to meet servicing standards. Our status as a Fannie Mae, Freddie Mac and Ginnie Mae approved seller and servicer is subject to compliance with guidelines and failure to meet such guidelines could result in the unilateral termination of our status as an approved seller or servicer. Changes in the existing government-sponsored mortgage programs or servicing eligibility standards through legislation or otherwise, or our failure to maintain a relationship with each of Fannie Mae, Freddie Mac and Ginnie Mae, could materially and adversely affect our business, financial position, results of operations and cash flows through negative impact on the pricing of mortgage related assets in the secondary market, higher mortgage rates to borrowers, or lower mortgage origination volumes and margins.

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, brokerages, 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. We also face competition from credit unions, government-sponsored enterprises, mutual fund companies, insurance companies and other non-bank businesses. The significant competition in attracting and retaining deposits and making loans, as well as 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. 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.

The failure to understand and adapt to continual technological changes could negatively impact our business.

The financial services industry is undergoing rapid technological change with frequent introductions of new technology-driven products and services by depository institutions and fintech companies. 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. Our future success depends, in part, upon our ability to address the needs of our customers by using technology to provide products and services that will satisfy customer demands, as well as to create additional efficiencies in operations. In addition, advances in technology such as digital, mobile, 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 store network and other assets. We may close or sell certain stores and restructure or reduce our remaining stores and work force. These actions could lead to losses on assets, expense to reconfigure stores and loss of customers in certain markets. As a result, our business, financial condition or results of operations may be adversely affected.

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We may not be able to successfully implement current or future information technology system enhancements and operational initiatives.

We are investing significant resources in information technology system enhancements and operational initiative to provide functionality, new and enhanced products and services, more efficient internal operations, meet regulatory requirements and streamline our customer experience. We may not be able to successfully implement and integrate such system enhancements and related operational initiatives or do so within budgets and on time. We may incur significant training, licensing, maintenance, consulting and amortization expenses during and after implementation, and may not realize the anticipated long-term benefits.

We are subject to extensive government regulation and supervision; compliance with new and existing legislation, regulation and supervisory requirements and expectations could detrimentally affect the Company's business.

Umpqua Holdings Corporation and its subsidiaries, primarily Umpqua Bank, are subject to extensive federal and state regulation and supervision, the primary focus of which is to protect customers, depositors, the deposit insurance fund and the safety and soundness of the banking system as a whole, and not shareholders. The quantity and scope of applicable federal and state regulations may place banks and brokerage firms at a competitive disadvantage compared to less regulated competitors such as fintech companies, finance companies, credit unions, mortgage banking companies and leasing companies. Banking and consumer lending laws and regulations apply to almost every aspect of our business, including lending, capital, investments, deposits, other services and products, risk management, dividends and acquisitions.

Legislation and regulation with respect to our industry has increased in recent years, and we expect that supervision and regulation will continue to expand in scope and complexity. Congress and federal regulatory agencies continually review banking laws, regulations and policies for possible changes. Changes to statutes, regulations or regulatory policies, including changes in interpretation or implementation of statutes, regulations or policies, could affect us in substantial and unpredictable ways, and could subject us to additional costs, limits on the services and products we may offer or limits on the pricing of banking services and products. In addition, establishing systems and processes to achieve compliance with laws and regulation increases our costs and could limit our ability to pursue business opportunities.

If we receive less than satisfactory results on regulatory examinations, we could be subject to damage to our reputation, significant fines and penalties, requirements to increase compliance and risk management activities and related costs and restriction on acquisitions, new locations, new lines of business, or continued growth. Future changes in federal and state banking and brokerage regulations could adversely affect our operating results and ability to continue to compete effectively. For example, the Dodd-Frank Act and related regulations subject us to additional restrictions, oversight and reporting obligations, which have significantly increased costs. And over the last several years, state and federal regulators have focused on enhanced risk management practices, compliance with the Bank Secrecy Act and anti-money laundering laws, data integrity and security, use of service providers, and fair lending and other consumer protection issues, which has increased our need to build additional processes and infrastructure. Government agencies charged with adopting and interpreting laws, rules and regulations, may do so in an unforeseen manner, including in ways that potentially expand the reach of the laws, rules or regulations more than initially contemplated or currently anticipated. We cannot predict the substance or impact of pending or future legislation or regulation, or the application thereof. Compliance with such current and potential regulation and scrutiny could significantly increase our costs, impede the efficiency of our internal business processes, require us to increase our regulatory capital and limit our ability to pursue business opportunities in an efficient manner. Our success depends on our ability to maintain compliance with both existing and new laws and regulations.

Interest rate volatility and credit risk adjusted rate spreads may impact our financial assets and liabilities measured at fair value, particularly the fair value of our junior subordinated debentures.

The widening of the credit risk adjusted rate spreads on potential new issuances of junior subordinated debentures above our contractual spreads and reductions in three-month LIBOR rates have contributed to the cumulative positive fair value adjustment in our junior subordinated debentures carried at fair value. Tightening of these credit risk adjusted rate spreads and interest rate volatility may result in recognizing negative fair value adjustments in the future.

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We may be required to raise additional capital in the future, but that capital may not be available when it is needed, or it may only be available on unacceptable terms, which could adversely affect our financial condition and results of operations.

We are required by federal and state regulatory authorities to maintain adequate levels of capital to support our operations. Our ability to raise additional capital, if needed, will depend on conditions in the capital markets at that time, which are outside our control, and on our financial performance. Accordingly, we may not be able to raise additional capital, if needed, on terms acceptable to us. If we cannot raise additional capital when needed, our ability to further expand our operations and pursue our growth strategy could be materially impaired. We and the Bank are currently well capitalized under applicable regulatory guidelines. However, our business could be negatively affected if we or the Bank failed to remain well capitalized. For example, because Umpqua Bank is well capitalized, and we otherwise qualify as a financial holding company, we are permitted to engage in a broader range of activities than are permitted to a bank holding company. Loss of financial holding company status could require that we cease these broader activities. The banking regulators are authorized (and sometimes required) to impose a wide range of requirements, conditions, and restrictions on banks, thrifts, and bank holding companies that fail to maintain adequate capital levels.

New rules will require increased capital.

In June 2013, federal banking regulators jointly issued the Basel III rules. The rules imposed new capital requirements and implement Section 171 of the Dodd Frank Act. The new rules were to be phased in through 2019, however, on November 21, 2017, the federal banking regulators finalized a halt in the phase-in of certain provisions of the rule for certain banks including Umpqua. Among other things, the Basel III rules require that we maintain a common equity Tier 1 capital ratio of 4.5%, a Tier 1 capital ratio of 6%, a total capital ratio of 8%, and a leverage ratio of 4%. In addition, we must maintain an additional capital conservation buffer of 2.5% of total risk weighted assets or be subject to limitations on dividends and other capital distributions, as well as limiting discretionary bonus payments to executive officers. It is possible the Company may accelerate redemption of the existing junior subordinated debentures to support regulatory total capital levels. This could result in adjustments to the fair value of these instruments including the acceleration of losses on junior subordinated debentures carried at fair value. The new rules may require us to raise more common capital or other capital that qualifies as Tier 1 capital. 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.

Conditions in the financial markets may limit our access to additional funding to meet our liquidity needs.

Liquidity is essential to our business. An inability to raise funds through deposits, borrowings, the sale or pledging as collateral of loans and other assets could have a substantial negative effect on our liquidity. Our access to funding sources in amounts adequate to finance our activities could be impaired by factors that affect us specifically or the financial services industry in general. An adverse regulatory action against us could detrimentally impact our access to liquidity sources. Our ability to borrow could also be impaired by factors that are nonspecific to us, such as severe disruption of the financial markets or negative news and expectations about the prospects for the financial services industry as a whole as evidenced by turmoil in the domestic and worldwide credit markets.

