

National Bank Holdings Corp
Form 10-K
March 01, 2019
Table of Contents

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-K

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

For the fiscal year ended December 31, 2018

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: 001-35654

NATIONAL BANK HOLDINGS CORPORATION

(Exact name of registrant as specified in its charter)

Delaware 27-0563799
(State or other jurisdiction of (I.R.S. Employer
incorporation or organization) Identification No.)

7800 East Orchard Road, Suite 300, Greenwood Village, Colorado 80111

(Address of principal executive offices) (Zip Code)

Edgar Filing: National Bank Holdings Corp - Form 10-K

Registrant's telephone, including area code:

(720) 529-3336

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

| Title of each class | Name of each exchange on which registered |
|--|---|
| Class A Common Stock, Par Value \$0.01 | New York Stock Exchange |

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

None

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

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

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

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

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

| | |
|-------------------------|---------------------------|
| Large accelerated filer | Accelerated filer |
| Non-accelerated filer | Smaller reporting company |
| | Emerging growth company |

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition

Edgar Filing: National Bank Holdings Corp - Form 10-K

period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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

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

As of June 30, 2018, the aggregate market value of the registrant's common stock held by non-affiliates of the registrant was approximately \$1,156,200,000 based on the closing sale price as reported on the New York Stock Exchange.

APPLICABLE ONLY TO CORPORATE ISSUERS:

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

As of February 27, 2019, NBHC had outstanding 30,862,685 shares of Class A voting common stock with \$0.01 par value per share, excluding 146,494 shares of restricted Class A common stock issued but not yet vested.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Registrant's definitive proxy statement for its 2019 Annual Meeting of Shareholders to be filed within 120 days of December 31, 2018 will be incorporated by reference into Part III of this form 10-K.

Table of Contents

INDEX

| | Page |
|---|------|
| <u>Cautionary Notes Regarding Forward Looking Statements</u> | 3 |
| <u>PART I Item 1. Business</u> | 5 |
| <u>Item 1A. Risk Factors</u> | 19 |
| <u>Item 1B. Unresolved Staff Comments</u> | 32 |
| <u>Item 2. Properties</u> | 32 |
| <u>Item 3. Legal Proceedings</u> | 32 |
| <u>Item 4. Mine Safety Disclosures</u> | 32 |
| <u>PART II Item 5. Market for Registrant’s Common Equity, Related Shareholder Matters and Issuer Purchases of Equity Securities</u> | 33 |
| <u>Item 6. Selected Financial Data</u> | 35 |
| <u>Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operations</u> | 43 |
| <u>Item 7A. Quantitative and Qualitative Disclosures about Market Risk</u> | 73 |
| <u>Item 8. Financial Statements and Supplementary Data</u> | 74 |
| <u>Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure</u> | 128 |
| <u>Item 9A. Controls and Procedures</u> | 128 |
| <u>Item 9B. Other Information</u> | 130 |
| <u>PART III Item 10. Directors, Executive Officers and Corporate Governance</u> | 130 |
| <u>Item 11. Executive Compensation</u> | 130 |
| <u>Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Shareholder Matters</u> | 130 |
| <u>Item 13. Certain Relationships and Related Transactions, and Director Independence</u> | 130 |

| | |
|--|-----|
| <u>Item 14. Principal Accountant Fees and Services</u> | 130 |
| <u>PART IV Item 15. Exhibits and Financial Statement Schedules</u> | 131 |
| <u>Signatures</u> | 134 |

Table of Contents

CAUTIONARY NOTE REGARDING FORWARD-LOOKING STATEMENTS

This report contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995, notwithstanding that such statements are not specifically identified. Any statements about our expectations, beliefs, plans, predictions, forecasts, objectives, assumptions or future events or performance are not historical facts and may be forward-looking. These statements are often, but not always, made through the use of words or phrases such as “anticipate,” “believe,” “can,” “would,” “should,” “could,” “may,” “predict,” “seek,” “potential,” “will,” “estimate,” “tend,” “continue,” “ongoing,” “expect,” “intend” and similar words or phrases. These statements are only predictions and involve estimates, known and unknown risks, assumptions and uncertainties. We have based these statements largely on our current expectations and projections about future events and financial trends that we believe may affect our financial condition, liquidity, results of operations, business strategy and growth prospects.

Forward-looking statements involve certain important risks, uncertainties and other factors, any of which could cause actual results to differ materially from those in such statements and, therefore, you are cautioned not to place undue reliance on such statements. Factors that could cause actual results to differ from those discussed in the forward-looking statements include, but are not limited to:

our ability to execute our business strategy, as well as changes in our business strategy or development plans;

business and economic conditions generally and in the financial services industry;

effects of a prolonged government shutdown;

economic, market, operational, liquidity, credit and interest rate risks associated with our business;

effects of any changes in trade, monetary and fiscal policies and laws, including the interest rate policies of the Federal Reserve Board;

changes imposed by regulatory agencies to increase our capital to a level greater than the current level required for well-capitalized financial institutions;

effects of inflation, as well as, interest rate, securities market and monetary supply fluctuations;

changes in the economy or supply-demand imbalances affecting local real estate values;

changes in consumer spending, borrowings and savings habits;

with respect to our mortgage business, our inability to negotiate our fees with Fannie Mae, Freddie Mac, Ginnie Mae or other investors for the purchase of our loans, our obligation to indemnify purchasers or to repurchase the related loans if the loans fail to meet certain criteria, or higher rate of delinquencies and defaults as a result of the geographic concentration of our servicing portfolio;

our ability to identify potential candidates for, obtain regulatory approval for, and consummate, acquisitions, consolidations or other expansion opportunities on attractive terms, or at all;

our ability to integrate acquisitions or consolidations and to achieve synergies, operating efficiencies and/or other expected benefits within expected time-frames, or at all, or within expected cost projections, and to preserve the goodwill of acquired financial institutions;

our ability to realize the anticipated benefits from enhancements or updates to our core operating systems from time to time without significant change in our client service or risk to our control environment;

our dependence on information technology and telecommunications systems of third party service providers and the risk of system failures, interruptions or breaches of security, including those that could result in disclosure or misuse of confidential or proprietary client or other information;

Table of Contents

our ability to achieve organic loan and deposit growth and the composition of such growth;

changes in sources and uses of funds, including loans, deposits and borrowings;

increased competition in the financial services industry, nationally, regionally or locally, resulting in, among other things, lower returns;

continued consolidation in the financial services industry;

our ability to maintain or increase market share and control expenses;

the effect of changes in accounting policies and practices, as may be adopted by the regulatory agencies, as well as the Public Company Accounting Oversight Board, the Financial Accounting Standards Board and other accounting standard setters;

the trading price of shares of the Company's stock;

the effects of tax legislation, including the potential of future increases to prevailing tax rates, or challenges to our tax position;

our ability to realize deferred tax assets or the need for a valuation allowance, or the effects of changes in tax laws on our deferred tax assets;

costs and effects of changes in laws and regulations and of other legal and regulatory developments, including, but not limited to, changes in regulation that affect the fees that we charge, the resolution of legal proceedings or regulatory or other governmental inquiries, and the results of regulatory examinations, reviews or other inquiries; and changes in regulations that apply to us as a Colorado state-chartered bank;

technological changes;

the timely development and acceptance of new products and services and perceived overall value of these products and services by our clients;

changes in our management personnel and our continued ability to attract, hire and retain qualified personnel;

ability to implement and/or improve operational management and other internal risk controls and processes and our reporting system and procedures;

regulatory limitations on dividends from our bank subsidiary;

changes in estimates of future loan reserve requirements based upon the periodic review thereof under relevant regulatory and accounting requirements;

widespread natural and other disasters, dislocations, political instability, acts of war or terrorist activities, cyberattacks or international hostilities through impacts on the economy and financial markets generally or on us or our counterparties specifically;

a cyber-security incident, data breach or a failure of a key information technology system;

impact of reputational risk on such matters as business generation and retention;

other risks and uncertainties listed from time to time in the Company's reports and documents filed with the Securities and Exchange Commission; and

our success at managing the risks involved in the foregoing items.

Table of Contents

Any forward-looking statement speaks only as of the date on which it is made, and we undertake no obligation to update any forward-looking statement to reflect events or circumstances after the date on which the statement is made or to reflect the occurrence of unanticipated events or circumstances, except as required by applicable law.

PART I: FINANCIAL INFORMATION

Item 1. BUSINESS.

Summary

National Bank Holdings Corporation ("NBHC" or the "Company") is a bank holding company that was incorporated in the State of Delaware in 2009 and is headquartered immediately south of Denver, in Greenwood Village, Colorado. Our primary operations are conducted through our wholly owned subsidiary, NBH Bank, referred to as the "Bank", or "NBH Bank", through which we provide a variety of banking products to both commercial and consumer clients. We service our clients through a network of 104 banking centers as of December 31, 2018, with the majority of those banking centers located in Colorado and the greater Kansas City region, and through online and mobile banking products and services. As of December 31, 2018, we had \$5.7 billion in assets, \$4.1 billion in loans, \$4.5 billion in deposits and \$0.7 billion in shareholders' equity.

The Company was formed through a private offering of our common stock in 2009. As part of our goal of becoming a leading regional community bank holding company, we are pursuing a strategy of organic growth through strong banking relationships with small- and medium-sized businesses and consumers in our markets, complemented by selective acquisitions of financial institutions and other complementary businesses. Our long-term business model utilizes our organic development infrastructure, low-risk balance sheet, continuous operational development and a disciplined acquisition strategy to create value and provide attractive returns.

NBH Bank is a Colorado state-chartered bank and a member of the Federal Reserve Bank of Kansas City. Through NBH Bank, we operate under the following brand names: Bank Midwest in Kansas and Missouri; Community Banks of Colorado in Colorado; and Hillcrest Bank in New Mexico, Texas and Utah. We believe that conducting our banking operations under a single state charter streamlines our operations and enables us to more effectively and efficiently execute our growth strategy.

Our Acquisitions

We began banking operations in October 2010 and, as of December 31, 2018, we have completed six bank acquisitions, three of which were FDIC-assisted. All loss share agreements associated with the FDIC-assisted acquisitions were terminated in 2015. We have transformed these six banks into one collective banking operation with strong organic growth, prudent underwriting, and meaningful market share with continued opportunity for expansion. We believe that we have established critical mass in our current markets and have structured acquisitions that limit our credit risk, which positions us for attractive returns.

Table of Contents

The following table summarizes certain highlights of our six historic acquisitions, including deposits and assets at fair value as of each acquisition date:

| | Peoples | Pine River | Community Banks of Colorado | Bank of Choice | Bank Midwest |
|---------------------|-----------------|----------------|--------------------------------|----------------|-------------------------------|
| Date acquired | January 1, 2018 | August 1, 2015 | October 21, 2011 | July 22, 2011 | December 10, 2010 |
| FDIC-assisted | No | No | Yes | Yes | No |
| Loss share | No | No | Yes(1) | No | No |
| Banking centers(3) | 19 | 4 | 40 | 16 | 39 |
| Deposits (millions) | \$ 730 | \$ 130 | \$ 1,195 | \$ 760 | \$ 2,386 |
| Assets (millions) | \$ 875 | \$ 142 | \$ 1,228 | \$ 950 | \$ 2,426 |
| Primary Market | Colorado | Colorado | Colorado | Colorado | Greater Kansas City Region |

-
- (1) Commercial loss-share agreement (terminated November 5, 2015).
(2) Single Family loss-share agreement and Commercial Shared-Loss Agreement (terminated November 5, 2015).
(3) During 2013, four California banking centers acquired with the Community Banks of Colorado acquisition and 32 retirement centers acquired with the Hillcrest Bank acquisition were closed. During 2015, three banking centers were consolidated in our Bank Midwest network. During 2016, seven banking centers were consolidated in our Community Banks of Colorado network. During 2017, six banking centers were consolidated or sold in our Bank Midwest and Community Banks of Colorado networks. One banking center in our Bank Midwest network was consolidated during 2018.

Peoples Acquisition

On January 1, 2018, the Company closed the acquisition of Peoples, Inc. (“Peoples”), the bank holding company of Colorado-based Peoples National Bank and Kansas-based Peoples Bank. The acquisition strengthened the NBH franchise in the attractive and growing markets along the Colorado Front Range, the greater Kansas City region, including expanding our existing Overland Park, Kansas market and extending into the college town markets of Lawrence and Ottawa, Kansas, and expands the NBH franchise into New Mexico. The transaction was valued at \$146.4 million, including \$36.2 million of cash consideration, and at the date of acquisition added \$875.4 million in assets, \$542.7 million in loans held for investment and \$729.9 million of low cost deposits. Peoples’ complementary, franchise-centric, retail mortgage platform added significant capabilities with over \$1 billion in mortgage production and primarily serving NBH’s markets with additional mortgage offices in Arizona, California and Utah. The acquisition added a solid core deposit base, expanding into New Mexico, with cost of deposits significantly below peers at 0.10%. All operating systems were converted during the first half of 2018. Refer to note 4 – Acquisition Activities for additional details.

All of our acquisitions were accounted for under the acquisition method of accounting, and accordingly, all assets acquired and liabilities assumed were recorded at their respective acquisition date fair values and the fair value discounts/premiums on loans are being accreted over the lives of the loans.

Our Market Area

Our core markets are broadly defined as Colorado, the greater Kansas City region, New Mexico, Texas and Utah. In January 2019, the Company announced its expansion into Utah with a focus on serving commercial and business banking clients in Salt Lake City's Wasatch Front. We are the second largest banking center network among Colorado-based banks and the fifth largest banking center network in the greater Kansas City MSA among Missouri- and Kansas-based banks ranked by deposits as of June 30, 2018 (the last date as of which data are available), according to S&P Global. Other major MSAs in which we operate include Dallas-Fort Worth-Arlington, Texas, Austin-Round Rock, Texas, and Salt Lake City, Utah.

We believe that our established presence positions us well for growth opportunities in our markets. An integral component of our foundation and growth strategy has been to capitalize on market opportunities and acquire financial services franchises. Our primary focus has been on markets that we believe are characterized by some or all of the following: (i) attractive demographics with household income and population growth above the national average; (ii) concentration of business activity; (iii) high quality deposit bases; (iv) an advantageous competitive landscape that provides opportunity to achieve meaningful market presence; (v) consolidation opportunities as well as potential for add-on transactions; and (vi) markets sizeable enough to support our long-term organic growth objectives.

Table of Contents

The table below describes certain key demographic statistics regarding our markets:

| | Deposits (billions) | # of businesses (thousands) | Population (millions) | Unemployment rate(1) | Population growth(2) | Median household income | Top 3 competitor combined deposit market share |
|---------------------------------|------------------------|-----------------------------------|--------------------------|-------------------------|-------------------------|-------------------------------|--|
| Denver, CO | \$ 83.4 | 114.9 | 3.0 | 3.3% | 16.4% | \$ 78,251 | 55% |
| Front Range, CO(3) | 113.7 | 182.7 | 4.7 | 3.3% | 16.5% | 75,762 | 53% |
| Kansas City, MO-KS MSA | 57.4 | 76.0 | 2.2 | 2.7% | 7.4% | 66,838 | 43% |
| Austin, TX | 42.3 | 68.1 | 2.2 | 3.2% | 27.4% | 78,089 | 56% |
| Dallas, TX | 271.0 | 240.9 | 7.6 | 3.3% | 17.9% | 69,458 | 58% |
| Salt Lake City, UT | 38.2 | 43.2 | 1.2 | 2.7% | 12.9% | 74,919 | 72% |
| U.S. | | | | 3.5% | 6.6% | 63,174 | 55%(4) |

(1) Unemployment data is as of November 30, 2018.

(2) For the period 2010 through 2018.

(3) CO Front Range is a population weighted average of the following Colorado MSAs: Denver, Boulder, Colorado Springs, Fort Collins and Greeley.

(4) Based on U.S. Top 20 MSAs (determined by population).

Source: S&P Global as of December 31, 2018, except Deposits and Top 3 Competitor Combined Deposit Market Shares, which reflects data as of June 30, 2018.

Our Business Strategy

As part of our goal of becoming a leading regional community bank holding company, we seek to continue to generate strong organic growth, as well as pursue selective acquisitions of financial institutions and other complementary businesses. Our focus is on building organic growth through strong banking relationships with small- and medium-sized businesses and consumers in our primary markets, while maintaining a low-risk profile designed to

generate reliable income streams and attractive returns. We view our core market areas as Colorado, the greater Kansas City region, New Mexico, Texas and Utah. The key components of our strategic plan are:

- Focus on client-centered, relationship-driven banking strategy. Our small business and commercial bankers focus on small- and medium-sized businesses with an advisory approach that emphasizes understanding the client's business and offering a complete array of loan, deposit and treasury management products and services. Our business and commercial bankers are supported by treasury management teams in each of their markets, which allows us to more effectively deliver a comprehensive suite of products and services to our business clients and further deepen our banking relationships. Our consumer bankers focus on knowing their clients in order to best meet their financial needs, offering a full complement of loan, deposit, online and mobile banking solutions.
- Expansion of commercial banking, business banking and specialty businesses. We have made significant investments in our commercial relationship managers, as well as developed significant capabilities across our business banking and several specialty commercial banking offerings. Our strategy is to originate a high-quality loan portfolio that is diversified across industries and granular in loan size. We have preferred lender status with the Small Business Administration ("SBA") providing a leveraged platform for growth in the business lending segment. We believe we are well-positioned to leverage our operating and risk management infrastructure through organic growth, and we intend to continue to add or repurpose our commercial relationship managers to higher growth opportunities and markets in order to drive increased profitability.
- Expansion through organic growth and competitive product offerings. We believe that our focus on serving consumers and small- to medium-sized businesses, coupled with our competitive product offerings, will provide an expanded revenue base and new sources of fee income. We conduct regular market and competitive analysis to determine which products and services are best suited for our clients. Our teams also continue to pursue

Table of Contents

opportunities to deepen client relationships, which we believe will further increase our organic loan origination volumes and attract new transaction accounts that offer lower cost of funds and higher fee generating activity.

- Continue to strengthen profitability through organic growth and operating efficiencies. We continue to utilize our comprehensive underwriting and risk management processes under one operating platform while maintaining local branding, leadership and decision making, which allows us to support growth and realize operating efficiencies throughout our enterprise. We believe that we have the infrastructure in place to support our future revenue growth without causing non-interest expenses to increase by a corresponding amount. Our growth strategy is focused on organic initiatives in order to accelerate our growth in profitability. Key priorities to strengthen profitability include the continued ramp-up of loan production, growing low-cost core deposits, implementing additional fee-based business initiatives and further enhancing operational efficiencies.
- Maintain conservative risk profile and sound risk management practices. Strong risk management is an important element of our operating philosophy. We maintain a conservative risk culture with adherence to mature and seasoned policies across all areas of the organization. We implement self-imposed concentration limits on our loan portfolio to ensure a granular and diverse loan portfolio and protect against downside risk to any particular industry or real estate sector. Our risk management approach seeks to identify, assess and mitigate risk and minimize any resulting losses. We have implemented processes to identify, measure, monitor, report and analyze the types of risk to which we are subject. We believe our risk management policies establish appropriate limitations that allow for the prudent oversight of such risks that include, but are not limited to the following: credit, liquidity, market, operational, legal and compliance, reputational, and strategic and business risk.
- Pursue disciplined acquisitions or other expansionary opportunities. We expect that acquisitions or other expansionary opportunities will continue to be a component of our growth strategy, and we intend to carefully select opportunities that we believe have stable core franchises, have significant local market share or will add asset generation capabilities or fee income streams while structuring the opportunities to limit risk. Further, we seek transactions that offer opportunities for clear financial benefits with valuations that have acceptable levels of earnings accretion, tangible book value dilution/earn-back, and internal rates of return. We seek to acquire or expand into financial services franchises in markets that exhibit attractive demographic attributes and business growth trends, and we believe that our focus on attractive markets will provide long-term opportunities for organic growth. Our focus is on our primary markets of Colorado, the greater Kansas City region, New Mexico, Texas and Utah, including teams, asset portfolios, specialty commercial finance businesses, and whole banks.

We believe our strategy of strong organic growth through the retention, expansion and development of client-centered relationships and growth through selective acquisitions or other expansionary opportunities in attractive markets provides flexibility regardless of economic conditions. Our established platform for assessing, executing and integrating acquisitions creates opportunities in an economic downturn, and our attractive market factors, franchise scale in our targeted markets and our relationship-centered banking focus create opportunities in an improving economic environment.

Products and Services

Through NBH Bank, our primary business is to offer a full range of traditional banking products and financial services to our commercial, business and consumer clients, who are predominantly located in Colorado, the greater Kansas City region, New Mexico, Texas and Utah. We conduct our banking business through 104 banking centers, with 50 of those located in Colorado, 46 in Kansas and Missouri, six in New Mexico and two in Texas as of December 31, 2018. Our distribution network also includes 128 ATMs as well as fully integrated online banking and mobile banking services. We offer a high level of personalized service to our clients through our relationship managers and banking center associates. We believe that a banking relationship that includes multiple services, such as loan and deposit services, online and mobile banking solutions and treasury management products and services, is the key to profitable and long-lasting client relationships and that our local focus and decision making provide us with a competitive advantage over banks that do not have these attributes.

