

COLUMBIA BANKING SYSTEM INC

Form 10-Q

November 08, 2010

Table of Contents

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended September 30, 2010.

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 0-20288

COLUMBIA BANKING SYSTEM, INC.

(Exact name of issuer as specified in its charter)

Edgar Filing: COLUMBIA BANKING SYSTEM INC - Form 10-Q

Washington
(State or other jurisdiction of
incorporation or organization)

91-1422237
(I.R.S. Employer
Identification Number)

1301 A Street

Tacoma, Washington
(Address of principal executive offices)

98402-2156
(Zip Code)

(253) 305-1900

(Issuer's telephone number, including area code)

(Former name, former address and former fiscal year, if changed since last report)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

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

Large accelerated filer Accelerated filer

Non-accelerated filer Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes No

The number of shares of common stock outstanding at October 29, 2010 was 39,335,365.

Table of Contents

TABLE OF CONTENTS

	Page
<u>PART I FINANCIAL INFORMATION</u>	
Item 1. <u>Financial Statements (unaudited)</u>	
<u>Consolidated Condensed Statements of Income - three and nine months ended September 30, 2010 and 2009</u>	1
<u>Consolidated Condensed Balance Sheets - September 30, 2010 and December 31, 2009</u>	2
<u>Consolidated Condensed Statements of Changes in Shareholders' Equity - nine months ended September 30, 2010 and 2009</u>	3
<u>Consolidated Condensed Statements of Cash Flows - nine months ended September 30, 2010 and 2009</u>	4
<u>Notes to Unaudited Consolidated Condensed Financial Statements</u>	5
Item 2. <u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	21
Item 3. <u>Quantitative and Qualitative Disclosures about Market Risk</u>	38
Item 4. <u>Controls and Procedures</u>	39
<u>PART II OTHER INFORMATION</u>	
Item 1. <u>Legal Proceedings</u>	40
Item 1A. <u>Risk Factors</u>	40
Item 2. <u>Unregistered Sales of Equity Securities and Use of Proceeds</u>	46
Item 3. <u>Defaults Upon Senior Securities</u>	46
Item 4. <u>[Removed and Reserved]</u>	46
Item 5. <u>Other Information</u>	46
Item 6. <u>Exhibits</u>	47
<u>Signatures</u>	48

Table of Contents**PART I - FINANCIAL INFORMATION****Item 1. FINANCIAL STATEMENTS****CONSOLIDATED CONDENSED STATEMENTS OF INCOME****Columbia Banking System, Inc.****(Unaudited)****Consolidated Statements of Income**

<i>(in thousands except per share)</i>	Three Months Ended September 30,		Nine Months Ended September 30,	
	2010	2009 (1)	2010	2009 (1)
Interest Income				
Loans	\$ 44,882	\$ 29,151	\$ 120,769	\$ 88,202
Taxable securities	4,660	4,327	14,113	12,730
Tax-exempt securities	2,252	2,169	6,988	6,258
Federal funds sold and deposits in banks	281	53	640	69
Total interest income	52,075	35,700	142,510	107,259
Interest Expense				
Deposits	4,007	5,531	13,282	18,297
Federal Home Loan Bank and Federal Reserve Bank borrowings	716	651	2,131	2,116
Long-term obligations	266	280	769	937
Other borrowings	121	120	357	357
Total interest expense	5,110	6,582	16,539	21,707
Net Interest Income	46,965	29,118	125,971	85,552
Provision for loan and lease losses	9,000	16,500	37,500	48,500
Provision for losses on covered loans	453		453	
Net interest income after provision	37,512	12,618	88,018	37,052
Noninterest Income				
Gain on bank acquisitions			9,818	
Service charges and other fees	6,518	3,806	18,384	10,982
Merchant services fees	2,051	1,957	5,700	5,607
Redemption of Visa and Mastercard shares			58	49
Bank owned life insurance	521	515	1,541	1,532
Change in indemnification asset	(4,536)		(1,137)	
Other	629	912	2,529	2,994
Total noninterest income	5,183	7,190	36,893	21,164
Noninterest Expense				
Compensation and employee benefits	17,574	11,869	52,057	36,017
Occupancy	4,278	3,023	12,554	9,005
Merchant processing	934	841	2,697	2,442
Advertising and promotion	630	296	2,253	1,675

Edgar Filing: COLUMBIA BANKING SYSTEM INC - Form 10-Q

Data processing and communications	2,477	1,010	6,923	2,974
Legal and professional fees	1,609	793	4,584	2,779
Taxes, licenses and fees	803	582	2,055	1,975
Regulatory premiums	1,952	1,220	4,910	4,719
Net cost of operation of other real estate	(1,442)	318	(802)	590
Amortization of intangibles	1,044	259	2,886	797
Other	3,661	2,935	12,045	8,668
Total noninterest expense	33,520	23,146	102,162	71,641
Income (loss) before income taxes	9,175	(3,338)	22,749	(13,425)
Income tax provision (benefit)	3,971	(1,836)	4,573	(7,905)
Net Income (Loss)	\$ 5,204	\$ (1,502)	\$ 18,176	\$ (5,520)
Net Income (Loss) Applicable to Common Shareholders	\$ 2,474	\$ (2,605)	\$ 13,229	\$ (8,818)
Earnings (loss) per common share				
Basic	\$ 0.06	\$ (0.11)	\$ 0.39	\$ (0.45)
Diluted	\$ 0.06	\$ (0.11)	\$ 0.38	\$ (0.45)
Dividends paid per common share	\$ 0.01	\$ 0.01	\$ 0.03	\$ 0.06
Weighted average number of common shares outstanding	38,976	23,468	33,938	19,837
Weighted average number of diluted common shares outstanding	39,137	23,468	34,142	19,837

(1) Reclassified to conform to the current period's presentation
See accompanying notes to unaudited consolidated condensed financial statements.

Table of Contents**CONSOLIDATED CONDENSED BALANCE SHEETS****Columbia Banking System, Inc.****(Unaudited)**

<i>(in thousands)</i>	September 30, 2010	December 31, 2009
ASSETS		
Cash and due from banks	\$ 77,235	\$ 55,802
Interest-earning deposits with banks	448,854	249,272
Total cash and cash equivalents	526,089	305,074
Securities available for sale at fair value (amortized cost of \$656,986 and \$602,675, respectively)	692,741	620,038
Federal Home Loan Bank stock at cost	17,908	11,607
Loans held for sale	1,513	
Loans, excluding covered loans, net of deferred loan fees of (\$3,662) and (\$4,616), respectively	1,934,162	2,008,884
Less: allowance for loan and lease losses	62,334	53,478
Loans, excluding covered loans, net	1,871,828	1,955,406
Covered loans	561,131	
Less: allowance for losses on covered loans	453	
Covered loans, net	560,678	
Total loans, net	2,432,506	1,955,406
Federal Deposit Insurance Corporation indemnification asset	166,696	
Interest receivable	11,441	10,335
Premises and equipment, net	62,824	62,670
Other real estate owned (\$17,017 and \$0 covered by Federal Deposit Insurance Corporation loss share, respectively)	40,276	19,037
Goodwill	109,639	95,519
Core deposit intangible, net	19,733	4,863
Other assets	163,894	116,381
Total Assets	\$ 4,245,260	\$ 3,200,930
LIABILITIES AND SHAREHOLDERS EQUITY		
Deposits:		
Non-interest bearing	\$ 864,920	\$ 574,687
Interest-bearing	2,441,966	1,908,018
Total deposits	3,306,886	2,482,705
Federal Home Loan Bank advances	119,584	100,000
Securities sold under agreements to repurchase	25,000	25,000
Other borrowings	1,599	86
Long-term subordinated debt	25,719	25,669
Other liabilities	61,780	39,331
Total liabilities	3,540,568	2,672,791

Edgar Filing: COLUMBIA BANKING SYSTEM INC - Form 10-Q

Commitments and contingent liabilities

Shareholders' equity:

	September 30, 2010	December 31, 2009		
Preferred stock (no par value, \$76,898 aggregate liquidation preference)				
Authorized shares	2,000	2,000		
Issued and outstanding		77		74,301
Common Stock (no par value)				
Authorized shares	63,033	63,033		
Issued and outstanding	39,328	28,129	576,438	348,706
Retained earnings			105,478	93,316
Accumulated other comprehensive income			22,776	11,816
Total shareholders' equity			704,692	528,139
Total Liabilities and Shareholders' Equity			\$ 4,245,260	\$ 3,200,930

See accompanying notes to unaudited consolidated condensed financial statements.

Table of Contents

CONSOLIDATED CONDENSED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY

Columbia Banking System, Inc.

(Unaudited)

(in thousands)	Preferred Stock		Common Stock		Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total Shareholders' Equity
	Number of Shares	Amount	Number of Shares	Amount			
Balance at January 1, 2009	77	\$ 73,743	18,151	\$ 233,192	\$ 103,061	\$ 5,389	\$ 415,385
Comprehensive income:							
Net income					(5,520)		(5,520)
Other comprehensive loss, net of tax:							
Net unrealized gain from securities, net of reclassification adjustments						8,717	8,717
Net change in cash flow hedging instruments						(1,264)	(1,264)
Net pension plan liability adjustment						(660)	(660)
Total comprehensive income							1,273
Accretion of preferred stock discount		414			(414)		
Issuance of common stock, net of offering costs			9,775	113,537			113,537
Issuance of common stock - stock option and other plans			88	928			928
Issuance of common stock - restricted stock awards, net of cancelled awards			85				
Share-based payment					857		857
Tax benefit deficiency associated with share-based compensation					(83)		(83)
Preferred dividends					(2,884)		(2,884)
Cash dividends paid on common stock					(1,093)		(1,093)
Balance at September 30, 2009	77	\$ 74,157	28,099	\$ 348,431	\$ 93,150	\$ 12,182	\$ 527,920
Balance at January 1, 2010	77	\$ 74,301	28,129	\$ 348,706	\$ 93,316	\$ 11,816	\$ 528,139
Comprehensive income:							
Net income					18,176		18,176
Other comprehensive income, net of tax:							
Net unrealized gain from securities, net of reclassification adjustments						11,859	11,859
Net change in cash flow hedging instruments						(943)	(943)
Net pension plan liability adjustment						44	44
Total comprehensive income							29,136
Redemption of preferred stock and common stock warrant	(77)	(76,898)		(3,302)			(80,200)
Accretion of preferred stock discount		2,597			(2,597)		
Issuance of common stock, net of offering costs			11,040	229,129			229,129
Issuance of common stock - stock option and other plans			65	864			864
			94				

Edgar Filing: COLUMBIA BANKING SYSTEM INC - Form 10-Q

Issuance of common stock - restricted stock awards, net of cancelled awards						
Share-based payment		1,054				1,054
Tax benefit deficiency associated with share-based compensation		(13)				(13)
Preferred dividends			(2,349)			(2,349)
Cash dividends paid on common stock			(1,068)			(1,068)
Balance at September 30, 2010	\$	39,328	\$ 576,438	\$ 105,478	\$	22,776 \$ 704,692

See accompanying notes to unaudited consolidated condensed financial statements.

Table of Contents**CONSOLIDATED CONDENSED STATEMENTS OF CASH FLOWS****Columbia Banking System, Inc.****(Unaudited)**

<i>(in thousands)</i>	Nine Months Ended September 30,	
	2010	2009
Cash Flows From Operating Activities		
Net Income (Loss)	\$ 18,176	\$ (5,520)
Adjustments to reconcile net income to net cash provided by operating activities		
Provision for loan and lease losses	37,953	48,500
Stock-based compensation expense	1,054	857
Depreciation, amortization and accretion	10,105	5,384
Net realized gain on Federal Deposit Insurance Corporation assisted bank acquisitions	(9,818)	
Net realized gain on sale of securities	(58)	
Net realized (gain) loss on sale of other assets	(16)	145
Net realized gain on sale of other real estate owned	(3,527)	
Gain on termination of cash flow hedging instruments	(1,463)	(1,960)
Write-down on other real estate owned	4,586	120
Net change in:		
Loans held for sale	(1,513)	1,964
Deferred federal income tax	(394)	(4,483)
Interest receivable	4,195	461
Interest payable	(625)	(2,165)
Other assets	771	(3,919)
Other liabilities	22,053	(2,588)
Net cash provided by operating activities	81,479	36,796
Cash Flows From Investing Activities		
Purchases of securities available for sale	(64,054)	(154,973)
Proceeds from sales of securities available for sale	69,328	
Proceeds from principal repayments and maturities of securities available for sale	66,118	49,878
Loans originated and acquired, net of principal collected	114,618	108,785
Increase in Small Business Administration secured borrowings	1,599	
Purchases of premises and equipment	(3,910)	(5,469)
Proceeds from disposal of premises and equipment	71	11
Proceeds from sales of covered other real estate owned	10,652	
Proceeds from sales of other real estate and other personal property owned	3,943	4,805
Capital improvements on other real estate properties	(1,147)	(380)
Net cash acquired in business combinations	155,910	
Net cash provided by investing activities	353,128	2,657
Cash Flows From Financing Activities		
Net (decrease) increase in deposits	(323,141)	61,416
Proceeds from Federal Home Loan Bank and Federal Reserve Bank borrowings		739,000
Repayment from Federal Home Loan Bank and Federal Reserve Bank borrowings	(36,237)	(838,000)
Net decrease in other borrowings	(86)	(150)
Cash dividends paid	(3,908)	(3,913)
Repurchase of preferred stock and common stock warrant	(80,200)	
Proceeds from issuance of common stock	229,129	113,537
Proceeds from exercise of stock options	851	845

Edgar Filing: COLUMBIA BANKING SYSTEM INC - Form 10-Q

Net cash (used in) provided by financing activities	(213,592)	72,735
Increase in cash and cash equivalents	221,015	112,188
Cash and cash equivalents at beginning of period	305,074	88,730

Cash and cash equivalents at end of period	\$ 526,089	\$ 200,918
--	------------	------------

Supplemental Information:

Cash paid for interest	\$ 17,164	\$ 23,872
Cash paid for income tax	\$ 3,015	\$ 500
Loans transferred to other real estate owned	\$ 27,266	\$ 19,998

See accompanying notes to unaudited consolidated condensed financial statements.

Table of Contents

NOTES TO UNAUDITED CONSOLIDATED CONDENSED FINANCIAL STATEMENTS

Columbia Banking System, Inc.

1. Basis of Presentation and Significant Accounting Policies

(a) Basis of Presentation

The interim unaudited consolidated condensed financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America for condensed interim financial information and with instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, certain financial information and footnotes have been omitted or condensed. The consolidated condensed financial statements include the accounts of Columbia Banking System, Inc. (the Company), and its wholly owned banking subsidiary Columbia State Bank (the Bank). All intercompany transactions and accounts have been eliminated in consolidation. In the opinion of management, all adjustments (consisting only of normal recurring adjustments) considered necessary for a fair statement of the results for the interim periods presented have been included. The results of operations for the nine months ended September 30, 2010 are not necessarily indicative of results to be anticipated for the year ending December 31, 2010. The accompanying interim unaudited consolidated condensed financial statements should be read in conjunction with the financial statements and related notes contained in the Company's 2009 Annual Report on Form 10-K.

Certain reclassifications have been made to the prior-period's financial statements to conform to the current period's presentation.

(b) Significant Accounting Policies

The significant accounting policies used in preparation of our consolidated financial statements are disclosed in our 2009 Annual Report on Form 10-K. With the exception of the significant accounting policies listed below, there have not been any other changes in our significant accounting policies compared to those contained in our 2009 10-K disclosure for the year ended December 31, 2009.

Loans

The Company's accounting methods for loans differ depending on whether the loans were originated or were acquired as a result of a business acquisition.

Originated Loans

Loans are generally carried at principal amounts less net deferred loan fees. Net deferred loan fees include deferred unamortized origination fees less direct incremental origination costs. Net deferred loan fees are amortized into interest income over the contractual life of the related loans. Interest income is accrued as earned. Fees related to lending activities other than the origination or purchase of loans are recognized as noninterest income during the period the related services are performed.

Loans are placed on nonaccrual status when a loan becomes contractually past due 90 days with respect to interest or principal unless the loan is both well secured and in the process of collection, or if full collection of interest or principal becomes uncertain. When a loan is placed on nonaccrual status, the accrued and unpaid interest receivable is reversed and the accretion of net deferred loan fees ceases. Thereafter, interest collected on the loan is accounted for on the cash collection or cost recovery method until qualifying for return to accrual status. Generally, a loan may be returned to accrual status when the delinquent principal and interest are brought current in accordance with the terms of the loan agreement and future payments are reasonably assured.

Loans are considered impaired when based on current information and events, it is probable that the Company will be unable to collect all amounts due according to the contractual terms of the loan agreement. The assessment for impairment occurs when and while such loans are designated as criticized/classified per the Company's internal risk rating system or when and while such loans are on nonaccrual. All nonaccrual loans greater than \$250,000 are considered impaired and analyzed individually on a quarterly basis. Criticized/classified loans with an outstanding balance greater than \$250,000 are evaluated for potential impairment on a quarterly basis.

When a loan with unique risk characteristics has been identified as being impaired, the amount of impairment will be measured by the Company using discounted cash flows, except when it is determined that the primary (remaining) source of repayment for the loan is the operation or

Edgar Filing: COLUMBIA BANKING SYSTEM INC - Form 10-Q

liquidation of the underlying collateral. In these cases, the current fair value of the collateral, reduced by costs to sell, will be used in place of discounted cash flows. As a final alternative, the observable market price of the debt may be used to assess impairment. Predominantly, the Company uses the fair value of collateral approach based upon a reliable valuation.

Table of Contents

NOTES TO UNAUDITED CONSOLIDATED CONDENSED FINANCIAL STATEMENTS (Continued)

Columbia Banking System, Inc.

When the measurement of the impaired loan is less than the recorded amount of the loan, an impairment is recognized by recording a charge-off to the allowance for loan and lease losses or by designating a specific reserve. The Company's policy is to record cash receipts received on impaired loans first as reductions to principal and then to interest income.

Unfunded loan commitments are generally related to providing credit facilities to clients of the Bank, and are not actively traded financial instruments.

Acquired Loans

Loans acquired in a business acquisition after December 31, 2008 are recorded at their fair value at acquisition date, factoring in credit losses expected to be incurred over the life of the loan. Accordingly, an allowance for loan losses is not carried over or recorded as of the acquisition date.

