

HomeStreet, Inc.
Form 10-K
March 15, 2013

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

FORM 10-K

(Mark One)

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

For the fiscal year ended December 31, 2012

OR

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

For the transition period from _____ to _____

Commission file number: 001-35424

HOMESTREET, INC.

(Exact name of registrant as specified in its charter)

Washington
(State or other jurisdiction of
incorporation or organization)
601 Union Street, Ste. 2000
Seattle, WA 98101

(Address of principal executive offices) (Zip Code)

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

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

Title of each class

Common Stock, no par value

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

None.

91-0186600
(I.R.S. Employer
Identification Number)

Name of each exchange on which registered
NASDAQ Stock Market LLC

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

Yes No

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

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes No

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

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

Yes No

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

Large accelerated filer Accelerated filer

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

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

As of June 30, 2012, the last day of the registrant's most recently completed second fiscal quarter, the aggregate market value of common stock held by non-affiliates was approximately \$198.9 million, based on a closing price of \$15.99, after giving effect to the 2 for 1 stock split which took place on November 5, 2012. Shares of common stock held by each executive officer and director and by each person known to the Company who beneficially owns more than 5% of the outstanding common stock have been excluded in that such persons may under certain circumstances be deemed to be affiliates. This determination of executive officer or affiliate status is not necessarily a conclusive determination for other purposes.

The number of outstanding shares of the registrant's common stock as of February 28, 2013 was 14,384,453.

DOCUMENTS INCORPORATED BY REFERENCE

Certain information that will be contained in the definitive proxy statement for the registrant's annual meeting to be held in 2013 is incorporated by reference into Part III of this Form 10-K.

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

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PART 1

FORWARD-LOOKING STATEMENTS

This Form 10-K and the documents incorporated by reference contain, in addition to historical information, “forward-looking statements” within the meaning of Section 27A of the Securities Act of 1933, as amended (the “Securities Act”) and Section 21E of the Securities Exchange Act of 1934, as amended (the “Exchange Act”). These statements relate to our future plans, objectives, expectations, intentions and financial performance, and assumptions that underlie these statements. All statements other than statements of historical fact are “forward-looking statements” for the purposes of these provisions. When used in this Form 10-K, terms such as “anticipates,” “believes,” “continue,” “could,” “estimates,” “expects,” “intends,” “may,” “plans,” “potential,” “predicts,” “should,” or “will” or the negative of those other comparable terms are intended to identify such forward-looking statements. These statements involve known and unknown risks, uncertainties and other factors that may cause industry trends or actual results, level of activity, performance or achievements to be materially different from any future results, levels of activity, performance or achievements expressed or implied by these statements. Our actual results may differ significantly from the results discussed in such forward-looking statements.

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

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

ITEM 1 BUSINESS

General

We are a 91-year-old diversified financial services company headquartered in Seattle, Washington, serving consumers and businesses primarily in the Pacific Northwest and Hawaii. The Company is principally engaged in real estate lending, including mortgage banking activities, and retail and commercial banking operations. Our primary subsidiaries are HomeStreet Bank (the “Bank”) and HomeStreet Capital Corporation. HomeStreet Bank is a Washington state-chartered savings bank that provides residential and commercial loans, deposit products and services, non-deposit investment products, and cash management services. HomeStreet Bank’s primary loan products include single family residential mortgages, loans secured by commercial real estate, loans for residential and commercial real estate construction, and commercial business loans. HomeStreet Capital Corporation, a Washington corporation, originates, sells and services multifamily mortgage loans under the Fannie Mae Delegated Underwriting and Servicing Program (“DUS[®]) (DUS[®] is a registered trademark of Fannie Mae.) in conjunction with HomeStreet Bank. Doing business as HomeStreet Insurance, we provide insurance products and services for consumers and businesses. We additionally offer single family home loans through our partial ownership in an affiliated business arrangement known as Windermere Mortgage Services Series LLC (“WMS LLC”). At December 31, 2012, we had total assets of \$2.63 billion.

We currently have a network of 22 bank branches in the Puget Sound region of Washington State, Portland, Oregon, Southwest Washington, and Hawaii, as well as 24 stand-alone lending centers located in these same areas and additionally in Aberdeen and Spokane, Washington, the Eugene and Salem regions of Oregon, and in the Boise and northern regions of Idaho. WMS LLC provides point-of-sale loan origination services at approximately 40

Windermere Real Estate offices in Washington and Oregon.