Our wholesale funding sources may prove insufficient to support our future growth or an unexpected reduction in deposits.

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. If we grow more rapidly than any increase in our deposit balances, we are likely to become more dependent on these sources, which include brokered deposits, Federal Home Loan Bank advances, proceeds from the sale of loans and liquidity resources at the holding company. Our financial flexibility will be severely 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, and our profitability would be adversely affected.

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As a bank holding company that conducts substantially all of our operations through the Bank, our ability to pay dividends, repurchase our shares or to repay our indebtedness depends upon liquid assets held by the holding company and the results of operations of our subsidiaries.

The Company is a separate and distinct legal entity from our subsidiaries and it receives substantially all of its revenue from dividends paid from the Bank. There are legal limitations on the extent to which the Bank may extend credit, pay dividends or otherwise supply funds to, or engage in transactions with, us. Our inability to receive dividends from the Bank could adversely affect our business, financial condition, results of operations and prospects.

Our net income depends primarily upon the Bank's net interest income, which is the income that remains after deducting from total income generated by earning assets the expense attributable to the acquisition of the funds required to support earning assets (primarily interest paid on deposits). The amount of interest income is dependent on many factors including the volume of earning assets, the general level of interest rates, the dynamics of changes in interest rates and the levels of nonperforming loans. All of those factors affect the Bank's ability to pay dividends to the Company.

Various statutory provisions restrict the amount of dividends the Bank can pay to us without regulatory approval. The Bank may not pay cash dividends if that payment could reduce the amount of its capital below that necessary to meet the "adequately capitalized" level in accordance with regulatory capital requirements. It is also possible that, depending upon the financial condition of the Bank and other factors, regulatory authorities could conclude that payment of dividends or other payments, including payments to us, is an unsafe or unsound practice and impose restrictions or prohibit such payments.
Under Oregon law, the Bank may not pay dividends in excess of unreserved retained earnings, deducting there from, to the extent not already charged against earnings or reflected in a reserve, the following: (1) all bad debts, which are debts on which interest is past due and unpaid for at least six months, unless the debt is fully secured and in the process of collection; (2) all other assets charged-off as required by Oregon bank regulators or a state or federal examiner; and (3) all accrued expenses, interest and taxes of the institution. The Federal Reserve has issued a policy statement on the payment of cash dividends by bank holding companies, which expresses the Federal Reserve's view that a bank holding company should pay cash dividends only to the extent that its net income for the past year is sufficient to cover both the cash dividends and a rate of earnings retention that is consistent with the holding company's capital needs, asset quality and overall financial condition.

Our business is highly reliant on technology and our ability to manage the operational risks associated with technology.

Our business involves storing and processing sensitive consumer and business customer data. We depend on internal systems and outsourced technology to support these data storage and processing operations. Despite our efforts to ensure the security and integrity of our systems, we may not be able to anticipate, detect or recognize threats to our systems or to implement effective preventive measures against all cyber security breaches. A cyber security breach or cyberattack could persist for a long time before being detected and could result in theft of sensitive data or disruption of our transaction processing systems. Our inability to use or access these information systems at critical points in time could unfavorably impact the timeliness and efficiency of our business operations.

We face significant cyber and data security risk that could result in the disclosures of confidential information.

A material breach of customer data security may negatively impact our business reputation and cause a loss of customers; result in increased expense to contain the event and/or require that we provide credit monitoring services for affected customers, result in regulatory fines or result in litigation. Cyberattack techniques change regularly and can originate from a wide variety of sources, including third parties who are or may be involved in organized crime or linked to terrorist organizations or hostile foreign governments, and such third parties may seek to gain access to systems directly or using equipment or security passwords belonging to employees, customers, third-party service providers or other users of our systems. Cyber security risk management programs are expensive to maintain and will not protect the Company from all risks associated with maintaining the security of customer data and the Company's proprietary data from external and internal intrusions, disaster recovery and failures in the controls used by our vendors. These risks may increase in the future as we continue to increase our mobile and other internet-based product offerings and expands our internal usage of web-based products and applications. In addition, Congress and the legislatures of states in which we operate regularly consider legislation that would impose more stringent data privacy requirements, resulting in increased compliance costs. A data security breach could adversely affect our business and expose us to significant liabilities. Our cybersecurity insurance may not provide sufficient coverage in the event of a breach, or may not be available in the future on acceptable terms.

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Our business is highly reliant on third party vendors and our ability to manage the operational risks associated with outsourcing those services.

We rely on third parties to provide services that are integral to our operations. These vendors provide services that support our operations, including the storage and processing of sensitive consumer and business customer data, as well as our sales efforts. A cyber security breach of a vendor's system may result in theft of our data or disruption of business processes. In most cases, we will remain primarily liable to our customers for losses arising from a breach of a vendor's data security system. We rely on our outsourced service providers to implement and maintain prudent cyber security controls. We have procedures in place to assess a vendor's cyber security controls prior to establishing a contractual relationship and to periodically review assessments of those control systems; however, these procedures are not infallible, and a vendor's system can be breached despite the procedures we employ. We cannot be sure that we will be able to maintain these relationships on favorable terms. In addition, some of our data processing services are provided by companies associated with our competitors. The loss of these vendor relationships could disrupt the services we provide to our customers and cause us to incur significant expense in connection with replacing these services.

Damage to our brand and reputation could significantly harm our business and prospects.

Our brand and reputation are important assets. Our relationship with many of our customers is predicated upon our reputation as a high-quality provider of financial services that adheres to the highest standards of ethics, service quality and regulatory compliance. We believe that our brand has been, and continues to be, well received in our industry, with current and potential customers, investors and employees. Our ability to attract and retain customers, investors and employees depends upon external perceptions of us. Damage to our reputation among existing and potential customers, investors and employees could cause significant harm to our business and prospects and may arise from numerous sources, including litigation or regulatory actions, failing to deliver minimum standards of service and quality, lending practices, inadequate protection of customer information, sales and marketing efforts, compliance failures, unethical behavior and the misconduct of employees. Adverse developments with respect to our industry may also, by association, negatively impact our reputation or result in greater regulatory or legislative scrutiny or litigation against us.

As we grow our digital, online and mobile business we are susceptible to fraud.

Fraud risk within digital channels is challenging to detect and prevent and we are expanding our business more deeply into these channels. Our business exposes us to fraud risk from our loan and deposit customers, the parties they do business with, and from employees and vendors. We rely on financial and other data from customers when we accept them as new customers and when they conduct transactions, which information could be fraudulent and expose us to losses that negatively impact our net income especially when delivered through digital channels. Our operational controls to prevent and detect such fraud may be ineffective in preventing new methods of fraud.

A decline in the Company's stock price or expected future cash flows, or a material adverse change in our results of operations or prospects, could result in impairment of our goodwill.

From time to time, the Company's common stock has traded at a price below its book value, including goodwill and other intangible assets. A significant and sustained decline in our stock price and market capitalization, a significant decline in our expected future cash flows, a significant adverse change in the business climate or slower growth rates could result in impairment of our goodwill. We have a significant goodwill asset on our balance sheet. If impairment was deemed to exist, a write down of goodwill would occur with a charge to earnings.