Loans purchased with evidence of credit deterioration since origination for which it is probable that all contractually required payments will not be collected are accounted for under Accounting Standards Codification (ASC) 310-30, *Loans and Debt Securities Acquired with Deteriorated Credit Quality*, formerly SOP 03-3 *Accounting for Certain Loans or Debt Securities Acquired in a Transfer*. In situations where such loans have similar risk characteristics, loans are aggregated into pools to estimate cash flows. The Company aggregated all of the loans acquired in the Federal Deposit Insurance Corporation (FDIC)-assisted acquisitions into pools, based on common risk characteristics. A pool is accounted for as a single asset with a single interest rate, cumulative loss rate and cash flow expectation. Expected cash flows at the acquisition date in excess of the fair value of loans are considered to be accretible yield, which is recognized as interest income over the life of the loan pool using a level yield method if the timing and amount of the future cash flows of the pool is reasonably estimable. Subsequent to the acquisition date, any increases in cash flow over those expected at purchase date in excess of fair value are recorded as interest income prospectively. Any subsequent decreases in cash flow over those expected at purchase date are recognized by recording an allowance for loan losses. Any disposals of loans, including sales of loans, payments in full or foreclosures result in the removal of the loan from the loan pool at the carrying amount. The Company elected to account for all acquired loans under ASC 310-30.

Covered Assets and Related FDIC Indemnification Asset

Assets subject to loss-sharing agreements with the FDIC are labeled "covered" on the Consolidated Condensed Balance Sheet and include certain loans and other real estate owned (OREO).

All OREO acquired in FDIC-assisted acquisitions are subject to FDIC loss-sharing agreements and are referred to as covered OREO. Covered OREO is reported exclusive of expected reimbursement cash flows from the FDIC. Upon transferring covered loan collateral to covered OREO status, acquisition date fair value discounts on the related loan are also transferred to covered OREO. Fair value adjustments on covered OREO result in a reduction of the covered OREO carrying amount and a corresponding increase in the expected FDIC reimbursement, with the estimated net loss to the Company, if any, charged against earnings.

The acquisition date fair value of the reimbursement the Company expected to receive from the FDIC under those agreements was recorded in the FDIC indemnification asset on the Consolidated Condensed Balance Sheet. Subsequent to the acquisition the indemnification asset is tied to the loss in the covered loans and covered OREO and is not being accounted for under fair value. The FDIC indemnification asset is accounted for on the same basis as the related covered loans and covered OREO and is the present value of the cash flows the Company expects to collect from the FDIC under the loss-sharing agreements. The difference between the present value and the undiscounted cash flow the Company expects to collect from the FDIC is accreted into noninterest income over the life of the FDIC indemnification asset. The FDIC indemnification asset is adjusted for any changes in expected cash flows based on the loan performance. Any projected increase in cash flows of the loans over those expected will result in a decrease in the accretion for the FDIC indemnification asset recognized in noninterest income. Any projected decrease in cash flows of the loans over those expected will result in an increase in the FDIC indemnification asset with a corresponding benefit recorded to the provision for loan and lease losses.

Core Deposit Intangible

Core Deposit Intangible (CDI) is a measure of the value of non-interest checking, savings, NOW and money market deposits that are acquired in a business combination. The fair value of the CDI stemming from any given business combination is based on the present value of the expected cost savings attributable to the core deposit funding, relative to an alternative source of funding. The CDI related to the Columbia River Bank and American Marine Bank acquisitions will be

Table of Contents

NOTES TO UNAUDITED CONSOLIDATED CONDENSED FINANCIAL STATEMENTS (Continued)

Columbia Banking System, Inc.

amortized over an estimated useful life of 10 years to approximate the existing deposit relationships acquired. The Company evaluates such identifiable intangibles for impairment when an indication of impairment exists.

2. Accounting Pronouncements Recently Issued

In July 2010, the Financial Accounting Standards Board (the FASB) issued Accounting Standards Update (ASU) 2010-20, an amendment of *Receivables - Disclosures about the Credit Quality of Financing Receivables and the Allowance for Credit Losses* (Topic 310). ASU 2010-20 attempts to provide financial statement users with greater transparency about an entity's allowance for credit losses and the credit quality of its financing receivables. The objective of the amendments in this update is for an entity to provide disclosures that facilitate financial statement users' evaluation of the following:

1. the nature of credit risk inherent in the entity's portfolio of financing receivables,
2. how that risk is analyzed and assessed in arriving at the allowance for credit losses and
3. the changes and reasons for those changes in the allowance for credit losses.

In addition to existing requirements, the amendments in this update require an entity to provide the following additional disclosures about its financing receivables:

1. credit quality indicators of financing receivables at the end of the reporting period by class of financing receivables,
2. the aging of past due financing receivables at the end of the reporting period by class of financing receivables,
3. the nature and extent of troubled debt restructurings that occurred during the period by class of financing receivables and their effect on the allowance for credit losses,
4. the nature and extent of financing receivables modified as troubled debt restructurings within the previous 12 months that defaulted during the reporting period by class of financing receivables and their effect on the allowance for credit losses and
5. significant purchases and sales of financing receivables during the reporting period disaggregated by portfolio segment.

The new guidance will become effective in the first interim or annual period ending on or after December 15, 2010. The new guidance will not have a material impact on the Company's consolidated financial statements.

In April 2010, the FASB issued ASU 2010-18, an amendment of *Receivables - Loans and Debt Securities Acquired with Deteriorated Credit Quality* (Topic 310-30). ASU 2010-18 attempts to eliminate diversity in practice related to loan modifications. Modifications of loans within a pool of loans accounted for as a single asset do not result in the removal of those loans from the pool even if the modification of those loans would otherwise be considered a troubled debt restructuring. The entity will continue to be required to consider whether the pool of assets in

which the loans are included is impaired if expected cash flows for the pool change. The new guidance became effective in the first reporting period ending on or after July 15, 2010 and is to be applied prospectively. The Company was already in compliance with the amendments of this topic prior to the release of ASU 2010-18. The new guidance did not have an impact on the Company's consolidated financial statements.

In January 2010, the FASB issued ASU 2010-06, *Fair Value Measurements and Disclosures* (Topic 820), which focuses on *Improving Disclosures about Fair Value Measurement*. ASU 2010-06 requires new disclosures about transfers in and out of Level 1 and Level 2 fair value measurements and the activity in Level 3 fair value measurements (i.e. purchases, sales, issuances, and settlements). ASU 2010-06 also amended disclosure requirements related to the level of disaggregation of assets and liabilities, as well as disclosures about input and valuation techniques used to measure fair value for both recurring and nonrecurring fair value measurements. The new guidance became effective for interim and annual reporting periods beginning after December 15, 2009, except for the disclosures about purchases, sales, issuances, and settlements in the roll forward of activity in Level 3 fair value measurements and did not have a material impact on the Company's consolidated financial statements. Those disclosures are effective for fiscal years beginning after December 15, 2010, and for interim periods within those fiscal years.

3. Earnings per Common Share

Basic EPS is computed by dividing income applicable to common shareholders by the weighted average number of common shares outstanding for the period. Common shares outstanding include common stock and vested restricted stock awards where recipients have satisfied the vesting terms. Diluted EPS reflects the assumed conversion of all dilutive securities, applying the treasury stock method. The Company calculates earnings per share using the two-class method as described in the Earnings per Share topic of the FASB ASC.

Table of Contents**NOTES TO UNAUDITED CONSOLIDATED CONDENSED FINANCIAL STATEMENTS (Continued)****Columbia Banking System, Inc.**

The following table sets forth the computation of basic and diluted earnings per share for the three and nine months ended September 30, 2010 and 2009:

<i>(in thousands except per share)</i>	Three Months Ended September 30,		Nine Months Ended September 30,	
	2010	2009	2010	2009
Basic EPS:				
Net income	\$ 5,204	\$ (1,502)	\$ 18,176	\$ (5,520)
Less: Preferred dividends and accretion of issuance discount for preferred stock	(2,730)	(1,103)	(4,947)	(3,298)
Net income applicable to common shareholders	\$ 2,474	\$ (2,605)	\$ 13,229	\$ (8,818)
Less: Earnings allocated to participating securities	(22)	(3)	(127)	(13)
Earnings allocated to common shareholders	\$ 2,452	\$ (2,608)	\$ 13,102	\$ (8,831)
Weighted average common shares outstanding	38,976	23,468	33,938	19,837
Basic earnings per common share	\$ 0.06	\$ (0.11)	\$ 0.39	\$ (0.45)
Diluted EPS:				
Earnings allocated to common shareholders	\$ 2,452	\$ (2,608)	\$ 13,102	\$ (8,831)
Weighted average common shares outstanding	38,976	23,468	33,938	19,837
Dilutive effect of equity awards and warrants	161		204	
Weighted average diluted common shares outstanding	39,137	23,468	34,142	19,837
Diluted earnings per common share	\$ 0.06	\$ (0.11)	\$ 0.38	\$ (0.45)
Potentially dilutive share options that were not included in the computation of diluted EPS because to do so would be anti-dilutive.	62	853	54	918

4. Business Combinations***Columbia River Bank***

On January 22, 2010 the Bank acquired certain assets and assumed certain liabilities of Columbia River Bank from the FDIC in an FDIC-assisted transaction. As part of the Purchase and Assumption Agreement, the Bank and the FDIC entered into loss-sharing agreements (each, a loss-sharing agreement and collectively, the loss-sharing agreements), whereby the FDIC will cover a substantial portion of any future losses on loans (and related unfunded loan commitments), OREO and certain accrued interest on loans. We refer to the acquired loans and OREO subject to the loss-sharing agreements collectively as covered assets. Under the terms of the loss-sharing agreements, the FDIC will absorb 80% of losses and share in 80% of loss recoveries on the first \$206 million on covered assets and absorb 95% of losses and share in 95% of loss recoveries exceeding \$206 million. The loss-sharing agreements for commercial and single family residential mortgage loans are in effect for five years and ten years, respectively, from the January 22, 2010 acquisition date and the loss recovery provisions for such loans are in effect for eight years and ten years, respectively, from the acquisition date.

Edgar Filing: COLUMBIA BANKING SYSTEM INC - Form 10-Q

The Bank acquired tangible assets with an acquisition date fair value of approximately \$885.3 million, including \$480.3 million of loans, an FDIC indemnification asset of \$143.6 million, \$100.7 million of investment securities, \$98.1 million of cash and cash equivalents and \$62.6 million of other assets. The Bank assumed liabilities with an acquisition date fair value of approximately \$912.9 million, including \$893.4 million of insured and uninsured deposits, \$18.4 million of Federal Home Loan Bank (FHLB) advances and \$1.1 million of other liabilities. Columbia River Bank was a full service commercial bank headquartered in The Dalles, Oregon that operated 21 branch locations, including 14 in the state of Oregon and seven in the State of Washington. We made this acquisition to expand our geographic footprint.

The assets acquired and liabilities assumed have been accounted for under the acquisition method of accounting (formerly the purchase method). The assets and liabilities, both tangible and intangible, were recorded at their estimated fair values as of the January 22, 2010 acquisition date. The application of the acquisition method of accounting resulted in the recognition in \$14.1 million of goodwill and a core deposit intangible of \$13.4 million. The goodwill represents the excess of the estimated fair value of the liabilities assumed over the estimated fair value of the assets acquired and is influenced significantly by the FDIC-assisted transaction process. All of the goodwill and core deposit intangible assets recognized are deductible for income tax purposes.

The operating results of the Company for the nine months ended September 30, 2010 include the operating results produced by the acquired assets and assumed liabilities for the period January 23, 2010 to September 30, 2010. Due primarily to the Company acquiring only certain assets and liabilities of Columbia River Bank, the significant amount of fair

Table of Contents**NOTES TO UNAUDITED CONSOLIDATED CONDENSED FINANCIAL STATEMENTS (Continued)****Columbia Banking System, Inc.**

value adjustments and the FDIC loss-sharing agreements now in place, historical results of Columbia River Bank are not meaningful to the Company's results and thus no pro forma information is presented.

On April 22, 2010, the Company notified the FDIC of its intent to purchase fourteen branch buildings from the Columbia River Bank Receivership. The fourteen branch buildings have an aggregate appraised value of \$15.8 million. Additionally, the Company accepted leases on nine former branch and administrative locations of Columbia River Bank.

The table below displays the amounts recognized as of the acquisition date for each major class of assets acquired and liabilities assumed:

	January 22, 2010
Assets	
Cash and due from banks	\$ 33,222
Interest-earning deposits with banks	64,921
Investment securities	100,650
Federal Home Loan Bank stock	3,045
Loans covered by loss sharing	480,306
Accrued interest receivable	4,021
FDIC receivable	46,213
Other real estate owned covered by loss sharing	8,714
Goodwill	14,120
Core deposit intangible	13,442
FDIC indemnification asset	143,609
Other assets	615
 Total assets acquired	 \$ 912,878
Liabilities	
Deposits	\$ 893,356
Federal Home Loan Bank advances	18,428
Accrued interest payable	524
Other liabilities	570
 Total liabilities assumed	 \$ 912,878

American Marine Bank

On January 29, 2010, the Bank acquired certain assets and assumed certain liabilities of American Marine Bank from the FDIC, which had been appointed receiver of the institution. As part of the Purchase and Assumption Agreement, the Bank and the FDIC entered into loss-sharing agreements whereby the FDIC will cover a substantial portion of any future losses on loans (and related unfunded loan commitments), OREO and certain accrued interest on loans. Under the terms of the loss-sharing agreements, the FDIC will absorb 80% of losses and share in 80% of loss recoveries on the first \$66 million on covered assets and absorb 95% of losses and share in 95% of loss recoveries exceeding \$66 million. The loss-sharing agreements for commercial and single family residential mortgage loans are in effect for five years and ten years, respectively, from the January 29, 2010 acquisition date and the loss recovery provisions for such loans are in effect for eight years and ten years, respectively, from the acquisition date.

Edgar Filing: COLUMBIA BANKING SYSTEM INC - Form 10-Q

The Bank acquired tangible assets with an acquisition date fair value of approximately \$303.5 million, including \$176.3 million of loans, an FDIC indemnification asset of \$66.8 million, \$28.6 million of investment securities, \$14.5 million of cash and cash equivalents and \$17.3 million of other assets. The Bank assumed liabilities with an acquisition date fair value of approximately \$292.6 million, including \$254.0 million of insured and uninsured deposits, \$37.7 million of FHLB advances and \$974 thousand of other liabilities. American Marine Bank was a full service commercial bank headquartered on Bainbridge Island, Washington that operated 11 branch locations in western Washington. In addition, as part of this acquisition, the Bank received regulatory approval to exercise trust powers and intends to continue to operate the Trust and Wealth Management Division of American Marine Bank. We made this acquisition to expand our geographic footprint.

The assets acquired and liabilities assumed have been accounted for under the acquisition method of accounting. The assets and liabilities, both tangible and intangible, were recorded at their estimated fair values as of the January 29, 2010 acquisition date. The application of the acquisition method of accounting resulted in the recognition of a bargain purchase gain of \$9.8 million, which is included in the *Gain on bank acquisition* line item in the Consolidated Condensed Statements

Table of Contents**NOTES TO UNAUDITED CONSOLIDATED CONDENSED FINANCIAL STATEMENTS (Continued)****Columbia Banking System, Inc.**

of Income, and a core deposit intangible of \$4.3 million. The transaction resulted in a bargain purchase gain as the fair value of assets acquired exceeded the fair value of liabilities assumed.

The operating results of the Company for the nine months ended September 30, 2010 include the operating results produced by the acquired assets and assumed liabilities for the period January 30, 2010 to September 30, 2010. Due primarily to the Company acquiring only certain assets and liabilities of American Marine Bank, the significant amount of fair value adjustments and the FDIC loss-sharing agreements now in place, historical results of American Marine Bank are not meaningful to the Company's results and thus no pro forma information is presented.

On April 22, 2010, the Company notified the FDIC of its intent to purchase four branch buildings from the American Marine Bank Receivership. The four branch buildings have an aggregate appraised value of \$7.4 million. Additionally, the Company accepted leases on six former branch locations of American Marine Bank.

The table below displays the amounts recognized as of the acquisition date for each major class of assets acquired and liabilities assumed:

	January 29, 2010
Assets	
Cash and cash equivalents	\$ 14,215
Federal funds sold	267
Investment securities	28,592
Federal Home Loan Bank stock	3,257
Loans covered by loss sharing	176,278
Accrued interest receivable	1,280
FDIC receivable	3,646
Other real estate owned covered by loss sharing	8,680
Core deposit intangible	4,313
FDIC indemnification asset	66,796
Other assets	498
Total assets acquired	307,822
Liabilities	
Deposits	253,965
Federal Home Loan Bank advances	37,682
Accrued interest payable	337
Deferred tax liability, net	5,383
Other liabilities	637
Total liabilities assumed	298,004
Net assets acquired	\$ 9,818

The following is a description of the methods used to determine the fair values of the significant assets and liabilities presented above for both the Columbia River Bank and American Marine Bank acquisitions.

Cash and cash equivalents - Cash and cash equivalents include cash and due from banks, interest-earning deposits with banks and the Federal Reserve Bank (FRB) and federal funds sold. Cash and cash equivalents have a maturity of 90 days or less at the time of purchase. The fair value of financial instruments that are short-term or re-price frequently and that have little or no risk are considered to have a fair value equal to carrying value.

Edgar Filing: COLUMBIA BANKING SYSTEM INC - Form 10-Q

Investment securities - The fair value for each purchased security was the quoted market price at the close of the trading day effective on the acquisition dates.

Federal Home Loan Bank stock - The fair value of acquired FHLB stock was estimated to be its redemption value, which is also the par value. The FHLB requires member banks to purchase its stock as a condition of membership and the amount of FHLB stock owned varies based on the level of FHLB advances outstanding. This stock is generally redeemable and is presented at the par value.

Loans - We refer to certain loans acquired in the Columbia River Bank and American Marine Bank acquisitions as covered loans as we will be reimbursed for a substantial portion of any future losses on them under the terms of the FDIC loss-sharing agreements. The estimated fair value of the loan portfolios at the acquisition dates represents the discounted expected cash flows from the portfolio. In estimating such fair value, we (a) calculated the contractual amount and timing of

Table of Contents

NOTES TO UNAUDITED CONSOLIDATED CONDENSED FINANCIAL STATEMENTS (Continued)

Columbia Banking System, Inc.

undiscounted principal and interest payments (the undiscounted contractual cash flows) and (b) estimated the amount and timing of undiscounted expected principal and interest payments (the undiscounted expected cash flows). The amount by which the undiscounted expected cash flows exceed the estimated fair value (the accretable yield) is accreted into interest income over the life of the loans. The difference between the undiscounted contractual cash flows and the undiscounted expected cash flows is the nonaccretable difference. The nonaccretable difference represents an estimate of the credit risk in the Columbia River Bank and American Marine Bank loan portfolios at the acquisition dates.

In calculating expected cash flows, management made several assumptions regarding prepayments, collateral cash flows, the timing of defaults and the loss severity of defaults. Other factors expected by market participants were considered in determining the fair value of acquired loans, including loan pool level estimated cash flows, type of loan and related collateral, risk classification status (i.e. performing or nonperforming), fixed or variable interest rate, term of loan and whether or not the loan was amortizing and current discount rates.