Our primary strategic objective is to serve small- to medium-sized businesses in our markets with a variety of unique and useful services, including a full array of banking products, while maintaining a strong and disciplined credit culture and delivering excellent client service. We offer a variety of products and services that are focused on the following areas:

Table of Contents

Commercial and Specialty Banking

Our commercial bankers focus on small- and medium-sized businesses with an advisory approach that emphasizes understanding the client's business and offering a complete suite of loan, deposit and treasury management products and services. We have invested significantly in our commercial banking capabilities, attracting experienced commercial bankers from competing institutions in our markets, which have resulted in significant growth in our originated loan portfolio. Our commercial relationship managers offer a wide range of commercial loan products, including:

Commercial and Industrial Loans—We originate commercial and industrial loans and leases, including working capital loans, equipment loans, lender finance loans, food and agriculture loans, government and non-profit loans, owner occupied commercial real estate loans and other commercial loans and leases. The terms of these loans vary by purpose and by type of underlying collateral, if any.

Working capital loans generally have terms of up to one year, are usually secured by accounts receivable and inventory and carry the personal guarantees of the principals of the business. Equipment loans are generally secured by the financed equipment at advance rates that we believe are appropriate for the equipment type. In the case of owner-occupied commercial real estate loans, we are usually the primary provider of financial services for the company and/or the principals and the primary source of repayment is through the cash flows generated by the borrowers' business operations. Owner-occupied commercial real estate loans are typically secured by a first lien mortgage on real property plus assignments of all leases related to the properties. Underwriting guidelines generally require borrowers to contribute cash equity that results in an 80% or less loan-to-value ratio on owner-occupied properties. As of December 31, 2018, substantially all of our commercial and industrial loans were secured.

Non-Owner Occupied Commercial Real Estate Loans—Non-owner occupied commercial real estate loans ("CRE") consist of loans to finance the purchase of commercial real estate and development loans. Our non-owner occupied CRE loans include commercial properties such as office buildings, warehouse/distribution buildings, multi-family and retail buildings. These loans are typically secured by a first lien mortgage or deed of trust, as well as assignments of all related leases. Underwriting guidelines generally require borrowers to contribute cash equity that results in a 75% or less loan to value ratio.

We seek to reduce the risks associated with commercial mortgage lending by focusing our lending in our primary markets. Although non-owner occupied CRE is not a primary focus of our lending strategy, we have developed teams of dedicated CRE bankers in each of our markets who possess the depth and breadth of both market knowledge and industry expertise, which serves to further mitigate risk of this product type.

Small Business Administration Loans—We offer a range of U.S. Small Business Administration, or SBA loans, to support manufacturers, distributors and service providers targeted to small businesses and entrepreneurs seeking growth capital, working capital, or other capital investments. As a Preferred Lender Provider of the SBA, we are able to expedite SBA loan approval, closing, and servicing functions through delegated authority to underwrite and approve loans on behalf of the SBA. We utilize the SBA 7(a) loan, SBA 504 loan, SBA Express loan, and CAP Line loan programs.

Commercial Deposit Products (including business online and mobile banking)—Our commercial bankers are focused on providing value-added deposit products to our clients that optimize their cash management program. We are focused on full-relationship banking, including banking core operating accounts and ancillary accounts. We also provide our commercial clients with money market accounts and short-term repurchase reserve accounts depending on their individual needs. In addition, we provide a wide array of treasury management solutions to our clients, including: business online and mobile banking, commercial credit card services, wire transfers, automated clearing house services, electronic bill payment, lock box services, remote deposit capture services, merchant processing services, cash vault, controlled disbursements, fraud prevention services through positive pay and other auxiliary services (including account reconciliation, collections, repurchase accounts, zero balance accounts and sweep accounts).

Table of Contents

Business, Residential and Consumer Banking

Our business and consumer bankers focus on knowing their clients in order to best meet their financial needs, offering a full complement of loan, deposit and online and mobile banking solutions. We strive to do business in the areas served by our banking centers, which is also where our marketing is focused, and the vast majority of our new loan and deposit clients are located in existing market areas.

All of our newly originated consumer loans are on a direct to consumer basis. We offer a variety of business and consumer loans, including:

Business Loans—Business loans consist of term loans, line of credit, and real estate secured loans. The terms of these loans vary by purpose and by type of underlying collateral, if any. Business loans generally require LTV ratios of not more than 75 percent. Business loans also assist in the growth of our deposits because many business loan borrowers establish noninterest-bearing and interest-bearing demand deposit accounts and treasury management relationships with us. Those deposit accounts help us to reduce our overall cost of funds, and those treasury management relationships provide us with a source of non-interest income.

Residential Real Estate Loans—Residential real estate loans consist of loans secured by the primary or secondary residence of the borrower. These loans consist of closed loans, which are typically amortizing over a 10 to 30-year term. Our loan-to-value (LTV) benchmark for these loans will generally be below 80% at inception unless related to certain internal or government programs where higher LTV's may be warranted, along with satisfactory debt-to-income ratios. We do not originate or purchase negatively amortizing or sub-prime residential loans. These residential real estate loans are generally originated under terms and conditions consistent with secondary market guidelines. Some of these loans will be placed in the Bank's loan portfolio; however, a majority are sold in the secondary market and provide a significant source of fee income. The mortgage operation acquired from Peoples added significant residential banking products, servicing capabilities and residential loan origination channels. In addition to the referral business through our existing consumer client base, we have a dedicated team of mortgage bankers who focus origination efforts primarily on new purchase activity and secondarily on refinance activity. We also offer open- and closed-ended home equity loans, which are loans generally secured by second lien positions on residential real estate, and residential construction loans to consumers and builders for the construction of residential real estate.

Consumer Loans—Consumer loans are structured as small personal lines of credit and term loans, with the latter generally bearing interest at a higher rate and having a shorter term than residential mortgage loans. Consumer loans are both secured (for example by deposit accounts, brokerage accounts or automobiles) and unsecured and carry either a fixed rate or variable rate. Examples of our consumer loans include home improvement loans not secured by real estate, new and used automobile loans and personal lines of credit.

Deposit Products (including online and mobile banking)—We offer a variety of deposit products to our clients, including checking accounts, savings accounts, money market accounts, health savings accounts and other deposit accounts, including fixed-rate, fixed maturity time deposits ranging in terms from 30 days to five years, and individual retirement accounts. We view deposits as an important part of the overall client relationship and believe they provide opportunities to cross-sell other products and services. We intend to continue our efforts to attract low-cost transaction deposits from our client relationships. Consumer deposit flows are significantly influenced by general and local economic conditions, changes in prevailing interest rates, internal pricing decisions and competition. Our deposits are primarily obtained from areas surrounding our banking centers. In order to attract and retain deposits, we rely on providing competitively priced high-quality service and introducing new products and services that meet our clients' needs.

We also offer comprehensive, user-friendly mobile and online banking platforms allowing our clients to pay bills, check statements, deposit checks and transfer funds, amongst other features, online or on-the-go.

Table of Contents

Lending Activities

Our loan portfolio includes commercial and industrial loans, commercial real estate loans, residential real estate loans, business loans and consumer loans. The principal risk associated with each category of loans we make is the creditworthiness of the borrower. Borrower creditworthiness is affected by general economic conditions and the attributes of the borrower's market or industry segment. Attributes of the relevant business market or industry segment include the economic and competitive environment, changes to supply or demand, threat of substitutes and barriers to entry and exit. In our credit underwriting process, we carefully evaluate the borrower's industry, operating performance, liquidity and financial condition. We underwrite credits based on multiple repayment sources, including operating cash flow, liquidation of collateral and guarantor support, where appropriate. We closely monitor the operating performance, liquidity and financial condition of borrowers through analysis of periodic financial statements and meetings with the borrower's management. As part of our credit underwriting process, we also review the borrower's total debt obligations on a global basis. Our credit policy requires that key risks be identified and measured, documented and mitigated, to the extent possible, to seek to ensure the soundness of our loan portfolio.

Our credit policy also provides detailed procedures for making loans to individual and business clients along with the regulatory requirements to ensure that all loan applications are evaluated subject to our fair lending policy. Our credit policy addresses the common credit standards for making loans to clients, the credit analysis and financial statement requirements, the collateral requirements, including insurance coverage where appropriate, as well as the documentation required. Our ability to analyze a borrower's current financial health and credit history, as well as the value of collateral as a secondary source of repayment, when applicable, are significant factors in determining the creditworthiness of loans to clients. We require various levels of internal approvals based on the characteristics of such loans, including the size, nature of the exposure and type of collateral, if any. We believe that the procedures required by our credit policies enhance internal responsibility and accountability for underwriting decisions and permit us to monitor the performance of credit decision-making. An integral element of our credit risk management strategy is the establishment and adherence to concentration limits for our portfolio. We have established concentration limits that apply to our portfolio based on product types such as commercial real estate, consumer lending, and various categories of commercial and industrial lending. For more detail on our credit policies, see "Management's Discussion and Analysis of Financial Condition and Results of Operations-Financial Condition-Asset Quality."

Competition

The banking landscape in our primary markets of Colorado, Kansas, Missouri, New Mexico, Texas and Utah is highly competitive and quite fragmented, with many small banks having limited market share while the large out-of-state national and super-regional banks control the majority of deposits and profitable banking relationships. We compete actively with national, regional and local financial services providers, including: banks, thrifts, credit unions, mortgage companies, finance companies and financial technology ("FinTech") companies.

Competition among providers of financial products and services continues to increase, with consumers having the opportunity to select from a variety of traditional brick and mortar banks and nontraditional alternatives, such as online banks and FinTech companies. Competition among providers is based on many factors. The primary factors driving commercial and consumer competition for loans and deposits are interest rates, the fees charged, client service levels and the range of products and services offered. In addition, other competitive factors include the location and hours of our banking centers, the client service orientation of our associates and the availability of digital banking products and services. We believe the most important of these competitive factors that determine our success are our consumer bankers' focus on knowing their individual clients in order to best meet their financial needs and our business and commercial bankers' focus on small- and medium-sized businesses with an advisory approach that emphasizes understanding the client's business and offering a complete array of loan, deposit and treasury management products and services through our banking centers and our digital banking platform.

We recognize that there are banks and other financial services companies with which we compete that have greater financial resources, access to more capital and higher lending capacity and offer a wider range of deposit and lending instruments. However, given our existing capital base, we expect to be able to meet the majority of small- to medium-sized business and consumer credit and depository service needs.

Table of Contents

Associates

At December 31, 2018, we had 1,252 full-time associates and 80 part-time associates.

SUPERVISION AND REGULATION

The U.S. banking industry is highly regulated under federal and state law. Banking laws, regulations, and policies affect the operations of the Company and its subsidiary. Investors should understand that the primary objective of the U.S. bank regulatory regime is the protection of depositors, the Depositors Insurance Fund (“DIF”), and the banking system as a whole, not the protection of the Company’s shareholders.

As a bank holding company, we are subject to inspection, examination, supervision and regulation by the Board of Governors of the Federal Reserve System (the “Federal Reserve”). Our bank subsidiary, NBH Bank, is a Colorado state-chartered bank and a member of the Federal Reserve Bank of Kansas City. As such, NBH Bank is subject to examination, supervision and regulation by both the Colorado Division of Banking and the Federal Reserve. In addition, we expect that any additional businesses that we may invest in or acquire will be regulated by various state and/or federal banking regulators.

Banking statutes and regulations are subject to continual review and revision by Congress, state legislatures and federal and state regulatory agencies. A change in such statutes or regulations, including changes in how they are interpreted or implemented, could have a material effect on our business. In addition to laws and regulations, state and federal bank regulatory agencies may issue policy statements, interpretive letters and similar written guidance pursuant to such laws and regulations, which are binding on us and our subsidiaries.

Banking statutes, regulations and policies could restrict our ability to diversify into other areas of financial services, acquire depository institutions and make distributions or pay dividends on our equity securities. They may also require us to provide financial support to any bank that we control, maintain capital balances in excess of those desired by management and pay higher deposit insurance premiums as a result of a general deterioration in the financial condition of NBH Bank or other depository institutions we control.

The description below summarizes certain elements of the applicable bank regulatory framework. This description is not intended to describe all laws and regulations applicable to us and our subsidiaries. The description is qualified in its entirety by reference to the full text of the statutes, regulations, policies, interpretive letters and other written

guidance that are described.

National Bank Holdings Corporation as a Bank Holding Company

As a bank holding company, we are subject to regulation under the Bank Holding Company Act (“BHCA”) and to supervision, examination, and enforcement by the Federal Reserve. Federal Reserve jurisdiction also extends to any company that we may directly or indirectly control, such as non-bank subsidiaries and other companies in which we have a controlling interest. While subjecting us to supervision and regulation, we believe that our status as a bank holding company (as opposed to being a non-controlling investor) broadens the investment opportunities available to us among public and private financial institutions.

The BHCA generally prohibits a bank holding company from engaging, directly or indirectly, in activities other than banking or managing or controlling banks, except for activities determined by the Federal Reserve to be so closely related to banking or managing or controlling banks as to be a proper incident thereto. Provisions of the Gramm-Leach-Bliley Financial Modernization Act of 1999 (the “GLB Act”) expanded the permissible activities of a bank holding company that qualifies as a financial holding company. Under the regulations implementing the GLB Act, a financial holding company may engage in additional activities that are financial in nature or incidental or complementary to financial activity. Those activities include, among other activities, certain insurance and securities activities. We have not yet determined whether it would be appropriate or advisable in the future to become a financial holding company.

Table of Contents

NBH Bank as a Colorado State-Chartered Bank

On December 31, 2015, our bank subsidiary, NBH Bank, N.A., converted to a Colorado state-chartered bank operating under the name of NBH Bank. NBH Bank is also a member of the Federal Reserve Bank of Kansas City. As such, NBH Bank is subject to examination, supervision and regulation by both the Colorado Division of Banking and the Federal Reserve. NBH Bank's deposits are insured by the Federal Deposit Insurance Corporation ("FDIC") through the DIF, in the manner and to the extent provided by law. As an insured bank, NBH Bank is subject to the provisions of the Federal Deposit Insurance Act, as amended (the "FDI Act"), and the FDIC's implementing regulations thereunder, and may also be subject to supervision and examination by the FDIC under certain circumstances.

Under the FDIC Improvement Act of 1991 ("FDICIA"), NBH Bank must submit financial statements prepared in accordance with GAAP and management reports signed by the Company's and NBH Bank's chief executive officer and chief accounting or financial officer concerning management's responsibility for the financial statements, an assessment of internal controls, and an assessment of NBH Bank's compliance with various banking laws and FDIC and other banking regulations. In addition, we must submit annual audit reports to federal regulators prepared by independent auditors. As allowed by regulations, we may use our audit report prepared for the Company to satisfy this requirement. We must provide our auditors with examination reports, supervisory agreements and reports of enforcement actions. The auditors must also attest to and report on the statements of management relating to the internal controls. FDICIA also requires that NBH Bank form an independent audit committee consisting of outside directors only, or that the Company's audit committee be entirely independent.

Broad Supervision, Examination and Enforcement Powers

The Federal Reserve, the FDIC and state bank regulators have broad regulatory, examination and enforcement authority over bank holding companies and banks, as applicable. Bank regulators regularly examine the operations of banks and bank holding companies. In addition, banks and bank holding companies are subject to periodic reporting and filing requirements.

Bank regulators have various remedies available if they determine that a banking organization has violated any law or regulation, that the financial condition, capital resources, asset quality, earnings prospects, management, liquidity or other aspects of a banking organization's operations are unsatisfactory, or that the banking organization is operating in an unsafe or unsound manner. The bank regulators have the power to, among other things: enjoin "unsafe or unsound" practices, require affirmative actions to correct any violation or practice, issue administrative orders that can be judicially enforced, direct increases in capital, direct the sale of subsidiaries or other assets, limit dividends and distributions, restrict growth, assess civil monetary penalties, remove officers and directors, terminate deposit insurance, and appoint a conservator or receiver.

Engaging in unsafe or unsound practices or failing to comply with applicable laws, regulations and supervisory agreements could subject the Company, its subsidiaries and their respective officers, directors and institution-affiliated parties to the remedies described above and other sanctions. In addition, the FDIC could terminate NBH Bank's deposit insurance if it determined that the Bank's financial condition was unsafe or unsound or that the bank engaged in unsafe or unsound practices or violated an applicable rule, regulation, order or condition enacted or imposed by the bank's regulators.

Regulatory Capital Requirements

In General

As a bank holding company, we are subject to regulatory capital adequacy requirements implemented by the Federal Reserve. The federal banking agencies have risk-based capital adequacy guidelines intended to provide a measure of capital adequacy that reflects the degree of risk associated with a banking organization's operations. NBH Bank also is, and other depository institution subsidiaries that we may acquire or control in the future will be, subject to capital adequacy guidelines as implemented by the relevant federal banking agency. In the case of the Company and NBH Bank, applicable capital guidelines can be found in the Federal Reserve's Regulations H and Q.

The capital rules require banks and bank holding companies to maintain a minimum common equity tier 1 capital ratio of 4.5%, a total tier 1 capital ratio of 6%, a total capital ratio of 8%, and a leverage ratio of 4%. Effective as of January 1, 2019,

Table of Contents

bank holding companies are required to hold a capital conservation buffer of common equity tier 1 capital of 2.5% to avoid limitations on capital distributions and executive compensation payments.

Further, the federal bank regulatory agencies may, however, set higher capital requirements for an individual bank or when a bank's particular circumstances warrant. At this time, the bank regulatory agencies are more inclined to impose higher capital requirements in order to be considered well-capitalized, and future regulatory change could impose higher capital standards as a routine matter.

The Federal Reserve may also set higher capital requirements for holding companies whose circumstances warrant it. For example, holding companies experiencing internal growth or making acquisitions are expected to maintain strong capital positions substantially above the minimum supervisory levels, without significant reliance on intangible assets.

Prompt Corrective Action

The FDI Act requires federal bank regulatory agencies to take "prompt corrective action" with respect to FDIC-insured depository institutions that do not meet minimum capital requirements. A depository institution's treatment for purposes of the prompt corrective action provisions will depend upon how its capital levels compare to various capital measures and certain other factors, as established by regulation. Federal banking regulators are required to take various mandatory supervisory actions and are authorized to take other discretionary actions with respect to institutions in the three undercapitalized categories. The severity of the action depends upon the capital category in which the institution is placed. Generally, subject to a narrow exception, the banking regulator must appoint a receiver or conservator for an institution that is critically undercapitalized. Our regulatory capital ratios and those of NBH Bank are in excess of the levels established for "well-capitalized" institutions.

Bank Holding Companies as a Source of Strength

The Federal Reserve requires that a bank holding company serve as a source of financial and managerial strength to each bank that it controls and, under appropriate circumstances, commit resources to support each such controlled bank. This support may be required at times when the bank holding company may not have the resources to provide the support. Because we are a bank holding company, the Federal Reserve views the Company (and its consolidated assets) as a source of financial and managerial strength for any controlled depository institutions.

Under the prompt corrective action provisions, if a controlled bank is undercapitalized, then the regulators could require its bank holding company to guarantee a capital restoration plan. In addition, if the Federal Reserve believes that a bank holding company's activities, assets or affiliates represent a significant risk to the financial safety,

soundness or stability of a controlled bank, then the Federal Reserve could require the bank holding company to terminate the activities, liquidate the assets or divest the affiliates. The regulators may require these and other actions in support of controlled banks even if such action is not in the best interests of the bank holding company or its shareholders.

The Dodd-Frank Act codified the requirement that holding companies, like the Company, serve as a source of financial strength for their subsidiary depository institutions, by providing financial assistance to its insured depository institution subsidiaries in the event of financial distress. Under the source of strength doctrine, the Company could be required to provide financial assistance to NBH Bank should it experience financial distress.

In addition, capital loans by us to NBH Bank will be subordinate in right of payment to deposits and certain other indebtedness of NBH Bank. In the event of our bankruptcy, any commitment by us to a federal bank regulatory agency to maintain the capital of NBH Bank will be assumed by the bankruptcy trustee and entitled to a priority of payment.

Table of Contents

Dividend Restrictions

The Company is a legal entity separate and distinct from its subsidiaries. Because the Company's consolidated net income consists largely of the net income of NBH Bank, the Company's ability to pay dividends depends upon its receipt of dividends from its subsidiary. The ability of a bank to pay dividends and make other distributions is limited by federal and state law. The specific limits depend on a number of factors, including the bank's type of charter, recent earnings, recent dividends, level of capital and regulatory status. As a member of the Federal Reserve System and a Colorado state-chartered bank, NBH Bank is subject to Regulation H and limitations under Colorado law with respect to the payment of dividends. Non-bank subsidiaries are also limited by certain federal and state statutory provisions and regulations covering the amount of dividends that may be paid in any given year.