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We may be impacted by the retirement of LIBOR as a reference rate

The Financial Conduct Authority ("FCA") announced that the London Interbank Offered Rate ("LIBOR") may no longer be published after 2021. In response, the Alternative Reference Rates Committee ("ARRC") was convened in the U.S. to explore alternative reference rates and supporting processes. The ARRC is made up of financial and capital market institutions, is convened by the Federal Reserve Board and the Federal Reserve Bank of New York, and includes participation by various regulators. The ARRC identified a potential successor rate to LIBOR in the Secured Overnight Financing Rate ("SOFR") and crafted the Paced Transition Plan to facilitate the transition. However, there are conceptual and technical differences between LIBOR and SOFR.

A significant portion of our loans and related derivative contracts within the Commercial & Industrial, Commercial Real Estate, and Residential Mortgage portfolios reference LIBOR. We have not yet determined the optimal reference rate(s) that we will ultimately use for our credit products going forward without additional guidance from ARRC and more SOFR historical data. We have organized an internal initiative to identify operational and contractual best practices, assess our risks, manage the transition, facilitate communication with our customers, and monitor the impacts. The LIBOR retirement is a significant shift in the industry. A transition away from LIBOR could impact our pricing and interest rate risk models, our loan product structures, our hedging strategies, and communication with our customers.

Involvement in non-bank business creates risks associated with the securities industry.

Umpqua Investments' retail brokerage operations present special risks not borne by financial institutions that focus exclusively on traditional community banking. For example, the brokerage industry is subject to fluctuations in the stock market that may have a significant adverse impact on transaction fees, customer activity and investment portfolio gains and losses. Likewise, additional or modified regulations may adversely affect Umpqua Investments' operations. Umpqua Investments is also dependent on a small number of established brokers, whose departure could result in the loss of a significant number of customer accounts. A significant decline in fees and commissions or trading losses suffered in the investment portfolio could adversely affect Umpqua Investments' income and potentially require the contribution of additional capital to support its operations. Umpqua Investments is subject to claim arbitration risk arising from customers who claim their investments were not suitable or that their portfolios were too actively traded. These risks increase when the market declines. The risks associated with retail brokerage may not be supported by the income generated by those operations.

The value of the securities in our investment securities portfolio may be negatively affected by disruptions in securities markets.

The market for some of the investment securities held in our portfolio has become volatile over the past three years. Volatile market conditions or deteriorating financial performance of the issuer or obligor may detrimentally affect the value of these securities. There can be no assurance that the declines in market value associated with these disruptions will not result in other-than-temporary or permanent impairments of these assets, which would lead to accounting charges that could have a material adverse effect on our net income and capital levels.

ITEM 1B. UNRESOLVED STAFF COMMENTS.
None.

ITEM 2. PROPERTIES.
The executive offices of Umpqua and Umpqua Investments are located at One SW Columbia Street in Portland, Oregon in office space that is leased. The Bank's headquarters, located in Roseburg, Oregon, is owned. At December 31, 2018, the Bank conducted community banking activities or operated Commercial Banking Centers at

299 locations, in Oregon, Washington, California, Idaho and Nevada, of which 119 are owned and 180 are leased under various agreements. As of December 31, 2018, the Bank also operated 22 facilities for the purpose of administrative and other functions, such as back-office support, of which 3 are owned and 19 are leased. All facilities are in a good state of repair and appropriately designed for use as banking or administrative office facilities. As of December 31, 2018, Umpqua Investments leased 4 stand-alone offices from unrelated third parties and also leased space in 7 Bank stores under lease agreements based on market rates.

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## ITEM 3. LEGAL PROCEEDINGS.

Due to the nature of our business, we are involved in legal proceedings that arise in the ordinary course of our business. While the outcome of all of these matters is currently not determinable, we do not expect that the ultimate costs to resolve these matters will have a material adverse effect on our consolidated financial position, results of operations, or cash flows.

## ITEM 4. MINE SAFETY DISCLOSURES.

Not applicable

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PART II

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

(a) Our common stock is traded on The NASDAQ Global Select Market under the symbol "UMPQ." As of December 31, 2018, our common stock was held by approximately 4,082 shareholders of record, a number that does not include beneficial owners who hold shares in "street name," or shareholders from previously acquired companies that have not exchanged their stock. At December 31, 2018, a total of 9,000 exercisable stock options and 979,000 shares of unvested restricted shares were outstanding.

During 2018, Umpqua's Board of Directors approved a quarterly cash dividend of $0.20 per common share for first and second quarters and $0.21 for the third and fourth quarters. These dividends were made pursuant to our existing dividend policy and in consideration of, among other things, earnings, regulatory capital levels, the overall payout ratio and expected asset growth. We expect that the dividend rate will be reassessed on a quarterly basis by the Board of Directors in accordance with the dividend policy.

The payment of future cash dividends is at the discretion of our Board of Directors and subject to a number of factors, including results of operations, general business conditions, growth, financial condition and other factors deemed relevant by the Board of Directors. Further, our ability to pay future cash dividends is subject to certain regulatory requirements and restrictions discussed in the Supervision and Regulation section in Item 1 above.

We have a dividend reinvestment plan that permits shareholder participants to purchase shares at the then-current market price in lieu of the receipt of cash dividends. Shares issued in connection with the dividend reinvestment plan are purchased in open market transactions.

Equity Compensation Plan Information

The following table sets forth information about equity compensation plans that provide for the award of securities or the grant of options to purchase securities to employees and directors of Umpqua and its subsidiaries and predecessors by merger that were in effect at December 31, 2018.

(shares in thousands)

| | Equity Compensation Plan Information | | |
|---|---|---|---|
| | (A) | (B) | (C) |
| Plan category | Number of securities to be issued upon exercise of outstanding options warrants and rights | Weighted average exercise price of outstanding options, warrants and rights [3] | Number of securities remaining available for future issuance under equity compensation plans excluding securities reflected in column (A) |
| Equity compensation plans approved by security holders | | | |
| 2013 Incentive Plan [1] | — | $ — | 6,415 |
| 2003 Stock Incentive Plan [1] | 2 | $ 10.49 | — |

| | | | | |
|---|---|---|---|---|
| Other [2] | 7 | $ | 12.16 | — |
| Total | 9 | $ | 11.80 | 6,415 |
| | | | | |
| Equity compensation plans not approved by security holders | — | $ | — | — |
| Total | 9 | $ | 11.80 | 6,415 |

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(1) Shareholders approved the Company's 2013 Incentive Plan (the "2013 Plan") on April 16, 2013, and approved an amendment to the 2013 plan to increase the number of authorized shares at the 2016 annual meeting of shareholders. The 2013 Plan authorizes the issuance of equity awards to directors and employees and reserves 12.0 million shares of the Company's common stock for issuance under the plan (up to 6 million shares for "full value awards" as described below). With the adoption of the 2013 Plan, no additional awards will be issued from prior plans. Under the terms of the 2013 Plan, options and awards generally vest ratably over a period of three to five years, the exercise price of each option equals the market price of the Company's common stock on the date of the grant, and the maximum term is ten years. The 2013 Plan weights "full value awards" (restricted shares and performance share awards) as two shares issued from the total authorized under the 2013 Plan; we have issued only full value awards under the 2013 Plan. For purposes of column (C) above, the total number of shares available for future issuance under the 2013 Plan for full value awards was 3.2 million at December 31, 2018. At December 31, 2018, 979,000 shares issued under the 2013 Plan as restricted stock/performance share awards were outstanding, but subject to forfeiture in the event time or performance based conditions are not met.

(2) Includes other Umpqua stock plans and stock plans assumed through previous mergers.