Other real estate owned - OREO is presented at its estimated fair value based on discounted expected cash flows and is also subject to the FDIC shared-loss agreements. Cash flows were estimated using expected selling price and date, less selling and carrying costs and were discounted to present value.

Goodwill - Goodwill represents the excess of the estimated fair value of the liabilities assumed over the estimated fair value of the assets acquired and is influenced significantly by the FDIC-assisted transaction process.

Core deposit intangible - In determining the estimated life and fair value of the core deposit intangible, deposits were analyzed based on factors such as type of deposit, deposit retention, interest rates, and age of the deposit relationships. Based on this valuation, the core deposit intangible asset will be amortized over the projected useful lives of the related deposits on an accelerated basis over 10 years.

FDIC indemnification asset - The FDIC indemnification asset is measured separately from each of the covered asset categories as it is not contractually embedded in any of the covered asset categories. For example, the FDIC indemnification asset related to estimated future loan losses is not transferable should we sell a loan prior to foreclosure or maturity. The fair value of the FDIC indemnification asset represents the present value of the estimated cash payments (net of amount owed to the FDIC) expected to be received from the FDIC for future losses on covered assets based on the credit adjustment on estimated cash flows for each covered asset pool and the loss-sharing percentages. The ultimate collectability of the FDIC indemnification asset is dependent upon the performance of the underlying covered loans, the passage of time and claims paid by the FDIC.

Deposit liabilities - The fair values used for demand and savings deposits are, by definition, equal to the amount payable on demand at the reporting date. The fair values for time deposits are estimated using a discounted cash flow method that applies interest rates currently being offered on time deposits to a schedule of aggregated contractual maturities of such time deposits.

Borrowings - The fair values for FHLB advances are estimated using a discounted cash flow method based on the current market rates.

Table of Contents**NOTES TO UNAUDITED CONSOLIDATED CONDENSED FINANCIAL STATEMENTS (Continued)****Columbia Banking System, Inc.****5. Securities**

The following table summarizes the amortized cost, gross unrealized gains and losses and the resulting fair value of securities available for sale:

Securities Available for Sale

<i>(in thousands)</i>	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
September 30, 2010:				
U.S. government agency and government-sponsored enterprise mortgage-backed securities and collateralized mortgage obligations	\$ 431,727	\$ 16,585	\$ (71)	\$ 448,241
State and municipal securities	221,978	19,238	(24)	241,192
Other securities	3,281	48	(21)	3,308
Total	\$ 656,986	\$ 35,871	\$ (116)	\$ 692,741
December 31, 2009:				
U.S. government agency and government-sponsored enterprise mortgage-backed securities and collateralized mortgage obligations	\$ 390,688	\$ 10,034	\$ (566)	\$ 400,156
State and municipal securities	210,987	8,545	(621)	218,911
Other securities	1,000		(29)	971
Total	\$ 602,675	\$ 18,579	\$ (1,216)	\$ 620,038

At September 30, 2010, available for sale securities with a carrying amount of \$28.7 million were pledged as collateral for repurchase agreement borrowings. In addition, available for sale securities with a carrying amount of \$14.8 million at September 30, 2010 were pledged as collateral for potential obligations under certain interest rate swap agreements.

The following tables show the gross unrealized losses and fair value of the Company's investments with unrealized losses that are not deemed to be other-than-temporarily impaired, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position at September 30, 2010 and December 31, 2009:

September 30, 2010

<i>(in thousands)</i>	Less than 12 Months		12 Months or More		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
U.S. government agency and government-sponsored enterprise mortgage-backed securities and collateralized mortgage obligations	\$ 29,197	\$ (71)	\$ 17	\$	\$ 29,214	\$ (71)
State and municipal securities	26	(1)	3,025	(23)	3,051	(24)
Other securities			979	(21)	979	(21)

Edgar Filing: COLUMBIA BANKING SYSTEM INC - Form 10-Q

Total \$ 29,223 \$ (72) \$ 4,021 \$ (44) \$ 33,244 \$ (116)

December 31, 2009

<i>(in thousands)</i>	Less than 12 Months		12 Months or More		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
U.S. government agency and government-sponsored enterprise mortgage-backed securities and collateralized mortgage obligations	\$ 87,879	\$ (566)	\$ 17	\$	\$ 87,896	\$ (566)
State and municipal securities	14,846	(42)	16,272	(579)	31,118	(621)
Other securities			971	(29)	971	(29)
Total	\$ 102,725	\$ (608)	\$ 17,260	\$ (608)	\$ 119,985	\$ (1,216)

The unrealized losses on the above securities are primarily attributable to increases in market interest rates subsequent to their purchase by the Company. Management does not intend to sell any impaired securities nor does available evidence suggest it is more likely than not that management will be required to sell any impaired securities. The Company's securities portfolio does not include any private label mortgage backed securities or investments in trust preferred securities. Management believes the nature of securities in the Company's investment portfolio present a very high probability of collecting all contractual amounts due, as the majority of the securities held are backed by government agencies or government-sponsored enterprises. However, this recovery in value may not occur for some time, perhaps greater than the one-year time horizon or perhaps even at maturity.

Table of Contents**NOTES TO UNAUDITED CONSOLIDATED CONDENSED FINANCIAL STATEMENTS (Continued)****Columbia Banking System, Inc.**

The scheduled contractual maturities of investment securities available for sale at September 30, 2010 are presented as follows:

<i>(in thousands)</i>	September 30, 2010	
	Amortized Cost	Fair Value
Due within one year	\$ 2,492	\$ 2,551
Due after one year through five years	64,617	67,400
Due after five years through ten years	102,197	108,232
Due after ten years	484,399	511,250
Total investment securities available-for-sale	\$ 653,705	\$ 689,433

6. Loans

The following is an analysis of the loan portfolio by major types of loans (net of deferred loan fees):

<i>(in thousands)</i>	September 30, 2010	December 31, 2009
Loans, excluding covered loans:		
Commercial business	\$ 761,113	\$ 744,440
Real Estate:		
One-to-four family residential	53,583	63,364
Commercial and five or more family residential properties	819,415	856,260
Total real estate	872,998	919,624
Real estate construction:		
One-to-four family residential	80,289	107,620
Commercial and five or more family residential properties	33,929	41,829
Total real estate construction	114,218	149,449
Consumer	189,495	199,987
Less: deferred loan fees	(3,662)	(4,616)
Total loans, excluding covered loans	1,934,162	2,008,884
Covered loans	561,131	
Total loans, net of deferred loan fees	\$ 2,495,293	\$ 2,008,884

At September 30, 2010 and December 31, 2009, the Company had no loans to foreign domiciled businesses or foreign countries, or loans related to highly leveraged transactions. The majority of the Company's loans and loan commitments are geographically concentrated in its service areas within the states of Washington and Oregon. At September 30, 2010, the Company had \$1.5 million in Small Business Administration (SBA) loans pledged as collateral for SBA-secured borrowings.

Edgar Filing: COLUMBIA BANKING SYSTEM INC - Form 10-Q

As of the acquisition dates, we estimated the fair value of the Columbia River Bank and American Marine Bank loan portfolios at \$480.3 million and \$176.3 million, respectively, which represents the expected cash flows from the portfolio discounted at market-based rates. In estimating such fair value, we (a) calculated the contractual amount and timing of the undiscounted principal and interest payments (the undiscounted contractual cash flows); and (b) estimated the amount and timing of the undiscounted expected principal and interest payments (the undiscounted expected cash flows). The amount by which the undiscounted expected cash flows exceed the estimated fair value (the accretable yield) is accreted into interest income over the lives of the loans. The difference between the undiscounted contractual cash flows and the undiscounted expected cash flows is referred to as the non-accretable difference. The non-accretable difference represents an estimate of credit risk in the covered loan portfolios on the acquisition dates. On the acquisition dates, the preliminary estimate of the undiscounted contractual principal and interest payments for the covered loans acquired in the Columbia River Bank and American Marine Bank acquisitions were \$799.8 million and \$259.6 million, respectively. The accretable yields were approximately \$101.1 million and \$21.6 million, respectively, and the non-accretable differences were \$217.9 million and \$65.5 million, respectively. The expected cash flows at acquisition date, which is the undiscounted contractual principal and interest payments, less the non-accretable differences were \$581.9 million and \$194.1 million, respectively.

Table of Contents**NOTES TO UNAUDITED CONSOLIDATED CONDENSED FINANCIAL STATEMENTS (Continued)****Columbia Banking System, Inc.**

The following table shows the changes in accretable yield for acquired loans for the nine months ended September 30, 2010:

<i>(in thousands)</i>	September 30, 2010
	Accretable Yield
Balance at beginning of period	\$
Established through acquisitions	122,705
Accretion	(39,255)
Transfers from nonaccretable difference	81,399
Disposals and other	(22,484)
Balance at end of period	\$ 142,365

FDIC indemnification asset - As of the acquisition dates, we recorded an FDIC indemnification asset consisting of the present value of the amounts the Company expects to receive from the FDIC under the loss-sharing agreements. The FDIC indemnification asset was \$166.7 million at September 30, 2010. The decrease in the indemnification asset since the acquisitions of Columbia River Bank and American Marine Bank included \$2.4 million and \$6.4 million of accretion into income for the three and nine months, respectively, ended September 30, 2010. Additionally, because of higher cash flows from principal amortization, partial prepayments, and loan payoffs during this timeframe, the Company reduced the indemnification asset by \$6.6 million for the three and nine months ended September 30, 2010 and recorded the adjustment as a reduction of noninterest income. The remainder of the change in the indemnification asset was due to charge-offs and losses on covered assets, which are primarily recoverable from the FDIC under the loss-sharing agreements and recorded in other assets.

7. Allowance for Loan and Lease Losses and Unfunded Loan Commitments and Letters of Credit

The following table presents activity in the allowance for noncovered loan and lease losses for the three and nine months ended September 30, 2010 and 2009:

<i>(in thousands)</i>	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2010	2009	2010	2009
Beginning balance	\$ 59,748	\$ 48,880	\$ 53,478	\$ 42,747
Provision charged to expense	9,000	16,500	37,500	48,500
Loans charged off	(7,540)	(13,826)	(31,466)	(40,330)
Recoveries	1,126	134	2,822	771
Ending balance	\$ 62,334	\$ 51,688	\$ 62,334	\$ 51,688

Covered loans acquired in the Columbia River Bank and American Marine Bank acquisitions are also subject to the Bank's internal and external credit review. Covered loans are accounted for under ASC Topic 310-30, and initially measured at fair value based on expected future cash flows over the lives of the loans. Over the life of the covered loan pools, management continues to monitor and estimate expected future cash flows on a quarterly basis. If expected future cash flows decline, a provision is recorded for estimated covered loan losses. During the quarter ended September 30, 2010, the Company recorded a provision expense of \$453 thousand on covered loans accounted for under ASC 310-30 as a result of a decrease in expected future cash flows. If expected cash flows on covered loans increase, subsequent to a loss provision being recorded, the loss provision will be reversed with any additional increases in expected cash flows made as an adjustment from non-accretable

difference to accretable yield. No such reversal occurred for the periods presented.

Table of Contents**NOTES TO UNAUDITED CONSOLIDATED CONDENSED FINANCIAL STATEMENTS (Continued)****Columbia Banking System, Inc.**

Changes in the allowance for unfunded loan commitments and letters of credit are summarized as follows:

<i>(in thousands)</i>	Three Months Ended September 30,		Nine Months Ended September 30,	
	2010	2009	2010	2009
Beginning balance	\$ 815	\$ 575	\$ 775	\$ 500
Net changes in the allowance for unfunded commitments and letters of credit	350	200	390	275
Ending balance	\$ 1,165	\$ 775	\$ 1,165	\$ 775

At September 30, 2010 and December 31, 2009, the total recorded investment in impaired loans was \$106.9 million and \$116.4 million, respectively. At September 30, 2010, \$22.1 million of impaired loans had a specific valuation allowance of \$3.8 million. At December 31, 2009, \$18.1 million of impaired loans had a specific valuation allowance of \$3.8 million.

8. Changes in Other Real Estate Owned

At September 30, 2010 OREO was \$40.3 million, which included \$17.0 million of covered OREO acquired in the FDIC-assisted acquisitions of Columbia River Bank and American Marine Bank. The acquired OREO is covered by loss-sharing agreements with the FDIC in which the FDIC will assume 80% of additional write-downs and losses on covered OREO sales, or 95% of additional write-downs and losses on covered OREO sales if the minimum loss share threshold has been met (see note 4 for threshold amounts).

The following table sets forth activity in noncovered OREO for the period:

<i>(in thousands)</i>	Three Months Ended September 30, 2010	Nine Months Ended September 30, 2010
Noncovered OREO:		
Balance, beginning of period	\$ 22,814	\$ 19,037
Transfers in, net of write-downs (\$14 and \$165 thousand, respectively)	778	8,791
OREO improvements	557	1,136
Additional OREO write-downs	(183)	(1,754)
Proceeds from sale of OREO property	(760)	(3,943)
Loss (gain) on sale of OREO	53	(8)
Total non-covered OREO, end of period	\$ 23,259	\$ 23,259

9. Goodwill and Intangible Assets

In accordance with the Intangibles – Goodwill and Other topic of the FASB ASC, goodwill is not amortized but is reviewed for potential impairment at the reporting unit level during the third quarter on an annual basis and between annual tests in certain circumstances such as material adverse changes in legal, business, regulatory and economic factors. An impairment loss is recorded to the extent that the carrying amount of goodwill exceeds its implied fair value. The Company completed its annual goodwill impairment test during the current quarter and

determined the fair value of the Company's single reporting unit exceeded its carrying value.

The core deposit intangible (CDI) is evaluated for impairment if events and circumstances indicate a possible impairment. The CDI is amortized on an accelerated basis over an estimated life of approximately 10 years.

Table of Contents**NOTES TO UNAUDITED CONSOLIDATED CONDENSED FINANCIAL STATEMENTS (Continued)****Columbia Banking System, Inc.**

The following table sets forth activity for goodwill and intangible assets for the period:

<i>(in thousands)</i>	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2010	2009	2010	2009
Total goodwill, beginning of period	\$ 109,639	\$ 95,519	\$ 95,519	\$ 95,519
Established through acquisitions			14,120	
Total goodwill, end of period	109,639	95,519	109,639	95,519
Gross core deposit intangible balance	26,651	8,896	8,896	8,896
Accumulated amortization at beginning of period	(5,874)	(3,528)	(4,032)	(2,988)
Core deposit intangible, net, beginning of period	20,777	5,368	4,864	5,908
Established through acquisitions			17,755	
CDI current period amortization	(1,044)	(256)	(2,886)	(796)
Total core deposit intangible, end of period	19,733	5,112	19,733	5,112
Total goodwill and intangible assets, end of period	\$ 129,372	\$ 100,631	\$ 129,372	\$ 100,631

The following table provides the estimated future amortization expense of core deposit intangibles for the three months ending December 31, 2010 and the succeeding four years:

Estimated Future Amortization Expense of Core Deposit Intangibles	Amount
	<i>(in thousands)</i>
Three months ending December 31, 2010	\$ 1,036
Year ending December 31, 2011	3,825
Year ending December 31, 2012	3,441
Year ending December 31, 2013	3,066
Year ending December 31, 2014	2,604

10. Shareholders Equity

Preferred Stock. On August 11, 2010, the Company redeemed all 76,898 shares of Fixed Rate Cumulative Perpetual Preferred Stock, Series A (Preferred Stock) originally issued to the U.S. Department of Treasury (the Treasury) on November 21, 2008 for approximately \$76.9 million in capital under its Capital Purchase Program (CPP). The Company paid a total of \$77.8 million to the Treasury, consisting of \$76.9 million in principal and \$919 thousand in accrued and unpaid dividends. Earnings available to the common shareholders were reduced by \$2.3 million upon repayment of the Preferred Stock, which represented the remaining unamortized discount on the Preferred Stock. Additionally, on September 1, 2010, the Company repurchased the common stock warrant issued to the Treasury pursuant to the Troubled Asset Relief Program (TARP) CPP for \$3.3 million. The warrant repurchase, together with the Company's redemption of its entire Preferred Stock issued to the Treasury, represents full repayment of all TARP obligations and cancellation of all equity interests in the Company held by the Treasury.

Edgar Filing: COLUMBIA BANKING SYSTEM INC - Form 10-Q

Common Stock. On January 28, 2010, the Company declared a quarterly cash dividend of \$0.01 per share, payable on February 24, 2010 to shareholders of record as of the close of business February 10, 2010. On April 28, 2010, the Company declared a quarterly cash dividend of \$0.01 per share, payable on May 26, 2010, to shareholders of record at the close of business May 12, 2010. On July 29, 2010, the Company declared a quarterly cash dividend of \$0.01 per share, payable on August 25, 2010, to shareholders of record at the close of business August 11, 2010. Subsequent to quarter end, on October 28, 2010 the Company declared a quarterly cash dividend of \$0.01 per share, payable on November 24, 2010, to shareholders of record at the close of business November 10, 2010.

The payment of cash dividends is subject to Federal regulatory requirements for capital levels and other restrictions. In addition, the cash dividends paid by the Bank to the Company are subject to both Federal and State regulatory requirements.

On May 5, 2010, the Company completed an underwritten public offering of 11,040,000 shares of our common stock at a purchase price to the public of \$21.75 per share, resulting in gross proceeds of approximately \$240.1 million and net proceeds to us of approximately \$229.1 million.

Table of Contents**NOTES TO UNAUDITED CONSOLIDATED CONDENSED FINANCIAL STATEMENTS (Continued)****Columbia Banking System, Inc.****11. Comprehensive Income**

The components of comprehensive income are as follows:

<i>(in thousands)</i>	Three Months Ended September 30,	
	2010	2009
Net income (loss) as reported	\$ 5,204	\$ (1,502)
Net unrealized holding gain from available for sale securities arising during the period, net of tax of (\$2,611) and (\$2,655)	4,739	4,655
Net change in cash flow hedging instruments, net of tax of \$119 and \$212	(216)	(384)
Pension plan liability adjustment, net of tax (\$4) and (\$5)	7	10
Total comprehensive income	\$ 9,734	\$ 2,779

<i>(in thousands)</i>	Nine Months Ended September 30,	
	2010	2009
Net income (loss) as reported	\$ 18,176	\$ (5,520)
Unrealized gain from securities:		
Net unrealized holding gain from available for sale securities arising during the period, net of tax of (\$6,553) and (\$4,802)	11,897	8,717
Reclassification adjustment of net gain included in income, net of tax of \$20 and \$0	(38)	
Net unrealized gain from securities, net of reclassification adjustment	11,859	8,717
Cash flow hedging instruments:		
Reclassification adjustment of net gain included in income, net of tax of \$520 and \$696	(943)	(1,264)
Net change in cash flow hedging instruments	(943)	(1,264)
Pension plan liability adjustment:		
Net unrealized gain (loss) from unfunded defined benefit plan liability arising during the period, net of tax of (\$12) and \$379	23	(689)
Less: amortization of unrecognized net actuarial loss included in net periodic pension cost, net of tax of (\$11) and (\$16)	21	29
Pension plan liability adjustment, net	44	(660)
Total comprehensive income	\$ 29,136	\$ 1,273

12. Fair Value Accounting and Measurement

The Fair Value Measurements and Disclosures topic of the FASB ASC defines fair value, establishes a consistent framework for measuring fair value and expands disclosure requirements about fair value. We hold fixed and variable rate interest-bearing securities, investments in marketable equity securities and certain other financial instruments, which are carried at fair value. Fair value is determined based upon quoted

Edgar Filing: COLUMBIA BANKING SYSTEM INC - Form 10-Q

prices when available or through the use of alternative approaches, such as matrix or model pricing, when market quotes are not readily accessible or available.