The ability of a bank holding company to pay dividends and make other distributions can also be limited. The Federal Reserve has authority to prohibit a bank holding company from paying dividends or making other distributions. A bank holding company should not pay cash dividends that exceed its net income or that can only be funded in ways that weaken the bank holding company's financial health, such as by borrowing. In addition, as a Delaware corporation, the Company is subject to certain limitations and restrictions under Delaware corporate law with respect to the payment of dividends and other distributions.

Depositor Preference

The FDI Act provides that, in the event of the "liquidation or other resolution" of an insured depository institution, the claims of depositors of the institution (including the claims of the FDIC as subrogee of insured depositors) and certain claims for administrative expenses of the FDIC as a receiver will have priority over other general unsecured claims against the institution. If our insured depository institution fails, insured and uninsured depositors, along with the FDIC, will have priority in payment ahead of unsecured, nondeposit creditors, including us, with respect to any extensions of credit they have made to such insured depository institution.

Limits on Transactions with Affiliates

Federal law restricts the amount and the terms of both credit and non-credit transactions (generally referred to as "Covered Transactions") between a bank and its non-bank affiliates. Covered Transactions with any single affiliate may not exceed 10% of the capital stock and surplus of the bank, and Covered Transactions with all affiliates may not exceed, in the aggregate, 20% of the bank's capital and surplus. For a bank, capital stock and surplus refers to the bank's tier 1 and tier 2 capital, as calculated under the risk-based capital guidelines, plus the balance of the allowance for credit losses excluded from tier 2 capital. The bank's transactions with all of its affiliates in the aggregate are limited to 20% of the foregoing capital. In addition, in connection with Covered Transactions that are extensions of credit, the bank may be required to hold collateral to provide added security to the bank, and the types of permissible

collateral may be limited. The Dodd-Frank Act generally enhances the restrictions on transactions with affiliates, including an expansion of what types of transactions are Covered Transactions to include credit exposures related to derivatives, repurchase agreements and securities lending arrangements and an increase in the amount of time for which collateral requirements regarding Covered Transactions must be satisfied. As of December 31, 2018, the Company did not have any outstanding Covered Transactions.

Regulatory Notice and Approval Requirements for Acquisitions of Control

We must generally receive federal bank regulatory approval before we can acquire an institution or business. Specifically, as a bank holding company, we must obtain prior approval of the Federal Reserve in connection with any acquisition that would result in the Company owning or controlling 5% or more of any class of voting securities of a bank or another bank holding company. Our ability to make investments in depository institutions will depend on our ability to obtain approval for such investments from the Federal Reserve. The Federal Reserve could deny our application based on the above criteria or other considerations. For example, we could be required to sell banking centers as a condition to receiving regulatory approval, which condition may not be acceptable to us or, if acceptable to us, may reduce the benefit of any acquisition.

Federal and state laws, including the BHCA and the Change in Bank Control Act, impose additional prior notice or approval requirements and ongoing regulatory requirements on any investor that seeks to acquire direct or indirect “control” of an

Table of Contents

FDIC-insured depository institution or bank holding company. Whether an investor “controls” a depository institution is based on all of the facts and circumstances surrounding the investment. As a general matter, an investor is deemed to control a depository institution or other company if the investor owns or controls 25% or more of any class of voting securities. Subject to rebuttal, an investor is presumed to control a depository institution or other company if the investor owns or controls 10% or more of any class of voting securities and either the depository institution or company is a public company or no other person will hold a greater percentage of that class of voting securities after the acquisition. If an investor’s ownership of our voting securities were to exceed certain thresholds, the investor could be deemed to “control” us for regulatory purposes. This could subject the investor to regulatory filings or other regulatory consequences.

Anti-Money Laundering Requirements

Under federal law, including the Bank Secrecy Act and the Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act of 2001 (the “USA PATRIOT Act”), certain types of financial institutions, including insured depository institutions, must maintain anti-money laundering programs that include established internal policies, procedures and controls; a designated compliance officer; an ongoing associate training program; and testing of the program by an independent audit function. Financial institutions are prohibited from entering into specified financial transactions and account relationships and must meet enhanced standards for due diligence, client identification, and recordkeeping, including in their dealings with non-U.S. financial institutions and non-U.S. clients. Financial institutions must take reasonable steps to conduct enhanced scrutiny of account relationships to guard against money laundering and to report any suspicious information maintained by financial institutions. Bank regulators routinely examine institutions for compliance with these obligations, and they must consider an institution’s anti-money laundering compliance when considering regulatory applications filed by the institution, including applications for banking mergers and acquisitions. The regulatory authorities have imposed “cease and desist” orders and civil money penalty sanctions against institutions found to be violating these obligations.

Consumer Laws and Regulations

Banks and other financial institutions are subject to numerous laws and regulations intended to protect consumers in their transactions with banks. These laws include, among others, laws regarding unfair and deceptive acts and practices and usury laws, as well as the following consumer protection statutes: Truth in Lending Act, Truth in Savings Act, Electronic Funds Transfer Act, Flood Disaster Protection Act, Expedited Funds Availability Act, Equal Credit Opportunity Act, Fair and Accurate Credit Transactions Act, Fair Housing Act, Fair Credit Reporting Act, Fair Debt Collection Act, GLB Act, Home Mortgage Disclosure Act, Right to Financial Privacy Act and Real Estate Settlement Procedures Act.

Many states and local jurisdictions have consumer protection laws analogous, and in addition, to those listed above. These state and local laws regulate the manner in which financial institutions deal with clients when taking deposits, making loans or conducting other types of transactions.

The Consumer Financial Protection Bureau (the “CFPB”) has broad rulemaking authority for a wide range of consumer financial laws that apply to all banks. The CFPB is authorized to issue rules for both bank and nonbank companies that offer consumer financial products and services, subject to consultation with the prudential banking regulators. In general, however, banks with assets of \$10 billion or less, such as NBH Bank, will continue to be examined for consumer compliance by their primary bank regulator.

Much of the CFPB’s rulemaking has focused on mortgage lending and servicing, including an important rule requiring lenders to ensure that prospective buyers have the ability to repay their mortgages. Other areas of current CFPB focus include consumer protections for prepaid cards, payday lending, debt collection, overdraft services and privacy notices. The CFPB has been particularly active in issuing rules and guidelines concerning residential mortgage lending and servicing, issuing numerous rules and guidance related to residential mortgages. Perhaps the most significant of these guidelines are the “Ability-to-Repay and Qualified Mortgage Standards under the Truth in Lending Act” portions of Regulation Z and the Know Before You Owe guidelines. Under the Dodd-Frank Act, creditors must make a reasonable and good faith determination, based on verified and documented information, that the consumer has a reasonable “ability to repay” a residential mortgage according to its terms as well as clearly and concisely disclose the terms and costs associated with these loans.

Table of Contents

The CFPB has actively issued enforcement actions against both large and small entities and to entities across the entire financial services industry. The CFPB has relied upon “unfair, deceptive, or abusive acts” prohibitions as its primary enforcement tool. However, the CFPB and DOJ continue to be focused on fair lending in taking enforcement actions against banks with renewed emphasis on alleged redlining practices. Failure to comply with these laws and regulations could give rise to regulatory sanctions, client rescission rights, actions by state and local attorneys general and civil or criminal liability.

The Community Reinvestment Act

The Community Reinvestment Act (“CRA”) is intended to encourage banks to help meet the credit needs of their entire communities, including low- and moderate-income neighborhoods, consistent with safe and sound operations. The regulators examine banks and assign each bank a public CRA rating. The CRA then requires bank regulators to take into account the bank’s record in meeting the needs of its community when considering certain applications by a bank, including applications to establish a banking center or to conduct certain mergers or acquisitions. The Federal Reserve is required to consider the CRA records of a bank holding company’s controlled banks when considering an application by the bank holding company to acquire a bank or to merge with another bank holding company.

When we apply for regulatory approval to make certain investments, the regulators will consider the CRA record of the target institution and our depository institution subsidiary. An unsatisfactory CRA record could substantially delay approval or result in denial of an application.

Reserve Requirements

Pursuant to regulations of the Federal Reserve, all banks are required to maintain average daily reserves at mandated ratios against their transaction accounts. In addition, reserves must be maintained on certain non-personal time deposits. These reserves must be maintained in the form of vault cash or in an account at a Federal Reserve Bank.

Deposit Insurance Assessments

All of a depositor’s accounts at an insured bank, including all non-interest bearing transaction accounts, are insured by the FDIC up to \$250,000. FDIC-insured banks are required to pay deposit insurance premiums to the FDIC. The FDIC has adopted a risk-based assessment system whereby FDIC-insured depository institutions pay insurance premiums at rates based on their risk classification. An institution’s risk classification is assigned based on its capital levels and the

level of supervisory concern the institution poses to the regulators.

Assessments are based on an institution's average total consolidated assets less average tangible equity (subject to risk-based adjustments that would further reduce the assessment base for custodial banks). NBH Bank may be able to pass part or all of this cost on to its clients, including in the form of lower interest rates on deposits, or fees to some depositors, depending on market conditions.

The FDIC may terminate a depository institution's deposit insurance upon a finding that the institution's financial condition is unsafe or unsound or that the institution has engaged in unsafe or unsound practices or has violated any applicable rule, regulation, order or condition enacted or imposed by the institution's regulatory agency. If deposit insurance for a banking business we invest in or acquire were to be terminated, that would have a material adverse effect on that banking business and potentially on the Company as a whole.

Interstate Banking

Under the Riegle-Neal Interstate Banking and Branching Efficiency Act (the "Riegle-Neal Act"), a bank holding company may acquire banks in states other than its home state, subject to any state requirement that the bank has been organized and operating for a minimum period of time, not to exceed five years, and the requirement that the bank holding company not control, prior to or following the proposed acquisition, more than 10% of the total amount of deposits of insured depository institutions nationwide or, unless the acquisition is the bank holding company's initial entry into the state, more than 30% of such deposits in the state (or such lesser or greater amount set by the state). Bank holding companies must be well capitalized

Table of Contents

and well managed, not merely adequately capitalized and adequately managed, in order to acquire a bank located outside of the bank holding company's home state.

The Riegle-Neal Act also authorizes banks to merge across state lines, thereby creating interstate banking centers. A national or state bank, with the approval of its regulator, may open a de novo banking center in any state if the law of the state in which the banking center is proposed would permit the establishment of the banking center if the bank were a bank chartered in that state.

The Federal Reserve, the Office of the Comptroller of the Currency ("OCC"), and FDIC jointly issued a final rule, effective October 10, 1977, that adopted uniform regulations implementing Section 109 of the Riegle-Neal Act. Section 109 prohibits any bank from establishing or acquiring a branch or branches outside of its home state primarily for the purpose of deposit production. Congress enacted Section 109 to ensure that interstate branches would not take deposits from a community without the bank reasonably helping to meet the credit needs of that community.

Changes in Laws, Regulations or Policies

Congress and state legislatures may introduce from time to time measures or take actions that would modify the regulation of banks or bank holding companies. In addition, federal and state regulatory agencies also periodically propose and adopt changes to their regulations or change the manner in which existing regulations are applied. Such changes could increase or decrease the cost of doing business, limit or expand permissible activities or affect the competitive balance among banks and other financial institutions, all of which could affect our investment opportunities and our assessment of how attractive such opportunities may be. We cannot predict whether potential legislation will be enacted and, if enacted, the effect that it or any implementing regulations would have on our business, results of operations, liquidity or financial condition.

2018 Regulatory Reform

In May 2018, the Economic Growth, Regulatory Relief and Consumer Protection Act ("EGRRCPA"), was enacted to modify or remove certain financial reform rules and regulations, including some of those implemented under the Dodd-Frank Act. While EGRRCPA maintains most of the regulatory structure established by the Dodd-Frank Act, it amends certain aspects of the regulatory framework for small depository institutions with assets of less than \$10 billion and for large banks with assets of more than \$50 billion. Many of these changes could result in meaningful regulatory changes for community banks such as NBH Bank, and their holding companies.

EGRRCPA, among other matters, expands the definition of qualified mortgages which may be held by a financial institution and simplifies the regulatory capital rules for financial institutions and their holding companies with total consolidated assets of less than \$10 billion by instructing the federal banking regulators to establish a single “Community Bank Leverage Ratio” of between 8 and 10 percent (currently proposed at 9 percent). Any qualifying depository institution or its holding company that exceeds the “community bank leverage ratio” will be considered to have met generally applicable leverage and risk-based regulatory capital requirements and any qualifying depository institution that exceeds the new ratio will be considered to be “well capitalized” under the prompt corrective action rules. A major effect of this change is to exclude such holding companies from the minimum capital requirements of the Dodd-Frank Act. In addition, EGRRCPA includes regulatory relief for community banks regarding the Volcker Rule (proprietary trading prohibitions), mortgage disclosures and risk weights for certain high-risk commercial real estate loans.

The OCC, the Federal Reserve Board and the FDIC also adopted a rule providing banking organizations with the option to phase in over a three-year period the day-one regulatory capital impact that may result from the adoption of ASU 2016-13,

Table of Contents

Measurement of Credit Losses on Financial Instruments, the new current expected credit loss methodology accounting under U. S. GAAP. See further discussion of ASU 2016-13 in note 3.

It is difficult at this time to predict when or how any new standards under EGRRCPA or other recent rules will ultimately be applied to us or what specific impact it and the yet-to-be-finalized implementing rules and regulations will have on community banks.

More Information

Our website is www.nationalbankholdings.com. We make available free of charge, through our website, annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and any amendments to those reports filed or furnished pursuant to Section 13(a) or Section 15(d) of the Securities Exchange Act of 1934, as soon as reasonably practicable after we electronically file such material with, or furnish such material to, the U.S. Securities and Exchange Commission ("SEC"). The SEC maintains an Internet site that contains reports, proxy and information statements, and other information regarding issuers that file electronically with the SEC at www.sec.gov.

Item 1A. RISK FACTORS

Risks Relating to Our Banking Operations

We are still a relatively young Company with a limited and complex operating history from which investors can evaluate our past financial and operating performance.

Because our banking operations began in late 2010, and because our acquisitions in 2010 and 2011 were of failed or troubled banks, we have a limited operating history upon which investors can evaluate our recent performance to historical performance. The business models and experiences of the depository institutions we have acquired to date, specifically our 2010 and 2011 acquisitions, may not be reflective of our plans. More importantly, because a portion of the loans and OREO we acquired were marked to fair value at the time of our acquisitions, we believe that the historical financial results of the acquisitions are less useful to an evaluation of our future prospects and financial and operating performance.

Certain other factors may also make it difficult for investors to evaluate our future prospects and financial and operating performance, including, among others:

our current asset mix is not fully representative of our anticipated future asset mix, which may change as we continue to undertake organic loan origination and banking activities and pursue future acquisitions; the income we report from certain acquired assets due to loan discounts and accretable yield may be higher than the returns available in the current market and, if we are unable to make new performing loans and acquire other performing assets in sufficient volume, we may be unable to generate the earnings necessary to implement our growth strategy; our excess cash reserves

and liquid investment securities portfolio may not be representative of our future cash position; and our historical cost structure and capital expenditure requirements are not necessarily reflective of our anticipated cost structure and capital spending as we continue to identify efficiencies and operate our organic banking platform.

Changes in general business and economic conditions could materially and adversely affect us.

Our business and operations are sensitive to general business and economic conditions in the United States and in our core markets of Colorado, the greater Kansas City region, New Mexico, Texas and Utah. If the economies in our core markets, or the U.S. economy more generally, experience worsening economic conditions, including industry-specific conditions, we could be materially and adversely affected. Weak economic conditions may be characterized by deflation, fluctuations in debt and equity capital markets, including a lack of liquidity and/or depressed prices in the secondary market for mortgage loans, increased delinquencies on loans, residential and commercial real estate price declines and lower home sales and commercial activity, and further or prolonged pressure on energy prices. All of these factors would be detrimental to our business. Our business is significantly affected by monetary and related policies of the U.S. federal government, its agencies and

Table of Contents

government-sponsored entities. Changes in any of these policies are influenced by macroeconomic conditions and other factors that are beyond our control and could have a material adverse effect on us.

Changes in the assumptions underlying our acquisition method of accounting, or other significant accounting estimates could affect our financial information and have a material adverse effect on us.

A material portion of our financial results is based on, and subject to, significant assumptions and subjective judgments. As a result of our acquisitions, our financial information is heavily influenced by the application of the acquisition method of accounting and was heavily influenced in prior periods by loss share accounting. Both methodologies require us to make complex assumptions, and these assumptions materially affect our financial results. As such, any financial information generated through the use of the acquisition method of accounting or loss share accounting is subject to modification or change. If our assumptions are incorrect and we change or modify our assumptions, it could have a material adverse effect on us or our previously reported results. Additionally, a change in our accounting estimates, such as our ability to realize deferred tax assets, the need for a valuation allowance or the recoverability of the goodwill recorded at the time of our acquisitions, could have a material adverse effect on our financial results.

Our business is highly susceptible to credit risk and fluctuations in the value of real estate and other collateral securing such credit.

As a lender, we are exposed to the risk that our clients will be unable to repay their loans according to their terms and that the collateral securing the payment of their loans (if any) may not be sufficient to assure repayment. The risks inherent in making any loan include risks with respect to the ability of borrowers to repay their loans and, if applicable, the period of time over which the loan is repaid, risks relating to proper loan underwriting and guidelines, risks resulting from changes in economic and industry conditions, risks inherent in dealing with individual borrowers and risks resulting from uncertainties as to the future value of collateral. Similarly, we have credit risk embedded in our securities portfolio. Our credit standards, procedures and policies may not prevent us from incurring substantial credit losses. A decline in residential real estate market prices and reduced levels of home sales, could adversely affect the value of collateral securing mortgage loans resulting in greater charge-offs in future periods, as well as adversely impact mortgage loan originations and gains on sale of mortgage loans. A decline in commercial real estate values would likewise adversely affect the value of collateral securing certain commercial loans and result in greater charge-offs in future periods. Declines in real estate values and home sales volumes, and financial stress on borrowers as a result of job losses or other factors, could have further adverse effects on borrowers that result in higher delinquencies and greater charge-offs in future periods, which could materially and adversely affect us.

We depend on our executive officers and key personnel to implement our strategy and could be harmed by the loss of their services.

The execution of our strategy depends in large part on the skills of our executive management team and our ability to motivate and retain these and other key personnel, including key personnel added through mergers and acquisitions. Accordingly, the loss of service of one or more of our executive officers or key personnel could reduce our ability to successfully implement our growth strategy and materially and adversely affect us. Our success also depends on the experience of our banking center managers and relationship managers and on their relationships with the clients and communities they serve. The loss of these key personnel could negatively impact our banking operations. The loss of key senior personnel, or the inability to recruit and retain qualified personnel in the future, could have a material adverse effect on us.

Our allowance for loan losses and fair value adjustments may prove to be insufficient to absorb losses inherent in our loan or OREO portfolio.

We maintain an allowance for loan losses (“ALL”), which is a reserve established through a provision for loan losses charged to expense, which we believe is appropriate to provide for probable losses inherent in our loan portfolio. The amount of this allowance is determined by our management through periodic reviews.

The determination of the appropriate level of the allowance for loan losses inherently involves a high degree of subjectivity and requires us to make significant estimates of current credit risks and future trends, all of which may undergo material

Table of Contents

changes. Changes in economic conditions affecting borrowers, new information regarding our loans, identification of additional problem loans by us and other factors, both within and outside of our control, may require an increase in the allowance for loan losses. If the real estate markets deteriorate, we expect that we will experience increased delinquencies and credit losses, particularly with respect to construction, land development and land loans. In addition, our regulators periodically review our allowance for loan losses and may require an increase in the allowance for loan losses or the recognition of further loan charge-offs, based on judgments different than those of management. In addition, if charge-offs in future periods exceed the allowance for loan losses, we will need additional provisions to increase the allowance for loan losses. Any increases in the allowance for loan losses will result in a decrease in net income and capital and may have a material adverse effect on us.

We hold and acquire an amount of OREO from time to time, which may lead to volatility in operating expenses and vulnerability to declines in real property values.

When necessary, we foreclose on and take title to the real estate serving as collateral for our loans as part of our business. Real estate that we own but do not use in the ordinary course of our operations is referred to as OREO property. Higher OREO balances as a result of our acquisitions have led to greater expenses as we incur costs to manage and dispose of the properties. We expect that our earnings will continue to be negatively affected by various expenses associated with OREO, including personnel costs, insurance and taxes, completion and repair costs, valuation adjustments and other expenses associated with property ownership, as well as by the funding costs associated with OREO assets. We evaluate OREO properties periodically and write down the carrying value of the properties if the results of our evaluation require it. The expenses associated with OREO and any further OREO write-downs could have a material adverse effect on us.

We are subject to environmental liability risk associated with lending activities.