(3) Weighted average exercise price is based solely on securities with an exercise price.

(b) Not applicable.

(c) The following table provides information about repurchases of common stock by the Company during the quarter ended December 31, 2018:

| Period | Total number of Common Shares Purchased (1) | Average Price Paid per Common Share | Total Number of Shares Purchased as Part of Publicly Announced Plan (2) | Maximum Number of Remaining Shares that May be Purchased at Period End under the Plan |
|---|---|---|---|---|
| 10/1/18 - 10/31/18 | 666 | $ 20.20 | — | 10,155,429 |
| 11/1/18 - 11/30/18 | 2,871 | $ 19.22 | — | 10,155,429 |
| 12/1/18 - 12/31/18 | — | $ — | — | 10,155,429 |
| Total for quarter | 3,537 | $ 19.40 | — | |

(1) Common shares repurchased by the Company during the quarter consist of cancellation of 3,537 shares to be issued upon vesting of restricted stock awards to pay withholding taxes. During the three months ended December 31, 2018, no shares were repurchased pursuant to the Company's publicly announced corporate stock repurchase plan described in (2) below.

(2) The Company's share repurchase plan, which was first approved by the Board and announced in August 2003, was amended on September 29, 2011 to increase the number of common shares available for repurchase under the plan to 15 million shares. The repurchase program has been extended multiple times by the board with the current expiration date of July 31, 2019. As of December 31, 2018, a total of 10.2 million shares remained available for repurchase. The Company repurchased 327,000 shares under the repurchase plan during 2018, repurchased 325,000 shares in 2017, and 635,000 shares under the repurchase plan in 2016. The timing and amount of future repurchases will depend upon the market price for our common stock, securities laws restricting repurchases, asset growth, earnings, and our capital plan.

There were 38,000 and 35,000 shares tendered in connection with option exercises during the years ended December 31, 2018 and 2017, respectively. Restricted shares cancelled to pay withholding taxes totaled 187,000 and 91,000 shares during the years ended December 31, 2018 and 2017, respectively. There were 6,000 restricted stock units cancelled to pay withholding taxes in 2018 and 17,000 in 2017.

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Stock Performance Graph

The following chart, which is furnished not filed, compares the yearly percentage changes in the cumulative shareholder return on our common stock during the five fiscal years ended December 31, 2018, with (i) the Total Return Index for The Nasdaq Stock Market (U.S. Companies) (ii) the Standard and Poor's 500 and (iii) the SNL U.S. Bank Nasdaq. This comparison assumes $100.00 was invested on December 31, 2013, in our common stock and the comparison indices, and assumes the reinvestment of all cash dividends prior to any tax effect and retention of all stock dividends. Price information from December 31, 2013 to December 31, 2018, was obtained by using the NASDAQ closing prices as of the last trading day of each year.

| | Period Ending | | | | | |
|---|---|---|---|---|---|---|
| | 12/31/2013 | 12/31/2014 | 12/31/2015 | 12/31/2016 | 12/31/2017 | 12/31/2018 |
| Umpqua Holdings Corporation | $100.00 | $91.99 | $89.19 | $109.61 | $125.80 | $100.21 |
| Nasdaq U.S. | $100.00 | $114.75 | $122.74 | $133.62 | $173.22 | $168.30 |
| S&P 500 | $100.00 | $113.69 | $115.26 | $129.05 | $157.22 | $150.33 |
| SNL U.S. Bank Nasdaq | $100.00 | $103.57 | $111.80 | $155.02 | $163.20 | $137.56 |

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ITEM 6. SELECTED FINANCIAL DATA.
Umpqua Holdings Corporation
Annual Financial Trends

| (in thousands, except per share data) | 2018 | 2017 (1) | 2016 (1) | 2015 (1) | 2014 (1) |
|---|---|---|---|---|---|
| Interest income | $1,067,149 | $943,901 | $904,163 | $898,044 | $789,008 |
| Interest expense | 128,510 | 78,216 | 66,051 | 58,232 | 48,693 |
| Net interest income | 938,639 | 865,685 | 838,112 | 839,812 | 740,315 |
| Provision for loan and lease losses | 55,905 | 47,254 | 41,674 | 36,589 | 40,241 |
| Non-interest income | 279,417 | 278,487 | 301,728 | 277,667 | 181,174 |
| Non-interest expense | 739,465 | 747,875 | 737,155 | 763,642 | 684,063 |
| Income before provision for income taxes | 422,686 | 349,043 | 361,011 | 317,248 | 197,185 |
| Provision for income taxes | 106,423 | 106,730 | 130,943 | 112,939 | 70,138 |
| Net income | 316,263 | 242,313 | 230,068 | 204,309 | 127,047 |
| Dividends and undistributed earnings allocated to participating securities | 16 | 55 | 123 | 326 | 415 |
| Net earnings available to common shareholders | $316,247 | $242,258 | $229,945 | $203,983 | $126,632 |
| YEAR END | | | | | |
| Assets | $26,939,781 | $25,680,447 | $24,771,406 | $23,367,540 | $22,600,354 |
| Earning assets | 23,959,168 | 22,707,469 | 21,707,267 | 20,246,182 | 19,347,898 |
| Loans and leases (2) | 20,422,666 | 19,019,192 | 17,440,583 | 16,803,144 | 15,305,281 |
| Deposits | 21,137,486 | 19,948,300 | 19,020,985 | 17,707,189 | 16,892,099 |
| Term debt | 751,788 | 802,357 | 852,397 | 888,769 | 1,006,395 |
| Junior subordinated debentures, at fair value | 300,870 | 277,155 | 262,209 | 255,457 | 249,294 |
| Junior subordinated debentures, at amortized cost | 88,724 | 100,609 | 100,931 | 101,254 | 101,576 |
| Total shareholders' equity | 4,056,442 | 3,969,367 | 3,875,082 | 3,810,493 | 3,757,015 |
| Common shares outstanding | 220,255 | 220,149 | 220,177 | 220,171 | 220,161 |
| AVERAGE | | | | | |
| Assets | $26,210,933 | $25,074,144 | $24,079,753 | $22,872,978 | $19,166,277 |
| Earning assets | 23,309,013 | 22,112,828 | 20,943,045 | 19,675,868 | 16,481,054 |
| Loans and leases (2) | 19,562,369 | 18,169,449 | 17,190,625 | 15,886,964 | 13,000,152 |
| Deposits | 20,519,609 | 19,351,738 | 18,347,451 | 17,250,810 | 14,407,331 |
| Term debt | 785,593 | 846,542 | 897,050 | 923,992 | 815,017 |
| Junior subordinated debentures | 370,518 | 365,196 | 359,003 | 352,872 | 301,525 |
| Total shareholders' equity | 4,002,700 | 3,929,566 | 3,856,890 | 3,787,962 | 3,146,902 |
| Basic common shares outstanding | 220,280 | 220,251 | 220,282 | 220,327 | 186,550 |
| Diluted common shares outstanding | 220,737 | 220,836 | 220,908 | 221,045 | 187,554 |
| PER COMMON SHARE DATA | | | | | |
| Basic earnings | $1.44 | $1.10 | $1.04 | $0.93 | $0.68 |
| Diluted earnings | 1.43 | 1.10 | 1.04 | 0.92 | 0.68 |
| Book value | 18.42 | 18.03 | 17.60 | 17.31 | 17.06 |
| Tangible book value (3) | 10.19 | 9.77 | 9.31 | 8.98 | 8.69 |
| Cash dividends declared | 0.82 | 0.68 | 0.64 | 0.62 | 0.60 |