The valuation techniques are based upon observable and unobservable inputs. Observable inputs reflect market data obtained from independent sources, while unobservable inputs reflect our own market assumptions. These two types of inputs create the following fair value hierarchy:

Level 1 Quoted prices for identical instruments in active markets that are accessible at the measurement date.

Level 2 Quoted prices for similar instruments in active markets; quoted prices for identical or similar instruments in markets that are not active; and model derived valuations whose inputs are observable or whose significant value drivers are observable.

Table of Contents

NOTES TO UNAUDITED CONSOLIDATED CONDENSED FINANCIAL STATEMENTS (Continued)

Columbia Banking System, Inc.

Level 3 Prices or valuation techniques that require inputs that are both significant to the fair value measurement and unobservable.

Fair values are determined as follows:

Securities at fair value are priced using matrix pricing based on the securities' relationship to other benchmark quoted prices, and under the provisions of the Fair Value Measurements and Disclosures topic of the FASB ASC are considered a Level 2 input method.

Interest rate contract positions are valued in models, which use as their basis, readily observable market parameters and are classified within level 2 of the valuation hierarchy.

The following table sets forth the Company's financial assets and liabilities that were accounted for at fair value on a recurring basis at September 30, 2010 by level within the fair value hierarchy. Financial assets and liabilities are classified in their entirety based on the lowest level of input that is significant to the fair value measurement:

<i>(in thousands)</i>	Fair value at September 30, 2010	Fair Value Measurements at Reporting Date Using		
		Level 1	Level 2	Level 3
Assets				
Securities available for sale	\$ 692,741	\$	\$ 692,741	\$
Other assets (Interest rate contracts)	\$ 13,623	\$	\$ 13,623	\$
Liabilities				
Other liabilities (Interest rate contracts)	\$ 13,623	\$	\$ 13,623	\$

Certain assets and liabilities are measured at fair value on a nonrecurring basis after initial recognition such as loans measured for impairment and OREO. The following methods were used to estimate the fair value of each such class of financial instrument:

Impaired loans - A loan is considered to be impaired when, based on current information and events, it is probable that the Company will be unable to collect all amounts due (both interest and principal) according to the contractual terms of the loan agreement. Impaired loans are measured by the fair market value of the collateral less estimated costs to sell.

Other real estate owned - OREO is real property that the Bank has taken ownership of in partial or full satisfaction of a loan or loans. OREO is recorded at the lower of the carrying amount of the loan or fair value less estimated costs to sell. This amount becomes the property's new basis. Any write-downs based on the property fair value less estimated cost to sell at the date of acquisition are charged to the allowance for loan and lease losses. Management periodically reviews OREO in an effort to ensure the property is carried at the lower of its new basis or fair value, net of estimated costs to sell. Any write-downs subsequent to acquisition are charged to earnings.

The following table sets forth the Company's financial assets that were accounted for at fair value on a nonrecurring basis at September 30, 2010:

<i>(in thousands)</i>	Fair value at September 30, 2010	Fair Value Measurements at Reporting Date Using			Losses During the Three Months Ended September 30, 2010	Losses During the Nine Months Ended September 30, 2010
		Level 1	Level 2	Level 3		

Edgar Filing: COLUMBIA BANKING SYSTEM INC - Form 10-Q

Impaired loans	\$	39,409	\$	\$	\$	39,409	\$	4,264	\$	28,376
Non-covered OREO		2,313				2,313		197		1,918
	\$	41,722	\$	\$	\$	41,722	\$	4,461	\$	30,294

The losses on impaired loans disclosed above represent the amount of the specific reserve and/or charge-offs during the period applicable to loans held at period end. The amount of the specific reserve is included in the allowance for loan and lease losses. The losses on non-covered OREO disclosed above represent the writedowns taken at foreclosure that were charged to the allowance for loan and lease losses, as well as subsequent writedowns from updated appraisals that were charged to earnings.

Table of Contents**NOTES TO UNAUDITED CONSOLIDATED CONDENSED FINANCIAL STATEMENTS (Continued)****Columbia Banking System, Inc.****13. Fair Value of Financial Instruments**

Because broadly traded markets do not exist for most of the Company's financial instruments, the fair value calculations attempt to incorporate the effect of current market conditions at a specific time. These determinations are subjective in nature, involve uncertainties and matters of significant judgment and do not include tax ramifications; therefore, the results cannot be determined with precision, substantiated by comparison to independent markets and may not be realized in an actual sale or immediate settlement of the instruments. There may be inherent weaknesses in any calculation technique, and changes in the underlying assumptions used, including discount rates and estimates of future cash flows, could significantly affect the results. For all of these reasons, the aggregation of the fair value calculations presented herein do not represent, and should not be construed to represent, the underlying value of the Company.

The following methods and assumptions were used to estimate the fair value of each class of financial instruments for which it is practicable to estimate that value:

Cash and due from banks and interest-earning deposits with banks - The fair value of financial instruments that are short-term or repriced frequently and that have little or no risk are considered to have a fair value that approximates carrying value.

Securities available for sale - The fair value of all investment securities are based upon the assumptions market participants would use in pricing the security. Such assumptions include observable and unobservable inputs such as quoted market prices, dealer quotes and discounted cash flows.

Federal Home Loan Bank stock - The fair value is based upon the par value of the stock which equates to its carrying value.

Loans - Originated Loans - Loans are not recorded at fair value on a recurring basis. Nonrecurring fair value adjustments are periodically recorded on impaired loans that are measured for impairment based on the fair value of collateral. See Note 12, *Fair Value Accounting and Measurement*. For most performing loans, fair value is estimated using expected duration and lending rates that would have been offered on September 30, 2010 for loans which mirror the attributes of the loans with similar rate structures and average maturities. Commercial loans and construction loans, which are variable rate and short-term are reflected with fair values equal to carrying value. The fair values resulting from these calculations are reduced by an amount representing the change in estimated fair value attributable to changes in borrowers' credit quality since the loans were originated. For nonperforming loans, fair value is estimated by applying a valuation discount based upon loan sales data from the Federal Deposit Insurance Corporation. **Acquired Loans** - Fair value of loans acquired in FDIC-assisted transactions was estimated by applying a valuation discount derived from recent loan sales data and based upon similar loan collateral and performance characteristics.

FDIC indemnification asset - The FDIC indemnification asset is considered to have a fair value that approximates carrying value.

Interest rate contracts - Interest rate swap positions are valued in models, which use as their basis, readily observable market parameters.

Deposits - For deposits with no contractual maturity, the fair value is equal to the carrying value. The fair value of fixed maturity deposits is based on discounted cash flows using the difference between the deposit rate and current market rates for deposits of similar remaining maturities.

FHLB and FRB borrowings - The fair value of FHLB advances and FRB borrowings are estimated based on discounting the future cash flows using the market rate currently offered.

Repurchase Agreements - The fair value of securities sold under agreement to repurchase are estimated based on discounting the future cash flows using the market rate currently offered.

Long-term subordinated debt - The fair value of long-term subordinated debt are estimated based on discounting the future cash flows using an estimated market rate.

Other Financial Instruments - The majority of our commitments to extend credit and standby letters of credit carry current market interest rates if converted to loans, as such, carrying value is assumed to equal fair value.

Table of Contents**NOTES TO UNAUDITED CONSOLIDATED CONDENSED FINANCIAL STATEMENTS (Continued)****Columbia Banking System, Inc.**

The following table summarizes carrying amounts and estimated fair values of selected financial instruments as well as assumptions used by the Company in estimating fair value:

	September 30, 2010		December 31, 2009	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
<i>(in thousands)</i>				
Assets				
Cash and due from banks	\$ 77,235	\$ 77,235	\$ 55,802	\$ 55,802
Interest-earning deposits with banks	448,854	448,854	249,272	249,272
Securities available for sale	692,741	692,741	620,038	620,038
Federal Home Loan Bank stock	17,908	17,908	11,607	11,607
Loans	2,432,506	2,192,796	1,955,406	1,808,256
FDIC indemnification asset	166,696	166,696		
Interest rate contracts	13,623	13,623	9,054	9,054
Liabilities				
Deposits	\$ 3,306,886	\$ 3,473,452	\$ 2,482,705	\$ 2,486,578
Federal Home Loan Bank advances	119,584	122,770	100,000	100,037
Repurchase agreements	25,000	28,657	25,000	29,884
Other borrowings	1,599	1,599	86	86
Long-term subordinated debt	25,719	20,523	25,669	20,296
Interest rate contracts	13,623	13,623	9,054	9,054

14. Derivatives and Hedging Activities

The Company periodically enters into certain commercial loan interest rate swap agreements in order to provide commercial loan customers the ability to convert from variable to fixed interest rates. Under these agreements, the Company enters into a variable-rate loan agreement with a customer in addition to a swap agreement. This swap agreement effectively converts the customer's variable rate loan into a fixed rate. The Company then enters into a corresponding swap agreement with a third party in order to offset its exposure on the variable and fixed components of the customer agreement. As the interest rate swap agreements with the customers and third parties are not designated as hedges under the Derivatives and Hedging topic of the FASB ASC, the instruments are marked to market in earnings.

The following table presents the fair value of derivative instruments at September 30, 2010 and 2009:

As of September 30, <i>(in thousands)</i>	Asset Derivatives				Liability Derivatives			
	2010		2009		2010		2009	
	Balance Sheet Location	Fair Value	Balance Sheet Location	Fair Value	Balance Sheet Location	Fair Value	Balance Sheet Location	Fair Value
Derivatives not designated as hedging instruments								
Interest rate contracts	Other assets	\$ 13,623	Other assets	\$ 11,371	Other liabilities	\$ 13,623	Other liabilities	\$ 11,371

Termination of Hedging Activities: On January 7, 2008, the Company discontinued its three prime rate floor derivative instruments that were previously utilized to hedge the variable cash flows associated with existing variable-rate loan assets based on the prime rate. The Company received \$8.1 million as a result of the termination transaction resulting in a net derivative gain of \$6.2 million. The interest rate floors had an

Edgar Filing: COLUMBIA BANKING SYSTEM INC - Form 10-Q

original maturity date of April 4, 2011. In accordance with the Derivatives and Hedging topic of the FASB ASC, the net derivative gain related to a discontinued cash flow hedge continues to be reported in accumulated other comprehensive income and is reclassified into earnings in the same periods during which the originally hedged forecasted transactions affect earnings. For the three and nine months ended September 30, 2010, \$335 thousand and \$1.5 million, respectively of the net derivative gain was reclassified into earnings.

Table of Contents

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

This discussion should be read in conjunction with the unaudited consolidated condensed financial statements of Columbia Banking System, Inc. (referred to in this report as "we", "our", and "the Company") and notes thereto presented elsewhere in this report and with the December 31, 2009 audited consolidated financial statements and its accompanying notes included in our Annual Report on Form 10-K. In the following discussion, unless otherwise noted, references to increases or decreases in average balances and in items of income and expense for a particular period and balances at a particular date refer to the comparison with corresponding amounts for the period or date one year earlier.

CAUTIONARY NOTE REGARDING FORWARD-LOOKING STATEMENTS

This quarterly report on Form 10-Q contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. These forward-looking statements include, but are not limited to, statements about our plans, objectives, expectations and intentions that are not historical facts, and other statements identified by words such as "expects", "anticipates", "intends", "plans", "believes", "should", "projects", "estimates" or words of similar meaning. These forward-looking statements are based on current beliefs and expectations of management and are inherently subject to significant business, economic and competitive uncertainties and contingencies, many of which are beyond our control. In addition, these forward-looking statements are subject to assumptions with respect to future business strategies and decisions that are subject to change. In addition to the factors set forth in the sections "Risk Factors" and "Management's Discussion and Analysis of Financial Condition and Results of Operations" in this report, the following factors, among others, could cause actual results to differ materially from the anticipated results:

local and national economic conditions could be less favorable than expected or could have a more direct and pronounced effect on us than expected and adversely affect our ability to continue internal growth at historical rates and maintain the quality of our earning assets;

risks presented by a continued economic downturn, which could adversely affect credit quality, collateral values, investment values, liquidity, loan portfolio delinquency rates and revenue growth;

integration of our two recent FDIC-assisted acquisitions may present unforeseen challenges;

efficiencies and enhanced financial and operating performance we expect to realize from investments in personnel, acquisitions and infrastructure could not be realized;

we may not be able to effectively deploy the net proceeds from our recent capital raise, including but not limited to, as a result of any unavailability of attractive acquisition targets such as FDIC-assisted acquisitions;

changes in FDIC policy may make the terms of future FDIC-assisted transaction opportunities less favorable to bidders such as the Company;

interest rate changes could significantly reduce net interest income and negatively affect funding sources;

projected business increases following strategic expansion or opening of new branches could be lower than expected;

Edgar Filing: COLUMBIA BANKING SYSTEM INC - Form 10-Q

the ultimate financial and operational burden of the recently enacted financial regulatory reform legislation and related rules;

changes in the scope and cost of FDIC insurance and other coverage could impose financial and operational burdens;

changes in accounting principles, policies and guidelines applicable to bank holding companies and banking;

competition among financial institutions could increase significantly;

the goodwill we have recorded in connection with acquisitions could become impaired, which may have an adverse impact on our earnings and capital;

the reputation of the financial services industry could deteriorate, which could adversely affect our ability to access markets for funding and to acquire and retain customers;

the terms and costs of the numerous actions taken by the Federal Reserve, the U.S. Congress, the Treasury, the FDIC, the SEC and others in response to the liquidity and credit crisis, or the failure of these actions to help stabilize the financial markets, asset prices, market liquidity or worsening of current financial market and economic conditions could materially and adversely affect our business, financial condition, results of operations and the trading price of our common stock; and

our ability to effectively manage credit risk, interest rate risk, market risk, operational risk, legal risk, liquidity risk and regulatory and compliance risk.

Please take into account that forward-looking statements speak only as of the date of this report. We do not undertake any obligation to publicly correct or update any forward-looking statement whether as a result of new information, future events or otherwise.

Table of Contents

CRITICAL ACCOUNTING POLICIES

Management has identified the accounting policies related to the allowance for loan and lease losses and the valuation and recoverability of goodwill as critical to an understanding of our financial statements. These policies and related estimates are discussed in Item 7. Management Discussion and Analysis of Financial Condition and Results of Operation under the headings Allowance for Loan and Lease Losses and Valuation and Recoverability of Goodwill in our 2009 Annual Report on Form 10-K. There have not been any material changes in our critical accounting policies relating to the allowance for loan and lease losses or the valuation and recoverability of goodwill as compared to those disclosed in our 2009 Annual Report on Form 10-K.

SIGNIFICANT INFLUENCES ON THE QUARTER AND NINE MONTHS ENDED SEPTEMBER 30, 2010

Redemption of preferred stock

On August 11, 2010, the Company redeemed all 76,898 shares of Series A preferred stock originally issued to the U.S. Department of Treasury on November 21, 2008 for approximately \$76.9 million in capital under its Capital Purchase Program (CPP). The Company paid a total of \$77.8 million to the Treasury, consisting of \$76.9 million in principal and \$918,504 in accrued and unpaid dividends.

Repurchase of common stock warrant

On September 1, 2010, the Company repurchased the common stock warrant issued to the U.S. Department of Treasury pursuant to the Troubled Asset Relief Program (TARP) CPP for \$3.3 million. The warrant repurchase, together with the Company's redemption of Series A preferred stock represents full repayment of all TARP obligations and cancellation of all equity interests in the Company held by the U.S. Treasury.

Acquisition of Columbia River Bank

On January 22, 2010, the Bank acquired certain assets and assumed certain liabilities of Columbia River Bank from the FDIC, which had been appointed receiver of the institution, including 21 branches located in Oregon and Washington. The Bank acquired tangible assets with a fair value of approximately \$885.3 million, including \$480.3 million of loans, an FDIC indemnification asset of \$143.6 million, \$100.7 million of investment securities, \$98.1 million of cash and cash equivalents and \$62.6 million of other assets. The Bank assumed liabilities with a fair value of approximately \$912.9 million, including \$893.4 million of insured and uninsured deposits, \$18.4 million of FHLB advances and \$1.1 million of other liabilities. In connection with this acquisition, The Bank entered into loss-sharing agreements with the FDIC which cover approximately \$676.1 million in face value of Columbia River Bank's loans and \$18.7 million of Columbia River Bank's OREO. The transaction resulted in goodwill of \$14.1 million and a core deposit intangible of \$13.4 million.

Acquisition of American Marine Bank

On January 29, 2010, The Bank acquired substantially all of the deposits and assets of American Marine Bank from the FDIC, which had been appointed receiver of the institution, including 11 branches located in western Washington. The Bank acquired tangible assets with a fair value of approximately \$303.5 million, including \$176.3 million of loans, an FDIC indemnification asset of \$66.8 million, \$28.6 million of investment securities, \$14.5 million of cash and cash equivalents and \$17.3 million of other assets. The Bank assumed liabilities with a fair value of approximately \$292.6 million, including \$254.0 million of insured and uninsured deposits, \$37.7 million of FHLB advances and \$974 thousand of other liabilities. In connection with this acquisition, The Bank entered into loss-sharing agreements with the FDIC which cover approximately \$243.8 million in face value of American Marine Bank's loans and \$15.8 million of American Marine Bank's OREO. In addition, as part of this acquisition, The Bank received regulatory approval to exercise trust powers and intends to continue to operate the Trust and Wealth Management Division of American Marine Bank. The transaction resulted in a bargain purchase gain of \$9.8 million, and a core deposit intangible of \$4.3 million.

RESULTS OF OPERATIONS

Earnings Summary

The Company reported net income for the third quarter of \$5.2 million and \$2.5 million in net income applicable to common shareholders or \$0.06 per diluted common share, compared to a net loss of \$1.5 million and a \$2.6 million net loss applicable to common shareholders or \$(0.11)

Edgar Filing: COLUMBIA BANKING SYSTEM INC - Form 10-Q

per diluted common share for the third quarter of 2009. Net income applicable to common shareholders for the third quarter of 2010 is net of the Preferred Stock dividend of \$427 thousand and the redemption of the Preferred Stock resulting in the recognition of the remaining \$2.3 million of the Preferred Stock discount. The increase in net income from the prior year period was primarily attributable to the \$15.8 million increase in revenue (net interest income plus noninterest income) coupled with the \$7.5 million decline in the provision for loan and lease losses partially offset by a \$10.4 million increase in noninterest expense. Return on average assets and return on average common

Table of Contents

equity were 0.47% and 1.39%, respectively, for the third quarter of 2010, compared with returns of (0.19)% and (2.56)%, respectively for the same period of 2009.