A significant portion of our loan portfolio is secured by real property, and we could become subject to environmental liabilities with respect to one or more of these properties. During the ordinary course of business, we may foreclose on and take title to properties securing defaulted loans. There is a risk that hazardous or toxic substances could be found on these properties, and we may be liable for remediation costs, as well as for personal injury and property damage, civil fines and criminal penalties regardless of when the hazardous conditions or toxic substances first affected any particular property. Environmental laws may require us to incur substantial expenses to address unknown liabilities and may materially reduce the affected property's value or limit our ability to use or sell the affected property. In addition, future laws or more stringent interpretations or enforcement policies with respect to existing laws may increase our exposure to environmental liability. Although we have policies and procedures to perform an environmental review before initiating any foreclosure action on nonresidential real property, these reviews may not be sufficient to detect all potential environmental hazards. The remediation costs and any other financial liabilities associated with an environmental hazard could have a material adverse effect on us.

The expanding body of federal, state and local regulation of loan servicing, collections or other aspects of our business may increase the cost of compliance and the risks of noncompliance.

We service the loans held on our balance sheet, and loan servicing is subject to extensive regulation by federal, state and local governmental authorities as well as to various laws and judicial and administrative decisions imposing requirements and restrictions on those activities. The volume of new or modified laws and regulations has increased in recent years and, in addition, some individual municipalities have begun to enact laws that restrict loan servicing activities including delaying or temporarily preventing foreclosures or forcing the modification of certain mortgages. If regulators impose new or more restrictive requirements, we may incur additional significant costs to comply with such requirements which may further adversely affect us. In addition, our failure to comply with these laws and regulations could possibly lead to: civil and criminal liability; damage to our reputation in the industry; fines and penalties and litigation, including class action lawsuits; and administrative enforcement actions. Any of these outcomes could materially and adversely affect us.

Table of Contents

Small Business Administration lending is an important and growing part of our business. Our SBA lending program is dependent upon the U.S. federal government, and we face specific risks associated with originating SBA loans.

As an approved participant in the SBA Preferred Lender's Program (an "SBA Preferred Lender"), we enable our clients to obtain SBA loans without being subject to the potentially lengthy SBA approval process necessary for lenders that are not SBA Preferred Lenders. The SBA periodically reviews the lending operations of participating lenders to assess, among other things, whether the lender exhibits prudent risk management. When weaknesses are identified, the SBA may request corrective actions or impose enforcement actions, including revocation of the lender's SBA Preferred Lender status.

If we were to lose our status as an SBA Preferred Lender, we may lose new opportunities, and a limited number of existing SBA loans, to lenders who are SBA Preferred Lenders. In addition, any changes to the SBA program, including changes to the level of guarantee provided by the federal government on SBA loans, changes to program-specific rules impacting volume eligibility under the guaranty program, as well as changes to the program amounts authorized by Congress, may have a material adverse effect on our SBA lending program. In addition, any default by the U.S. government on its obligations or any prolonged government shutdown could, among other things, impede our ability to originate SBA loans or collect on guarantees in the event a borrower defaults on its obligations, and could materially adversely affect our SBA lending business.

If we violate U.S. Department of Housing and Urban Development ("HUD") lending requirements or if the federal government shuts down or otherwise fails to fully fund the federal budget, our commercial FHA origination business could be adversely affected.

We originate, sell and service loans under FHA insurance programs, and make certifications regarding compliance with applicable requirements and guidelines. If we were to violate these requirements and guidelines, or other applicable laws, or if the FHA loans we originate show a high frequency of loan defaults, we could be subject to monetary penalties and indemnification claims, and could be declared ineligible for FHA programs. Any inability to engage in our commercial FHA origination and servicing business would lead to a decrease in our net income.

In addition, disagreement over the federal budget has caused the U.S. federal government to shut down for periods of time in recent years. Federal governmental entities, such as HUD, that rely on funding from the federal budget, could be adversely affected in the event of a government shutdown, which could have a material adverse effect on our commercial FHA origination business and our results of operations.

The fair value of our investment securities can fluctuate due to market conditions outside of our control.

We have historically taken a conservative investment strategy with our securities portfolio, with concentrations of securities that are primarily backed by government sponsored enterprises. In the future, we may seek to increase yields through different strategies, which may include a greater percentage of corporate securities and structured credit products. Factors beyond our control can significantly influence the fair value of securities in our portfolio and can cause potential adverse changes to the fair value of these securities. These factors include, but are not limited to, rating agency actions in respect of the securities, defaults by the issuer or with respect to the underlying securities, and changes in market interest rates and instability in the capital markets. These factors, among others, could cause other-than-temporary impairments and realized and/or unrealized losses in future periods and declines in other comprehensive income, which could have a material adverse effect on us. The process for determining whether impairment of a security is other-than-temporary usually requires complex, subjective judgments about the future financial performance and liquidity of the issuer and any collateral underlying the security in order to assess the probability of receiving all contractual principal and interest payments on the security.

Table of Contents

We face significant competition from other financial institutions and financial services providers, which may materially and adversely affect us.

Consumer and commercial banking is highly competitive. Our markets contain a large number of community and regional banks as well as a significant presence of the country's largest commercial banks. We compete with other state and national financial institutions, including savings and loan associations, savings banks and credit unions, for deposits and loans. In addition, we compete with financial intermediaries, such as consumer finance companies, mortgage banking companies, insurance companies, securities firms, mutual funds and several government agencies, as well as major retailers, in providing various types of loans and other financial services. Some of these competitors have a long history of successful operations in our markets, greater ties to local businesses and more expansive banking relationships, as well as better established depositor bases. Some of our competitors also have greater resources and access to capital and possess an advantage by being capable of maintaining numerous banking locations in more convenient sites, operating more ATMs and conducting extensive promotional and advertising campaigns or operating a more developed internet platform. Competitors may also exhibit a greater tolerance for risk and behave more aggressively with respect to pricing in order to increase their market share. In addition, the effects of disintermediation can also impact the banking business because of the fast growing body of FinTech companies that use software to deliver mortgage lending, payment services and other financial services.

Our ability to compete successfully depends on a number of factors, including, among others:

- the ability to develop, maintain and build upon long-term client relationships based on quality service, effective and efficient products and services, high ethical standards and safe and sound assets;
- the scope, relevance and pricing of products and services offered to meet client needs and demands;
- the rate at which we introduce new products and services relative to our competitors;
- the ability to attract and retain highly qualified associates to operate our business;
- the ability to expand our market position;
- client satisfaction with our level of service;
- the ability to invest in new technologies;
- the ability to operate our business effectively and efficiently; and
- industry and general economic trends.

Failure to perform in any of these areas could significantly weaken our competitive position, which could materially and adversely affect us.

We may not be able to meet the cash flow requirements of deposit withdrawals and other business needs unless we maintain sufficient liquidity.

We require liquidity to make loans and to repay deposit and other liabilities as they become due or are demanded by clients. We principally depend on checking, savings and money market deposit account balances and other forms of client deposits as our primary source of funding for our lending activities. As a result of a decline in overall depositor confidence, an increase in interest rates paid by competitors, general interest rate levels, higher returns being available to clients on alternative investments and general economic conditions, a substantial number of our clients could withdraw their bank deposits with us from time to time, resulting in our deposit levels decreasing substantially, and our cash on hand may not be able to cover such withdrawals and our other business needs, including amounts necessary to operate and grow our business. This would require us to seek third party funding or other sources of liquidity, such as asset sales. Our access to third party funding sources, including our ability to raise funds through the issuance of additional shares of our common stock or other equity or equity-related securities, incurrence of debt, and federal funds purchased, may be impacted by our financial strength, performance and prospects and may also be impaired by factors that are not specific to us, such as a disruption in the financial markets or negative views and expectations about the prospects for the financial services industry, all of which may make potential funding sources more difficult to access, less reliable and more expensive. We may not have access to third party funding in sufficient amounts on favorable terms, or the ability to undertake asset sales or access other sources of liquidity, when needed, or at all, which could materially and adversely affect us.

Table of Contents

Like other financial services institutions, our asset and liability structures are monetary in nature. Such structures are affected by a variety of factors, including changes in interest rates, which can impact the value of financial instruments held by us.

Like other financial services institutions, we have asset and liability structures that are essentially monetary in nature and are directly affected by many factors, including domestic and international economic and political conditions, broad trends in business and finance, legislation and regulation affecting the national and international business and financial communities, monetary and fiscal policies, inflation, currency values, market conditions, the availability and terms (including cost) of short-term or long-term funding and capital, the credit capacity or perceived creditworthiness of clients and counterparties and the level and volatility of trading markets. Such factors can impact clients and counterparties of a financial services institution and may impact the value of financial instruments held by a financial services institution.

Our earnings and cash flows largely depend upon the level of our net interest income, which is the difference between the interest income we earn on loans, investments and other interest earning assets, and the interest we pay on interest bearing liabilities, such as deposits and borrowings. Because different types of assets and liabilities may react differently and at different times to market interest rate changes, changes in interest rates can increase or decrease our net interest income. When interest-bearing liabilities mature or reprice more quickly than interest earning assets in a period, an increase in interest rates would reduce net interest income. Similarly, when interest earning assets mature or reprice more quickly, and because the magnitude of repricing of interest earning assets is often greater than interest bearing liabilities, falling interest rates would reduce net interest income.

Accordingly, changes in the level of market interest rates affect our net yield on interest earning assets and liabilities, loan and investment securities portfolios and our overall results. Changes in interest rates may also have a significant impact on any future loan origination revenues. Historically, there has been an inverse correlation between the demand for loans and interest rates. Loan origination volume and revenues usually decline during periods of rising or high interest rates and increase during periods of declining or low interest rates. Changes in interest rates also have a significant impact on the carrying value of a significant percentage of the assets, both loans and investment securities, on our balance sheet. We may incur debt in the future and that debt may also be sensitive to interest rates and any increase in interest rates could materially and adversely affect us. Interest rates are highly sensitive to many factors beyond our control, including general economic conditions and policies of various governmental and regulatory agencies, particularly the Federal Reserve. Changes in the Federal Reserve's interest rate policies or other changes in monetary policies and economic conditions could materially and adversely affect us.

Reforms to and uncertainty regarding LIBOR and certain other indices may adversely affect our business.

The U.K. Financial Conduct Authority announced in July 2017 that it will no longer persuade or require banks to submit rates for LIBOR after 2021. This announcement, in conjunction with financial benchmark reforms more generally and changes in the interbank lending markets, have resulted in uncertainty about the future of LIBOR and

certain other rates or indices that are used as interest rate “benchmarks.” These actions and uncertainties may have the effect of triggering future changes in the rules or methodologies used to calculate benchmarks or lead to the discontinuance or unavailability of benchmarks. Uncertainty as to the nature and effect of such reforms and actions, and the potential or actual discontinuance of benchmark quotes, may adversely affect our financial condition or results of operations, including the value of, return on and trading market for our financial assets and liabilities that are based on or are linked to benchmarks, including any LIBOR-based securities, loans and derivatives. Furthermore, there can be no assurances that we and other market participants will be adequately prepared for an actual discontinuation of benchmarks, including LIBOR, that may have an unpredictable impact on contractual mechanics (including, but not limited to, interest rates to be paid to or by us), which may also result in adversely affecting our financial condition or results of operations.

We are dependent on our information technology and telecommunications systems and third-party providers, and systems failures or interruptions could have a material adverse effect on us.

Our business is highly dependent on the successful and uninterrupted functioning of our information technology and telecommunications systems and third-party providers. We outsource many of our major systems, such as data processing, loan servicing and deposit processing systems. The failure of these systems, or the termination of a third-party software

Table of Contents

license or service agreement on which any of these systems is based, could interrupt our operations. Because our information technology and telecommunications systems interface with and depend on third-party systems, we could experience service denials if demand for such services exceeds capacity or such third-party systems fail or experience interruptions. If significant, sustained or repeated, a system failure or service denial could compromise our ability to operate effectively, damage our reputation, result in a loss of client business, and/or subject us to additional regulatory scrutiny and possible financial liability, any of which could have a material adverse effect on us.

A failure in or breach of our security systems or infrastructure, or those of our third-party providers, could result in financial losses to us or in the disclosure or misuse of confidential or proprietary information, including client information, and could have a material adverse effect on us, or noncompliance with evolving privacy and data protection laws could have a material adverse effect on us.

As a financial institution, we may be the target of fraudulent activity that may result in financial losses to us or our clients, privacy breaches against our clients or damage to our reputation. Such fraudulent activity may take many forms, including check fraud, electronic fraud, wire fraud, phishing, unauthorized intrusion into or use of our systems, ATM skimming or jackpotting, and other dishonest acts. We provide our clients with the ability to bank remotely, including via online, mobile and phone. The secure transmission of confidential information over the internet and other remote channels is a critical element of remote banking.

Our network could be vulnerable to unauthorized access, computer viruses, phishing schemes, ransomware and other security breaches. We may be required to spend significant capital and other resources to protect against the threat of security breaches and computer viruses, or to alleviate problems caused by security breaches or viruses. Given the increasingly high volume of our transactions, certain errors may be repeated or compounded before they can be discovered and rectified. To the extent that our activities or the activities of our clients involve the storage and transmission of confidential information, security breaches and viruses could expose us to reputational damage, claims, regulatory scrutiny, litigation and other possible liabilities. Any inability to prevent security breaches or computer viruses could also cause existing clients to lose confidence in our systems and could materially and adversely affect us. Our risk and exposure to these matters remains heightened because of the evolving nature and complexity of the threats from organized cybercriminals and hackers, and our plans to continue to provide digital banking products and services to our clients.

Information security risks for financial institutions like us have increased recently in part because of new technologies, the use of the internet and telecommunications technologies (including mobile devices) to conduct financial and other business transactions and the increased sophistication and activities of organized crime, perpetrators of fraud, hackers, terrorists and others. In addition to cyber-attacks or other security breaches involving the theft of sensitive and confidential information, hackers have engaged in attacks against large financial institutions, particularly denial of service attacks, that are designed to disrupt key business services, such as client-facing web sites. We are not able to anticipate or implement effective preventive measures against all security breaches of these types, especially because the techniques used change frequently and because attacks can originate from a wide variety of sources. We employ detection and response mechanisms designed to contain and mitigate security incidents, but early detection may be thwarted by sophisticated attacks and malware designed to avoid detection.

We also face risks related to cyber-attacks and other security breaches in connection with credit or debit card, including ATM-related, transactions that typically involve the transmission of sensitive information regarding our clients through various third parties, including merchant acquiring banks, payment processors, payment card networks (e.g., Visa, MasterCard) and our processors. Some of these parties have in the past been the target of security breaches and cyber-attacks, and because the transactions involve third parties and environments such as the point of sale that we do not control or secure, future security breaches or cyber-attacks affecting any of these third parties could impact us through no fault of our own, and in some cases we may have exposure and suffer losses for breaches or attacks relating to them. We also rely on numerous other third party service providers to conduct other aspects of our business operations and face similar risks relating to them. While we regularly conduct security assessments on these third parties, we cannot be sure that their information security protocols are sufficient to withstand a cyber-attack or other security breach.

25

Table of Contents

Our growth and expansion may also subject us to evolving laws and regulations regarding privacy and data protections, including the EU General Data Protection Regulation (“GDPR”) and the California Consumer Privacy Act of 2018. It is possible that these laws may be interpreted and applied by various jurisdictions in a manner inconsistent with our current or future practices, or that is inconsistent with one another. If personal, confidential or proprietary information of customers or clients in our possession is mishandled or misused, we may face regulatory, reputational and operational risks which could have an adverse effect on our financial condition and results of operations.

The value of our mortgage servicing rights can decline during periods of falling interest rates, and we may be required to take a charge against earnings for the decreased value.

A mortgage servicing right (“MSR”) is the right to service a mortgage loan for a fee. We capitalize MSRs when we originate mortgage loans and retain the servicing rights after we sell the loans. We carry MSRs at the lower of amortized cost or estimated fair value. Fair value is the present value of estimated future net servicing income, calculated based on a number of variables, including assumptions about the likelihood of prepayment by borrowers. Changes in interest rates can affect prepayment assumptions. When interest rates fall, borrowers are more likely to prepay their mortgage loans by refinancing them at a lower rate. As the likelihood of prepayment increases, the fair value of our MSRs can decrease. Each quarter we evaluate our MSRs for impairment based on the difference between the carrying amount and fair value, and, if a temporary impairment exists, we establish a valuation allowance through a charge that negatively affects our earnings.

We may be required to repurchase mortgage loans or reimburse investors and others as a result of breaches in contractual representations and warranties.

We sell residential mortgage loans to various parties, including GSEs and other financial institutions that purchase mortgage loans for investment or private label securitization. The agreements under which we sell mortgage loans and the insurance or guaranty agreements with the FHA and VA contain various representations and warranties regarding the origination and characteristics of the mortgage loans, including ownership of the loan, compliance with loan criteria set forth in the applicable agreement, validity of the lien securing the loan, absence of delinquent taxes or liens against the property securing the loan, and compliance with applicable origination laws. We may be required to repurchase mortgage loans, indemnify the investor or insurer, or reimburse the investor or insurer for credit losses incurred on loans in the event of a breach of contractual representations or warranties that is not remedied within a period (usually 90 days or less) after we receive notice of the breach. Contracts for mortgage loan sales to the GSEs include various types of specific remedies and penalties that could be applied to inadequate responses to repurchase requests. Similarly, the agreements under which we sell mortgage loans require us to deliver various documents to the investor, and we may be obligated to repurchase any mortgage loan as to which the required documents are not delivered or are defective. We establish a mortgage repurchase liability related to the various representations and warranties that reflect management's estimate of losses for loans which we have a repurchase obligation. Our mortgage repurchase liability represents management's best estimate of the probable loss that we may expect to incur for the representations and warranties in the contractual provisions of our sales of mortgage loans. Because the level of mortgage loan repurchase losses depends upon economic factors, investor demand strategies and other external conditions that may change over the life of the underlying loans, the level of the liability for mortgage loan repurchase

losses is difficult to estimate and requires considerable management judgment. If economic conditions and the housing market deteriorate or future investor repurchase demand and our success at appealing repurchase requests differ from past experience, we could experience increased repurchase obligations and increased loss severity on repurchases, requiring additions to the repurchase liability.

The required accounting treatment of loans we acquire through acquisitions, including purchase credit impaired loans, could result in higher net interest margins and interest income in current periods and lower net interest margins and interest income in future periods.

Under U.S. GAAP, we are required to record loans acquired through acquisitions, including purchase credit impaired loans, at fair value. Estimating the fair value of such loans requires management to make estimates based on available information, facts, and circumstances on the acquisition date. Any discount, which is the excess of the amount of reasonably estimable and probable discounted future cash collections over the purchase price, is accreted into interest income over the weighted average remaining contractual life of the loans. Therefore, our net interest margins may initially increase due to the discount accretion. We expect the yields on the total loan portfolio will decline as our acquired loan portfolios pay down or mature and the corresponding accretion of the discount decreases. We expect downward pressure on our interest income to the extent that the

Table of Contents

runoff of our acquired loan portfolios is not replaced with comparable high-yielding loans. This could result in higher net interest margins and interest income in current periods and lower net interest margins and interest income in future periods.

We have recorded goodwill as a result of acquisitions that can significantly affect our earnings if it becomes impaired.

Under current accounting standards, goodwill is not amortized but, instead, is subject to impairment tests on at least an annual basis or more frequently if an event occurs or circumstances change that reduce the fair value of a reporting unit below its carrying value.

Risks Relating to our Growth Strategy

We may not be able to effectively manage our growth or other expansionary activity.

Our expansionary activity, whether through de novo branching, acquisitions or organic growth has placed, and it may continue to place, significant demands on our operations and management. The success of our expansionary activity is dependent upon our ability to:

continue to
implement
and improve
our
operational,
credit,
financial,
legal,
management
and other
internal risk
controls and
processes and
our reporting
systems and
procedures in
order to
manage a

growing
number of
client
relationships;
scale our
technology
platform;
integrate our
acquisitions
and develop
consistent
policies
throughout
the various
lines of
businesses;
attract and
retain the
client base;
and
attract and
retain
management
talent.

We may not successfully implement improvements to, or integrate, our management information and control systems, procedures and processes in an efficient or timely manner and may discover deficiencies in existing systems and controls. In particular, our controls and procedures must be able to accommodate an increase in loan volume in various markets and the infrastructure that comes with new banking centers and banks. Thus, our growth strategy may divert management from our existing franchises and may require us to incur additional expenditures to expand our administrative and operational infrastructure and, if we are unable to effectively manage and grow our financial services franchise, we could be materially and adversely affected. In addition, if we are unable to manage future expansion in our operations, we may experience compliance and operational problems, have to slow the pace of growth, or have to incur additional expenditures beyond current projections to support such growth, any one of which could materially and adversely affect us.

Our acquisitions generally will require regulatory approvals, and failure to obtain them would restrict our growth.

We intend to complement and expand our business by pursuing strategic acquisitions of financial services franchises. Generally, any acquisition of target financial institutions, banking centers or other banking assets by us will require approval by, and cooperation from, a number of governmental regulatory agencies, including the Federal Reserve and Colorado Division of Banking. In acting on applications, our banking regulators consider, among other factors:

the effect of the acquisition on competition;
the financial condition, liquidity, results of operations, capital levels and future prospects of the applicant and the bank(s) involved;
the quantity and complexity of previously consummated acquisitions;
the managerial resources of the applicant and the bank(s) involved;
the convenience and needs of the community, including the record of performance under the Community Reinvestment Act (which we refer to as the “CRA”); and
the effectiveness of the applicant in combating money laundering activities.