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| (dollars in thousands) | 2018 | | 2017 (1) | | 2016 (1) | | 2015 (1) | | 2014 (1) | |
|---|---|---|---|---|---|---|---|---|---|---|
| PERFORMANCE RATIOS | | | | | | | | | | |
| Return on average assets (4) | 1.21 | % | 0.97 | % | 0.95 | % | 0.89 | % | 0.66 | % |
| Return on average common shareholders' equity (5) | 7.90 | % | 6.17 | % | 5.96 | % | 5.39 | % | 4.02 | % |
| Return on average tangible common shareholders' equity (6) | 14.45 | % | 11.49 | % | 11.34 | % | 10.47 | % | 7.85 | % |
| Efficiency ratio (7) | 60.61 | % | 65.11 | % | 64.41 | % | 68.03 | % | 73.81 | % |
| Average common shareholders' equity to average assets | 15.27 | % | 15.67 | % | 16.02 | % | 16.56 | % | 16.42 | % |
| Leverage ratio (8) | 9.31 | % | 9.38 | % | 9.21 | % | 9.73 | % | 10.99 | % |
| Net interest margin (fully tax equivalent) (9) | 4.04 | % | 3.94 | % | 4.02 | % | 4.29 | % | 4.52 | % |
| Non-interest income to total net revenue (10) | 22.94 | % | 24.34 | % | 26.47 | % | 24.85 | % | 19.66 | % |
| Dividend payout ratio (11) | 56.94 | % | 61.82 | % | 61.54 | % | 66.67 | % | 88.24 | % |
| | | | | | | | | | | |
| ASSET QUALITY | | | | | | | | | | |
| Non-performing loans and leases (12) | $87,267 | | $82,318 | | $56,134 | | $44,384 | | $59,553 | |
| Non-performing assets (12) | 98,225 | | 94,052 | | 62,872 | | 66,691 | | 97,495 | |
| Allowance for loan and lease losses | 144,871 | | 140,608 | | 133,984 | | 130,322 | | 116,167 | |
| Net charge-offs | 51,642 | | 40,630 | | 38,012 | | 22,434 | | 19,159 | |
| Non-performing loans and leases to loans and leases | 0.43 | % | 0.43 | % | 0.32 | % | 0.26 | % | 0.39 | % |
| Non-performing assets to total assets | 0.36 | % | 0.37 | % | 0.25 | % | 0.29 | % | 0.43 | % |
| Allowance for loan and lease losses to total loans and leases | 0.71 | % | 0.74 | % | 0.77 | % | 0.78 | % | 0.76 | % |
| Allowance for credit losses to loans and leases | 0.73 | % | 0.76 | % | 0.79 | % | 0.80 | % | 0.78 | % |
| Net charge-offs to average loans and leases | 0.26 | % | 0.22 | % | 0.22 | % | 0.14 | % | 0.15 | % |

(1) See Note 1 to the Consolidated Financial Statements included in Item 8 of this Form 10-K for disclosure of the nature and impact of the correction for the prior period balances on our selected financial data as of December 31, 2017 and for the fiscal years ended December 31, 2017 and 2016. The selected financial data as of December 31, 2016, 2015 and 2014 and for the fiscal years ended December 31, 2015 and 2014 have also been revised for the impact of the correction of the prior period balances associated with the purchase accounting discount on the loans acquired in April 2014 from Sterling Financial Corporation. Loans and leases and earning assets have decreased by $68.1 million, $63.4 million and $33.5 million, respectively, and assets and shareholders' equity have decreased by $41.7 million, $38.8 million and $20.6 million, respectively, as of December 31, 2016, 2015 and 2014. For the fiscal year ended December 31, 2015, interest income and net interest income have decreased by $31.8 million, non-interest income has increased by $1.9 million, income before provision for income taxes has decreased by $29.9 million, provision for income taxes has decreased by $11.6 million, and net income has decreased by $18.2 million. For the fiscal year ended December 31, 2014, interest income, net interest income and income before provision for income taxes have decreased by $33.5 million, provision for income taxes has decreased by $12.9 million, and net income has decreased by $20.6 million.

(2) Excludes loans held for sale

(3) Common shareholders' equity less intangible assets (excluding MSR) divided by shares outstanding at the end of the year. See Management's Discussion and Analysis of Financial Condition and Results of Operations-"Results of Operations - Overview" for the reconciliation of non-GAAP financial measures, in Item 7 of this report.

(4) Net earnings available to common shareholders divided by average assets.

(5) Net earnings available to common shareholders divided by average common shareholders' equity.

(6) Net earnings available to common shareholders divided by average common shareholders' equity less average intangible assets. See Management's Discussion and Analysis of Financial Condition and Results of Operations-"Results of Operations - Overview" for the reconciliation of non-GAAP financial measures, in Item 7 of this report.

(7) Non-interest expense divided by the sum of net interest income (fully tax equivalent) and non-interest income.

(8)

Tier 1 capital divided by leverage assets. Leverage assets are defined as quarterly average total assets, net of goodwill, intangibles and certain other items as required by the Federal Reserve.

(9) Net interest margin (fully tax equivalent) is calculated by dividing net interest income (fully tax equivalent) by average interest earnings assets.

(10) Non-interest income divided by the sum of non-interest income and net interest income.

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(11) Dividends declared per common share divided by basic earnings per common share.

(12) Excludes government guaranteed GNMA mortgage loans that Umpqua has the right but not the obligation to repurchase that are past due 90 days or more totaling $8.9 million, $12.4 million, $10.9 million, $19.2 million and $11.1 million, as of December 31, 2018, 2017, 2016, 2015, and 2014, respectively.

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

FORWARD LOOKING STATEMENTS AND RISK FACTORS

See the discussion of forward-looking statements and risk factors in Part I Item 1 and Item 1A of this report.

EXECUTIVE OVERVIEW

Significant items for the year ended December 31, 2018 were as follows:

Financial Performance

- Net earnings available to common shareholders per diluted common share were $1.43 for the year ended December 31, 2018, compared to $1.10 for the year ended December 31, 2017.

- Net interest income was $938.6 million for the year ended December 31, 2018, compared to $865.7 million for the year ended December 31, 2017. The increase in net interest income compared to the same period in the prior year was driven by growth in interest-earning assets, along with an increase in net interest margin.

- Net interest margin, on a tax equivalent basis, was 4.04% for the year ended December 31, 2018, compared to 3.94% for the year ended December 31, 2017. The increase in net interest margin compared to the same period in the prior year was driven by higher average yields on the loans and lease portfolio, loans held for sale and taxable investments, offset by an increase in the cost of interest-bearing liabilities, a lower yield on tax-exempt securities due to the change in tax rates, and a lower level of discount accretion on acquired loans.

- Residential mortgage banking revenue was $118.2 million for the year ended December 31, 2018, compared to $136.3 million for year ended December 31, 2017. The decrease for the year ended December 31, 2018 was driven by a 16% decrease in closed loans for sale volume, as well as a lower gain on sale margin of 3.09%, compared to 3.51% in the same period of the prior year. These were partially offset by a lower loss on fair value of the MSR asset, which decreased to $13.2 million, compared to $23.3 million for the year ended December 31, 2017.

- Non-interest expense was $739.5 million for the year ended December 31, 2018, compared to $747.9 million for the year ended December 31, 2017. The decrease in non-interest expense compared to the same period in the prior year was driven by lower salaries and benefits and lower merger-related expense, partially offset by higher services costs.