The Company reported net income for the first nine months of \$18.2 million and \$13.2 million in net income applicable to common shareholders or \$0.38 per diluted common share, compared to a net loss of \$5.5 million and an \$8.8 million net loss applicable to common shareholders or \$(0.45) per diluted common share for the first nine months of 2009. Net income applicable to common shareholders for the first nine months of 2010 is net of the Preferred Stock dividend of \$2.3 million, the accretion of the Preferred Stock discount totaling \$300 thousand and recognizing the remaining \$2.3 million of the Preferred Stock discount as a result of redeeming the entire Preferred Stock issued to the Treasury. The increase in net income from the prior year period was primarily attributable to the \$9.8 million pre-tax gain on the acquisition of American Marine Bank in the first quarter and a \$11.0 million decline in the provision for loan losses for the nine months ended September 30, 2010. Return on average assets and return on average common equity were 0.58% and 2.97%, respectively, for the first nine months of 2010, compared with returns of (0.24)% and (3.23)%, respectively for the same period of 2009.

Revenue (net interest income plus noninterest income) for the three months ended September 30, 2010 was \$52.1 million, 44% higher than the same period in 2009. The increase was primarily a result of higher net interest income driven by the accretion of income on acquired loans and noninterest income driven by the acquisitions of Columbia River Bank and American Marine Bank.

Revenue (net interest income plus noninterest income) for the nine months ended September 30, 2010 was \$162.9 million, 53% higher than the same period in 2009. The increase was primarily a result of higher net interest income driven by the accretion of income on acquired loans and noninterest income driven by the acquisitions of Columbia River Bank and American Marine Bank, including the \$9.8 million pre-tax gain on the acquisition of American Marine Bank.

Total noninterest expense in the quarter ended September 30, 2010 was \$33.5 million, a 45% increase from the third quarter of 2009. The increase was primarily due to the addition of operating expenses of Columbia River Bank and American Marine Bank in January 2010.

Total noninterest expense in the nine months ended September 30, 2010 was \$102.2 million, a 43% increase from the first nine months of 2009. The increase was primarily due to the addition of operating expenses of Columbia River Bank and American Marine Bank in January 2010.

The provision for loan and lease losses for the third quarter of 2010 was \$9.0 million compared with \$16.5 million for the third quarter of 2009. The provision reflects management's continuing evaluation of the loan portfolio's credit quality, which is affected by a broad range of economic metrics. Additional factors affecting the provision include, but are not limited to, net-loan charge-offs, non-accrual loans, specific reserves and risk-rating migration. The provision increased the Company's total allowance for loan and lease losses to 3.22% of loans, excluding covered loans at September 30, 2010 from 2.66% at year-end 2009 and 2.50% at the end of the third quarter 2009. Net charge-offs for the current quarter were \$6.4 million compared to \$13.7 million for the third quarter of 2009.

The provision for loan and lease losses for the first nine months of 2010 was \$37.5 million compared with \$48.5 million for the first nine months of 2009. Net charge-offs for the first nine months of 2010 were \$28.6 million compared to \$39.6 million for the first nine months of 2009.

RESULTS OF OPERATIONS

Our results of operations are dependent to a large degree on our net interest income. We also generate noninterest income through service charges and fees, merchant services fees, and bank owned life insurance. Our operating expenses consist primarily of compensation and employee benefits, occupancy, merchant card processing, data processing and legal and professional fees. Like most financial institutions, our interest income and cost of funds are affected significantly by general economic conditions, particularly changes in market interest rates, and by government policies and actions of regulatory authorities.

Table of Contents**Net Interest Income**

Net interest income is the difference between interest income (which includes yield-related loan fees) and interest expense. Net interest income on a fully taxable-equivalent basis expressed as a percentage of average total interest-earning assets is referred to as the net interest margin. The following tables set forth the components of net interest income on a fully taxable-equivalent basis for the three and nine months ended September 30, 2010 and 2009.

<i>(in thousands)</i>	Three months ended September 30, 2010			Three months ended September 30, 2009		
	Average Balances (1)	Interest Earned / Paid	Average Rate	Average Balances (1)	Interest Earned / Paid	Average Rate
ASSETS						
Loans, net (1)(2)	\$ 2,500,302	\$ 44,989	7.14%	\$ 2,088,478	\$ 29,260	5.56%
Securities (2)	715,201	8,151	4.52%	593,516	7,701	5.15%
Interest-earning deposits with banks and federal funds sold	439,429	281	0.25%	101,126	53	0.21%
Total interest-earning assets	3,654,932	\$ 53,421	5.80%	2,783,120	\$ 37,014	5.28%
Other earning assets	51,684			49,696		
Noninterest-earning assets	654,297			244,271		
Total assets	\$ 4,360,913			\$ 3,077,087		
LIABILITIES AND SHAREHOLDERS EQUITY						
Certificates of deposit	\$ 729,053	\$ 1,958	1.07%	\$ 685,621	\$ 3,687	2.13%
Savings accounts	202,669	70	0.14%	136,132	89	0.26%
Interest-bearing demand	641,070	489	0.30%	448,778	515	0.46%
Money market accounts	894,971	1,490	0.66%	587,177	1,240	0.84%
Total interest-bearing deposits	2,467,763	4,007	0.64%	1,857,708	5,531	1.18%
Federal Home Loan Bank and Federal Reserve Bank borrowings	122,250	716	2.32%	110,783	651	2.33%
Securities sold under agreements to repurchase	25,000	121	1.92%	25,000	120	1.91%
Other borrowings			0.00%			0.00%
Long-term subordinated debt	25,708	266	4.10%	25,642	280	4.33%
Total interest-bearing liabilities	2,640,721	\$ 5,110	0.77%	2,019,133	\$ 6,582	1.29%
Noninterest-bearing deposits	829,820			537,603		
Other noninterest-bearing liabilities	151,217			41,762		
Shareholders equity	739,155			478,589		
Total liabilities & shareholders equity	\$ 4,360,913			\$ 3,077,087		
Net interest income (2)		\$ 48,311			\$ 30,432	
Net interest margin			5.24%			4.34%

(1) Nonaccrual loans have been included in the tables as loans carrying a zero yield. Amortized net deferred loan fees were included in the interest income calculations. The amortization of net deferred loan fees was \$401 thousand and \$792 thousand for the three months ended

Edgar Filing: COLUMBIA BANKING SYSTEM INC - Form 10-Q

September 30, 2010 and 2009, respectively.

- (2) Tax-exempt income is calculated on a tax equivalent basis, based on a marginal tax rate of 35%.

Table of Contents

<i>(in thousands)</i>	Nine months ended September 30, 2010			Nine months ended September 30, 2009		
	Average Balances (1)	Interest Earned / Paid	Average Rate	Average Balances (1)	Interest Earned / Paid	Average Rate
ASSETS						
Loans, net (1)(2)	\$ 2,497,396	\$ 121,088	6.48%	\$ 2,154,793	\$ 88,528	5.49%
Securities (2)	718,023	24,955	4.65%	563,914	22,467	5.33%
Interest-earning deposits with banks and federal funds sold	334,871	640	0.26%	35,170	69	0.26%
Total interest-earning assets	3,550,290	\$ 146,683	5.52%	2,753,877	\$ 111,064	5.39%
Other earning assets	51,178			49,234		
Noninterest-earning assets	611,398			250,078		
Total assets	\$ 4,212,866			\$ 3,053,189		
LIABILITIES AND SHAREHOLDERS EQUITY						
Certificates of deposit	\$ 799,011	\$ 7,042	1.18%	\$ 718,276	\$ 12,707	2.37%
Savings accounts	195,916	237	0.16%	132,321	291	0.29%
Interest-bearing demand	631,401	1,730	0.37%	460,008	1,744	0.51%
Money market accounts	824,297	4,273	0.69%	548,372	3,555	0.87%
Total interest-bearing deposits	2,450,625	13,282	0.72%	1,858,977	18,297	1.32%
Federal Home Loan Bank and Federal Reserve Bank borrowings	124,234	2,131	2.29%	165,813	2,116	1.71%
Securities sold under agreements to repurchase	25,000	357	1.91%	25,000	356	1.91%
Other borrowings			0.00%	108	1	0.70%
Long-term subordinated debt	25,692	769	4.00%	25,626	937	4.89%
Total interest-bearing liabilities	2,625,551	\$ 16,539	0.84%	2,075,524	\$ 21,707	1.40%
Noninterest-bearing deposits	795,698			493,797		
Other noninterest-bearing liabilities	136,240			44,885		
Shareholders equity	655,377			438,983		
Total liabilities & shareholders equity	\$ 4,212,866			\$ 3,053,189		
Net interest income (2)		\$ 130,144			\$ 89,357	
Net interest margin			4.90%			4.34%

(1) Nonaccrual loans have been included in the tables as loans carrying a zero yield. Amortized net deferred loan fees were included in the interest income calculations. The amortization of net deferred loan fees was \$ 1.7 million and \$2.2 million for the nine months ended September 30, 2010 and 2009, respectively.

(2) Tax-exempt income is calculated on a tax equivalent basis, based on a marginal tax rate of 35%.

Table of Contents

Net interest income is impacted by the volume (changes in volume multiplied by prior rate), interest rate (changes in rate multiplied by prior volume) and mix of interest-earning assets and interest-bearing liabilities. The following tables set forth the total dollar amount of change in net interest income on a fully taxable-equivalent basis due to volume and rate between the third quarter and first nine months of 2010 and 2009. Changes attributable to the combined effect of volume and interest rates have been allocated proportionately to the changes due to volume and the changes due to interest rates:

<i>(in thousands)</i>	Three Months Ended September 30, 2010 Compared to 2009 Increase (Decrease) Due to		
	Volume	Rate	Total
Interest earning assets			
Loans (1)	\$ 6,442	\$ 9,287	\$ 15,729
Securities (2)	1,387	(937)	450
Interest earning deposits with banks and federal funds sold	215	13	228
Interest income (2)	\$ 8,044	\$ 8,363	\$ 16,407
Interest bearing liabilities			
Deposits:			
Certificates of deposit	\$ 220	\$ (1,949)	\$ (1,729)
Savings accounts	33	(52)	(19)
Interest-bearing demand	179	(205)	(26)
Money market accounts	552	(302)	250
Total interest on deposits	984	(2,508)	(1,524)
FHLB and Federal Reserve Bank borrowings	67	(2)	65
Other borrowings and interest bearing liabilities	1		1
Long-term subordinated debt	1	(15)	(14)
Interest expense	\$ 1,053	\$ (2,525)	\$ (1,472)

- (1) Nonaccrual loans have been included in the tables as loans carrying a zero yield. Amortized net deferred loan fees were included in the interest income calculations. The amortization of net deferred loan fees was \$401 thousand and \$792 thousand for the three months ended September 30, 2010 and 2009, respectively.
- (2) Tax-exempt income is calculated on a tax equivalent basis, based on a marginal tax rate of 35%.

Table of Contents

<i>(in thousands)</i>	Nine Months Ended September 30, 2010 Compared to 2009		
	Increase (Decrease) Due to		
	Volume	Rate	Total
Interest earning assets			
Loans (1)	\$ 15,264	\$ 17,296	\$ 32,560
Securities (2)	5,290	(2,802)	2,488
Interest earning deposits with banks and federal funds sold	573	(2)	571
Interest income (2)	\$ 21,127	\$ 14,492	\$ 35,619
Interest bearing liabilities			
Deposits:			
Certificates of deposit	\$ 1,297	\$ (6,962)	\$ (5,665)
Savings accounts	107	(161)	(54)
Interest-bearing demand	546	(560)	(14)
Money market accounts	1,532	(814)	718
Total interest on deposits	3,482	(8,497)	(5,015)
FHLB and Federal Reserve Bank borrowings	(608)	623	15
Other borrowings and interest bearing liabilities	(1)		(1)
Long-term subordinated debt	2	(170)	(168)
Interest expense	\$ 2,875	\$ (8,044)	\$ (5,169)

(1) Nonaccrual loans have been included in the tables as loans carrying a zero yield. Amortized net deferred loan fees were included in the interest income calculations. The amortization of net deferred loan fees was \$1.7 million and \$2.2 million for the nine months ended September 30, 2010 and 2009, respectively.

(2) Tax-exempt income is calculated on a tax equivalent basis, based on a marginal tax rate of 35%.

The Company's net interest margin increased to 5.24% in the third quarter of 2010, up from 4.34% for the prior-year period. The net interest margin in the third quarter was positively impacted by the \$7.2 million of discount accretion on our acquired loan portfolios. The net interest margin was negatively affected by larger levels of interest-earning cash invested at lower yields. We continue to seek investment opportunities to reduce our level of overnight funds invested at those lower yields.

For the nine months ended September 30, 2010, the Company's net interest margin increased to 4.90%, up from 4.34% for the prior-year period. As discussed above, the net interest margin was positively impacted by the \$8.2 million of discount accretion on our acquired loan portfolios.

Provision for Loan and Lease Losses

During the third quarter of 2010, the Company recorded \$9.0 million to its provision for loan and lease losses, compared to \$16.5 million for the same period in 2009. The provision increased the Company's total allowance for loan losses to 3.22% of net loans, excluding covered loans at September 30, 2010.

Provision for Losses on Covered Loans

During the third quarter of 2010, the Company recorded a non-cash net impairment charge of \$453 thousand for FDIC-covered loans. The provision expense is primarily a result of a decrease in projected cash flows due to the Company's revised estimate of the timing of cash flow receipts. The third quarter revision of the cash flow receipts is based on the results of management's review of the credit quality of the covered loans and the analysis of the loan performance data since the acquisition of the covered loans. The Company will continue updating cash flow

projections on the covered loans on a quarterly basis.

Noninterest Income

Noninterest income was \$5.2 million for the third quarter of 2010, compared to \$7.2 million for the prior-year period. The decrease was primarily due to the \$4.5 million net change in the indemnification asset. This reduction was related to higher cash flows received from principal amortization, partial prepayments, and loan payoffs. The decrease in the

Table of Contents

indemnification asset was partially offset by an increase in service charges and other fees of \$2.7 million primarily resulting from the addition of Columbia River Bank and American Marine Bank operations.

For the nine months ended September 30, 2010, noninterest income increased \$15.7 million or 74%, compared to the first nine months of 2009. The increase was primarily due to the \$9.8 million pre-tax gain on the American Marine Bank acquisition, and an increase of \$7.4 million in service charges and other fees primarily resulting from the impact of the normal operations of Columbia River Bank and American Marine Bank.

Noninterest Expense

Total noninterest expense for the third quarter of 2010 was \$33.5 million, an increase of 45% from \$23.1 million for the same quarter in 2009. Additionally, total noninterest expense for the first nine months of 2010 was \$102.2 million, an increase of 43% from \$71.6 million for the first nine months of 2009. The increase was primarily due to the addition of operating expenses of Columbia River Bank and American Marine Bank in January 2010.

The following table presents the significant components of noninterest expense and the related dollar and percentage change from period to period:

	Three months ended September 30,			Nine months ended September 30,				
	2010	\$ Change	% Change	2009 <i>(dollars in thousands)</i>	2010	\$ Change	% Change	2009
Compensation	\$ 14,867	\$ 5,397	57%	\$ 9,470	\$ 40,767	\$ 11,932	41%	\$ 28,835
Employee benefits	2,532	133	6%	2,399	7,820	638	9%	7,182
Contract labor	175	175	NM		3,470	3,470	NM	
	17,574	5,705	48%	11,869	52,057	16,040	45%	36,017
All other noninterest expense:								
Occupancy	4,278	1,255	42%	3,023	12,554	3,549	39%	9,005
Merchant processing	934	93	11%	841	2,697	255	10%	2,442
Advertising and promotion	630	334	113%	296	2,253	578	35%	1,675
Data processing and communications	2,477	1,467	145%	1,010	6,923	3,949	133%	2,974
Legal and professional services	1,609	816	103%	793	4,584	1,805	65%	2,779
Taxes, license and fees	803	221	38%	582	2,055	80	4%	1,975
Regulatory premiums	1,952	732	60%	1,220	4,910	191	4%	4,719
Net cost of operation of other real estate owned	(1,442)	(1,760)	-553%	318	(802)	(1,392)	-236%	590
Amortization of intangibles	1,044	785	303%	259	2,886	2,089	262%	797
Other	3,661	726	25%	2,935	12,045	3,377	39%	8,668
Total all other noninterest expense	15,946	4,669	41%	11,277	50,105	14,481	41%	35,624
Total noninterest expense	\$ 33,520	\$ 10,374	45%	\$ 23,146	\$ 102,162	\$ 30,521	43%	\$ 71,641

NM Not Meaningful

Table of Contents

The following table presents selected items included in other noninterest expense and the associated change from period to period:

<i>(in thousands)</i>	Three months ended		Increase	Nine months ended		Increase
	September 30,	2009	(Decrease)	September 30,	2009	(Decrease)
	2010		Amount	2010		Amount
Software support & maintenance	\$ 267	\$ 165	\$ 102	\$ 793	\$ 486	\$ 307
Federal Reserve Bank processing fees	100	83	17	240	259	(19)
Supplies	438	199	239	1,147	630	517
Postage	430	302	128	1,404	932	472
Investor relations	35	15	20	117	189	(72)
Travel	296	104	192	709	283	426
ATM Network	223	156	67	608	444	164
Sponsorships and charitable contributions	145	99	46	584	437	147
Directors fees	104	115	(11)	328	328	
Employee expenses	100	82	18	353	270	83
Insurance	207	125	82	582	357	225
CRA partnership investment expense	73	164	(91)	219	354	(135)
Miscellaneous	1,243	1,326	(83)	4,961	3,699	1,262
Total other noninterest expense	\$ 3,661	\$ 2,935	\$ 726	\$ 12,045	\$ 8,668	\$ 3,377

In managing our business, we review the efficiency ratio, on a fully taxable-equivalent basis, which is not defined in accounting principles generally accepted in the United States. Our efficiency ratio [noninterest expense, excluding net cost of operation of OREO divided by the sum of net interest income and noninterest income on a tax equivalent basis, excluding gain/loss on sale of investment securities, proceeds from redemption of Visa and Mastercard shares, gain on bank acquisition, incremental income accretion on the acquired loan portfolio and the change in FDIC indemnification asset] was 68.33% for the third quarter 2010 and 68.32% for the first nine months of 2010, compared to 60.85% for the third quarter 2009 and 62.72% for the first nine months of 2009, respectively. The efficiency ratio increased due to increased expenses associated with managing our problem assets, increased regulatory premiums and expenses resulting from our FDIC-assisted transactions.