Such regulators could deny our application based on the above criteria or other considerations, which would restrict our growth, or the regulatory approvals may not be granted on terms that are acceptable to us. For example, we could be required

Table of Contents

to sell banking centers as a condition to receiving regulatory approvals, and such a condition may not be acceptable to us or may reduce the benefit of any acquisition. In addition, prior to the submission of an application our regulators could discourage us from pursuing strategic acquisitions or indicate that regulatory approvals may not be granted on terms that would be acceptable to us, which could have the same effect of restricting our growth or reducing the benefit of any acquisitions.

The success of future transactions will depend on our ability to successfully identify and consummate acquisitions of financial services franchises that meet our investment objectives. Because of the intense competition for acquisition opportunities and the limited number of potential targets, we may not be able to successfully consummate acquisitions on attractive terms.

There are significant risks associated with our strategy to identify and successfully consummate acquisitions. There are a limited number of acquisition opportunities, and we expect to encounter intense competition from other banking organizations competing for acquisitions and also from other investment funds and entities looking to acquire financial institutions and financial services franchises. Many of these entities are well established and have extensive experience in identifying and consummating acquisitions directly or through affiliates. Many of these competitors possess ongoing banking operations with greater financial, technical, human and other resources and access to capital than we do, which could limit the acquisition opportunities we pursue. Our competitors may be able to achieve greater cost savings, through consolidating operations or otherwise, than we could. These competitive limitations give others an advantage in pursuing certain acquisitions. In addition, increased competition may drive up the prices for the acquisitions we pursue and make the other acquisition terms more onerous, which would make the identification and successful consummation of those acquisitions less attractive to us. Competitors may be willing to pay more for acquisitions than we believe are justified, which could result in us having to pay more for them than we prefer or to forego the opportunity. The trading price of our common stock and of the stock of other potential acquirers may affect our ability to offer a competitive price for acquisitions where stock is proposed as acquisition consideration. As a result of the foregoing, we may be unable to successfully identify and consummate acquisitions on attractive terms, or at all, that are necessary to grow our business.

To the extent that we are unable to identify and consummate attractive acquisitions, or continue to increase loans through organic loan growth, we may be unable to successfully implement our growth strategy, which could materially and adversely affect us.

We intend to continue to grow our business through strategic acquisitions of financial services franchises coupled with organic loan growth. Previous availability of attractive acquisition targets may not be indicative of future acquisition opportunities, and we may be unable to identify any acquisition targets that meet our investment objectives. As our acquired loan portfolio, which generally produces higher yields than our originated loans due to loan discounts and accretable yield, is paid down, we expect downward pressure on our income to the extent that the runoff is not replaced with other high-yielding loans. As a result of the foregoing, if we are unable to replace loans in our existing portfolio with comparable high-yielding loans, we could be materially and adversely affected. We could also be materially and adversely affected if we choose to pursue riskier higher-yielding loans that fail to perform.

Projected operating results for businesses acquired by us may be inaccurate and may vary significantly from actual results. To the extent that we make acquisitions that involve distressed assets, we may not be able to realize the value we predict from these assets or make sufficient provision for future losses in the value of, or accurately estimate the future writedowns to be taken in respect of, these assets.

We will generally establish the pricing of transactions and the capital structure of financial services franchises to be acquired by us on the basis of financial projections for such financial services franchises. In general, projected operating results will be based on the judgment of our management team. In all cases, projections are only estimates of future results that are based upon assumptions made at the time that the projections are developed and the projected results may vary significantly from actual results. General economic, political and market conditions can have a material adverse impact on the reliability of such projections. In the event that the projections made in connection with our acquisitions, or future projections with respect to new acquisitions, are not accurate, such inaccuracies could materially and adversely affect us.

Delinquencies and losses in the loan portfolios and other assets we acquire may exceed our initial forecasts developed during our due diligence investigation prior to their acquisition and, thus, produce lower returns than we believed our purchase price

Table of Contents

supported. Furthermore, our due diligence investigation may not reveal all material issues. If, during the diligence process, we fail to identify all relevant issues related to an acquisition, we may be forced to later write down or write off assets, restructure our operations, or incur impairment or other charges that could result in significant losses. Any of these events could materially and adversely affect us. Economic conditions may create an uncertain environment with respect to asset valuations and there is no certainty that we will be able to sell assets or institutions after we acquire them if we determine it would be in our best interests to do so. In addition, there may be limited liquidity for certain asset classes we hold, including commercial real estate and construction and development loans. Any of the foregoing matters could materially and adversely affect us.

We face additional risks due to our increased mortgage banking activities that could negatively impact net income and profitability.

We sell substantially all of the mortgage loans that we originate. The sale of these loans generates non-interest income and can be a source of liquidity for the Bank. Disruption in the secondary market for residential mortgage loans as well as declines in real estate values could result in one or more of the following:

- our inability to sell mortgage loans on the secondary market, which could negatively impact our liquidity position;
- declines in real estate values could decrease the potential of mortgage originations, which could negatively impact our earnings;
- if it is determined that loans were made in breach of our representations and warranties to the secondary market, we could incur losses associated with the loans;
- increased compliance requirements could result in higher compliance costs, higher foreclosure proceedings or lower loan origination volume, all which could negatively impact future earnings; and
- a rise in interest rates could cause a decline in mortgage originations, which could negatively impact our earnings.

Our use of appraisals in deciding whether to make loans secured by real property does not ensure that the value of the real property collateral will be sufficient to repay our loans.

In considering whether to make a loan secured by real property, we require an appraisal of the property. However, an appraisal is only an estimate of the value of the property at the time the appraisal is made and requires the exercise of a considerable degree of judgment. If the appraisal does not accurately reflect the amount that may be obtained upon sale or foreclosure of the property, whether due to a decline in property value after the date of the original appraisal or defective preparation of the appraisal, we may not realize an amount equal to the indebtedness secured by the property and as a result, we may suffer losses.

Risks Relating to the Regulation of Our Industry

The Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 continues to materially affect our business.

The key effects of the Dodd-Frank Act on our business are:

changes to regulatory capital requirements; creation of new government regulatory agencies (such as the Financial Stability Oversight Council, which oversees systemic risk, and the Consumer Financial Protection Bureau, which develops and enforces rules for bank and non-bank providers of consumer financial products); potential limitations on federal preemption; changes to deposit insurance

assessments;
regulation of
debit
interchange
fees we earn;
changes in
retail banking
regulations,
including
potential
limitations on
certain fees
we may
charge; and
changes in
regulation of
consumer
mortgage loan
origination
and risk
retention.

Several provisions still require regulations to be promulgated by various federal agencies in order to be implemented, some of which have been proposed by the applicable federal agencies. The changes resulting from the Dodd-Frank Act have limited our business activities, required changes to certain of our business practices, imposed upon us more stringent capital,

Table of Contents

liquidity and leverage requirements or otherwise materially and may continue to adversely affect us. Failure to comply with the requirements could also materially and adversely affect us. Furthermore, additional uncertainties surrounding the Dodd-Frank Act, its implementation, and enforcement persist as a result of the current presidential administration. Any changes in the laws or regulations or their interpretations could be materially adverse to investors in our common stock.

We operate in a highly regulated environment and the laws and regulations that govern our operations, corporate governance, executive compensation and accounting principles, or changes in them, or our failure to comply with them, could materially and adversely affect us.

We are subject to extensive regulation, supervision, and legislation by federal and state regulators and bodies that govern almost all aspects of our operations. Intended to protect clients, depositors and the DIF, these laws and regulations, among other matters, prescribe minimum capital requirements, impose limitations on the business activities in which we can engage (including foreclosure and collection practices), limit the dividends or distributions that we can pay, restrict the ability of institutions to guarantee our debt, and impose certain specific accounting requirements on us that may be more restrictive and may result in greater or earlier charges to earnings or reductions in our capital than GAAP. Compliance with laws and regulations can be difficult and costly, and changes to laws and regulations often impose additional compliance costs. Our failure to comply with these laws and regulations, even if the failure follows good faith effort or reflects a difference in interpretation, could subject us to restrictions on our business activities, fines and other penalties, any of which could materially and adversely affect us. Further, any new laws, rules and regulations could make compliance more difficult or expensive and also materially and adversely affect us.

The FDIC's restoration plan for the DIF and any related increased assessment rates could materially and adversely affect us.

The FDIC insures deposits at FDIC-insured depository institutions, such as our subsidiary bank, up to applicable limits. The amount of a particular institution's deposit insurance assessment is based on that institution's risk classification under an FDIC risk-based assessment system. An institution's risk classification is assigned based on its capital levels and the level of supervisory concern the institution poses to its regulators. If current assessments imposed by the FDIC are insufficient for the DIF to meet its funding requirements, there may need to be further special assessments or increases in deposit insurance premiums. We are generally unable to control the amount of premiums that we are required to pay for FDIC insurance. Any future additional assessments, increases or required prepayments in FDIC insurance premiums may materially and adversely affect us, including by reducing our profitability or limiting our ability to pursue certain business opportunities.

Federal and state banking agencies periodically conduct examinations of our business, including compliance with laws and regulations, and our failure to comply with any supervisory actions to which we become subject as a result of such examinations could materially and adversely affect us.

Federal and state banking agencies periodically conduct examinations of our business, including compliance with laws and regulations. If, as a result of an examination, a federal or state banking agency were to determine that the financial condition, capital resources, asset quality, earnings prospects, management, liquidity or other aspects of any of our operations had become unsatisfactory, or that we or our management was in violation of any law or regulation, it may take a number of different remedial actions as it deems appropriate. These actions include the power to enjoin “unsafe or unsound” practices, to require affirmative actions to correct any conditions resulting from any violation or practice, to issue an administrative order that can be judicially enforced, to direct an increase in our capital, to restrict our growth, to assess civil monetary penalties against our officers or directors, to remove officers and directors and, if it is concluded that such conditions cannot be corrected or there is an imminent risk of loss to depositors, to terminate our deposit insurance. If we become subject to such regulatory actions, we could be materially and adversely affected.

Table of Contents

We are subject to the Community Reinvestment Act and fair lending laws, and failure to comply with these laws could lead to a wide variety of sanctions.

The CRA, the Equal Credit Opportunity Act, the Fair Housing Act and other fair lending laws and regulations impose nondiscriminatory lending requirements on financial institutions. The Department of Justice and other federal agencies are responsible for enforcing these laws and regulations. A successful challenge to an institution's performance under the CRA or fair lending laws and regulations could result in a wide variety of sanctions, including damages and civil money penalties, injunctive relief, restrictions on mergers and acquisitions activity, and restrictions on expansion activity. Private parties may also have the ability to challenge an institution's performance under fair lending laws in private class action litigation.

The Federal Reserve may require us to commit capital resources to support our subsidiary bank.

As a matter of policy, the Federal Reserve, which examines us and our subsidiaries, expects a bank holding company to act as a source of financial and managerial strength to a subsidiary bank and to commit resources to support such subsidiary bank. Under the "source of strength" doctrine, the Federal Reserve may require a bank holding company to make capital injections into a troubled subsidiary bank and may charge the bank holding company with engaging in unsafe and unsound practices for failure to commit resources to such a subsidiary bank. In addition, the Dodd-Frank Act directs the federal bank regulators to require that all companies that directly or indirectly control an insured depository institution serve as a source of strength for the institution. Under this requirement, we could be required to provide financial assistance to our subsidiary bank should our subsidiary bank experience financial distress.

A capital injection may be required at times when we do not have the resources to provide it and therefore we may be required to borrow the funds or raise additional equity capital from third parties. Any loans by a holding company to its subsidiary bank are subordinate in right of payment to deposits and to certain other indebtedness of the subsidiary bank. In the event of a bank holding company's bankruptcy, the bankruptcy trustee will assume any commitment by the holding company to a federal bank regulatory agency to maintain the capital of a subsidiary bank. Moreover, bankruptcy law provides that claims based on any such commitment will be entitled to a priority of payment over the claims of the holding company's general unsecured creditors, including the holders of its indebtedness. Any financing that must be done by the holding company in order to make the required capital injection may be difficult and expensive and may not be available on attractive terms, or at all, which likely would have a material adverse effect on us.

We face a risk of noncompliance and enforcement action with the Bank Secrecy Act and other anti-money laundering statutes and regulations.

The federal Bank Secrecy Act, the USA PATRIOT Act and other laws and regulations require financial institutions, among other duties, to institute and maintain an effective anti-money laundering program and file suspicious activity and currency transaction reports as appropriate. The federal Financial Crimes Enforcement Network, established by the U.S. Treasury Department to administer the Bank Secrecy Act, is authorized to impose significant civil money penalties for violations of those requirements, and engages in coordinated enforcement efforts with the individual federal banking regulators, as well as the Department of Justice, Drug Enforcement Administration, and Internal Revenue Service. There is also increased scrutiny of compliance with the rules enforced by the Office of Foreign Assets Control. If our policies, procedures and systems are deemed deficient or the policies, procedures and systems of the financial institutions that we may acquire in the future are deficient, we would be subject to liability, including fines and regulatory actions (such as restrictions on our ability to pay dividends and the necessity to obtain regulatory approvals to proceed with certain aspects of our business plan, including our acquisition plans), which could materially and adversely affect us. Failure to maintain and implement adequate programs to combat money laundering and terrorist financing could also have serious reputational consequences for us.

Federal, state and local consumer lending laws may restrict our ability to originate certain mortgage loans or increase our risk of liability with respect to such loans and could increase our cost of doing business.

Federal, state and local laws have been adopted that are intended to eliminate certain lending practices considered “predatory.” These laws prohibit practices such as steering borrowers away from more affordable products, selling unnecessary insurance to borrowers, repeatedly refinancing loans and making loans without a reasonable expectation that the borrowers will be able to repay the loans irrespective of the value of the underlying property. It is our policy not to make

Table of Contents

predatory loans, but these laws create the potential for liability with respect to our lending and loan investment activities. They increase our cost of doing business and, ultimately, may prevent us from making certain loans and cause us to reduce the average percentage rate or the points and fees on loans that we do make.

Our ability to pay dividends is subject to regulatory limitations and our bank subsidiary's ability to pay dividends to us is also subject to regulatory limitations.

Our ability to declare and pay dividends depends both on the ability of our bank subsidiary to pay dividends to us and on certain federal regulatory considerations, including the guidelines of the Federal Reserve regarding capital adequacy and dividends. Because we are a separate legal entity from our bank subsidiary and we do not have significant operations of our own, any dividends paid by us to our shareholders would have to be paid from funds at the holding company level that are legally available therefor. However, as a bank holding company, we are subject to general regulatory restrictions on the payment of cash dividends. Federal bank regulatory agencies have the authority to prohibit bank holding companies from engaging in unsafe or unsound practices in conducting their business, which depending on the financial condition and liquidity of the holding company at the time, could include the payment of dividends. Additionally, various federal and state statutory provisions limit the amount of dividends that our bank subsidiary can pay to us as its holding company without regulatory approval. Finally, holders of our common stock are only entitled to receive such dividends as our board of directors may, in its unilateral discretion, declare out of funds legally available for such purpose based on a variety of considerations, including, without limitation, our historical and projected financial condition, liquidity and results of operations, capital levels, tax considerations, statutory and regulatory prohibitions and other limitations, general economic conditions and other factors deemed relevant by our board of directors. Accordingly, we may not pay the amount of dividends referenced in our current intention above, or any dividends at all, to our shareholders in the future.

Tax legislation initiatives or challenges to our tax positions could adversely affect our results of operations and financial condition.

We operate in multiple jurisdictions and we are subject to tax laws and regulations of the U.S. federal, state and local governments. From time to time, legislative initiatives may be adopted, such as the recent tax reform in the United States, which may impact our effective tax rate and could adversely affect our deferred tax assets, tax positions and/or our tax liabilities. In addition, U.S. federal, state and local tax laws and regulations are extremely complex and subject to varying interpretations. There can be no assurance that our historical tax positions will not be challenged by relevant tax authorities or that we would be successful in defending our positions in connection with any such challenge.

Item 1B. UNRESOLVED STAFF COMMENTS.

None

Item 2. PROPERTIES.

Our principal executive offices are located in the Denver Tech Center area immediately south of Denver, Colorado. We also have approximately 70,000 square feet of office and operations space in Kansas City, Missouri. At December 31, 2018, we operated 50 banking centers in Colorado, 46 in Kansas and Missouri, six in New Mexico and two in Texas. Of these banking centers, 31 locations were leased and 73 were owned.

Item 3. LEGAL PROCEEDINGS.

From time to time, we are a party to various litigation matters incidental to the conduct of our business. We are not presently party to any legal proceedings the resolution of which we believe would have a material adverse effect on our business, prospects, financial condition, results of operations or liquidity.

Item 4. MINE SAFETY DISCLOSURES.

None.

32

Table of Contents

PART II

Item 5. MARKET FOR REGISTRANT’S COMMON EQUITY, RELATED SHAREHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES.

Market for Registrant’s Common Equity

Shares of the Company’s common stock began trading on the New York Stock Exchange (“NYSE”) under the symbol “NBHC”. The following table presents the cash dividends paid for the periods indicated:

| Quarter | 2018 | 2017 |
|---------|---------|---------|
| Fourth | \$ 0.17 | \$ 0.09 |
| Third | 0.14 | 0.09 |
| Second | 0.14 | 0.09 |
| First | 0.09 | 0.07 |
| Total | \$ 0.54 | \$ 0.34 |

In October 2012, the Company commenced the payment of a \$0.05 per share quarterly cash dividend to holders of its common stock. As of December 31, 2018, the quarterly cash dividend was \$0.17 per share, representing a cumulative increase of 240% within six years.

Table of Contents

Performance Graph

The following graph presents a comparison of the Company's performance to the indices named below. It assumes \$100 invested on December 31, 2013, with dividends invested on a total return basis.

| Index | Period Ending | | | | | |
|----------------------------|---------------|----------|----------|----------|----------|----------|
| | 12/31/13 | 12/31/14 | 12/31/15 | 12/31/16 | 12/31/17 | 12/31/18 |
| NBHC | 100.00 | 104.31 | 116.00 | 174.77 | 179.62 | 173.45 |
| KBW Regional Banking Index | 100.00 | 150.39 | 159.41 | 221.77 | 225.78 | 186.30 |
| Russell 2000 Index | 100.00 | 145.62 | 139.19 | 168.81 | 193.50 | 172.16 |

The following table sets forth information about our repurchases of our common stock during the fourth quarter of 2018:

| Period | Total number of shares (or units) purchased | Average price paid per share (or unit) | Total number of shares (or units) purchased as part of publicly announced plans or programs | Maximum number (or approximate dollar value) of shares (or units) that may yet be purchased under the plans or programs (2) |
|---------------------------------|---|--|---|---|
| October 1 - October 31, 2018(1) | 3,514 | \$ 34.58 | — | \$ 12,562,825 |
| Total | 3,514 | \$ 34.58 | — | \$ 12,562,825 |

- (1) These shares represent shares purchased other than through publicly announced plans and were purchased pursuant to the Company's stock incentive plans. Pursuant to the plans, shares were purchased from plan participants at the then current market value in satisfaction of stock option exercise prices, settlements of restricted stock and tax withholdings.
- (2) On August 5, 2016, the Company's Board of Directors authorized the repurchase of up to an additional \$50.0 million of common stock. Under this authorization, \$12,562,825 remained available for purchase at December 31, 2018.

Table of Contents

Securities Authorized for Issuance under Equity Compensation Plans

During the second quarter of 2014, shareholders approved the 2014 Omnibus Incentive Plan (the “2014 Plan”). Under the 2014 Plan, the Compensation Committee of the Board of Directors has the authority to grant, from time to time, awards of options, stock appreciation rights, restricted stock, restricted stock units, performance units, other stock-based awards, or any combination thereof to eligible persons. As of December 31, 2018, the aggregate number of Company common stock available for issuance under the 2014 Plan was 5,254,682 shares.

During the second quarter of 2015, shareholders approved the Company’s 2014 Employee Stock Purchase Plan (“ESPP”). The ESPP allows employees to purchase shares of common stock through payroll deductions up to a limit of \$25,000 per calendar year or 2,000 shares per offering period. The price an employee pays for shares is 90.0% of the fair market value of Company common stock on the last day of the offering period. As of December 31, 2018, the aggregate number of Company common stock available for issuance under the ESPP was 342,644 shares.

See note 16 to the consolidated financial statements for further detail related to these equity compensation plans.

| Plan Category | Number of securities to be issued upon exercise of outstanding options, warrants and rights | Weighted-average exercise price of outstanding options, warrants and rights | Number of securities remaining available for future issuance under equity compensation plans |
|---|---|---|--|
| Equity plans approved by security holders | 1,264,876 | \$ 22.33 | 5,597,326 |
| Equity plans not approved by security holders | — | — | — |
| Total | 1,264,876 | \$ 22.33 | 5,597,326 |

Item 6. SELECTED FINANCIAL DATA.