We operate four primary business segments: Community Banking, Single Family Mortgage Lending, Income Property Lending and Residential Construction Lending. For a discussion of operating results of each of these lines of business, see "Business Segments" within Management's Discussion and Analysis of this Form 10-K.

Community Banking. We provide a diversified set of financial products and services to our consumer and business customers, including deposit products, investment products, insurance products, cash management services, consumer and business loans and Small Business Administration loans.

Single Family Mortgage Lending. We originate and sell residential mortgage loans into the secondary market both directly and through our affiliated business arrangement with WMS LLC. This business line also originates and services loans for our

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portfolio on a selective basis including home equity loans. We originate mortgages using secondary market standards and the majority are sold to or securitized by Fannie Mae, Freddie Mac or Ginnie Mae, while we retain the right to service these loans. In addition, the Company originates Federal Housing Administration ("FHA")-insured and Department of Veterans' Affairs ("VA")-guaranteed mortgage loans that are used to back Ginnie Mae-guaranteed securities. A small percentage of loans are brokered or sold on a servicing-released basis to correspondent lenders.

Income Property Lending. We originate commercial real estate loans, including multifamily lending through our Fannie Mae DUS business. These loans are sold to or securitized by Fannie Mae and we generally continue to service those loans after the sale. We also originate commercial construction loans, bridge loans and permanent loans for our own portfolio and for sale to other investors such as insurance companies.

Residential Construction Lending. We originate residential construction loans for our own portfolio, focusing on loans to developers for single family home construction that are short duration in nature. Generally, we do not make loans secured by or for the purchase of raw land.

Initial Public Offering

On February 15, 2012, we completed our initial public offering of 8,723,632 shares of common stock for an initial offering price of \$11.00 per share (after giving effect to the 2-for-1 forward stock split effective March 6, 2012 and the 2-for-1 forward stock split effective November 5, 2012). The net increase in HomeStreet's capital was \$86.4 million, which included net cash proceeds of \$87.7 million received in 2012, less \$1.4 million of issuance costs paid in 2011. The Company contributed \$55.0 million to the Bank on February 24, 2012 and an additional \$10.0 million on April 26, 2012, leaving approximately \$22.7 million of net proceeds at the Company to be used for general corporate purposes. Shares of our common stock are traded on the NASDAQ Global Select Market under the symbol "HMST."

Recent Developments

On March 12, 2013, the Company received notification from the Federal Reserve Bank permitting the Company to pay all past deferred interest due on its outstanding debt securities (Trust Preferred Securities, or "TruPS") and the interest payment due on March 15, 2013, for a total of \$13.5 million. The Company intends to replenish its liquidity through payment of dividends from the Bank for which the Bank has made regulatory application and sought regulatory non-objection. No assurances can be given that such non-objection has or will be obtained from the relevant regulators.

The March 15, 2013 payment of the deferred and current interest lifts the restrictions under the terms of the TruPS indentures that prohibited the Company from making cash dividends or distributions to shareholders if the TruPS interest is not paid current. However, the Company remains under a cease and desist order which restricts the Company from making cash dividends or distributions without regulatory consent.

Regulatory Update

On March 26, 2012, the Federal Deposit Insurance Corporation ("FDIC") and the Washington State Department of Financial Institutions ("WDFI") terminated the cease and desist order for the Bank ("Bank Order"), dated May 8, 2009 and the Bank Order was replaced with a memorandum of understanding ("MOU"). On December 27, 2012, the Bank was notified by the FDIC and the WDFI that the Bank had taken appropriate corrective actions to address the MOU and consequently the Bank's MOU was terminated effective December 27, 2012. The Bank is no longer considered a "troubled institution" and is now considered "well-capitalized" within the meaning of the FDIC's prompt corrective action rules. The Company remains under a cease and desist order (the "Company Order") supervised by the Federal Reserve Bank.