- Total gross loans and leases were $20.4 billion as of December 31, 2018, an increase of $1.4 billion, or 7%, compared to December 31, 2017. This increase reflects balanced growth across the Company's commercial, commercial real estate and residential real estate portfolios.

- Total deposits were $21.1 billion as of December 31, 2018, an increase of $1.2 billion, or 6%, from December 31, 2017. The increase was primarily attributable to growth in time deposits and non-interest bearing demand deposits, partially offset by decreases in interest bearing demand and money market accounts.

- Total consolidated assets were $26.9 billion as of December 31, 2018, compared to $25.7 billion at December 31, 2017.

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Credit Quality

- Non-performing assets increased to $98.2 million, or 0.36% of total assets, as of December 31, 2018, compared to $94.1 million, or 0.37% of total assets, as of December 31, 2017. Non-performing loans were $87.3 million, or 0.43% of total loans, as of December 31, 2018, compared to $82.3 million, or 0.43% of total loans, as of December 31, 2017.

- The provision for loan and lease losses was $55.9 million for 2018, compared to $47.3 million for 2017. The increase was principally attributable to strong growth in the loan and lease portfolio and higher net charge-offs. Net charge-offs on loans and leases were $51.6 million for the year ended December 31, 2018, or 0.26% of average loans and leases, compared to net charge-offs of $40.6 million, or 0.22% of average loans and leases, for the year ended December 31, 2017.

Capital and Growth Initiatives

- The Company's total risk based capital was 13.5% and its Tier 1 common to risk weighted assets ratio was 10.7% as of December 31, 2018. As of December 31, 2017, the Company's total risk based ratio was 14.1% and its Tier 1 common to risk weighted assets ratio was 11.1%.

- Declared cash dividends of $0.82 per common share for 2018, up from $0.68 per common share for 2017.

- Repurchased 327,000 shares of common stock for $8.0 million.

- We continue to make progress on "Umpqua Next Gen," an initiative started in late 2017 designed to modernize and evolve the Bank. We focused on operational excellence, balanced growth and human-digital programs in 2018. As a part of the operational excellence program, the Bank consolidated 36 stores and sold one since the third quarter of 2017. We also completed an organizational simplification and design exercise to streamline and align functions and bring associates closer to customers. We plan to use savings generated from store consolidations to reinvest in technology, such as our Go-To app, data and analytics, including new customer-focused technologies, associate training, a re-designed corporate website, digital marketing efforts, and new online account origination capabilities.

- The strong growth of 2018 shows the success of our balanced growth initiatives, which is focused on generating new, multi-faceted relationships across the bank, to deliver more consistent and diversified growth, driven by stronger, deeper, and more profitable customer relationships.

The presentation within has been revised to reflect the effects of the Correction of the Prior Period Balances disclosed in Note 1 to the Consolidated Financial Statements.

SUMMARY OF CRITICAL ACCOUNTING POLICIES

The SEC defines "critical accounting policies" as those that require application of management's most difficult, subjective or complex judgments, often as a result of the need to make estimates about the effect of matters that are inherently uncertain and may change in future periods. Our significant accounting policies are described in Note 1 in the Notes to Consolidated Financial Statements in Item 8 of this report. Not all of our significant accounting policies require management to make difficult, subjective or complex judgments or estimates. Management believes that the following policies would be considered critical under the SEC's definition.

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Allowance for Loan and Lease Losses and Reserve for Unfunded Commitments

The Bank performs regular credit reviews of the loan and lease portfolio to determine the credit quality and adherence to underwriting standards. When loans and leases are originated, they are assigned a risk rating that is reassessed periodically during the term of the loan through the credit review process. The Bank's risk rating methodology assigns risk ratings ranging from 1 to 10, where a higher rating represents higher risk. The 10 risk rating categories are a primary factor in determining an appropriate amount for the allowance for loan and lease losses. The Bank has a management Allowance for Loan and Lease Losses ("ALLL") Committee, which is responsible for, among other things, regularly reviewing the ALLL methodology, including loss factors, and ensuring that it is designed and applied in accordance with generally accepted accounting principles. The ALLL Committee reviews and approves loans and leases recommended for impaired status. The ALLL Committee also approves removing loans and leases from impaired status. The Bank's Audit and Compliance Committee provides board oversight of the ALLL process and reviews and approves the ALLL methodology on a quarterly basis.

Each risk rating is assessed an inherent credit loss factor that determines the amount of the allowance for loan and lease losses provided for that group of loans and leases with similar risk rating. Credit loss factors may vary by region based on management's belief that there may ultimately be different credit loss rates experienced in each region. Regular credit reviews of the portfolio also identify loans that are considered potentially impaired. Potentially impaired loans are referred to the ALLL Committee which reviews and approves designated loans as impaired. A loan is considered impaired when based on current information and events, we determine that we will probably not be able to collect all amounts due according to the loan contract, including scheduled interest payments. When we identify a loan as impaired, we measure the impairment using discounted cash flows, except when the sole remaining source of the repayment for the loan is the liquidation of the collateral. In these cases, we use the current fair value of the collateral, less selling costs, instead of discounted cash flows.

If we determine that the value of the impaired loan is less than the recorded investment in the loan, we either recognize an impairment reserve as a specific component to be provided for in the allowance for loan and lease losses or charge-off the impaired balance on collateral dependent loans if it is determined that such amount represents a confirmed loss. The combination of the risk rating-based allowance component and the impairment reserve allowance component lead to an allocated allowance for loan and lease losses.

The Bank may also maintain an unallocated allowance amount to provide for other credit losses inherent in a loan and lease portfolio that may not have been contemplated in the credit loss factors. This unallocated amount generally comprises less than 5% of the allowance, but may be maintained at higher levels during times of economic conditions characterized by falling real estate values. The unallocated amount is reviewed periodically based on trends in credit losses, the results of credit reviews and overall economic trends. As of December 31, 2018, there was no unallocated allowance amount.

The reserve for unfunded commitments ("RUC") is established to absorb inherent losses associated with our commitment to lend funds, such as with a letter or line of credit. The adequacy of the ALLL and RUC are monitored on a regular basis and are based on management's evaluation of numerous factors. These factors include the quality of the current loan portfolio; the trend in the loan portfolio's risk ratings; current economic conditions; loan concentrations; loan growth rates; past-due and non-performing trends; evaluation of specific loss estimates for all significant problem loans; historical charge-off and recovery experience; and other pertinent information.

Management believes that the ALLL was adequate as of December 31, 2018. There is, however, no assurance that future loan losses will not exceed the levels provided for in the ALLL and could possibly result in additional charges to the provision for loan and lease losses. In addition, bank regulatory authorities, as part of their periodic examination of the Bank, may require additional charges to the provision for loan and lease losses in future periods if warranted as a result of their review. A substantial percentage of our loan portfolio is secured by real estate; as a result, a significant decline in real estate market values may require an increase in the allowance for loan and lease losses.

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Residential Mortgage Servicing Rights ("MSR")

The Company determines its classes of servicing assets based on the asset type being serviced along with the methods used to manage the risk inherent in the servicing assets, which includes the market inputs used to value the servicing assets. The Company measures its residential mortgage servicing assets at fair value and reports changes in fair value through earnings. Fair value adjustments encompass market-driven valuation changes and the runoff in value that occurs from the passage of time, which are separately reported. Under the fair value method, the MSR is carried in the balance sheet at fair value and the changes in fair value are reported in earnings in residential mortgage banking revenue in the period in which the change occurs.