The following table sets forth summary selected historical financial information as of and for the five years ended December 31, 2018. The summary selected historical consolidated financial information set forth below is derived from our audited consolidated financial statements.

The summary of selected historical consolidated financial data set forth below is derived from our audited consolidated financial statements and should be read together with the related notes thereto as well as “Management’s Discussion and Analysis of Financial Condition and Results of Operations” included elsewhere in this annual report. Such information is not necessarily indicative of anticipated future results. All amounts are presented in thousands, except share data, or as otherwise noted.

Table of Contents

Summary of Selected Historical Consolidated Financial Data

| | December 31, 2018 | December 31, 2017 | December 31, 2016 | December 31, 2015 | December 31, 2014 |
|--|----------------------|----------------------|----------------------|----------------------|----------------------|
| Consolidated Statements of Financial Condition Data: | | | | | |
| Cash and cash equivalents | \$ 109,556 | \$ 257,364 | \$ 152,736 | \$ 166,092 | \$ 256,979 |
| Investment securities available-for-sale (at fair value) | 791,102 | 855,345 | 884,232 | 1,157,246 | 1,479,214 |
| Investment securities held-to-maturity | 235,398 | 258,730 | 332,505 | 427,503 | 530,590 |
| Non-marketable securities | 27,555 | 15,030 | 14,949 | 22,529 | 27,045 |
| Loans (1) | 4,092,308 | 3,178,947 | 2,860,921 | 2,587,673 | 2,162,409 |
| Allowance for loan losses | (35,692) | (31,264) | (29,174) | (27,119) | (17,613) |
| Loans, net | 4,056,616 | 3,147,683 | 2,831,747 | 2,560,554 | 2,144,796 |
| Loans held for sale | 48,120 | 4,629 | 24,187 | 13,292 | 5,146 |
| FDIC indemnification asset, net | — | — | — | — | 39,082 |
| Other real estate owned | 10,596 | 10,491 | 15,662 | 20,814 | 29,120 |
| Premises and equipment, net | 109,986 | 93,708 | 95,671 | 103,103 | 106,341 |
| Goodwill and other intangible assets, net | 128,497 | 61,237 | 66,579 | 72,059 | 76,513 |
| Other assets | 159,240 | 139,248 | 154,778 | 140,716 | 124,820 |
| Total assets | \$ 5,676,666 | \$ 4,843,465 | \$ 4,573,046 | \$ 4,683,908 | \$ 4,819,646 |
| Deposits | \$ 4,535,621 | \$ 3,979,559 | \$ 3,868,649 | \$ 3,840,677 | \$ 3,766,188 |
| Other liabilities | 446,039 | 331,499 | 168,208 | 225,687 | 258,883 |
| Total liabilities | 4,981,660 | 4,311,058 | 4,036,857 | 4,066,364 | 4,025,071 |
| Total shareholders' equity | 695,006 | 532,407 | 536,189 | 617,544 | 794,575 |
| Total liabilities and shareholders' equity | \$ 5,676,666 | \$ 4,843,465 | \$ 4,573,046 | \$ 4,683,908 | \$ 4,819,646 |

(1) Total loans are net of unearned discounts and deferred fees and costs.

Table of Contents

| | As of and for the years ended | | | | |
|---|-------------------------------|----------------------|----------------------|----------------------|----------------------|
| | December 31, 2018 | December 31, 2017 | December 31, 2016 | December 31, 2015 | December 31, 2014 |
| Consolidated Statements of Operations Data: | | | | | |
| Interest income | \$ 221,391 | \$ 164,421 | \$ 160,448 | \$ 171,407 | \$ 184,662 |
| Interest expense | 23,954 | 18,115 | 14,808 | 14,462 | 14,413 |
| Net interest income | 197,437 | 146,306 | 145,640 | 156,945 | 170,249 |
| Provision for loan losses | 5,197 | 12,972 | 23,651 | 12,444 | 6,209 |
| Net interest income after provision for loan losses | 192,240 | 133,334 | 121,989 | 144,501 | 164,040 |
| Non-interest income | 70,775 | 39,205 | 40,027 | 21,448 | (1,696) |
| Non-interest expense | 189,334 | 136,677 | 136,009 | 158,024 | 150,003 |
| Income before income taxes | 73,681 | 35,862 | 26,007 | 7,925 | 12,341 |
| Income tax expense | 12,230 | 21,283 | 2,947 | 3,044 | 3,165 |
| Net income | \$ 61,451 | \$ 14,579 | \$ 23,060 | \$ 4,881 | \$ 9,176 |
| Share Information(1): | | | | | |
| Income per share, basic | \$ 2.00 | \$ 0.54 | \$ 0.81 | \$ 0.14 | \$ 0.22 |
| Income per share, diluted | \$ 1.95 | \$ 0.53 | \$ 0.79 | \$ 0.14 | \$ 0.22 |
| Dividends paid | \$ 0.54 | \$ 0.34 | \$ 0.22 | \$ 0.20 | \$ 0.20 |
| Book value per share | \$ 22.59 | \$ 19.81 | \$ 20.32 | \$ 20.34 | \$ 20.43 |
| Tangible common book value per share(2) | \$ 18.77 | \$ 17.94 | \$ 18.15 | \$ 18.22 | \$ 18.63 |
| Total shareholders' equity to total assets | 12.24% | 10.99% | 11.72% | 13.18% | 16.49% |
| Tangible common equity to tangible assets(2) | 10.39% | 10.06% | 10.61% | 11.98% | 15.25% |
| Weighted average common shares outstanding, basic | 30,748,234 | 26,928,763 | 28,313,061 | 34,349,996 | 42,404,609 |
| Weighted average common shares outstanding, diluted | 31,430,074 | 27,709,659 | 29,091,343 | 34,363,487 | 42,421,014 |
| Common shares outstanding | 30,769,063 | 26,875,585 | 26,386,583 | 30,358,509 | 38,884,953 |

(1) Per share information is calculated based on the aggregate number of our shares of Class A common stock and Class B

non-voting
common
stock
outstanding.
During 2015,
all Class B
shares were
either
repurchased
by the
Company or
converted to
Class A
common
shares.

- (2) Tangible book
value per
share and
tangible
common
equity to
tangible assets
are
non-GAAP
financial
measures.
Tangible book
value per
share is
computed as
total
shareholders'
equity less
goodwill
(adjusted for
deferred
taxes) and
other
intangible
assets, net,
divided by
common
shares
outstanding at
the balance
sheet date.
For purposes
of computing
tangible
common
equity to

tangible
assets,
tangible
common
equity is
calculated as
common
shareholders'
equity less
goodwill
(adjusted for
deferred
taxes) and
other
intangible
assets, net,
and tangible
assets is
calculated as
total assets
less goodwill
(adjusted for
deferred
taxes) and
other
intangible
assets, net.
We believe
that the most
directly
comparable
GAAP
financial
measures are
book value
per share and
total
shareholders'
equity to total
assets. See the
reconciliation
under "About
Non-GAAP
Financial
Measures."

Table of Contents

| | As of and for the years ended | | | | |
|---|-------------------------------|----------------------|----------------------|----------------------|----------------------|
| | December 31, 2018 | December 31, 2017 | December 31, 2016 | December 31, 2015 | December 31, 2014 |
| Key Ratios | | | | | |
| Return on average assets | 1.10% | 0.31% | 0.50% | 0.10% | 0.19% |
| Return on average tangible assets(1) | 1.15% | 0.38% | 0.57% | 0.17% | 0.26% |
| Return on average tangible assets, adjusted(1)(8) | 1.26% | 0.82% | 0.57% | 0.17% | 0.26% |
| Return on average equity | 9.28% | 2.67% | 3.95% | 0.70% | 1.07% |
| Return on average tangible common equity(1) | 11.60% | 3.61% | 5.04% | 1.29% | 1.58% |
| Return on average tangible common equity, adjusted(1)(8) | 12.76% | 7.75% | 5.04% | 1.29% | 1.58% |
| Loans to deposits ratio (end of period) | 90.23% | 80.00% | 74.58% | 67.72% | 57.55% |
| Non-interest bearing deposits to total deposits (end of period) | 23.64% | 22.68% | 21.89% | 21.22% | 19.45% |
| Net interest margin(3) | 3.85% | 3.36% | 3.39% | 3.54% | 3.83% |
| Net interest margin FTE(1)(3)(8) | 3.93% | 3.50% | 3.49% | 3.60% | 3.85% |
| Interest rate spread FTE(4)(8) | 3.77% | 3.35% | 3.38% | 3.48% | 3.72% |
| Yield on earning assets(2) | 4.31% | 3.78% | 3.74% | 3.86% | 4.15% |
| Yield on earning assets FTE(1)(2)(8) | 4.40% | 3.91% | 3.84% | 3.92% | 4.17% |
| Cost of interest bearing liabilities(2) | 0.63% | 0.56% | 0.46% | 0.44% | 0.45% |
| Cost of deposits | 0.45% | 0.41% | 0.36% | 0.36% | 0.37% |
| Non-interest income (loss) to total revenue FTE | 25.95% | 20.49% | 21.09% | 11.84% | (1.00)% |
| Non-interest expense to average assets | 3.38% | 2.90% | 2.92% | 3.27% | 3.08% |
| Efficiency ratio | 69.78% | 70.80% | 70.30% | 85.55% | 85.82% |
| Efficiency ratio FTE(1)(8) | 68.64% | 68.63% | 68.79% | 84.28% | 85.35% |

| | | | | | |
|---|---------|---------|--------|---------|---------|
| Total Loans Asset Quality Data(5)(6)(7) | | | | | |
| Non-performing loans to total loans | 0.60% | 0.66% | 1.07% | 0.99% | 0.50% |
| Non-performing assets to total loans and OREO | 0.85% | 0.99% | 1.61% | 1.81% | 1.86% |
| Allowance for loan losses to total loans | 0.87% | 0.98% | 1.02% | 1.05% | 0.81% |
| Allowance for loan losses to non-performing loans | 145.94% | 148.88% | 94.98% | 105.74% | 162.89% |
| Net charge-offs to average loans | 0.02% | 0.36% | 0.80% | 0.12% | 0.05% |

- (1) Ratio represents non-GAAP financial measure. See non-GAAP reconciliation below.
- (2) Interest earning assets include assets that earn interest/accretion or dividends. Any market value adjustments on investment securities are excluded from interest-earning assets. Interest bearing liabilities include liabilities that must be paid interest.
- (3) Net interest margin represents net interest income, including accretion income on interest earning assets, as a percentage of average interest earning assets.
- (4) Interest rate spread represents the difference between the weighted average yield on interest earning assets and the weighted average cost of interest bearing liabilities.
- (5) Non-performing loans were redefined during the third quarter of 2014 to only include non-accrual loans and restructured loans on non-accrual, and exclude any loans accounted for under ASC 310-30 in which the pool is still performing. All previous periods have been restated.
- (6) Non-performing assets include non-performing loans, other real estate owned and other repossessed assets.
- (7) Total loans are net of unearned discounts and fees.
- (8) Presented on a fully taxable equivalent basis using the statutory rate of 21% for 2018 and 35% for prior years. The taxable equivalent adjustments included above are \$4,482, \$5,852, \$4,081, \$2,695, and \$930 for the years ended 2018, 2017, 2016, 2015, and 2014, respectively.

Table of Contents

About Non-GAAP Financial Measures

Certain of the financial measures and ratios we present, including “tangible assets,” “return on average tangible assets,” “return on average tangible common equity,” “tangible common book value,” “tangible common book value per share,” “tangible common equity,” “tangible common equity to tangible assets,” “adjusted non-interest expense,” “adjusted non-interest expense to average assets,” “adjusted net income,” “adjusted earnings per share - diluted,” “adjusted return on average tangible assets,” “adjusted return on average tangible common equity,” and “fully taxable equivalent (FTE)” metrics, are supplemental measures that are not required by, or are not presented in accordance with, U.S. generally accepted accounting principles (GAAP). We refer to these financial measures and ratios as “non-GAAP financial measures.” We consider the use of select non-GAAP financial measures and ratios to be useful for financial and operational decision making and useful in evaluating period-to-period comparisons. We believe that these non-GAAP financial measures provide meaningful supplemental information regarding our performance by excluding certain expenses or assets that we believe are not indicative of our primary business operating results or by presenting certain metrics on an FTE basis. We believe that management and investors benefit from referring to these non-GAAP financial measures in assessing our performance and when planning, forecasting, analyzing and comparing past, present and future periods.

These non-GAAP financial measures should not be considered a substitute for financial information presented in accordance with GAAP and you should not rely on non-GAAP financial measures alone as measures of our performance. The non-GAAP financial measures we present may differ from non-GAAP financial measures used by our peers or other companies. We compensate for these limitations by providing the equivalent GAAP measures whenever we present the non-GAAP financial measures and by including a reconciliation of the impact of the components adjusted for in the non-GAAP financial measure so that both measures and the individual components may be considered when analyzing our performance.

Table of Contents

A reconciliation of our GAAP financial measures to the comparable non-GAAP financial measures is as follows.

Tangible Common Book Value Ratios

| | December 31, 2018 | December 31, 2017 | December 31, 2016 | December 31, 2015 | December 31, 2014 |
|--|----------------------|----------------------|----------------------|----------------------|----------------------|
| Total shareholders' equity | \$ 695,006 | \$ 532,407 | \$ 536,189 | \$ 617,544 | \$ 794,575 |
| Less: goodwill and core deposit intangible assets, net | (124,941) | (61,237) | (66,580) | (72,060) | (76,513) |
| Add: deferred tax liability related to goodwill | 7,327 | 10,873 | 9,323 | 7,772 | 6,222 |
| Tangible common equity (non-GAAP) | \$ 577,392 | \$ 482,043 | \$ 478,932 | \$ 553,256 | \$ 724,284 |
| Total assets | \$ 5,676,666 | \$ 4,843,465 | \$ 4,573,046 | \$ 4,683,908 | \$ 4,819,646 |
| Less: goodwill and core deposit intangible assets, net | (124,941) | (61,237) | (66,580) | (72,060) | (76,513) |
| Add: deferred tax liability related to goodwill | 7,327 | 10,873 | 9,323 | 7,772 | 6,222 |
| Tangible assets (non-GAAP) | \$ 5,559,052 | \$ 4,793,101 | \$ 4,515,789 | \$ 4,619,620 | \$ 4,749,355 |
| Tangible common equity to tangible assets calculations: | | | | | |
| Total shareholders' equity to total assets | 12.24% | 10.99% | 11.72% | 13.18% | 16.49% |
| Less: impact of goodwill and core deposit intangible assets, net | (1.85)% | (0.93)% | (1.11)% | (1.20)% | (1.24)% |
| Tangible common equity to tangible assets (non-GAAP) | 10.39% | 10.06% | 10.61% | 11.98% | 15.25% |
| Tangible common book value per share calculations: | | | | | |
| | \$ 577,392 | \$ 482,043 | \$ 478,932 | \$ 553,256 | \$ 724,284 |

Edgar Filing: National Bank Holdings Corp - Form 10-K

| | | | | | |
|--|------------|------------|------------|------------|------------|
| Tangible common equity (non-GAAP) | | | | | |
| Divided by: ending shares outstanding | 30,769,063 | 26,875,585 | 26,386,583 | 30,358,509 | 38,884,953 |
| Tangible common book value per share (non-GAAP) | \$ 18.77 | \$ 17.94 | \$ 18.15 | \$ 18.22 | \$ 18.63 |
| Tangible common book value per share, excluding accumulated other comprehensive loss (income) (AOCI) calculations: | | | | | |
| Tangible common equity (non-GAAP) | \$ 577,392 | \$ 482,043 | \$ 478,932 | \$ 553,256 | \$ 724,284 |
| Accumulated other comprehensive loss (income), net of tax | 11,275 | 6,242 | 1,762 | (95) | (5,839) |
| Tangible common book value, excluding AOCI, net of tax (non-GAAP) | 588,667 | 488,285 | 480,694 | 553,161 | 718,445 |
| Divided by: ending shares outstanding | 30,769,063 | 26,875,585 | 26,386,583 | 30,358,509 | 38,884,953 |
| Tangible common book value per share, excluding AOCI, net of tax (non-GAAP) | \$ 19.13 | \$ 18.17 | \$ 18.22 | \$ 18.22 | \$ 18.48 |

Table of Contents

Return on Average Tangible Assets and Return on Average Tangible Equity

| | As of and for the years ended | | | | |
|--|-------------------------------|----------------------|----------------------|----------------------|----------------------|
| | December 31, 2018 | December 31, 2017 | December 31, 2016 | December 31, 2015 | December 31, 2014 |
| Net income | \$ 61,451 | \$ 14,579 | \$ 23,060 | \$ 4,881 | \$ 9,176 |
| Add: impact of core deposit intangible amortization expense, after tax | 1,649 | 3,259 | 3,343 | 3,295 | 3,260 |
| Net income adjusted for impact of core deposit intangible amortization expense, after tax | \$ 63,100 | \$ 17,838 | \$ 26,403 | \$ 8,176 | \$ 12,436 |
| Average assets | \$ 5,607,532 | \$ 4,705,241 | \$ 4,651,953 | \$ 4,831,070 | \$ 4,867,929 |
| Less: average goodwill and core deposit intangible asset, net of deferred tax liability related to goodwill | (118,546) | (52,958) | (59,977) | (66,549) | (73,074) |
| Average tangible assets (non-GAAP) | \$ 5,488,986 | \$ 4,652,283 | \$ 4,591,976 | \$ 4,764,521 | \$ 4,794,855 |
| Average shareholders' equity | \$ 662,420 | \$ 546,716 | \$ 583,686 | \$ 701,476 | \$ 860,691 |
| Less: average goodwill and core deposit intangible asset, net of deferred tax liability related to goodwill | (118,546) | (52,958) | (59,977) | (66,549) | (73,074) |
| Average tangible common equity (non-GAAP) | \$ 543,874 | \$ 493,758 | \$ 523,709 | \$ 634,927 | \$ 787,617 |
| Return on average assets | 1.10% | 0.31% | 0.50% | 0.10% | 0.19% |
| Return on average tangible assets (non-GAAP) | 1.15% | 0.38% | 0.57% | 0.17% | 0.26% |
| Return on average equity | 9.28% | 2.67% | 3.95% | 0.70% | 1.07% |
| Return on average tangible common equity (non-GAAP) | 11.60% | 3.61% | 5.04% | 1.29% | 1.58% |

Fully Taxable Equivalent Yield on Earning Assets and Net Interest Margin

| | As of and for the years ended | | | | |
|--|-------------------------------|----------------------|----------------------|----------------------|----------------------|
| | December 31, 2018 | December 31, 2017 | December 31, 2016 | December 31, 2015 | December 31, 2014 |

Edgar Filing: National Bank Holdings Corp - Form 10-K

| | | | | | |
|--|--------------|--------------|--------------|--------------|--------------|
| Interest income | \$ 221,391 | \$ 164,421 | \$ 160,448 | \$ 171,407 | \$ 184,662 |
| Add: impact of taxable equivalent adjustment | 4,482 | 5,852 | 4,081 | 2,695 | 930 |
| Interest income FTE (non-GAAP) | \$ 225,873 | \$ 170,273 | \$ 164,529 | \$ 174,102 | \$ 185,592 |
| Net interest income | \$ 197,437 | \$ 146,306 | \$ 145,640 | \$ 156,945 | \$ 170,249 |
| Add: impact of taxable equivalent adjustment | 4,482 | 5,852 | 4,081 | 2,695 | 930 |
| Net interest income FTE (non-GAAP) | \$ 201,919 | \$ 152,158 | \$ 149,721 | \$ 159,640 | \$ 171,179 |
| Average earning assets | \$ 5,131,694 | \$ 4,353,320 | \$ 4,290,171 | \$ 4,439,139 | \$ 4,446,903 |
| Yield on earning assets | 4.31% | 3.78% | 3.75% | 3.86% | 4.15% |
| Yield on earning assets FTE (non-GAAP) | 4.40% | 3.91% | 3.84% | 3.92% | 4.17% |
| Net interest margin | 3.85% | 3.36% | 3.39% | 3.54% | 3.83% |
| Net interest margin FTE (non-GAAP) | 3.93% | 3.50% | 3.49% | 3.60% | 3.85% |