The termination of the Bank Order provided several benefits, including a reduction in our FDIC assessment and examination fees; resumption of portfolio lending for certain lending products; the ability to open or re-locate retail deposit branches; access to federal funds lines from correspondent banks; the re-opening of certain correspondent lending channels that had previously been restricted; and the ability to increase the amount of trading partner relationships used for hedging purposes. Additionally, as a result of the termination of the Bank Order and the related impact on certain rating agency metrics, the Bank now fully complies with the seller servicer requirements of government-sponsored entities such as Fannie Mae and Freddie Mac.

In recognition of the significant improvement in the Bank's financial condition, results of operations and risk profile, on July 10, 2012 the Federal Reserve Bank granted full access to all Federal Reserve Bank lending and depository services.

Changes in Management

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On July 26, 2012, the Company announced the appointment of Cory D. Stewart as the Company's Executive Vice President and Chief Accounting Officer, which became effective in the third quarter of 2012, upon receipt of the necessary regulatory approvals.

On July 26, 2012, the Company also announced the appointment of Darrell van Amen as the Company's Executive Vice President and Chief Investment Officer, which became effective in the third quarter of 2012, upon receipt of the necessary regulatory approvals.

On October 15, 2012, in connection with Mr. Stewart and Mr. van Amen assuming their respective positions with the Company, Mark K. Mason relinquished his role as acting Chief Financial Officer and Principal Accounting Officer of the Company. Mr. Mason continues to serve as the Company's Vice Chairman, President and Chief Executive Officer.

Business Strategy

During 2012, we recapitalized the Company through our initial public offering. In addition, our performance over the course of 2012 was characterized by strong mortgage banking results and significant improvement in asset quality. We now believe we have sufficient capital to be a source of strength to the Bank, provide for payment of our obligations under our outstanding TruPS, and pursue our business strategy.

We are pursuing the following strategies in our business segments:

Community Banking. Our Community Banking strategy involves the development of an integrated consumer and business financial services delivery platform. We seek to meet the financial needs of our consumer and business customers by providing targeted banking products and services, investment advice and products, and insurance products through our bank branches and through dedicated investment advisors, insurance agents and business banking officers. We currently plan to expand our bank branch network primarily focusing on high-growth areas of Puget Sound. We also intend to grow our core deposits by increasing business deposits from new cash management and business lending customers.

Single Family Mortgage Lending. We have leveraged our reputation for high quality service and reliable loan closing to increase our single family mortgage market share significantly over the last three years. In early 2012, we took advantage of an opportunity to add experienced loan originators and accelerated our plans to expand our single family mortgage origination business by hiring approximately 170 mortgage personnel formerly associated with MetLife Home Loans. HomeStreet continued recruiting throughout 2012, ultimately hiring 389 mortgage lending and support personnel, an increase of 146%. HomeStreet added 15 lending offices, including expansion into Idaho. The addition of these employees contributed to the significant increase in our single family mortgage loan origination volume during 2012. We intend to continue to focus on conventional conforming and government insured or guaranteed single family mortgage origination. We also expect to use portfolio lending to complement secondary market lending, particularly for well-qualified borrowers with loan sizes greater than the conventional conforming limits.

Income Property Lending. We currently plan to grow our commercial real estate business, with a focus on our multifamily lending mortgage origination business, particularly through our Fannie Mae DUS origination and servicing relationships. We plan to expand beyond our current markets by adding loan origination personnel and by forming strategic alliances with multifamily property service providers inside and outside our existing lending areas. We expect to continue to benefit from being one of only 25 companies nationally that is an approved Fannie Mae DUS seller and servicer. In addition, we have historically supported our DUS program by providing short-term bridge loans to experienced borrowers who purchase apartment buildings for renovation, which we then seek to replace with permanent financing through the Fannie Mae DUS program upon completion of the renovations. We also originate

commercial construction real estate loans, bridge loans and permanent loans for our portfolio, primarily on office, retail, industrial and multifamily property types located within the Company's geographic footprint. We also may place loans with capital market sources, such as life insurance companies.

Residential Construction Lending. We have resumed originating residential construction loans under enhanced underwriting standards with a significantly reduced portfolio concentration and a focus on home construction loans as opposed to land development projects or raw land.