Income Taxes

We recorded an income tax provision of \$4.0 million and \$4.6 million for the third quarter and the first nine months of 2010, compared with a benefit of \$1.8 million and \$7.9 million for the same periods in 2009. Our effective tax rate remains lower than the statutory tax rate due to our nontaxable income generated from tax-exempt municipal bonds, investments in bank owned life insurance, and low income housing credits. For additional information, please refer to the Company's annual report on Form 10-K for the year ended December 31, 2009.

Credit Risk Management

The extension of credit in the form of loans or other credit products to individuals and businesses is one of our principal business activities. Our policies and applicable laws and regulations require risk analysis as well as ongoing portfolio and credit management. We manage our credit risk through lending limit constraints, credit review, approval policies, and extensive, ongoing internal monitoring. We also manage credit risk through diversification of the loan portfolio by type of loan, type of industry, type of borrower and by limiting the aggregation of debt limits to a single borrower. In analyzing our existing portfolio, we review our consumer and residential loan portfolios by their performance as a pool of loans since no single loan is individually significant or judged by its risk rating, size, or potential risk of loss. In contrast, the monitoring process for the commercial business, private banking, real estate construction, and commercial real estate portfolios includes periodic reviews of individual loans with risk ratings assigned to each loan and performance judged on a loan by loan basis. We review these loans to assess the ability of the borrower to service all of its interest and principal obligations and, as a result, the risk rating may be adjusted accordingly. In the event that full collection of principal and interest is not reasonably assured, the loan is appropriately downgraded and, if warranted, placed on nonaccrual status even though the loan may be current as to principal and interest payments. Additionally, we review these types of loans for impairment in accordance with the Receivables topic of the FASB ASC. Impaired loans are considered for nonaccrual status.

Table of Contents

and will typically remain as such until all principal and interest payments are brought current and the prospects for future payments in accordance with the loan agreement appear relatively certain.

Loan policies, credit quality criteria, portfolio guidelines and other controls are established under the guidance of our Chief Credit Officer and approved, as appropriate, by the Board. Credit Administration, together with the loan committee, has the responsibility for administering the credit approval process. As another part of its control process, we use an independent internal credit review and examination function to provide assurance that loans and commitments are made and maintained as prescribed by our credit policies. This includes a review of documentation when the loan is initially extended and subsequent monitoring to assess continued performance and proper risk assessment.

We have diversification of loan types within our portfolio. However, we are not immune to either the current instability in the residential real estate markets and mortgage-related industries or the increasing economic stress in the commercial market. Accordingly, we will continue to be diligent in our risk management practices and maintain, what we believe, are adequate reserves for probable loan losses.

Loan Portfolio Analysis

We are a full service commercial bank, originating a wide variety of loans, but concentrating our lending efforts on originating commercial business and commercial real estate loans.

The following table sets forth the Company's loan portfolio by type of loan for the dates indicated:

<i>(in thousands)</i>	September 30, 2010	% of Total	December 31, 2009	% of Total
Commercial business	\$ 761,113	30.5%	\$ 744,440	37.1%
Real estate:				
One-to-four family residential	53,583	2.2%	63,364	3.2%
Commercial and five or more family residential properties	819,415	32.8%	856,260	42.6%
Total real estate	872,998	35.0%	919,624	45.8%
Real estate construction:				
One-to-four family residential	80,289	3.2%	107,620	5.3%
Commercial and five or more family residential properties	33,929	1.4%	41,829	2.1%
Total real estate construction	114,218	4.6%	149,449	7.4%
Consumer	189,495	7.6%	199,987	9.9%
Subtotal	1,937,824	77.7%	2,013,500	100.2%
Less: Deferred loan fees	(3,662)	-0.2%	(4,616)	-0.2%
Total loans, excluding covered loans	1,934,162		2,008,884	
Covered loans	561,131	22.5%		0.0%
Total loans, net of deferred loan fees	\$ 2,495,293	100.0%	\$ 2,008,884	100.0%
Loans Held for Sale	\$ 1,513		\$	

Total loans increased \$486.4 million, or 24%, from year-end 2009. The increase in total loans was driven primarily by FDIC-assisted acquisitions of Columbia River Bank and American Marine Bank. Although the acquisitions of Columbia River and American Marine Banks increased our loan portfolio by \$656.6 million, the credit risk associated with the acquired loans was substantially mitigated by the loss-sharing agreements with the FDIC. Total noncovered loans decreased \$74.7 million, or 4%, from December 31, 2009. This decrease was attributable to low loan demand due to current business and economic conditions.

Edgar Filing: COLUMBIA BANKING SYSTEM INC - Form 10-Q

Commercial Loans: We are committed to providing competitive commercial lending in our primary market areas. Management expects a continued focus within its commercial lending products and to emphasize, in particular, relationship banking with businesses, and business owners.

Table of Contents

Real Estate Loans: These loans are used to collateralize outstanding advances from the FHLB. Residential loans are secured by properties located within our primary market areas, and typically have loan-to-value ratios of 80% or lower.

Generally, commercial and five-or-more family residential real estate loans are made to borrowers who have existing banking relationships with us. Our underwriting standards generally require that the loan-to-value ratio for these loans not exceed 75% of appraised value, cost, or discounted cash flow value, as appropriate, and that commercial properties maintain debt coverage ratios (net operating income divided by annual debt servicing) of 1.2 or better. However, underwriting standards can be influenced by competition and other factors. We endeavor to maintain the highest practical underwriting standards while balancing the need to remain competitive in our lending practices.

Real Estate Construction Loans: We originate a variety of real estate construction loans. One-to-four family residential construction loans are originated for the construction of custom homes (where the home buyer is the borrower) and to provide financing to builders for the construction of pre-sold homes and speculative residential construction. Underwriting guidelines for these loans vary by loan type but include loan-to-value limits, term limits and loan advance limits, as applicable.

Our underwriting guidelines for commercial and five-or-more family residential real estate construction loans generally require that the loan-to-value ratio not exceed 75% and stabilized debt coverage ratios (net operating income divided by annual debt servicing) of 1.2 or better. As noted above, underwriting standards can be influenced by competition and other factors. However, we endeavor to maintain the highest practical underwriting standards while balancing the need to remain competitive in our lending practices.

Consumer Loans: Consumer loans include automobile loans, boat and recreational vehicle financing, home equity and home improvement loans and miscellaneous personal loans.

Foreign Loans: Our banking subsidiaries are not involved with loans to foreign companies or foreign countries.

Allowance for Loan and Lease Losses

We maintain an allowance for loan and lease losses (ALLL) to absorb losses inherent in the loan portfolio. The size of the ALLL is determined through quarterly assessments of the probable estimated losses in the loan portfolio. Our methodology for making such assessments and determining the adequacy of the ALLL includes the following key elements:

1. General valuation allowance consistent with the Contingencies topic of the FASB ASC.
2. Criticized/classified loss reserves on specific relationships. Specific allowances for identified problem loans are determined in accordance with the Receivables topic of the FASB ASC.
3. The unallocated allowance provides for other credit losses inherent in our loan portfolio that may not have been contemplated in the general and specific components of the allowance. This unallocated amount generally comprises less than 1.5% of the allowance. The unallocated amount is reviewed periodically based on trends in credit losses, the results of credit reviews and overall economic trends.

On a quarterly basis our Chief Credit Officer reviews with Executive Management and the Board of Directors the various additional factors that management considers when determining the adequacy of the ALLL, including economic and business condition reviews. Factors which influenced management's judgment in determining the amount of the additions to the ALLL charged to operating expense include the following as of the applicable balance sheet dates:

1. Existing general economic and business conditions affecting our market place

Edgar Filing: COLUMBIA BANKING SYSTEM INC - Form 10-Q

2. Credit quality trends, including trends in nonperforming loans
3. Collateral values
4. Seasoning of the loan portfolio
5. Bank regulatory examination results
6. Findings of internal credit examiners
7. Duration of current business cycle

The ALLL is increased by provisions for loan and lease losses (provision) charged to expense, and is reduced by loans charged off, net of recoveries. While we believe the best information available is used by us to determine the ALLL, changes in market conditions could result in adjustments to the ALLL, affecting net income, if circumstances differ from the assumptions used in determining the ALLL.

Table of Contents

In addition to the ALLL, we maintain an allowance for unfunded loan commitments and letters of credit. We report this allowance as a liability on our Consolidated Balance Sheet. We determine this amount using estimates of the probability of the ultimate funding and losses related to those credit exposures. This methodology is similar to the methodology we use for determining the adequacy of our ALLL. For additional information on our allowance for unfunded loan commitments and letters of credit, see Note 7 to the Consolidated Condensed Financial Statements.

At September 30, 2010, our allowance for noncovered loan and lease losses was \$62.3 million, or 3.22% of total noncovered loans and 64% of nonperforming, noncovered loans and 51% of nonperforming, noncovered assets. This compares with an allowance of \$51.7 million, or 2.50% of the total loan portfolio, 48% of nonperforming loans and 41% of nonperforming assets at December 31, 2009.

At September 30, 2010, our allowance for covered loan losses was \$453 thousand, or 0.08% of the total covered loan pools. Covered loans accounted for under ASC 310-30 are generally considered accruing and performing as the loans accrete interest income over the estimated lives of the loans when cash flows are reasonably estimable. Accordingly, covered impaired loans contractually past due are still considered to be accruing and performing loans. The loans acquired in the Columbia River Bank and American Marine Bank acquisitions are also subject to the Bank's internal and external credit review and are accounted for under ASC Topic 310-30. Covered loans are initially measured at fair value based on expected future cash flows over the lives of the loans, which management continues to monitor and estimate on a quarterly basis. If expected future cash flows decline, a provision is recorded for estimated cash flow losses on covered loans. If expected cash flows on covered loans increase, subsequent to a loss provision being recorded, the loss provision will be reversed with any additional increases in expected cash flows made as an adjustment from non-accretable difference to accretable yield.

Table of Contents

The following tables summarize the activity in the allowance for loan and lease losses and unfunded loan commitments and letters of credit for the three and nine month periods ended September 30, 2010 and 2009:

**Changes in Allowance for Loan and Lease Losses and
Unfunded Loan Commitments and Letters of Credit**

<i>(in thousands)</i>	Three Months Ended September 30,		Nine Months Ended September 30,	
	2010	2009	2010	2009
Beginning balance	\$ 59,748	\$ 48,880	\$ 53,478	\$ 42,747
Charge-offs:				
Commercial business	(1,760)	(4,889)	(9,405)	(8,200)
One-to-four family residential			(104)	(220)
Commercial and five-or-more family residential	(1,976)	(237)	(4,958)	(956)
One-to-four family residential construction	(1,291)	(5,704)	(8,955)	(21,750)
Commercial and five-or-more family residential construction		(2,180)	(3,079)	(7,542)
Consumer	(2,513)	(816)	(4,965)	(1,662)
Total charge-offs	(7,540)	(13,826)	(31,466)	(40,330)
Recoveries				
Commercial business	122	127	778	531
One-to-four family residential			15	68
Commercial and five-or-more family residential	5		46	22
One-to-four family residential construction	573		1,481	92
Consumer	426	7	502	58
Total recoveries	1,126	134	2,822	771
Net charge-offs	(6,414)	(13,692)	(28,644)	(39,559)
Provision charged to expense	9,000	16,500	37,500	48,500
Ending balance	\$ 62,334	\$ 51,688	\$ 62,334	\$ 51,688
Total loans, net at end of period, excluding covered loans and loans held for sale (1)	\$ 1,934,162	\$ 2,063,398	\$ 1,934,162	\$ 2,063,398
Allowance for loan and lease losses to period-end loans, excluding covered loans	3.22%	2.50%	3.22%	2.50%

Allowance for unfunded commitments and letters of credit

Beginning balance	\$ 815	\$ 575	\$ 775	\$ 500
Net changes in the allowance for unfunded commitments and letters of credit	350	200	390	275
Ending balance	\$ 1,165	\$ 775	\$ 1,165	\$ 775

Nonperforming Assets

Edgar Filing: COLUMBIA BANKING SYSTEM INC - Form 10-Q

Nonperforming assets consist of: (i) nonaccrual loans; (ii) restructured loans, for which concessions, including the reduction of interest rates below a rate otherwise available to that borrower or the deferral of interest or principal, have been granted due to the borrower's weakened financial condition (interest on restructured loans is accrued at the restructured rates when it is anticipated that no loss of original principal will occur); (iii) OREO; and (iv) other personal property owned. Collectively, nonaccrual and restructured loans are considered nonperforming loans.

Nonaccrual noncovered loans: The consolidated financial statements are prepared according to the accrual basis of accounting. This includes the recognition of interest income on the loan portfolio, unless a loan is placed on a nonaccrual basis, which occurs when there are serious doubts about the collectability of principal or interest per the contractual terms. Generally our policy is to discontinue the accrual of interest on all loans past due 90 days or more and place them on nonaccrual status. When a noncovered loan is placed on nonaccrual status, any accrued but unpaid interest on that date is removed from interest income.

Table of Contents

The following tables set forth, at the dates indicated, information with respect to our nonperforming assets, excluding covered assets:

<i>(in thousands)</i>	September 30, 2010	December 31, 2009
Nonperforming assets, excluding covered assets		
Nonaccrual loans:		
Commercial business	\$ 17,490	\$ 18,979
Real estate:		
One-to-four family residential	3,063	1,860
Commercial and five or more family residential real estate	25,282	24,354
Total real estate	28,345	26,214
Real estate construction:		
One-to-four family residential	25,653	47,653
Commercial and five or more family residential real estate	14,771	16,230
Total real estate construction	40,424	63,883
Consumer	5,147	1,355
Total nonaccrual loans	91,406	110,431
Restructured loans:		
Commercial and five or more family residential real estate	5,777	
One-to-four family residential construction	705	60
Total restructured loans	6,482	60
Total nonperforming loans	97,888	110,491
Other real estate owned and other personal property owned	23,259	19,037
Total nonperforming assets, excluding covered assets	\$ 121,147	\$ 129,528

The following table summarizes activity in nonaccrual loans, excluding covered loans:

Changes in Nonaccrual Loans

<i>(in thousands)</i>	Three months ended September 30,		Nine months ended September 30,	
	2010	2009	2010	2009
Balance, beginning of period	\$ 108,409	\$ 127,767	\$ 110,431	\$ 106,750
Loans placed on nonaccrual	8,206	30,706	46,651	97,357
Advances	1,246	747	3,357	2,058
Charge-offs	(5,904)	(9,997)	(24,406)	(34,075)
Loans returned to accrual status	(11,059)	(241)	(15,301)	(2,316)
Repayments (including interest applied to principal)	(8,714)	(7,508)	(19,241)	(19,058)
Transfers to OREO / OPPO	(778)	(10,756)	(10,085)	(19,998)
Balance, end of period	\$ 91,406	\$ 130,718	\$ 91,406	\$ 130,718

Edgar Filing: COLUMBIA BANKING SYSTEM INC - Form 10-Q

Loans are considered impaired when based on current information and events, it is probable that the Company will be unable to collect all amounts due according to the contractual terms of the loan agreement, including scheduled interest payments. The assessment for impairment occurs when and while loans with outstanding balances greater than \$250,000 are designated as criticized/classified per the Company's internal risk rating system or when and while such loans are on nonaccrual. Such loans are analyzed individually, on a quarterly basis, under the guidance of the Receivables topic of the FASB ASC to determine if impairment exists. The Company's policy is to record cash receipts on impaired loans first as reductions in principal and then as interest income.

Table of Contents

The following table summarizes impaired loan financial data:

<i>in millions</i>	Sep 30, 2010	Dec 31, 2009	Sep 30, 2009
Impaired loans	\$ 106.9	\$ 116.4	\$ 123.2
Impaired loans with specific allocations	\$ 22.1	\$ 18.1	\$ 45.7
Amount of the specific allocations	\$ 3.8	\$ 3.8	\$ 12.6

When a loan with unique risk characteristics has been identified as being impaired, the amount of impairment will be measured by the Company using discounted cash flows, except when it is determined that the primary (remaining) source of repayment for the loan is the operation or liquidation of the underlying collateral. In these cases, the current fair value of the collateral, reduced by costs to sell, will be used in place of discounted cash flows. As a final alternative, the observable market price of the debt may be used to assess impairment. Predominately, the Company uses the fair value of collateral approach based upon a reliable valuation.

When a loan secured by real estate migrates to non-performing and impaired status and it does not have a market valuation less than one year old, the Company secures an updated market valuation by a third-party appraiser. This updated appraisal is then subject to two reviews, one by a third-party appraisal reviewer and another by the Company's on-staff appraiser. Subsequently, the asset will be appraised annually by a third party appraiser or the Company's on staff appraiser. The evaluation may occur more frequently if management determines that there has been increased market deterioration within a specific geographical location. Upon receipt and verification of the market valuation, the Company will record the loan at the lower of cost or market (less costs to sell) by recording a charge-off to the allowance for loan and lease losses or by designating a specific reserve in accordance with accounting principles generally accepted in the United States.

Securities

All of our securities are classified as available for sale and carried at fair value. These securities are used by the Company as a component of its balance sheet management strategies. From time to time securities may be sold to reposition the portfolio in response to strategies developed by the Company's asset liability committee. In accordance with our investment strategy, management monitors market conditions with a view to realize gains on its available for sale securities portfolio when prudent.

At September 30, 2010, the market value of securities available for sale had an unrealized gain, net of tax, of \$23.1 million compared to an unrealized gain, net of tax, of \$11.2 million at December 31, 2009. The change in market value of securities available for sale is due primarily to fluctuations in interest rates. The Company does not consider these investment securities to be other than temporarily impaired. In the future, if the impairment is judged to be other than temporary, the cost basis of the individual impaired securities will be written down to fair value; the amount of the write-down could be included in earnings as a realized loss.

During the nine months ended September 30, 2010, \$69.3 million of investment securities were sold resulting in a net gain of approximately \$58 thousand. The majority of securities sold were acquired in the Columbia River Bank acquisition. Those investment securities were sold as the characteristics of those securities either did not fit well within the Company's existing investment securities portfolio or align with its investment strategy.

The following table sets forth our securities portfolio by type for the dates indicated:

<i>(in thousands)</i>	September 30, 2010	December 31, 2009
Securities Available for Sale		
U.S. government agency and government-sponsored enterprise mortgage-backed securities and collateralized mortgage obligations	\$ 448,241	\$ 400,156
State and municipal securities	241,192	218,911
Other securities	3,308	971

Total	\$ 692,741	\$ 620,038
-------	------------	------------

Table of Contents

FHLB Stock

As a condition of membership in the FHLB of Seattle, the Company is required to purchase and hold a certain amount of FHLB stock. Our stock purchase requirement is based, in part, upon the outstanding principal balance of advances from the FHLB and is calculated in accordance with the Capital Plan of the FHLB. Our FHLB stock has a par value of \$100 and is redeemable at par for cash.