Table of Contents

Efficiency Ratio

| | As of and for the year ended | | | | |
|---|------------------------------|-------------------|-------------------|-------------------|-------------------|
| | December 31, 2018 | December 31, 2017 | December 31, 2016 | December 31, 2015 | December 31, 2014 |
| Net interest income | \$ 197,437 | \$ 146,306 | \$ 145,640 | \$ 156,945 | \$ 170,249 |
| Add: impact of taxable equivalent adjustment | 4,482 | 5,852 | 4,081 | 2,695 | 930 |
| Net interest income, FTE (non-GAAP) | \$ 201,919 | \$ 152,158 | \$ 149,721 | \$ 159,640 | \$ 171,179 |
| Non-interest income | \$ 70,775 | \$ 39,205 | \$ 40,027 | \$ 21,448 | \$ (1,696) |
| Non-interest expense | \$ 189,334 | \$ 136,677 | \$ 136,009 | \$ 158,024 | \$ 150,003 |
| Less: core deposit intangible asset amortization | (2,170) | (5,342) | (5,480) | (5,401) | (5,344) |
| Non-interest expense, adjusted for core deposit intangible asset amortization | \$ 187,164 | \$ 131,335 | \$ 130,529 | \$ 152,623 | \$ 144,659 |
| Efficiency ratio | 69.78% | 70.80% | 70.30% | 85.55% | 85.82% |
| Efficiency ratio FTE (non-GAAP) | 68.64% | 68.63% | 68.79% | 84.28% | 85.35% |

Adjusted Financial Results

| | As of and for the years ended | | | | |
|--------------------------------|-------------------------------|-------------------|-------------------|-------------------|-------------------|
| | December 31, 2018 | December 31, 2017 | December 31, 2016 | December 31, 2015 | December 31, 2014 |
| Adjustments to net income: | | | | | |
| Net income | \$ 61,451 | \$ 14,579 | \$ 23,060 | \$ 4,881 | \$ 9,176 |
| Adjustments(1) | 6,321 | 20,430 | — | — | — |
| Adjusted net income (non-GAAP) | \$ 67,772 | \$ 35,009 | \$ 23,060 | \$ 4,881 | \$ 9,176 |

Edgar Filing: National Bank Holdings Corp - Form 10-K

Adjustments to earnings (loss)
per share:

| | | | | | |
|---|---------|---------|---------|---------|---------|
| Earnings per share | \$ 1.95 | \$ 0.53 | \$ 0.79 | \$ 0.14 | \$ 0.22 |
| Adjustments(1) | 0.21 | 0.73 | — | — | — |
| Adjusted earnings per share - diluted (non-GAAP) | \$ 2.16 | \$ 1.26 | \$ 0.79 | \$ 0.14 | \$ 0.22 |

Adjustments to return on
average tangible assets:

| | | | | | |
|---|-----------|-----------|-----------|-----------|-----------|
| Adjusted net income (non-GAAP) | \$ 67,772 | \$ 35,009 | \$ 23,060 | \$ 4,881 | \$ 9,176 |
| Add: impact of core deposit intangible amortization expense, after tax | 1,649 | 3,259 | 3,343 | 3,295 | 3,260 |
| Net income adjusted for impact of core deposit intangible amortization expense, after tax | 69,421 | 38,268 | 26,403 | 8,176 | 12,436 |
| Average tangible assets (non-GAAP) | 5,488,986 | 4,652,283 | 4,591,976 | 4,764,521 | 4,794,855 |
| Adjusted return on average tangible assets (non-GAAP) | 1.26% | 0.82% | 0.57% | 0.17% | 0.26% |

Adjustments to return on
average tangible common
equity:

| | | | | | |
|---|-----------|-----------|-----------|----------|-----------|
| Net income adjusted for impact of core deposit intangible amortization expense, after tax | \$ 69,421 | \$ 38,268 | \$ 26,403 | \$ 8,176 | \$ 12,436 |
| Average tangible common equity (non-GAAP) | 543,874 | 493,758 | 523,709 | 634,927 | 787,617 |
| Adjusted return on average tangible common equity (non-GAAP) | 12.76% | 7.75% | 5.04% | 1.29% | 1.58% |

(1) Adjustments:

Non-interest expense
adjustments:

| | | | | | |
|--|----------|----------|------|------|------|
| Acquisition-related(2) | \$ 7,957 | \$ 2,691 | \$ — | \$ — | \$ — |
| Tax reform bonus(3) | — | 491 | — | — | — |
| Total non-interest expense adjustments (non-GAAP) | \$ 7,957 | \$ 3,182 | \$ — | \$ — | \$ — |

Total pre-tax adjustments
(non-GAAP)

| | | | | | |
|-------------------------------------|----------|-----------|------|------|------|
| Collective tax expense impact | (1,636) | (1,209) | — | — | — |
| Deferred tax asset remeasurement | — | 18,457 | — | — | — |
| Adjustments (non-GAAP) | \$ 6,321 | \$ 20,430 | \$ — | \$ — | \$ — |

(2) Represents non-recurring acquisition expenses in 2018 and 2017 related to the Peoples acquisition.

- (3) Represents a special \$1,000 bonus payment to 491 associates made in connection with the Tax Cuts and Jobs Act enacted in 2017.

42

Table of Contents

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

The following management's discussion and analysis of our financial condition and results of operations should be read in conjunction with our consolidated financial statements and related notes as of and for the years ended December 31, 2018, 2017, and 2016, and with the other financial and statistical data presented in this annual report. This discussion and analysis contains forward-looking statements that involve risks, uncertainties and assumptions that may cause actual results to differ materially from management's expectations. Factors that could cause such differences are discussed in the section entitled "Cautionary Note Regarding Forward-Looking Statements" and "Risk Factors" and should be read herewith.

All amounts are in thousands, except share and per share data, or as otherwise noted.

Overview

Our focus is on building strong banking relationships with small- to medium-sized businesses and consumers, while maintaining a low risk profile designed to generate reliable income streams and attractive returns. We have established a solid financial services franchise with a sizable presence for deposit gathering and building client relationships necessary for growth. We believe that our established presence in core markets that are outperforming national averages positions us well for growth opportunities. As of December 31, 2018, we had \$5.7 billion in assets, \$4.1 billion in loans, \$4.5 billion in deposits and \$0.7 billion in equity.

Operating Highlights and Key Challenges

Beginning in the first quarter 2018, loans previously referred to as "non 310-30 loans" are referred to as "originated and acquired loans," which include originated loans and acquired loans not accounted for under ASC 310-30. No amounts were reclassified resulting from this change in terminology.

On January 1, 2018, the Company completed its acquisition of Peoples, Inc. ("Peoples"), the bank holding company of Colorado-based Peoples National Bank and Kansas-based Peoples Bank. At the close of the acquisition, the Company acquired 20 banking centers located in the highly-attractive and geographically-relevant markets of Colorado Springs in Colorado, Overland Park and Lawrence in Kansas, and Taos and Albuquerque in New Mexico, and an in-market mortgage origination business. At the acquisition date, \$842 million was added to total assets, net of Federal Home Loan Bank ("FHLB") payoffs, \$543 million in loans and \$730 million in deposits. The merger consideration totaled \$146.4 million and consisted of \$110.2 million in Company stock and \$36.2 million in cash. All operating systems

were converted during the first half of 2018.

Increased profitability and returns

Net income was \$61.5 million, or \$1.95 per diluted share, for 2018, compared to net income of \$14.6 million, or \$0.53 per diluted share, for 2017. Net income during 2018 included \$6.3 million, after tax, of expenses related to the acquisition of Peoples. Adjusting for these expenses, net income would have been \$67.8 million, or \$2.16 per diluted share.

The return on average tangible assets was 1.15% for 2018, compared to 0.38% for 2017. Adjusting for the one-time expense items above, the return on average tangible assets was 1.26% for 2018, compared to 0.82% for 2017.

The return on average tangible common equity was 11.60% for 2018, compared to 3.61% for 2017. Adjusting for the one-time expense items above, the return on average tangible common equity was 12.76% for 2018, compared to 7.75% for 2017.

Strategic execution

Completed the acquisition of Peoples on January 1, 2018.

Announced expansion into Utah in January 2019, with a focus on serving commercial and business banking clients in the Salt Lake City's Wasatch Front.

Table of Contents

Originated loans and acquired loans exceeded \$4.0 billion for the first time in the Company's history at December 31, 2018, increasing \$963.1 million, or 31.5%, since prior year led by originated and acquired commercial loan growth of \$779.0 million, or 42.2%.

Maintained a conservatively structured loan portfolio represented by diverse industries and concentrations with most industry sector concentrations at 5% or less of total loans and all concentration levels remain well below our self-imposed limits.

Continued to build and deepen relationships with our clients resulting in strong average deposit growth of \$717.7 million since December 31, 2017, due in part to the Peoples acquisition as well as to demand, savings, and money market deposit ("transaction deposits") growth during the period.

Loan portfolio

Total loans ended the year at \$4.1 billion and increased \$913.4 million, or 28.7%, since December 31, 2017, driven by the Peoples acquisition and new loan originations of a record \$1.2 billion, led by commercial and industrial loan originations of \$909.6 million.

Originated loans increased \$615.6 million, or 20.8%, due to a 35.4% increase in commercial loans, partially offset by expected payoffs of non-owner occupied commercial real estate.

Credit quality

Credit quality remained strong, as non-performing loans (comprised of non-accrual loans and non-accrual TDRs) were 0.60% of total loans at December 31, 2018 compared to 0.66% at December 31, 2017. Non-performing assets to total loans and OREO totaled 0.85% at December 31, 2018 compared to 0.99% at December 31, 2017. Net charge-offs totaled 0.02%, compared to 0.36% in the prior year.

Provision for loan losses on originated and acquired loans totaled \$5.0 million during 2018, compared to \$13.1 million in the prior year, a decrease of \$8.1 million. The current provision was recorded to support the increase in originated loans.

Client deposit funded balance sheet

Total deposits averaged \$4.6 billion during the fourth quarter of 2018, increasing \$600.2 million, or 14.9%, compared to the fourth quarter of 2017. The increase was driven by \$729.9 million in total deposits added on January 1, 2018 from the Peoples acquisition, coupled with transaction deposit growth.

Demand deposits averaged \$1.1 billion during the fourth quarter of 2018 and grew \$170.8 million, or 18.3%, compared to the fourth quarter of 2017 due to organic growth and the Peoples acquisition.

Average transaction deposits totaled \$3.5 billion during the fourth quarter of 2018, increasing \$629.1 million, or 21.8%, for the fourth quarter of 2018 compared to the fourth quarter of 2017.

Time deposits averaged \$1.1 billion during the fourth quarter of 2018, decreasing \$28.9 million, compared to the fourth quarter of 2017. An increase from the Peoples acquisition was offset by a decrease from legacy accounts. The mix of transaction deposits to total deposits improved to 76.2% at December 31, 2018 from 71.9% at December 31, 2017 due to the Peoples acquisition and our continued focus on developing long-term banking relationships.

Cost of deposits totaled 0.45%, increasing from 0.41% in the prior year, due to higher cost of savings, money market and time deposits.

Revenues

Fully taxable equivalent (FTE) net interest income totaled \$201.9 million and increased \$49.8 million, or 32.7% compared to prior year.

The FTE net interest margin widened 0.43% to 3.93% from 2017 as the yield on earning assets increased 0.49%, led by a 0.44% increase in the originated portfolio yields due to short-term rate increases, partially offset by an increase in the cost of deposits of 0.04%. Our ability to maintain a low deposit beta during 2018 was a key contributor in the expansion of our net interest margin.

Non-interest income totaled \$70.8 million, increasing \$31.6 million from prior year primarily due to the Peoples acquisition.

Table of Contents

Expenses

Non-interest expense totaled \$189.3 million, representing an increase of \$52.7 million from prior year, primarily driven by the Peoples acquisition. Included in 2018 were \$8.0 million of pre-tax acquisition costs compared to \$3.2 million for the year ended December 31, 2017.

Income tax expense totaled \$12.2 million during 2018 compared to \$21.3 million during 2017, a decrease of \$9.1 million. Included in income tax expense was \$1.3 million and \$4.2 million of tax benefits from stock compensation activity during 2018 and 2017, respectively. In addition, income tax expense during 2017 included an \$18.5 million non-cash, one-time charge related to the deferred tax asset re-measurement, due to the Tax Cuts and Jobs Act (the "Act"). Adjusting for the above mentioned stock compensation activity and deferred tax assets re-measurement, the effective tax rate for 2018 would be 18.3% compared to an adjusted 2017 rate of 19.7%.

Strong capital position

Capital ratios are strong as our capital position remains in excess of federal bank regulatory thresholds. As of December 31, 2018, our consolidated tier 1 leverage ratio was 10.5% and our consolidated tier 1 risk-based capital and common equity tier 1 risk-based capital ratios were both 12.9%.

At December 31, 2018, common book value per share was \$22.59, while tangible common book value per share was \$18.77, or \$19.40 after consideration of the excess accretable yield value of \$0.63 per share.

Since early 2013, we have repurchased 26.6 million shares, or 50.9% of the outstanding shares, at an attractive weighted average price of \$20.03 per share.

Key Challenges

There are a number of significant challenges confronting us and our industry. We began banking operations in 2010 by acquiring distressed financial institutions, and sought to rebuild them and implement operational efficiencies across the enterprise as a whole. We face continual challenges implementing our business strategy, including growing the assets, particularly loans, and deposits of our business amidst intense competition, raising interest rates from an extended low interest rate environment, adhering to changes in the regulatory environment and identifying and consummating disciplined acquisition and other expansionary opportunities in a very competitive environment.

General economic conditions remained stable in 2018. Residential real estate values remain strong in our markets and nationally, with many markets, including Denver, hitting new post-crisis highs. Commercial real estate property fundamentals also remain strong, with stable occupancy and increasing lease rates, along with cyclically low capitalization rates leading to increasing valuations. A significant portion of our loan portfolio is secured by real estate

and any deterioration in real estate values or credit quality or elevated levels of non-performing assets would ultimately have a negative impact on the quality of our loan portfolio.

The agriculture industry is in the fourth year of depressed commodity prices. Our food and agriculture portfolio is only 5.6% of total loans and is well-diversified across food production, crop and livestock types. Crop and livestock loans represent 23.1% of the food and agriculture loan portfolio. We have maintained relationships with agriculture clients that generally possess low leverage and, correspondingly, low bank debt to assets, minimizing any potential credit losses in the future.

Our originated and acquired loans outstanding portfolio at December 31, 2018 totaled \$4.0 billion, representing an increase of \$963.1 million, or 31.5% compared to December 31, 2017, driven by Peoples acquired loans and a record \$1.2 billion in loan originations in 2018, partially offset by loan paydowns and payoffs during 2018. Our 310-30 loans have produced higher yields than our originated and acquired loans, due to accretion of fair value adjustments. During 2018, our weighted average rate on new loans funded at the time of origination was 5.20% (fully taxable equivalent), compared to the weighted average yield of our originated loan portfolio of 4.50% (fully taxable equivalent). Fully taxable equivalent net interest income reached an inflection point in the second quarter of 2017 and continued through the fourth quarter of 2018 as the yields and volumes of originated and acquired loans outpaced the decrease in higher yielding 310-30 loan balances. The inflection point was driven by both the strong new loan originations as well as the short-term market rate increases in 2017 and 2018. Future

Table of Contents

growth in our interest income will ultimately be dependent on our ability to continue to generate sufficient volumes of high-quality originated loans.

Continued regulation, impending new liquidity and capital constraints, and a continual need to bolster cybersecurity are adding costs and uncertainty to all U.S. banks and could affect profitability. Also, nontraditional participants in the market may offer increased competition as non-bank payment businesses are expanding into traditional banking products. While certain external factors are out of our control and may provide obstacles to our business strategy, we are prepared to deal with these challenges. We seek to remain flexible, yet methodical and proactive, in our strategic decision making so that we can quickly respond to market changes and the inherent challenges and opportunities that accompany such changes.

Application of Critical Accounting Policies

We use accounting principles and methods that conform to GAAP and general banking practices. We are required to apply significant judgment and make material estimates in the preparation of our financial statements and with regard to various accounting, reporting and disclosure matters. Assumptions and estimates are required to apply these principles where actual measurement is not possible or practical. The most significant of these estimates relate to the accounting for acquired loans and the determination of the ALL. These critical accounting policies and estimates are summarized below, and are further analyzed with other significant accounting policies in note 2 – Summary of Significant Accounting Policies in the notes to our consolidated financial statements for the year ended December 31, 2018.

Accounting for Acquired Loans

Included in our loan portfolio are originated loans and acquired loans. The estimated fair values of acquired loans at the acquisition date are based on a discounted cash flow methodology that considers various factors, including the type of loan or pool of loans with similar characteristics, and related collateral, classification status, fixed or variable interest rate, maturity and any prepayment terms of the loan, whether or not the loan is amortizing, and a discount rate reflecting our assessment of risk inherent in the cash flow estimates. The determination of the fair value of acquired loans takes into account credit quality deterioration and probability of loss, and as a result the related allowance for loan losses is not carried forward at the time of acquisition.

A significant portion of the loans acquired in the Hillcrest Bank, Bank of Choice, and Community Banks of Colorado acquisitions had deteriorated credit quality at the date of acquisition and management accounted for all loans acquired through these acquisitions under ASC 310-30 (with the exception of loans with revolving privileges, which were outside the scope of ASC 310-30). These loans are grouped into pools based on purpose and/or type of loan, geography and risk rating, and take into account the sources of repayment and collateral. Each pool is accounted for as

a single loan for which the integrity is maintained throughout the life of the asset. When a pool exhibits evidence of credit deterioration since origination and it is probable at the date of acquisition that we will not collect all principal and interest payments in accordance with the terms of the loan agreement, the expected shortfall in the expected future cash flows compared to the contractual amount due is recognized as a non-accretable difference. Any excess of the expected future cash flows over the acquisition date fair value is known as the accretable discount, or accretable yield, and through accretion is recognized as interest income over the remaining life of the respective pool. Contractual fees not expected to be collected are not included in ASC 310-30 contractual cash flows. Should fees be subsequently collected, the cash flows are accounted for as originated and acquired fee income in the period they are received. Loans that meet the criteria for non-accrual of interest at the time of acquisition may be considered performing at and subsequent to acquisition, regardless of whether the client is contractually delinquent, if the timing and expected cash flows on such loans can be reasonably estimated and if collection of the new carrying value of such loans is expected. If the timing and expected cash flows of a pool cannot be reasonably estimated, that pool may be placed on non-accrual status, the accretion of income will cease, and interest income will be recognized on a cash basis. In addition, a pool will be accounted for on a cash basis to the extent the remaining discount on the pool is equal its unpaid principal balance.

Loan pools accounted for under ASC 310-30 are periodically remeasured to determine expected future cash flows. In determining the expected cash flows, we evaluate the credit profile, contractual interest rates, collateral values and expected prepayments of the loan pools. Prepayment assumptions are based on statistical models that take into account factors such as the loan interest rate, credit profile of the borrowers, the years in which the loans were originated, and whether the loans were

Table of Contents

fixed or variable rate loans. Decreases to the expected future cash flows in the applicable pool generally result in an immediate provision for loan losses charged to the consolidated statements of operations. Conversely, subsequent increases in the expected future cash flows result in a transfer from the non-accretable difference to the accretable yield, which is then accreted as a yield adjustment over the remaining life of the pool once any previously recorded impairment expense has been recouped. These cash flow estimations are inherently subjective as they require material estimates, all of which may be susceptible to significant change.

Loans outside the scope of ASC 310-30 are accounted for under ASC Topic 310, Receivables. Discounts created when the loans are recorded at their estimated fair values at acquisition are accreted over the remaining life of the loan as an adjustment to the respective loan's yield. Similar to originated loans, the accrual of interest income is discontinued on acquired loans that are not accounted for under ASC 310-30 when the collection of principal or interest, in whole or in part, is doubtful. Interest is not accrued on loans 90 days or more past due unless they are well secured and in the process of collection.

Allowance for Loan Losses

The determination of the ALL, which represents management's estimate of probable losses inherent in our loan portfolio at the balance sheet date, including acquired loans to the extent necessary, involves a high degree of judgment and complexity. The determination of the ALL takes into consideration, among other matters, the estimated fair value of the underlying collateral, economic conditions, particularly as such conditions relate to the market areas in which we operate, historical net loan losses and other factors that warrant recognition. Any change in these factors, or the rise of any other factors that we, or our regulators, may deem necessary to consider when estimating the ALL, may materially affect the ALL and provisions for loan losses. For further discussion of the ALL, see “—Financial Condition—Asset Quality” and “—Financial Condition—Allowance for Loan Losses” and notes 2 and 8 to our consolidated financial statements.

Financial Condition

Total assets increased to \$5.7 billion at December 31, 2018 from \$4.8 billion at December 31, 2017. Total loans were \$4.1 billion at December 31, 2018, and grew \$913.4 million, or 28.7% from December 31, 2017. Originated and acquired loans outstanding totaled \$4.0 billion and increased \$963.1 million, or 31.5%, from December 31, 2017 driven by the Peoples acquisition and originated loan growth. We originated a record \$1.2 billion in loans during 2018, led by commercial originations of \$909.6 million. The acquired 310-30 loan portfolio declined \$49.7 million, or 41.2%, from December 31, 2017. During 2018, loans held for sale grew \$43.5 million compared to 2017 due to the addition of the Peoples mortgage business. Cash and cash equivalents totaled \$109.6 million and decreased \$147.8 million, or 57.4%, from December 31, 2017 due to cash held for the Peoples acquisition at December 31, 2017 and cash used to fund loan growth. The investment securities portfolio decreased \$87.6 million, or 7.9%, to \$1.0 billion at December 31, 2018, due to paydowns within the portfolio. During 2018, transaction deposits increased \$593.6 million, or 20.7%, while time deposits decreased \$37.5 million, or 3.4%. FHLB advances increased \$172.5 million,

when compared to December 31, 2017, to fund new loan originations.