Market and Competition

The financial services industry is highly competitive. We compete with banks, savings and loan associations, credit unions, mortgage banking companies, insurance companies, finance companies, and investment and mutual fund companies. In

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particular, we compete with several financial institutions with greater resources, including the capacity to make larger loans, fund extensive advertising and offer a broader array of products and services. The number of competitors for middle-market business customers has, however, decreased in recent years due to bank failures and consolidations. In recent years national banks have focused on larger customers to achieve economies of scale in lending and depository relationships and have also consolidated business banking operations and support and reduced service levels in the Pacific Northwest. We have taken advantage of the failures and takeovers of certain of our competitors by recruiting well-qualified employees and attracting new customers who seek long-term stability, local decision-making, quality services, products and expertise. We believe there is a significant opportunity for a well-capitalized, community-focused bank that emphasizes responsive and personalized service to provide a full range of financial services to small- and middle-market commercial and consumer customers in those markets where we do business.

In addition, we believe we are well positioned to take advantage of changes in the single family mortgage origination and servicing industry that have helped to reduce the number of competitors. The mortgage industry is compliance-intensive and requires significant expertise and internal control systems to ensure mortgage loan origination and servicing providers meet all origination, processing, underwriting, servicing and disclosure requirements. These requirements are causing some competitors to exit the industry. New entrants must make significant investments in experienced personnel and specialized systems to manage the compliance process. These investments represent a significant barrier to entry. In addition, lending in conventional and government guaranteed or insured mortgage products, including FHA and VA loans, requires significantly higher capitalization than had previously been required for mortgage brokers and non-bank mortgage companies.

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

We currently intend to expand our commercial real estate mortgage lending business by targeting strong apartment markets and experienced borrowers. We expect to continue to benefit from being one of only 25 companies nationally that is approved Fannie Mae DUS sellers and servicers. The Fannie Mae DUS program became a key multifamily funding source nationally during the turmoil in the financial services industry and the resulting loss of other financing sources. During 2012, an increasing number of banks began competing for multifamily permanent loans for their portfolios. We expect to continue to be in a strong competitive position versus other banks due to our ability to offer both portfolio and Fannie Mae DUS products, depending on the needs of the customer.

Employees

As of December 31, 2012 the Company employed approximately 1,099 full-time equivalent employees compared to 613 full-time equivalents at December 31, 2011.

Where You Can Obtain Additional Information

We file annual, quarterly, current and other reports with the Securities and Exchange Commission (the "SEC"). We make available free of charge on or through our website <http://www.homestreet.com> all of these reports (and all amendments thereto), as soon as reasonably practicable after we file these materials with the SEC. You may review a copy of these reports, including exhibits and schedules filed therewith, and obtain copies of such materials at the SEC's Public Reference Room at 100 F Street, NE, Washington, D.C. 20549. You may obtain information on the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0330. The SEC maintains a website

(<http://www.sec.gov>) that contains reports, proxy and information statements and other information regarding registrants, such as HomeStreet, Inc., that file electronically with the SEC.

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REGULATION AND SUPERVISION

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

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

General

The Company is a savings and loan holding company and is regulated by the Board of Governors at the Federal Reserve System (the "Federal Reserve"), and the Washington State Department of Financial Institutions, Division of Banks (the "WDFI"). The Company is required to register and file reports with, and otherwise comply with, the rules and regulations of the Federal Reserve and the WDFI.

The Office of Thrift Supervision, or the OTS, previously was the Company's primary federal regulator. Under the Dodd-Frank Act, the OTS was dissolved on July 21, 2011 and its authority to supervise and regulate the Company and its non-bank subsidiaries was transferred to the Federal Reserve. References to the Federal Reserve in this document should be read to include the OTS prior to the date of the transfer with respect to those functions transferred to the Federal Reserve.

The Bank is a Washington state-chartered savings bank. The Bank is subject to regulation, examination and supervision by the WDFI and the FDIC.

As a result of the recent financial crisis, regulation of the financial services industry has been undergoing major changes. Among these is the Dodd-Frank Act, which makes significant modifications to and expansions of the rulemaking, supervisory and enforcement authority of the federal banking regulators. Some of the changes were effective immediately, but others are being phased in over time. The Dodd-Frank Act requires various regulators, including the banking regulators, to adopt numerous regulations, not all of which have been finalized. Accordingly, in many instances, the precise requirements of the Dodd-Frank Act are not yet known.