Retained mortgage servicing rights are measured at fair value as of the date of the related loan sale. We use quoted market prices when available. Subsequent fair value measurements are determined using a discounted cash flow model. In order to determine the fair value of the MSR, the present value of expected net future cash flows is estimated. Assumptions used include market discount rates, anticipated prepayment speeds, delinquency and foreclosure rates, and ancillary fee income net of servicing costs. This model is periodically validated by an independent model validation group. The model assumptions and the MSR fair value estimates are also compared to observable trades of similar portfolios as well as to MSR broker valuations and industry surveys, as available.

Valuation of Goodwill

Goodwill is not amortized but instead is periodically tested for impairment. Management performs this impairment analysis on an annual basis as of December 31. Additionally, events or circumstances are analyzed on an interim basis to determine if there is an indication of a potential impairment. The impairment analysis requires management to make subjective judgments. Events and factors that may significantly affect the estimates include, among others, competitive forces, customer behaviors and attrition, changes in revenue growth trends, cost structures, technology, changes in discount rates and specific industry and market conditions. There can be no assurance that changes in circumstances, estimates or assumptions may result in additional impairment of all, or some portion of, goodwill.

The Company performed its annual goodwill impairment analysis as of December 31, 2018. The Company assessed qualitative factors to determine whether the existence of events and circumstances indicated that it is more likely than not that the indefinite-lived intangible asset is impaired, and determined no factors indicated an impairment. Goodwill is allocated between the reporting units of Wholesale Bank, Retail Bank, and Wealth Management. The Company performed its analysis of goodwill at the reporting unit level analyzing any factors that would impact the estimated fair value of the reporting unit compared to its carrying value.

Fair Value

A hierarchical disclosure framework associated with the level of pricing observability is utilized in measuring financial instruments at fair value. The degree of judgment utilized in measuring the fair value of financial instruments generally correlates to the level of pricing observability. Financial instruments with readily available active quoted prices or for which fair value can be measured from actively quoted prices generally will have a higher degree of pricing observability and a lesser degree of judgment utilized in measuring fair value. Conversely, financial instruments rarely traded or not quoted will generally have little or no pricing observability and a higher degree of judgment utilized in measuring fair value. Pricing observability is impacted by a number of factors, including the type of financial instrument, whether the financial instrument is new to the market and not yet established and the characteristics specific to the transaction.

RECENT ACCOUNTING PRONOUNCEMENTS

Information regarding Recent Accounting Pronouncements is included in Note 1 of the Notes to Consolidated Financial Statements in Item 8 below.

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## RESULTS OF OPERATIONS

For the year ended December 31, 2018, net earnings available to common shareholders were $316.2 million, or $1.43 per diluted common share, compared to net earnings available to common shareholders of $242.3 million, or $1.10 per diluted common share for the year ended December 31, 2017. The increase in net earnings available to common shareholders in 2018 is principally attributable to an increase in net interest income and a decrease in non-interest expense, offset by an increase in the provision for loan and lease losses. The increase in net interest income was driven primarily by higher average yields on interest-earning assets, specifically within the loan and lease and investment security portfolios, and growth in the loan and lease portfolio. The increase is partially offset by a higher cost of funds, due to a rising rate environment.

The decrease in non-interest expense was driven by cost reductions from the organizational simplification as well as the procurement phases of the operational excellence component of Umpqua Next Gen, and there were no merger-related expenses in the period compared to $9.3 million of merger-related expenses for the year ended December 31, 2017. The decrease in non-interest expense in 2018 was partially offset by an increase in consulting expenses, severance costs, and exit and disposal costs that were directly associated with the implementation of the Umpqua Next Gen efforts. The increase in the provision for loan and lease losses was principally due to growth in the loan and lease portfolio and higher net charge-offs.

For the year ended December 31, 2017, net earnings available to common shareholders were $242.3 million, or $1.10 per diluted common share, compared to net earnings available to common shareholders of $229.9 million, or $1.04 per diluted common share for the year ended December 31, 2016. The increase for the year ended December 31, 2017 compared to the prior year was mainly attributable to the $20.0 million net benefit to the provision for income taxes related to the revaluation of the net deferred tax liability and amortization of tax credit investments associated with the passage of the Tax Cuts and Jobs Act in December 2017 ("Tax Act"), partially offset by the non-deductibility of certain executive compensation. The Company also had an increase in net interest income, which was driven primarily by higher average balances of loans and leases. The increase in net interest income was offset by a decrease in non-interest income and an increase in non-interest expense. The decrease in non-interest income was driven primarily by lower residential mortgage banking revenue and higher net loss on junior subordinated debentures carried at fair value. The increase in non-interest expense was primarily driven by higher salaries and benefits expense, offset by lower merger related expenses.

The following table presents the returns on average assets, average common shareholders' equity and average tangible common shareholders' equity for the years ended December 31, 2018, 2017, and 2016. For each of the periods presented, the table includes the calculated ratios based on reported net earnings available to common shareholders. Our return on average common shareholders' equity is negatively impacted as the result of capital required to support goodwill. To the extent this performance metric is used to compare our performance with other financial institutions that do not have merger and acquisition-related intangible assets, we believe it is beneficial to also consider the return on average tangible common shareholders' equity. The return on average tangible common shareholders' equity is calculated by dividing net earnings available to common shareholders by average shareholders' common equity less average goodwill and intangible assets, net (excluding MSRs). The return on average tangible common shareholders' equity is considered a non-GAAP financial measure and should be viewed in conjunction with the return on average common shareholders' equity.

Return on Average Assets, Common Shareholders' Equity and Tangible Common Shareholders' Equity
For the Years Ended December 31,

| (dollars in thousands) | 2018 | 2017 | 2016 |
|---|---|---|---|

| | | | |
|---|---|---|---|
| Return on average assets | 1.21 % | 0.97 % | 0.95 % |
| Return on average common shareholders' equity | 7.90 % | 6.17 % | 5.96 % |
| Return on average tangible common shareholders' equity | 14.45 % | 11.49 % | 11.34 % |
| Calculation of average common tangible shareholders' equity: | | | |
| Average common shareholders' equity | $4,002,700 | $3,929,566 | $3,856,890 |
| Less: average goodwill and other intangible assets, net | (1,814,756 ) | (1,821,223 ) | (1,828,575 ) |
| Average tangible common shareholders' equity | $2,187,944 | $2,108,343 | $2,028,315 |

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Additionally, management believes tangible common equity and the tangible common equity ratio are meaningful measures of capital adequacy. Umpqua believes the exclusion of certain intangible assets in the computation of tangible common equity and tangible common equity ratio provides a meaningful base for period-to-period and company-to-company comparisons, which management believes will assist investors in analyzing the operating results and capital of the Company. Tangible common equity is calculated as total shareholders' equity less preferred stock and less goodwill and other intangible assets, net (excluding MSRs). In addition, tangible assets are total assets less goodwill and other intangible assets, net (excluding MSRs). The tangible common equity ratio is calculated as tangible common shareholders' equity divided by tangible assets. The tangible common equity and tangible common equity ratio is considered a non-GAAP financial measure and should be viewed in conjunction with the total shareholders' equity and the total shareholders' equity ratio.