FHLB stock is carried at cost and is subject to recoverability testing per the Financial Services Depository and Lending topic of the FASB ASC. The FHLB is currently classified as undercapitalized by the Federal Housing Finance Agency (Finance Agency). Under Finance Agency regulations, a FHLB that fails to meet any regulatory capital requirement may not declare a dividend or redeem or repurchase capital stock.

Subsequent to quarter-end, on October 25, 2010, the Finance Agency announced that the Board of Directors of the FHLB of Seattle agreed to the stipulation and issuance of a Consent Order by the Finance Agency that resolves certain outstanding capital and supervisory matters. The Consent Order and associated agreement with the FHLB Board of Directors constituted the FHLB's capital restoration plan, which included steps the FHLB would take to resume timely repurchases and redemptions of member capital stock. We will continue to monitor the financial condition of the FHLB as it relates to the recoverability of our investment in FHLB stock.

Goodwill

The carrying amount of goodwill was \$109.6 million as of September 30, 2010 and \$95.5 million as of December 31, 2009. Goodwill is tested for impairment on an annual basis, or more frequently as events occur, or as current circumstances and conditions warrant. Under the Intangibles

Goodwill and Other topic of the FASB ASC, the testing for impairment of goodwill is a two-step process performed at the reporting level. In the first step of the goodwill impairment test (Step I), the fair value of a reporting unit is compared with its carrying amount. If the fair value of a reporting unit exceeds its carrying amount, there is no indication of impairment and further testing is not required. If the carrying amount of a reporting unit exceeds its fair value, then a second step of testing is required.

The Company performed its annual goodwill impairment test during the current quarter to determine whether and to what extent, if any, recorded goodwill was impaired. The analysis compared the fair value of the Company's single reporting unit, including goodwill, to its carrying amounts utilizing a market approach to valuation. The results of the Step I Analysis indicated no impairment in the single, reporting unit of the Company. Accordingly, no further testing was required.

Liquidity and Sources of Funds

Our primary sources of funds are customer deposits. Additionally, we utilize advances from the FHLB of Seattle. The FRB of San Francisco, and wholesale repurchase agreements to supplement our funding needs. These funds, together with loan repayments, loan sales, retained earnings, equity and other borrowed funds are used to make loans, to acquire securities and other assets, and to fund continuing operations.

Deposit Activities

Our deposit products include a wide variety of transaction accounts, savings accounts and time deposit accounts. Core deposits (demand deposit, savings, money market accounts and certificates of deposit less than \$100,000) increased \$861.6 million, or 42%, since year-end 2009 while certificates of deposit greater than \$100,000 increased \$43.7 million, or 17%, from year-end 2009. The increase in deposits was primarily the result of the Columbia River Bank and American Marine Bank acquisitions, which resulted in the addition of \$893.4 million and \$254.0 million, respectively, from each acquisition.

We have established a branch system to serve our consumer and business depositors. In addition, management's strategy for funding asset growth is to make use of brokered and other wholesale deposits on an as-needed basis. At September 30, 2010 brokered and other wholesale deposits (excluding public deposits) totaled \$67.9 million, or 2% of total deposits, compared to \$150.1 million, or 6% of total deposits, at year-end 2009. The brokered deposits have varied maturities.

Table of Contents

The following table sets forth the Company's deposit base by type of product for the dates indicated:

<i>(in thousands)</i>	September 30, 2010		December 31, 2009		September 30, 2009	
	Balance	% of Total	Balance	% of Total	Balance	% of Total
Core deposits:						
Demand and other non-interest bearing	\$ 864,920	26.2%	\$ 574,687	23.1%	\$ 490,512	20.1%
Interest bearing demand	645,875	19.5%	499,922	20.1%	447,019	18.3%
Money market	896,135	27.1%	604,229	24.3%	691,399	28.3%
Savings	206,713	6.3%	139,406	5.6%	136,739	5.6%
Certificates of deposit less than \$100,000	320,808	9.7%	254,577	10.3%	261,813	10.7%
Total core deposits	2,934,451	88.8%	2,072,821	83.4%	2,027,482	83.0%
Certificates of deposit greater than \$100,000	303,527	9.2%	259,794	10.5%	264,982	10.8%
Wholesale certificates of deposit (CDARS®)	44,786	1.3%	96,314	3.9%	92,890	3.8%
Wholesale certificates of deposit	23,155	0.7%	53,776	2.2%	58,213	2.4%
Subtotal	3,305,919	100.0%	2,482,705	100.0%	2,443,567	100.0%
Premium resulting from acquisition date fair value adjustment	967					
Total deposits	\$ 3,306,886		\$ 2,482,705		\$ 2,443,567	

Borrowings

We rely on FHLB advances and FRB borrowings as another source of both short and long-term funding. FHLB advances and FRB borrowings are secured by bonds within our investment portfolio, one-to-four family real estate mortgages, and other loans. At September 30, 2010, we had FHLB advances of \$119.6 million, before acquisition date fair value adjustments, compared to \$100 million at December 31, 2009. The increase in FHLB advances was the result of acquiring Columbia River Bank and American Marine Bank in FDIC-assisted acquisitions. The Bank assumed \$18.4 million in FHLB advances from Columbia River Bank, of which \$18.0 million matured and was repaid. The Bank also assumed \$36.5 million in FHLB advances from American Marine Bank of which \$18.0 million matured and was repaid. The Bank had no other borrowing activity other than repayment on assumed borrowings from the banks acquired in the FDIC-assisted acquisitions.

We also utilize wholesale repurchase agreements as a supplement to our funding sources. Our wholesale repurchase agreements are secured by mortgage-backed securities. At September 30, 2010 and December 31, 2009 we had a repurchase agreement of \$25.0 million. Management anticipates we will continue to rely on FHLB advances, FRB borrowings, and wholesale repurchase agreements in the future and we will use those funds primarily to make loans and purchase securities.

During 2001, the Company, through a special purpose trust (the Trust) participated in a pooled trust preferred offering, whereby the Trust issued \$22.0 million of 30-year floating rate capital securities. The capital securities constitute guaranteed preferred beneficial interests in debentures issued by the Company to the Trust. The debentures had an initial rate of 7.29% and a rate of 4.05% at September 30, 2010. The floating rate is based on the 3-month LIBOR plus 3.58% and is adjusted quarterly. Through the Trust, we may call the debentures at any time for a premium and after ten years at par, allowing us to retire the debt early if market conditions are favorable. Through the 2007 Town Center Bancorp acquisition, the Company assumed an additional \$3.0 million in floating rate trust preferred obligations; these debentures had a rate of 4.28% at September 30, 2010. The floating rate is based on the 3-month LIBOR plus 3.75% and is adjusted quarterly.

The trust preferred obligations are classified as long-term subordinated debt and our related investment in the Trust is recorded in other assets on the consolidated balance sheets. The balance of the long-term subordinated debt was \$25.7 million at September 30, 2010 and December 31, 2009. The subordinated debt payable to the Trust is on the same interest and payment terms as the trust preferred obligations issued by the Trust.

Contractual Obligations & Commitments

We are party to many contractual financial obligations, including repayment of borrowings, operating and equipment lease payments, commitments to extend credit and investments in affordable housing partnerships. At September 30, 2010, we had commitments to extend credit of \$578.7 million compared to \$587.5 million at December 31, 2009.

Capital Resources

Shareholders' equity at September 30, 2010 was \$704.7 million, up from \$528.1 million at December 31, 2009. Shareholders' equity was 16.6% and 16.5% of total period-end assets at September 30, 2010 and December 31, 2009, respectively. The Company's tangible common equity to tangible assets ratio was 14.0% at September 30, 2010 compared to 11.4% at December 31, 2009. Tangible common equity to tangible assets is defined as total shareholders' equity, less any

Table of Contents

outstanding preferred stock, reduced by recorded goodwill and other intangible assets divided by total assets reduced by recorded goodwill and other intangible assets.

Capital Ratios: Banking regulations require bank holding companies to maintain a minimum leverage ratio of core capital to adjusted quarterly average total assets of at least 3%. In addition, banking regulators have adopted risk-based capital guidelines, under which risk percentages are assigned to various categories of assets and off-balance sheet items to calculate a risk-adjusted capital ratio. Tier I capital generally consists of preferred stock, common shareholders' equity, and trust preferred obligations, less goodwill and certain identifiable intangible assets, while Tier II capital includes the allowance for loan losses and subordinated debt, both subject to certain limitations. Regulatory minimum risk-based capital guidelines require Tier I capital of 4% of risk-adjusted assets and total capital (combined Tier I and Tier II) of 8% to be considered adequately capitalized.

Federal Deposit Insurance Corporation regulations set forth the qualifications necessary for a bank to be classified as well capitalized, primarily for assignment of FDIC insurance premium rates. To qualify as well capitalized, banks must have a Tier I risk-adjusted capital ratio of at least 6%, a total risk-adjusted capital ratio of at least 10%, and a leverage ratio of at least 5%. Failure to qualify as well capitalized can negatively impact a bank's ability to expand and to engage in certain activities.

The Company and its subsidiaries qualify as well-capitalized at September 30, 2010 and December 31, 2009.

	Company		Columbia Bank		Requirements	
	9/30/2010	12/31/2009	9/30/2010	12/31/2009	Adequately capitalized	Well-Capitalized
Total risk-based capital ratio	24.39%	19.60%	18.01%	16.17%	8%	10%
Tier 1 risk-based capital ratio	23.13%	18.34%	16.74%	14.91%	4%	6%
Leverage ratio	13.65%	14.33%	10.01%	11.73%	4%	5%
Tangible common equity to tangible assets	13.98%	11.40%	n/a	n/a	n/a	n/a

In May 2010, the Company completed an underwritten public offering of 11,040,000 shares of our common stock at a purchase price to the public of \$21.75 per share, resulting in gross proceeds of \$240.1 million and net proceeds to us of approximately \$229.1 million.

Item 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

A number of measures are used to monitor and manage interest rate risk, including income simulations and interest sensitivity (gap) analyses. An income simulation model is the primary tool used to assess the direction and magnitude of changes in net interest income resulting from changes in interest rates. Basic assumptions in the model include prepayment speeds on mortgage-related assets, cash flows and maturities of other investment securities, loan and deposit volumes and pricing. These assumptions are inherently subjective and, as a result, the model cannot precisely estimate net interest income or precisely predict the impact of higher or lower interest rates on net interest income. Actual results will differ from simulated results due to timing, magnitude and frequency of interest rate changes and changes in market conditions and management strategies, among other factors. At September 30, 2010, based on the measures used to monitor and manage interest rate risk, there has not been a material change in the Company's interest rate risk since December 31, 2009. For additional information, refer to Management's Discussion and Analysis of Financial Condition and Results of Operation referenced in the Company's 2009 Annual Report on Form 10-K.

Table of Contents

Item 4. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

An evaluation was carried out under the supervision and with the participation of the Company's management, including the Chief Executive Officer (CEO) and Chief Financial Officer (CFO), of the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934). Based on that evaluation, the CEO and CFO have concluded that as of the end of the period covered by this report, our disclosure controls and procedures are effective in ensuring that the information required to be disclosed by us in the reports we file or submit under the Securities Exchange Act of 1934 is (i) accumulated and communicated to our management (including the CEO and CFO) to allow timely decisions regarding required disclosure, and (ii) recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms.

Changes in Internal Controls Over Financial Reporting

There was no change in our internal controls over financial reporting during our most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, our internal controls over financial reporting.

Table of Contents

PART II - OTHER INFORMATION

Item 1. LEGAL PROCEEDINGS

The Company and its banking subsidiaries are parties to routine litigation arising in the ordinary course of business. Management believes that, based on the information currently known to them, any liabilities arising from such litigation will not have a material adverse impact on the Company's financial condition, results of operations or cash flows.

ITEM 1A. RISK FACTORS

Our business exposes us to certain risks. The following is a discussion of what we currently believe are the most significant risks and uncertainties that may affect our business, financial condition and future results.

A slow or fragile economic recovery could adversely affect our future results of operations or market price of our stock.

The national economy and the financial services sector in particular are currently facing challenges of a scope unprecedented in recent history. We cannot accurately predict how quickly the economy will recover from the recent recession, which has adversely impacted the markets we serve. The U.S. economy has also experienced substantial volatility in the financial markets. Any further deterioration in the economies of the nation as a whole or in our markets would have an adverse effect, which could be material, on our business, financial condition, results of operations and prospects, and could also cause the market price of our stock to decline. While it is impossible to predict how long adverse economic conditions may exist, a slow or fragile recovery could continue to present risks for some time for the industry and our company.

Economic conditions in the market areas we serve may continue to adversely impact our earnings and could increase our credit risk associated with our loan portfolio and the value of our investment portfolio.

Substantially all of our loans are to businesses and individuals in Washington and Oregon, and a continuing decline in the economies of these market areas could have a material adverse effect on our business, financial condition, results of operations and prospects. A series of large Puget Sound-based businesses have implemented substantial employee layoffs and scaled back plans for future growth. Additionally, acquisitions and consolidations have resulted in substantial employee layoffs, along with a significant increase in office space availability in downtown Seattle. Oregon has also seen a similar pattern of large layoffs in major metropolitan areas. There has been a decline in housing prices in both Washington and Oregon. A further deterioration in the market areas we serve could result in the following consequences, any of which could have an adverse impact, which could be material, on our business, financial condition, results of operations and prospects:

commercial and consumer loan delinquencies may increase further;

problem assets and foreclosures may increase;

collateral for loans made may decline further in value, in turn reducing customers' borrowing power, reducing the value of assets and collateral associated with existing loans;

certain securities within our investment portfolio could become other than temporarily impaired, requiring a write-down through earnings to fair value, thereby reducing equity;

low cost or non-interest bearing deposits may decrease; and

demand for our loan and other products and services may decrease.

Our loan portfolio mix, which has a concentration of loans secured by real estate, could result in increased credit risk in a challenging economy.

Our loan portfolio is concentrated in commercial real estate and commercial business loans. These types of loans, as well as real estate construction loans and land development loans, acquisition and development loans related to the for-sale housing industry, generally are viewed as having more risk of default than residential real estate loans or certain other types of loans or investments. In fact, the FDIC has issued pronouncements alerting banks of its concern about heavy loan concentrations. Because our loan portfolio contains a significant number of construction, commercial business and commercial real estate loans with relatively large balances, the deterioration of one or a few of these loans may cause a significant increase in our non-performing loans. An increase in non-performing loans could result in a loss of earnings from these loans, an increase in the provision for loan losses, or an increase in loan charge-offs, which could have an adverse impact on our results of operations and financial condition.

A further downturn in the economies or real estate values in the markets we serve could have a material adverse effect on both borrowers' ability to repay their loans and the value of the real property securing such loans. Our ability to recover on defaulted loans would then be diminished, and we would be more likely to suffer losses on defaulted loans.

Table of Contents

Our Allowance for Loan and Lease Losses (ALLL) may not be adequate to cover future loan losses, which could continue to adversely affect earnings.

We maintain an ALLL in an amount that we believe is adequate to provide for losses inherent in our portfolio. While we strive to carefully monitor credit quality and to identify loans that may become non-performing, at any time there are loans in the portfolio that could result in losses, but that have not been identified as non-performing or potential problem loans. We cannot be sure that we will be able to identify deteriorating loans before they become non-performing assets, or that we will be able to limit losses on those loans that have been identified. Additionally, the process for determining the ALLL requires different, subjective and complex judgments about the future impact from current economic conditions that might impair the ability of borrowers to repay their loans. As a result, future significant increases to the ALLL may be necessary. Additionally, future increases to the ALLL may be required based on changes in the composition of the loans comprising the portfolio, deteriorating values in underlying collateral (most of which consists of real estate) and changes in the financial condition of borrowers, such as may result from changes in economic conditions, or as a result of incorrect assumptions by management in determining the ALLL. Additionally, banking regulators, as an integral part of their supervisory function, periodically review our ALLL. These regulatory agencies may require us to increase the ALLL which could have a negative effect on our financial condition and results of operation. Any increase in the ALLL would have an adverse effect, which could be material, on our financial condition and results of operations.

Nonperforming assets take significant time to resolve and adversely affect our results of operations and financial condition.

Our nonperforming assets adversely affect our net income in various ways. Until economic and market conditions improve, we expect to continue to incur additional losses relating to elevated levels of nonperforming loans. We do not record interest income on non-accrual loans, thereby adversely affecting our income, and increasing loan administration costs. When we receive collateral through foreclosures and similar proceedings, we are required to mark the related loan to the then fair market value of the collateral, which may result in a loss. An increase in the level of nonperforming assets also increases our risk profile and may impact the capital levels our regulators believe is appropriate in light of such risks. We utilize various techniques such as loan sales, workouts, and restructurings to manage our problem assets. Decreases in the value of these problem assets, the underlying collateral, or in the borrowers' performance or financial condition, could adversely affect our business, results of operations and financial condition. In addition, the resolution of nonperforming assets requires significant commitments of time from management and staff, which can be detrimental to performance of their other responsibilities. There can be no assurance that we will not experience further increases in nonperforming loans in the future.

Our acquisitions and the integration of acquired businesses may not result in all of the benefits anticipated, and future acquisitions may be dilutive to current shareholders.

We have in the past and may in the future seek to grow our business by acquiring other businesses. In January 2010, we acquired assets and deposits of Columbia River Bank and American Marine Bank in FDIC-assisted transactions. There can be no assurance that our acquisitions will have the anticipated positive results, including results relating to: correctly assessing the asset quality of the assets being acquired; the total cost of integration including management attention and resources; the time required to complete the integration successfully; the amount of longer-term cost savings; being able to profitably deploy funds acquired in an acquisition; or the overall performance of the combined entity.

We also may encounter difficulties in obtaining required regulatory approvals and unexpected contingent liabilities can arise from the businesses we acquire. Integration of an acquired business can be complex and costly, sometimes including combining relevant accounting and data processing systems and management controls, as well as managing relevant relationships with employees, clients, suppliers and other business partners. Integration efforts could divert management attention and resources, which could adversely affect our operations or results.

Given the continued market volatility and uncertainty, notwithstanding our loss-sharing arrangements with the FDIC with respect to the assets we acquired of Columbia River Bank and American Marine Bank, we may continue to experience increased credit costs or need to take additional markdowns and allowances for loan losses on the assets and loans acquired that could adversely affect our financial condition and results of operations in the future. We may also experience difficulties in complying with the technical requirements of our loss-sharing agreements with the FDIC, which could result in some assets which we acquire in FDIC-assisted transactions losing their coverage under such agreements. There is no assurance that as our integration efforts continue in connection with these transactions, other unanticipated costs, including the diversion of personnel, or losses, will not be incurred.