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

Our operations and earnings will be affected by domestic economic conditions and the monetary and fiscal policies of the United States government and its agencies. In addition to its role as the regulator of savings and loan holding companies, the Federal Reserve has, and is likely to continue to have, an important impact on the operating results of financial institutions through its power to implement national monetary and fiscal policy including, among other things, actions taken in order to curb inflation or combat a recession. The Federal Reserve affects the levels of bank loans, investments and deposits through its control over the issuance of United States government securities, its regulation of the discount rate applicable to member banks and its influence over reserve requirements to which banks are subject. In recent years, in response to the financial crisis, the Federal Reserve has created several innovative programs to stabilize certain financial institutions, to help ensure the availability of credit and to purchase financial assets through programs such as quantitative easing or "QE". Quantitative easing has had a significant impact on the market for mortgage-backed securities and by some accounts has stimulated the national economy. We believe these policies have had a beneficial effect on the Company and the mortgage banking industry as a whole. We cannot

predict the nature or impact of future changes in monetary and fiscal policies of the Federal Reserve. The Company is currently operating under a cease and desist order issued by our primary federal regulator, the Federal Reserve, as described below under “Company Order.” Under the cease and desist order, we are required to notify, and in certain cases receive the permission of, the Federal Reserve prior to taking certain actions.
Company Order

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The Company is currently operating under an Order to Cease and Desist issued by the OTS on May 18, 2009 and now administered by the Federal Reserve. Under the Company Order, HomeStreet, Inc. agreed to refrain from engaging in all unsafe and unsound practices that had resulted in the operation of HomeStreet, Inc. with low earnings and inadequate capital. In addition, for so long as the Company Order remains in place, HomeStreet, Inc. has also agreed to not do any of the following without the consent of the Federal Reserve:

- pay dividends or make any other capital distributions;
- incur, issue, renew, repurchase, make payments on or roll over any debt (including payments on trust preferred securities);
- increase any current lines of credit;
- guarantee the debt of any entity;
- make any “golden parachute” or “prohibited indemnification payments” unless we have complied with certain statutory and regulatory requirements; and
- make changes in our Board of Directors or senior executive officers without meeting certain prior notification requirements.

Pursuant to the Company Order, we developed a plan to manage our liquidity, capital and risk profile, and to address our financial obligations, including deferring interest payments on the TruPS, without relying on dividends from the Bank. Following the closing of our initial public offering in February 2012 and the subsequent contribution of \$55.0 million to the Bank on February 24, 2012 with an additional \$10.0 million contributed on April 26, 2012, we retained capital at the Company that management believes is adequate to meet the needs of the Company without requiring additional dividends from the Bank for the near future.

The Company Order will remain in effect until terminated, modified or suspended by the Federal Reserve. We are currently in compliance with the Company Order, although the requirements imposed by the Company Order do not include quantitative capital ratio or asset quality targets. We send quarterly status reports to the Federal Reserve at their request. While management believes that the Company Order will be lifted, we cannot give assurance as to the timing of such action.

Consent Agreement/Memorandum of Understanding

The Bank had previously consented to the issuance by the FDIC and the WDFI of an Order to Cease and Desist dated May 8, 2009. The Bank Order was terminated on March 26, 2012. Also on March 26, 2012, the Bank entered into a MOU with the FDIC and the WDFI. The MOU was terminated on December 27, 2012.

Regulation of the Company

General

Because we have made an election under Section 10(1) of the Home Owners' Loan Act (“HOLA”) for the Bank to be treated as a “savings association” for purposes of Section 10 of HOLA, the Company is registered as a savings and loan holding company with the Federal Reserve and is subject to Federal Reserve regulations, examinations, supervision and reporting requirements relating to savings and loan holding companies. Among other things, the Federal Reserve is authorized to restrict or prohibit activities that are determined to be a serious risk to the financial safety, soundness or stability of a subsidiary savings bank. Unlike bank holding companies, savings and loan holding companies have not been subject to any specific regulatory capital ratios, although they have been subject to review by the Federal Reserve and approval of capital levels as part of its examination process. However, under the Dodd-Frank Act, the Company will become subject to capital requirements. Our continued ability to use the provisions of Section 10(1) of HOLA - which allow the Company to be registered as a savings and loan holding company rather than as a bank holding company - is conditioned upon the Bank's continued qualification as a qualified thrift lender under the Qualified Thrift Lender test set forth in HOLA. See “- Regulation and Supervision of HomeStreet Bank - Qualified Thrift Lender Test.” Since the Bank is chartered under Washington law, the WDFI has authority to regulate the Company generally relating to its conduct affecting the Bank. As a subsidiary of a savings and loan holding company, the Bank is subject to certain restrictions in its dealings with the Company and affiliates thereof.