The following table provides a reconciliation of ending shareholders' equity (GAAP) to ending tangible common equity (non-GAAP), and ending assets (GAAP) to ending tangible assets (non-GAAP) as of December 31, 2018 and December 31, 2017:

Reconciliations of Total Shareholders' Equity to Tangible Common Shareholders' Equity and Total Assets to Tangible Assets

| (dollars in thousands) | December 31, 2018 | December 31, 2017 |
|---|---|---|
| Total shareholders' equity | $4,056,442 | $3,969,367 |
| Subtract: | | |
| Goodwill | 1,787,651 | 1,787,651 |
| Other intangible assets, net | 23,964 | 30,130 |
| Tangible common shareholders' equity | $2,244,827 | $2,151,586 |
| Total assets | $26,939,781 | $25,680,447 |
| Subtract: | | |
| Goodwill | 1,787,651 | 1,787,651 |
| Other intangible assets, net | 23,964 | 30,130 |
| Tangible assets | $25,128,166 | $23,862,666 |
| Tangible common equity ratio | 8.93 % | 9.02 % |

Non-GAAP financial measures have inherent limitations, are not required to be uniformly applied, and are not audited. Although we believe these non-GAAP financial measures are frequently used by stakeholders in the evaluation of a company, they have limitations as analytical tools, and should not be considered in isolation or as a substitute for analyses of results as reported under GAAP.

## NET INTEREST INCOME

Net interest income is the largest source of our income. Net interest income for 2018 was $938.6 million, an increase of $73.0 million or 8% compared to the same period in 2017. The increase in net interest income in 2018 compared to 2017 was driven by growth in interest-earning assets, specifically the loan and lease portfolio, reflecting strong growth during the year, along with higher average yields on loans and leases, taxable investments and an increase in yields on loans held for sale related to higher mortgage rates during the period. The increase was partially offset by increased volumes of interest-bearing liabilities and an increase in the average cost of funds due to rising interest rates. In addition, the accretion of the purchase discount on acquired loans continued to decline in 2018.

Net interest income for 2017 was $865.7 million, an increase of $27.6 million or 3% compared to the same period in 2016. The increase in net interest income in 2017 compared to 2016 was driven primarily by higher average balances of loans and leases and investment securities, partially offset by lower average yields on loans and leases including a lower level of accretion of the purchase discount on acquired loans. The increase in net interest income was also offset by increased volumes of interest-bearing liabilities and an increase in the average cost of funds due to rising market rates in 2017.

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The net interest margin (net interest income as a percentage of average interest-earning assets) on a fully tax equivalent basis was 4.04% for 2018, an increase of 10 basis points compared to 2017. The increase in net interest margin primarily resulted from higher average yields on the loan and lease portfolio, the loans held for sale, and taxable investments, offset by an increase in the cost of interest-bearing liabilities. In addition, yields on tax-exempt investments decreased due to the impact of the decline in the tax-effect adjustment on these securities. The yield on loans and leases for 2018 increased by 18 basis points compared to 2017. The total cost of interest-bearing liabilities for 2018 was 0.84%, representing an increase of 31 basis points compared to 2017, driven largely by the four federal funds rate increases during the year. The cost of time deposits was 1.57% in 2018 compared to 1.05% in 2017, reflecting significant growth of the time deposit portfolio driven by promotional retail offers and brokered time deposits.

The net interest margin on a fully tax-equivalent basis was 3.94% for 2017, a decrease of 8 basis points compared to the same period in 2016. The decrease in net interest margin primarily resulted from the lower average yields on the loan and lease portfolio, as well as an increase in the cost of interest-bearing liabilities. The yield on loans and leases for 2017 decreased by 9 basis points compared to 2016. The total cost of interest-bearing liabilities for 2017 was 0.53%, representing an increase of 7 basis points compared to 2016. The cost of time deposits was 1.05% in 2017 compared to 0.86% in 2016.

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Our net interest income is affected by changes in the amount and mix of interest-earning assets and interest-bearing liabilities, as well as changes in the yields earned on interest-earning assets and rates paid on deposits and borrowed funds. The following table presents condensed average balance sheet information, together with interest income and yields on average interest-earning assets, and interest expense and rates paid on average interest-bearing liabilities for years ended December 31, 2018, 2017 and 2016:

Average Rates and Balances

| (dollars in thousands) | 2018 | | | 2017 | | | 2016 | | |
|---|---|---|---|---|---|---|---|---|---|
| | Average Balance | Interest Income or Expense | Average Yields or Rates | Average Balance | Interest Income or Expense | Average Yields or Rates | Average Balance | Interest income or Expense | Average Yields or Rates |
| INTEREST-EARNING ASSETS: | | | | | | | | | |
| Loans held for sale | $288,288 | $14,475 | 5.02% | $383,802 | $14,374 | 3.75% | $416,724 | $15,995 | 3.84% |
| Loans and leases (1) | 19,562,369 | 957,639 | 4.90% | 18,169,449 | 856,944 | 4.72% | 17,190,625 | 827,596 | 4.81% |
| Taxable securities | 2,729,950 | 78,002 | 2.86% | 2,851,136 | 59,478 | 2.09% | 2,314,062 | 47,826 | 2.07% |
| Non-taxable securities (2) | 281,906 | 10,316 | 3.66% | 286,605 | 13,244 | 4.62% | 284,780 | 13,426 | 4.71% |
| Temporary investments and interest-bearing deposits | 446,500 | 8,665 | 1.94% | 421,836 | 4,380 | 1.04% | 736,854 | 3,918 | 0.53% |
| Total interest earning assets | 23,309,013 | 1,069,097 | 4.59% | 22,112,828 | 948,420 | 4.29% | 20,943,045 | 908,761 | 4.34% |
| Allowance for loan and lease losses | (144,243) | | | (138,587) | | | (132,492) | | |
| Other assets | 3,046,163 | | | 3,099,903 | | | 3,269,200 | | |
| Total assets | $26,210,933 | | | $25,074,144 | | | $24,079,753 | | |
| INTEREST-BEARING LIABILITIES: | | | | | | | | | |
| Interest-bearing checking | $2,333,662 | $7,675 | 0.33% | $2,322,194 | $3,725 | 0.16% | $2,189,589 | $2,415 | 0.11% |
| Money market deposits | 6,438,175 | 27,599 | 0.43% | 6,741,983 | 13,069 | 0.19% | 6,773,939 | 10,499 | 0.15% |
| Savings deposits | 1,473,134 | 1,356 | 0.09% | 1,412,039 | 699 | 0.05% | 1,248,831 | 655 | 0.05% |
| Time deposits | 3,575,526 | 56,055 | 1.57% | 2,672,687 | 28,089 | 1.05% | 2,518,507 | 21,671 | 0.86% |
| Total interest-bearing deposits | 13,820,497 | 92,685 | 0.67% | 13,148,903 | 45,582 | 0.35% | 12,730,866 | 35,240 | 0.28% |
| Federal funds purchased and repurchase agreements | 287,767 | 506 | 0.18% | 344,200 | 475 | 0.14% | 333,919 | 132 | 0.04% |
| Term debt | 785,593 | 13,604 | 1.73% | 846,542 | 14,159 | 1.67% | 897,050 | 15,005 | 1.67% |
| Junior subordinated debentures | 370,518 | 21,715 | 5.86% | 365,196 | 18,000 | 4.93% | 359,003 | 15,674 | 4.37% |
| Total interest-bearing liabilities | 15,264,375 | 128,510 | 0.84% | 14,704,841 | 78,216 | 0.53% | 14,320,838 | 66,051 | 0.46% |
| Non-interest-bearing deposits | 6,699,112 | | | 6,202,835 | | | 5,616,585 | | |
| Other liabilities | 244,746 | | | 236,902 | | | 285,440 | | |

| | | | |
|---|---|---|---|
| Total liabilities | 22,208,233 | 21,144,578 | 20,222,863 |
| Common equity | 4,002,700 | 3,929,566 | 3,856,890 |
| Total liabilities and shareholders' equity | $ | | |