Acquisitions may also result in business disruptions that cause us to lose customers or cause customers to remove their accounts from us and move their business to competing financial institutions. It is possible that the integration process related to acquisitions could result in the disruption of our ongoing businesses or inconsistencies in standards, controls, procedures

Table of Contents

and policies that could adversely affect our ability to maintain relationships with clients, customers, depositors and employees. The loss of key employees in connection with an acquisition could adversely affect our ability to successfully conduct our business.

We may engage in future acquisitions involving the issuance of additional common stock and/or cash. Any such acquisitions and related issuances of stock may have a dilutive effect on earnings per share and the percentage ownership of current shareholders. The use of cash as consideration in any such acquisitions could impact our capital position and may require us to raise additional capital.

Furthermore, notwithstanding our recent acquisitions, we cannot provide any assurance as to the extent to which we can continue to grow through acquisitions as this will depend on the availability of prospective target opportunities at valuations we find attractive and the competition for such opportunities from other parties.

FDIC-assisted acquisition opportunities may not become available and increased competition may make it more difficult for us to successfully bid on failed bank transactions.

A part of our near-term business strategy is to pursue failing banks that the FDIC plans to place in receivership. The FDIC may not place banks that meet our strategic objectives into receivership. Failed bank transactions are attractive opportunities in part because of loss-sharing arrangements with the FDIC that limit the acquirer's downside risk on the purchased loan portfolio and, apart from our assumption of deposit liabilities, we have significant discretion as to the non-deposit liabilities that we assume in such transactions. In addition, assets purchased from the FDIC are marked to their fair value and in many cases there is little or no addition to goodwill arising from an FDIC-assisted transaction. The bidding process for failing banks could become very competitive and the FDIC does not provide information about bids until after the failing bank has been closed. We may not be able to match or beat the bids of other acquirers unless we bid aggressively by increasing the premium paid on assumed deposits or reducing the discount bid on assets purchased, which could make the acquisition less attractive to us.

Our profitability measures could be adversely affected if we are unable to effectively deploy recently raised capital.

We may use the net proceeds of our recently completed offering for selective acquisitions that meet our disciplined acquisition criteria, to fund internal growth, or for general corporate purposes. Although we are periodically engaged in discussions with potential acquisition candidates, we are not currently a party to any purchase or merger agreement. There can be no assurance that we will be able to negotiate future acquisitions on terms acceptable to us. Investing the proceeds of our recent offering in securities until we are able to deploy the proceeds would provide lower margins than we generally earn on loans, potentially adversely impacting shareholder returns, including earnings per share, net interest margin, return on assets and return on equity.

If the goodwill we have recorded in connection with acquisitions becomes impaired, it could have an adverse impact on our earnings and capital.

Accounting standards require that we account for acquisitions using the acquisition method of accounting. Under acquisition accounting, if the purchase price of an acquired company exceeds the fair value of its net assets, the excess is carried on the acquirer's balance sheet as goodwill. In accordance with generally accepted accounting principles, our goodwill is evaluated for impairment on an annual basis or more frequently if events or circumstances indicate that a potential impairment exists. Such evaluation is based on a variety of factors, including the quoted price of our common stock, market prices of common stock of other banking organizations, common stock trading multiples, discounted cash flows, and data from comparable acquisitions. There can be no assurance that future evaluations of goodwill will not result in impairment and ensuing write-down, which could be material, resulting in an adverse impact on our earnings and capital.

We may pursue additional capital, which may not be available on acceptable terms or at all, could dilute the holders of our outstanding common stock and may adversely affect the market price of our common stock.

In the current economic environment, we believe it is prudent to consider alternatives for raising capital when opportunities to raise capital at attractive prices present themselves, in order to further strengthen our capital and better position ourselves to take advantage of opportunities that may arise in the future. Such alternatives may include issuance and sale of common or preferred stock, trust preferred securities, or borrowings by the Company, with proceeds contributed to our banking subsidiary, Columbia State Bank (the "Bank"). Our ability to raise additional capital, if needed, will depend on, among other things, conditions in the capital markets at the time, which are outside of our control, and our financial performance. We cannot assure you that such capital will be available to us on acceptable terms or at all. Any such capital

Table of Contents

raising alternatives could dilute the holders of our outstanding common stock, and may adversely affect the market price of our common stock and our performance measures such as earnings per share.

Fluctuating interest rates can adversely affect our profitability.

Our profitability is dependent to a large extent upon net interest income, which is the difference (or spread) between the interest earned on loans, securities and other interest-earning assets and the interest paid on deposits, borrowings, and other interest-bearing liabilities. Because of the differences in maturities and repricing characteristics of our interest-earning assets and interest-bearing liabilities, changes in interest rates do not produce equivalent changes in interest income earned on interest-earning assets and interest paid on interest-bearing liabilities. Accordingly, fluctuations in interest rates could adversely affect our interest rate spread, and, in turn, our profitability.

Fluctuations in interest rates on loans could adversely affect our business.

Significant increases in market interest rates on loans, or the perception that an increase may occur, could adversely affect both our ability to originate new loans and our ability to grow. Conversely, decreases in interest rates could result in an acceleration of loan prepayments. An increase in market interest rates could also adversely affect the ability of our floating-rate borrowers to meet their higher payment obligations. If this occurred, it could cause an increase in nonperforming assets and charge offs, which could adversely affect our business.

The FDIC has increased insurance premiums to restore and maintain the federal deposit insurance fund, which has increased our costs and could adversely affect our business.

The FDIC recently adopted a new deposit insurance fund restoration plan to ensure that the fund reserve ratio reaches 1.35 percent by September 30, 2020, as required by financial reform legislation passed in 2010.

The FDIC has required insured institutions to prepay estimated quarterly risk-based assessments for the fourth quarter of 2009 and for 2010, 2011 and 2012. The prepayment was collected on December 30, 2009, and was accounted for as a prepaid expense amortized over the prepayment period. In 2009, the FDIC also adopted a final rule revising its risk-based assessment system, which became effective April 1, 2009. The changes to the assessment system involve adjustments to the risk-based calculation of an institution's unsecured debt, secured liabilities and brokered deposits.

In 2009 the FDIC also imposed a special deposit insurance assessment of five basis points on all insured institutions. Based on our assets subject to the FDIC assessment, the special assessment was approximately \$1.4 million. This special assessment was in addition to the regular quarterly risk-based assessment.

Additional increases in FDIC insurance premiums could have a significant impact on Columbia.

Despite the FDIC's recently adopted plan to restore the deposit insurance fund, the fund may suffer additional losses in the future due to bank failures. There can be no assurance that there will not be additional significant deposit insurance premium increases or special assessments imposed in order to restore the insurance fund's reserve ratio. Any significant premium increases or special assessments could have a material adverse effect on our financial condition and results of operations.

We operate in a highly regulated environment and changes of or increases in, or supervisory enforcement of, banking or other laws and regulations or governmental fiscal or monetary policies could adversely affect us.

We are subject to extensive regulation, supervision and examination by federal and state banking authorities. In addition, as a publicly-traded company, we are subject to regulation by the Securities and Exchange Commission. Any change in applicable regulations or federal, state or local legislation or in policies or interpretations or regulatory approaches to compliance and enforcement, income tax laws and accounting principles could have a substantial impact on us and our operations. Changes in laws and regulations may also increase our expenses by imposing additional fees or taxes or restrictions on our operations. Additional legislation and regulations that could significantly affect our powers, authority and operations may be enacted or adopted in the future, which could have a material adverse effect on our financial condition and results of operations. Failure to appropriately comply with any such laws, regulations or principles could result in sanctions by regulatory agencies, or damage to our reputation, all of which could adversely affect our business, financial condition or results of operations.

In that regard, the Dodd-Frank Wall Street Reform and Consumer Protection Act was enacted in July 2010. Among other provisions, the new legislation (i) creates a new Bureau of Consumer Financial Protection with broad powers to regulate consumer financial products such as credit cards and mortgages, (ii) creates a Financial Stability Oversight Council comprised of the heads of other regulatory agencies, (iii) will lead to

new capital requirements from federal banking agencies,

Table of Contents

(iv) places new limits on electronic debt card interchange fees and (v) will require the Securities and Exchange Commission and national stock exchanges to adopt significant new corporate governance and executive compensation reforms. The new legislation and regulations are expected to increase the overall costs of regulatory compliance.

Further, regulators have significant discretion and authority to prevent or remedy unsafe or unsound practices or violations of laws or regulations by financial institutions and holding companies in the performance of their supervisory and enforcement duties. Recently, these powers have been utilized more frequently due to the serious national, regional and local economic conditions we are facing. The exercise of regulatory authority may have a negative impact on our financial condition and results of operations. Additionally, our business is affected significantly by the fiscal and monetary policies of the U.S. federal government and its agencies, including the Federal Reserve Board.

We cannot accurately predict the full effects of recent legislation or the various other governmental, regulatory, monetary and fiscal initiatives which have been and may be enacted on the financial markets, on the Company and on the Bank. The terms and costs of these activities, or the failure of these actions to help stabilize the financial markets, asset prices, market liquidity and a continuation or worsening of current financial market and economic conditions could materially and adversely affect our business, financial condition, results of operations, and the trading price of our common stock.

A continued tightening of the credit markets and credit market volatility may make it difficult to maintain adequate funding for loan growth, which could adversely affect our earnings.

A continued tightening of the credit markets and the inability to maintain adequate liquidity to fund continued loan growth may negatively affect asset growth and, therefore, our earnings capability. In addition to deposit growth and payments of principal and interest received on loans and investment securities, we also rely on borrowing lines with the FHLB of Seattle and the FRB of San Francisco to fund loans. However, the FHLB has discontinued the repurchase of its stock and discontinued the distribution of dividends. Based on the foregoing, there can be no assurance the FHLB will have sufficient resources to continue to fund our borrowings at their current levels. In the event of a deterioration in our financial condition or a further downturn in the economy, particularly in the housing market, our ability to access these funding resources could be negatively affected, which could limit the funds available to us making it difficult for us to maintain adequate funding for loan growth. In addition, our customers' ability to raise capital and refinance maturing obligations could be adversely affected, resulting in a further unfavorable impact on our business, financial condition and results of operations.

We may be required, in the future, to recognize impairment with respect to investment securities, including the FHLB stock we hold.

Our securities portfolio currently includes securities with unrecognized losses. We may continue to observe declines in the fair market value of these securities. We evaluate the securities portfolio for any other than temporary impairment each reporting period, as required by generally accepted accounting principles in the United States of America, and as of September 30, 2010, we did not recognize any securities as other-than-temporarily impaired. There can be no assurance, however, that future evaluations of the securities portfolio will not require us to recognize an impairment charge with respect to these and other holdings.

In addition, as a condition to membership in the FHLB, we are required to purchase and hold a certain amount of FHLB stock. Our stock purchase requirement is based, in part, upon the outstanding principal balance of advances from the FHLB. At September 30, 2010, we had stock in the FHLB totaling \$17.9 million. The FHLB stock held by us is carried at cost and is subject to recoverability testing under applicable accounting standards. The FHLB has discontinued the repurchase of their stock and discontinued the distribution of dividends. As of September 30, 2010, we did not recognize an impairment charge related to our FHLB stock holdings. There can be no assurance, however, that future negative changes to the financial condition of the FHLB may not require us to recognize an impairment charge with respect to such holdings.

Our ability to access markets for funding and acquire and retain customers could be adversely affected by negative public opinion, the deterioration of other financial institutions or the further deterioration of the financial services industry's reputation.

The financial services industry continues to be featured in negative headlines about the global and national credit crisis and the resulting stabilization legislation enacted by the U.S. federal government. These reports can be damaging to the industry's image and potentially erode consumer confidence in insured financial institutions, such as our banking subsidiary. In addition, our ability to engage in routine funding and other transactions could be adversely affected by the actions and financial condition of other financial institutions or negative public opinion resulting from our actual or alleged conduct in any number of activities, including lending practices, governmental enforcement actions taken by regulators or community organizations in response to those activities. Financial services institutions are interrelated as a result of trading, clearing,

Table of Contents

correspondent, counterparty or other relationships. As a result, defaults by, or even rumors or questions about, one or more financial services institutions, or the financial services industry in general, could lead to market-wide liquidity problems, losses of depositor, creditor and counterparty confidence and to losses or defaults by us or by other institutions. We could experience material changes in the level of deposits as a direct or indirect result of other banks' difficulties or failure, which could affect the amount of capital we need. In addition, negative perceptions associated with our continued participation in the CPP may adversely affect our ability to retain customers, attract investors and compete for new business opportunities.

Substantial competition in our market areas could adversely affect us.

Commercial banking is a highly competitive business. We compete with other commercial banks, savings and loan associations, credit unions, finance, insurance and other non-depository companies operating in our market areas. We also experience competition, especially for deposits, from internet-based banking institutions, which have grown rapidly in recent years. We are subject to substantial competition for loans and deposits from other financial institutions. Some of our competitors are not subject to the same degree of regulation and restriction as we are. Some of our competitors have greater financial resources than we do. Some of our competitors have severe liquidity issues, which could impact the pricing of deposits in our marketplace. If we are unable to effectively compete in our market areas, our business, results of operations and prospects could be adversely affected.

Changes in accounting standards could materially impact our financial statements.

From time to time the Financial Accounting Standards Board and the SEC change the financial accounting and reporting standards that govern the preparation of our financial statements. These changes can be very difficult to predict and can materially impact how we record and report our financial condition and results of operations. In some cases, we could be required to apply a new or revised standard retroactively, resulting in our restating prior period financial statements.

There can be no assurance as to the level of dividends we may pay on our common stock.

Holders of our common stock are only entitled to receive such dividends as our Board of Directors may declare out of funds legally available for such payments. Although we have historically declared cash dividends on our common stock, we are not required to do so and there may be circumstances under which we would eliminate our common stock dividend in the future. This could adversely affect the market price of our common stock.

Our ability to receive dividends from our banking subsidiary accounts for most of our revenue and could affect our liquidity and ability to pay dividends.

We are a separate and distinct legal entity from our banking subsidiary, Columbia State Bank. We receive substantially all of our revenue from dividends from our banking subsidiary. These dividends are the principal source of funds to pay dividends on our common and preferred stock and principal and interest on our outstanding debt. Various federal and/or state laws and regulations limit the amount of dividends that our bank may pay us. Also, our right to participate in a distribution of assets upon a subsidiary's liquidation or reorganization is subject to the prior claims of the subsidiary's creditors. Limitations on our ability to receive dividends from our subsidiary could have a material adverse effect on our liquidity and on our ability to pay dividends on common or preferred stock. Additionally, if our subsidiary's earnings are not sufficient to make dividend payments to us while maintaining adequate capital levels, we may not be able to make dividend payments to our common and preferred shareholders or principal and interest payments on our outstanding debt.

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

We are from time to time subject to claims and proceedings related to our operations. These claims and legal actions, which could include supervisory or enforcement actions by our regulators, or criminal proceedings by prosecutorial authorities, could involve large monetary claims, including civil money penalties or fines imposed by government authorities, and significant defense costs. To mitigate the cost of some of these claims, we maintain insurance coverage in amounts and with deductibles that we believe are appropriate for our operations. However, our insurance coverage does not cover any civil money penalties or fines imposed by government authorities and may not cover all other claims that might be brought against us or continue to be available to us at a reasonable cost. As a result, we may be exposed to substantial uninsured liabilities, which could adversely affect our business, prospects, results of operations and financial condition. Substantial legal liability or significant regulatory action against us could have material adverse financial effects or cause significant reputational harm to us, which in turn

could seriously harm our business prospects.

Table of Contents

We are subject to a variety of operational risks, including reputational risk, legal risk and compliance risk, and the risk of fraud or theft by employees or outsiders, which may adversely affect our business and results of operations.

We are exposed to many types of operational risks, including reputational risk, legal and compliance risk, the risk of fraud or theft by employees or outsiders, and unauthorized transactions by employees or operational errors, including clerical or record-keeping errors or those resulting from faulty or disabled computer or telecommunications systems.

If personal, non-public, confidential or proprietary information of customers in our possession were to be mishandled or misused, we could suffer significant regulatory consequences, reputational damage and financial loss. Such mishandling or misuse could include, for example, if such information were erroneously provided to parties who are not permitted to have the information, either by fault of our systems, employees, or counterparties, or where such information is intercepted or otherwise inappropriately taken by third parties.

Because the nature of the financial services business involves a high volume of transactions, certain errors may be repeated or compounded before they are discovered and successfully rectified. Our necessary dependence upon automated systems to record and process transactions and our large transaction volume may further increase the risk that technical flaws or employee tampering or manipulation of those systems will result in losses that are difficult to detect. We also may be subject to disruptions of our operating systems arising from events that are wholly or partially beyond our control (for example, computer viruses or electrical or telecommunications outages, or natural disasters, disease pandemics or other damage to property or physical assets) which may give rise to disruption of service to customers and to financial loss or liability. We are further exposed to the risk that our external vendors may be unable to fulfill their contractual obligations (or will be subject to the same risk of fraud or operational errors by their respective employees as we are) and to the risk that we (or our vendors) business continuity and data security systems prove to be inadequate. The occurrence of any of these risks could result in a diminished ability of us to operate our business (for example, by requiring us to expend significant resources to correct the defect), as well as potential liability to clients, reputational damage and regulatory intervention, which could adversely affect our business, financial condition and results of operations, perhaps materially.

We have various anti-takeover measures that could impede a takeover.

Our articles of incorporation include certain provisions that could make more difficult the acquisition of us by means of a tender offer, a proxy contest, merger or otherwise. These provisions include certain non-monetary factors that our board of directors may consider when evaluating a takeover offer, and a requirement that any Business Combination be approved by the affirmative vote of no less than 66 2/3% of the total shares attributable to persons other than a Control Person. These provisions may have the effect of lengthening the time required for a person to acquire control of us through a tender offer, proxy contest or otherwise, and may deter any potentially hostile offers or other efforts to obtain control of us. This could deprive our shareholders of opportunities to realize a premium for their Columbia common stock, even in circumstances where such action is favored by a majority of our shareholders.

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

None.

Item 3. DEFAULTS UPON SENIOR SECURITIES

None.

Item 4. [REMOVED AND RESERVED.]

Item 5. OTHER INFORMATION

None.

Table of Contents

Item 6. EXHIBITS

- 31.1 Certification of Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- 31.2 Certification of Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- 32 Certification Pursuant to 18 U.S.C. Section 1350, As Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

Table of Contents

SIGNATURES

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

COLUMBIA BANKING SYSTEM, INC.

Date: November 8, 2010

By */s/ MELANIE J. DRESSEL*
Melanie J. Dressel
President and Chief Executive Officer

(Principal Executive Officer)

Date: November 8, 2010

By */s/ GARY R. SCHMINKEY*
Gary R. Schminkey
Executive Vice President and

Chief Financial Officer

(Principal Financial Officer)

Table of Contents

INDEX TO EXHIBITS

- 31.1 Certification of Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- 31.2 Certification of Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- 32 Certification Pursuant to 18 U.S.C. Section 1350, As Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002