Numerous provisions of the Dodd-Frank Act affect the Company and its business and operations. Some of the provisions are:

New capital requirements for savings and loan holding companies.

All holding companies of depository institutions are required to serve as a source of strength for their depository subsidiaries.

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The Federal Reserve is given heightened authority to examine, regulate and take action with respect to all of a holding company's subsidiaries.

The Company is a unitary savings and loan holding company within the meaning of federal law. Generally, companies that become savings and loan holding companies following the May 4, 1999 grandfather date in the Gramm-Leach-Bliley Act of 1999 may engage only in the activities permitted for financial institution holding companies as well as activities that are permitted for multiple savings and loan holding companies. Because the Company became a savings and loan holding company prior to that grandfather date, the activities in which the Company and its subsidiaries (other than the Bank and its subsidiaries) may engage generally are not restricted by HOLA. If, however, we are acquired by a non-financial company, or if we acquire another savings association subsidiary (and become a multiple savings and loan holding company), we will terminate our “grandfathered” unitary savings and loan holding company status and become subject to certain limitations on the types of business activities in which we could engage. The Company may not engage in any activity or render any service for or on behalf of the Bank for the purpose of or with the effect of evading any law or regulation applicable to the Bank.

Because the Bank is treated as a savings association subsidiary of a savings and loan holding company, we must give the Federal Reserve at least 30 days' advance notice of the proposed declaration of a dividend by the Bank. In addition, the financial impact of a holding company on its subsidiary institution is a matter that is evaluated by the Federal Reserve, and the Federal Reserve has authority to order cessation of activities or divestiture of subsidiaries deemed to pose a threat to the safety and soundness of the Bank.

As described above, the Company Order prohibits us, among other things, from (1) paying any dividends or making any other capital distributions, (2) incurring, issuing, renewing, repurchasing, making payment on or rolling over any debt, (3) increasing any current lines of credit or (4) guaranteeing the debt of any entity, in each case without the prior written approval of the Federal Reserve.

Capital / Source of Strength

Under the Dodd-Frank Act, capital requirements will be imposed on savings and loan holding companies such as the Company. See “Regulation and Supervision of HomeStreet Bank - Capital and Prompt Corrective Action Requirements - Proposed Capital Regulations.”

Regulations and historical practice of the Federal Reserve have required bank holding companies to serve as a “source of strength” for their subsidiary banks. The Dodd-Frank Act codifies this requirement and extends it to all companies that control an insured depository institution. Accordingly, the Company is now required to act as a source of strength for the Bank. The appropriate federal banking regulators are required by the Dodd-Frank Act to issue final rules to carry out this requirement but have not yet done so.

Restrictions Applicable to Savings and Loan Holding Companies

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

- control (as defined under HOLA) of another savings institution (or a holding company parent) without prior written approval of the Federal Reserve;
- through merger, consolidation or purchase of assets, another savings institution or a holding company thereof, or acquiring all or substantially all of the assets of such institution (or a holding company) without prior Federal Reserve or FDIC approval;
- with certain exceptions, more than 5.0% of the voting shares of a non-subsidiary savings association or a non-subsidiary holding company; or
- control of any depository institution not insured by the FDIC (except through a merger with and into the holding company's savings institution subsidiary that is approved by the FDIC).

In evaluating applications by holding companies to acquire savings associations, the Federal Reserve must consider the financial and managerial resources and future prospects of the company and institution involved, the effect of the acquisition on the risk to the insurance funds, the convenience and needs of the community and competitive factors.

A savings and loan holding company generally may not acquire as a separate subsidiary a savings association in a different state from where its current savings association is located, except:

- in the case of certain emergency acquisitions approved by the FDIC;

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if such holding company controls a savings association that operated a home or branch office in such additional state as of March 5, 1987; or

if the laws of the state in which the savings association to be acquired is located specifically authorize a savings association chartered by that state to be acquired by a savings institution chartered by the state where the acquiring savings association or savings and loan holding company is located, or by a holding company that controls such a state-chartered association.

Acquisition of Control

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

Change in Management

Pursuant to the Company Order, we are required to give 30 days prior written notice to the Federal Reserve before adding or replacing a director, employing any person as a senior executive officer or changing the responsibility of any senior executive officer so that such person would assume a different senior executive position. Our regulators then have the opportunity to disapprove any such appointment.

Dividend Policy

Under Washington law, the Company is generally permitted to make a distribution, including payments of dividends, only if, after giving effect to the distribution, in the judgment of the board of directors, (1) the Company would be able to pay its debts as they become due in the ordinary course of business and (2) the Company's total assets would at least equal the sum of its total liabilities plus the amount that would be needed if the Company were to be dissolved at the time of the distribution to satisfy the preferential rights upon dissolution of shareholders whose preferential rights are superior to those receiving the distribution.

The Company Order prohibits us from paying dividends or making other capital distributions without the prior written consent of the Federal Reserve. In addition, the Company's ability to pay dividends to shareholders is significantly dependent on the Bank's ability to pay dividends to the Company.

Compensation Policies

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

Guidance on Sound Incentive Compensation Policies. Effective on June 25, 2010, the Office of the Comptroller of the Currency, the Federal Reserve, the FDIC and the OTS adopted Sound Incentive Compensation Policies Final Guidance (the “Final Guidance”) designed to help ensure that incentive compensation policies at banking organizations do not encourage imprudent risk-taking and are consistent with the safety and soundness of the organization.

The Final Guidance applies to senior executives and others who are responsible for oversight of HomeStreet's company-wide activities and material business lines, as well as other employees who, either individually or as a part of a group, have the ability to expose the Bank to material amounts of risk.

Dodd-Frank Act. In addition to the Final Guidance, the Dodd-Frank Act contains a number of provisions relating to compensation applying to public companies such as the Company. The Dodd-Frank Act added a new Section 14A(a) to the Exchange Act that requires companies to include a separate non-binding resolution subject to shareholder vote in their proxy materials approving the executive compensation disclosed in the materials. In addition, a new Section 14A(b) to the Exchange Act requires any proxy or consent solicitation materials for a meeting seeking shareholder approval of an acquisition, merger, consolidation or disposition of all or substantially all of the company's assets to include a separate non-binding shareholder

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resolution approving certain “golden parachute” payments made in connection with the transaction. A new Section 10D to the Exchange Act requires the SEC to direct the national securities exchanges to require companies to implement a policy to “claw back” certain executive payments that were made based on improper financial statements.

In addition, Section 956 of the Dodd-Frank Act requires certain regulators (including the FDIC, SEC and Federal Reserve) to adopt requirements or guidelines prohibiting excessive compensation or compensation that could lead to material loss as well as rules relating to disclosure of compensation. On April 14, 2011, these regulators published a joint proposed rulemaking to implement Section 956 of Dodd-Frank for depository institutions, their holding companies and various other financial institutions with \$1 billion or more in assets. Section 956 prohibits incentive-based compensation arrangements which encourage inappropriate risk taking by covered financial institutions and are deemed to be excessive, or that may lead to material losses. The proposed rule would (1) prohibit incentive-based compensation arrangements for covered persons that would encourage inappropriate risks by providing excess compensation, (2) prohibit incentive-based compensation arrangements for covered persons that would expose the institution to inappropriate risks by providing compensation that could lead to a material financial loss, (3) require policies and procedures for incentive-based compensation arrangements that are commensurate with the size and complexity of the institutions and (4) require annual reports on incentive compensation structures to the institution's appropriate federal regulator.

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

Emerging Growth Company

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

We will remain an Emerging Growth Company for up to five years from the end of the year of our initial public offering, or until (1) we have total annual gross revenues of at least \$1 billion, (2) we qualify as a large accelerated filer, or (3) we issue more than \$1 billion in nonconvertible debt in a three year period.

Regulation and Supervision of HomeStreet Bank