Investment Securities

Available-for-sale

Total investment securities available-for-sale were \$791.1 million at December 31, 2018, compared to \$855.3 million at December 31, 2017, a decrease of \$64.2 million, or 7.5%. During 2018 and 2017, sales of investment securities available-for-sale totaled \$33.6 million and \$0.0 million, respectively. During 2018 and 2017, maturities and pay downs of available-for-sale securities totaled \$216.1 million and \$224.3 million, respectively. Purchases of available-for-sale securities during 2018 and 2017 totaled \$40.7 million and \$202.7 million, respectively.

Table of Contents

Our available-for-sale investment securities portfolio is summarized as follows for the periods indicated:

| | December 31, 2018 | | | | December 31, 2017 | | | |
|--|-------------------|------------|----------------------|------------------------|-------------------|------------|----------------------|------------------------|
| | Amortized cost | Fair value | Percent of portfolio | Weighted average yield | Amortized cost | Fair value | Percent of portfolio | Weighted average yield |
| Mortgage-backed securities: | | | | | | | | |
| Residential mortgage pass-through securities issued or guaranteed by U.S. Government agencies or sponsored enterprises | \$ 147,283 | \$ 146,642 | 18.5% | 2.53% | \$ 167,269 | \$ 168,648 | 19.8% | 2.39% |
| Other residential MBS issued or guaranteed by U.S. Government agencies or sponsored enterprises | 661,354 | 643,381 | 81.3% | 2.15% | 702,107 | 685,230 | 80.1% | 1.93% |
| Municipal securities | 619 | 610 | 0.1% | 3.67% | 1,054 | 1,048 | 0.1% | 2.60% |
| Other securities | 469 | 469 | 0.1% | 0.00% | 419 | 419 | 0.0% | 0.00% |
| Total investment securities available-for-sale | \$ 809,725 | \$ 791,102 | 100.0% | 2.22% | \$ 870,849 | \$ 855,345 | 100.0% | 2.02% |

As of December 31, 2018 and 2017, generally the entire available-for-sale investment portfolio was backed by mortgages. The residential mortgage pass-through securities portfolio is comprised of both fixed rate and adjustable rate Federal Home Loan Mortgage Corporation (“FHLMC”), Federal National Mortgage Association (“FNMA”) and Government National Mortgage Association (“GNMA”) securities. The other mortgage-backed securities are comprised of securities backed by FHLMC, FNMA and GNMA securities.

At December 31, 2018 and 2017, adjustable rate securities comprised 3.7% and 4.9%, respectively, of the available-for-sale MBS portfolio. The remainder of the portfolio was comprised of fixed rate amortizing securities with 10 to 30 year contractual maturities, with a weighted average coupon of 2.39% per annum and 2.18% per annum at December 31, 2018 and 2017, respectively.

Edgar Filing: National Bank Holdings Corp - Form 10-K

The available-for-sale investment portfolio included \$20.9 million and \$18.2 million of gross unrealized losses at December 31, 2018 and 2017, respectively, which were partially offset by \$2.3 million and \$2.7 million of gross unrealized gains, respectively. We believe any unrecognized losses are a result of prevailing interest rates, and as such, we do not believe that any of the securities with unrealized losses were other-than-temporarily-impaired.

Held-to-maturity

At December 31, 2018, we held \$235.4 million of held-to-maturity investment securities, compared to \$258.7 million at December 31, 2017, a decrease of \$23.3 million, or 9.0%. During 2018 and 2017, maturities and paydowns of held-to-maturity securities totaled \$61.9 million and \$71.1 million, respectively. Purchases of held-to-maturity securities totaled \$40.2 million during 2018.

Held-to-maturity investment securities are summarized as follows as of the date indicated:

| | December 31, 2018 | | | | December 31, 2017 | | | |
|--|-------------------|------------|----------------------|------------------------|-------------------|------------|----------------------|------------------------|
| | Amortized cost | Fair value | Percent of portfolio | Weighted average yield | Amortized cost | Fair value | Percent of portfolio | Weighted average yield |
| Mortgage-backed securities: | | | | | | | | |
| Residential mortgage pass-through securities issued or guaranteed by U.S. Government agencies or sponsored enterprises | \$ 157,115 | \$ 154,412 | 66.7% | 3.24% | \$ 204,352 | \$ 204,048 | 79.0% | 3.23% |
| Other residential MBS issued or guaranteed by U.S. Government agencies or sponsored enterprises | 78,283 | 76,514 | 33.3% | 2.25% | 54,378 | 52,723 | 21.0% | 1.66% |
| | \$ 235,398 | \$ 230,926 | 100.0% | 2.91% | \$ 258,730 | \$ 256,771 | 100.0% | 2.90% |

Total investment
securities
held-to-maturity

48

Table of Contents

The residential mortgage pass-through and other residential MBS held-to-maturity investment portfolios are comprised of fixed rate FHLMC, FNMA and GNMA securities.

The fair value of the held-to-maturity investment portfolio was \$230.9 million and \$256.8 million, at December 31, 2018 and 2017, respectively, and included \$4.5 million and \$2.0 million of net unrealized losses for the respective periods. We believe any unrecognized losses are a result of prevailing interest rates, and as such, we do not believe that any of the securities with unrealized losses were other-than-temporarily-impaired.

Loans Overview

At December 31, 2018, our loan portfolio was comprised of new loans that we have originated and loans that were acquired in connection with our six acquisitions to date. Beginning in the first quarter 2018, loans previously referred to as "non 310-30 loans" are referred to as "originated and acquired loans," which include originated loans and acquired loans not accounted for under ASC 310-30. No amounts were reclassified resulting from this change in terminology.

As discussed in note 2 to our consolidated financial statements, in accordance with applicable accounting guidance, all acquired loans are recorded at fair value at the date of acquisition, and an allowance for loan losses is not carried over with the loans but, rather, the fair value of the loans encompasses both credit quality and contractual interest rate considerations. Loans that exhibit signs of credit deterioration at the date of acquisition are accounted for in accordance with the provisions of ASC 310-30. Management accounted for all loans acquired in the Hillcrest Bank, Bank of Choice and Community Banks of Colorado acquisitions under ASC 310-30, with the exception of loans with revolving privileges, which were outside the scope of ASC 310-30. In our Bank Midwest transaction, we did not acquire all of the loans of the former Bank Midwest but, rather, selected certain loans based upon specific criteria of performance, adequacy of collateral, and loan type that were performing at the time of acquisition. As a result, none of the loans acquired in the Bank Midwest transaction are accounted for under ASC 310-30 nor are any of the loans acquired in the Pine River or Peoples acquisitions.

Table of Contents

The table below shows the loan portfolio composition and the breakout of the portfolio between originated loans, acquired loans, and ASC 310-30 loans at the respective dates:

| | December 31, 2018 | December 31, 2017 | December 31, 2018 vs. December 31, 2017 % Change |
|---|-------------------|-------------------|--|
| Originated: | | | |
| Commercial: | | | |
| Commercial and industrial | \$ 1,877,221 | \$ 1,375,028 | 36.5% |
| Owner-occupied commercial real estate | 337,258 | 264,357 | 27.6% |
| Food and agriculture | 217,294 | 135,397 | 60.5% |
| Energy | 49,204 | 57,460 | (14.4)% |
| Total commercial | 2,480,977 | 1,832,242 | 35.4% |
| Commercial real estate non-owner occupied | 407,431 | 464,121 | (12.2)% |
| Residential real estate | 657,633 | 633,578 | 3.8% |
| Consumer | 22,895 | 23,398 | (2.1)% |
| Total originated | 3,568,936 | 2,953,339 | 20.8% |
| Acquired: | | | |
| Commercial: | | | |
| Commercial and industrial | 53,926 | 994 | >100% |
| Owner-occupied commercial real estate | 84,408 | 8,396 | >100% |
| Food and agriculture | 4,862 | 3,498 | 39.0% |
| Total commercial | 143,196 | 12,888 | >100% |
| Commercial real estate non-owner occupied | 144,388 | 21,020 | >100% |
| Residential real estate | 163,187 | 69,900 | >100% |
| Consumer | 1,722 | 1,177 | 46.3% |
| Total acquired | 452,493 | 104,985 | >100% |
| ASC 310-30 loans | 70,879 | 120,623 | (41.2)% |
| Total loans | \$ 4,092,308 | \$ 3,178,947 | 28.7% |

Our loan portfolio totaled \$4.1 billion at December 31, 2018, increasing \$913.4 million, or 28.7%, year-over-year on the strength of a record \$1.2 billion in loan originations between the two periods. The strong originations were the result of continued market penetration benefiting from our focus on building client relationships. Originated and acquired loans outstanding totaled \$4.0 billion, representing an increase of \$963.1 million, or 31.5%, year-over-year, driven by Peoples acquired loans and an increase in originated loans of \$615.6 million, or 20.8%. The acquired 310-30 loan portfolio declined \$49.7 million, or 41.2%, from December 31, 2017, largely due to the transfer of one large acquired 310-30 problem loan transferred to OREO and sold during 2018 as part of the asset resolution process.

We have successfully generated new relationships with small- to medium-sized businesses and consumers, experiencing particularly strong loan growth in our commercial and industrial portfolio, which, at December 31, 2018, was comprised of diverse industry segments. These segments included government and municipal loans of \$501.0 million, finance and financial services loans, primarily lender finance, of \$355.2 million, healthcare-related loans of \$194.7 million, manufacturing-related loans of \$138.2 million, and a variety of smaller subcategories of commercial

and industrial loans.

Originated and acquired non-owner occupied CRE loans were 89.0% of the Company's risk based capital, or 13.5% of total loans, and no specific property type comprised more than 4.0% of total loans. The Company maintains very little exposure to retail properties, comprising less than 2.2% of total loans. Multi-family loans totaled \$56.7 million, or 1.4% of total loans as of December 31, 2018. Originated and acquired food and agriculture loans totaled \$222.2 million and were 35.8% of the Company's risk-based capital and 5.4% of total loans, and are well diversified across food production, crop and livestock types as of December 31, 2018.

When considering the loan portfolio in its entirety, 77.0% of loans were located within our footprint of Colorado, the greater Kansas City region, New Mexico, Texas and Utah as of December 31, 2018, based on the domicile of the borrower or, in the case of collateral-dependent loans, the geographical location of the collateral.

Table of Contents

New loan origination is a direct result of our ability to recruit and retain top banking talent, connect with clients in our markets and provide needed services at competitive rates. Loan originations totaled a record \$1.2 billion during 2018, led by commercial loan originations of \$909.6 million. Originations are defined as closed end funded loans and revolving lines of credit advances, net of any current period paydowns. Management utilizes this more conservative definition of originations to better approximate the impact of originations on loans outstanding and ultimately net interest income. The following tables represent new loan originations during 2018 and 2017:

| | Fourth quarter 2018 | Third quarter 2018 | Second quarter 2018 | First quarter 2018 | Total 2018 |
|---|------------------------|-----------------------|------------------------|-----------------------|---------------|
| Commercial: | | | | | |
| Commercial and industrial | \$ 213,335 | \$ 123,440 | \$ 232,643 | \$ 123,984 | \$ 693,402 |
| Owner occupied commercial real estate | 34,727 | 35,549 | 19,009 | 23,576 | 112,861 |
| Food and agriculture | 14,046 | 23,833 | 38,220 | 25,873 | 101,972 |
| Energy | 7,640 | 5,412 | (929) | (10,778) | 1,345 |
| Total commercial | 269,748 | 188,234 | 288,943 | 162,655 | 909,580 |
| Commercial real estate non-owner occupied | 41,031 | 42,300 | 28,316 | 20,694 | 132,341 |
| Residential real estate | 51,017 | 40,293 | 30,259 | 21,698 | 143,267 |
| Consumer | 2,592 | 3,797 | 3,588 | 3,238 | 13,215 |
| Total | \$ 364,388 | \$ 274,624 | \$ 351,106 | \$ 208,285 | \$ 1,198,403 |

Included in originations are net fundings under revolving lines of credit of \$6,263, \$34,070, \$151,888, and \$59,236 as of the fourth quarter 2018, third quarter 2018, second quarter 2018 and first quarter 2018, respectively.

| | Fourth quarter 2017 | Third quarter 2017 | Second quarter 2017 | First quarter 2017 | Total 2017 |
|---|------------------------|-----------------------|------------------------|-----------------------|---------------|
| Commercial: | | | | | |
| Commercial and industrial | \$ 167,699 | \$ 73,917 | \$ 159,340 | \$ 114,414 | \$ 515,370 |
| Owner occupied commercial real estate | 8,937 | 32,787 | 6,899 | 16,988 | 65,611 |
| Food and agriculture | 14,050 | 3,335 | 16,696 | (3,644) | 30,437 |
| Energy | (8,121) | (6,993) | 9,120 | (81) | (6,075) |
| Total Commercial | 182,565 | 103,046 | 192,055 | 127,677 | 605,343 |
| Commercial real estate non-owner occupied | 21,323 | 46,654 | 47,312 | 36,962 | 152,251 |
| Residential real estate | 25,995 | 28,471 | 26,979 | 29,616 | 111,061 |
| Consumer | 1,815 | 3,122 | 3,233 | 2,378 | 10,548 |
| Total | \$ 231,698 | \$ 181,293 | \$ 269,579 | \$ 196,633 | \$ 879,203 |

Edgar Filing: National Bank Holdings Corp - Form 10-K

Included in originations are net fundings under revolving lines of credit of \$65,686, \$(12,804), \$68,305 and \$33,397 as of the fourth quarter 2017, third quarter 2017, second quarter 2017 and first quarter 2017, respectively.

The tables below show the contractual maturities of our loans for the dates indicated:

| | December 31, 2018 | | | Total |
|---|----------------------|-----------------------------------|----------------------|--------------|
| | Due within 1 year | Due after 1 but within 5 years | Due after 5 years | |
| Commercial: | | | | |
| Commercial and industrial | \$ 191,088 | \$ 844,015 | \$ 896,910 | \$ 1,932,013 |
| Owner occupied commercial real estate | 37,284 | 124,289 | 273,737 | 435,310 |
| Food and agriculture | 53,845 | 143,909 | 30,290 | 228,044 |
| Energy | 9,397 | 39,807 | — | 49,204 |
| Total commercial | 291,614 | 1,152,020 | 1,200,937 | 2,644,571 |
| Commercial real estate non-owner occupied | 87,581 | 330,282 | 174,349 | 592,212 |
| Residential real estate | 30,376 | 56,914 | 743,525 | 830,815 |
| Consumer | 7,748 | 12,997 | 3,965 | 24,710 |
| Total loans | \$ 417,319 | \$ 1,552,213 | \$ 2,122,776 | \$ 4,092,308 |

Table of Contents

| | December 31, 2017 | | | Total |
|---|----------------------|-----------------------------------|----------------------|--------------|
| | Due within 1 year | Due after 1 but within 5 years | Due after 5 years | |
| Commercial: | | | | |
| Commercial and industrial | \$ 83,314 | \$ 551,567 | \$ 745,746 | \$ 1,380,627 |
| Owner occupied commercial real estate | 18,044 | 115,421 | 156,306 | 289,771 |
| Food and agriculture | 14,513 | 102,390 | 29,845 | 146,748 |
| Energy | 25,970 | 31,489 | — | 57,459 |
| Total commercial | 141,841 | 800,867 | 931,897 | 1,874,605 |
| Commercial real estate non-owner occupied | 118,980 | 316,242 | 127,827 | 563,049 |
| Residential real estate | 6,820 | 38,824 | 670,593 | 716,237 |
| Consumer | 5,909 | 15,014 | 4,133 | 25,056 |
| Total loans | \$ 273,550 | \$ 1,170,947 | \$ 1,734,450 | \$ 3,178,947 |

The stated interest rate (which excludes the effects of non-refundable loan origination and commitment fees, net of costs and the accretion of fair value marks) of originated and acquired loans with maturities over one year is as follows at the dates indicated:

| | December 31, 2018 | | | | | |
|---|-------------------|--------------------------|--------------|--------------------------|--------------|--------------------------|
| | Fixed | | Variable | | Total | |
| | Balance | Weighted average rate | Balance | Weighted average rate | Balance | Weighted average rate |
| Commercial | | | | | | |
| Commercial and industrial(1) | \$ 933,202 | 3.92% | \$ 807,139 | 4.98% | \$ 1,740,341 | 4.41% |
| Owner occupied commercial real estate | 195,354 | 4.61% | 192,133 | 5.09% | 387,487 | 5.04% |
| Food and agriculture | 44,351 | 5.00% | 124,234 | 5.21% | 168,585 | 5.15% |
| Energy | 21 | 4.50% | 39,786 | 4.81% | 39,807 | 4.81% |
| Total commercial | 1,172,928 | 4.14% | 1,163,292 | 5.02% | 2,336,220 | 4.58% |
| Commercial real estate non-owner occupied | 209,759 | 4.70% | 273,115 | 5.11% | 482,874 | 4.93% |
| Residential real estate | 361,147 | 3.56% | 429,909 | 4.61% | 791,056 | 4.13% |
| Consumer | 13,672 | 5.27% | 3,196 | 5.57% | 16,868 | 5.33% |
| Total loans with > 1 year maturity | \$ 1,757,506 | 4.10% | \$ 1,869,512 | 4.94% | \$ 3,627,018 | 4.53% |

Table of Contents

| | December 31, 2017 | | | | | |
|---|-------------------|-----------------------|--------------|-----------------------|--------------|-----------------------|
| | Fixed | | Variable | | Total | |
| | Balance | Weighted average rate | Balance | Weighted average rate | Balance | Weighted average rate |
| Commercial and industrial(1) | \$ 696,224 | 3.34% | \$ 597,253 | 4.14% | \$ 1,293,477 | 3.71% |
| Owner occupied commercial real estate | 125,821 | 4.20% | 133,408 | 4.26% | 259,229 | 4.39% |
| Food and agriculture | 35,605 | 4.70% | 89,487 | 4.42% | 125,092 | 4.50% |
| Energy | 132 | 4.37% | 31,357 | 4.57% | 31,489 | 4.57% |
| Total commercial | 857,782 | 3.57% | 851,505 | 4.20% | 1,709,287 | 3.89% |
| Commercial real estate non-owner occupied | 161,846 | 4.42% | 237,772 | 4.46% | 399,618 | 4.44% |
| Residential real estate | 372,104 | 3.40% | 325,227 | 3.94% | 697,331 | 3.65% |
| Consumer | 15,883 | 4.68% | 2,805 | 4.59% | 18,688 | 4.67% |
| Total loans with > 1 year maturity | \$ 1,407,615 | 3.64% | \$ 1,417,309 | 4.19% | \$ 2,824,924 | 3.91% |

- (1) Included in commercial fixed rate loans are loans totaling \$473,440 and \$417,660 as of December 31, 2018 and 2017, respectively, that have been swapped to variable rates at current market pricing. Included in the commercial segment are tax exempt loans totaling \$685,644 and \$617,889 with a weighted average rate of 3.27% and 3.15% at December 31, 2018 and 2017, respectively.

Accretable Yield

At December 31, 2018, the accretable yield balance was \$35.9 million compared to \$46.6 million at December 31, 2017. We remeasure the expected cash flows quarterly for all 24 remaining loan pools accounted for under ASC 310-30 utilizing the same cash flow methodology used at the time of acquisition. This re-measurement resulted in a net \$8.5 million and \$8.6 million reclassification from non-accretable difference to accretable yield during 2018 and 2017, respectively.

In addition to the accretable yield on loans accounted for under ASC 310-30, the fair value adjustments on loans outside the scope of ASC 310-30 are also accreted to interest income over the life of the loans. The Peoples acquisition added accretable fair value marks of \$9.8 million on originated and acquired loans. Total remaining accretable yield and fair value mark was as follows for the dates indicated:

| | December 31, 2018 | December 31, 2017 |
|---|-------------------|-------------------|
| Remaining accretable yield on loans accounted for under ASC 310-30 | \$ 35,901 | \$ 46,568 |
| Remaining accretable fair value mark on originated and acquired loans | 8,659 | 1,771 |
| Total remaining accretable yield and fair value mark | \$ 44,560 | \$ 48,339 |

Asset Quality

All of the assets acquired in our acquisitions were marked to fair value at the date of acquisition, and the fair value adjustments to loans included a credit quality component. We utilize traditional credit quality metrics to evaluate the overall credit quality of our loan portfolio; however, our historical credit quality ratios are somewhat limited in their comparability to industry averages or to other financial institutions because of the percentage of acquired problem loans and given that any asset quality deterioration that existed at the date of acquisition was considered in the original fair value adjustments.

Asset quality is fundamental to our success and remains a strong point, driven by our disciplined adherence to our self-imposed concentration limits across industry sector and real estate property type. Accordingly, for the origination of loans, we have established a credit policy that allows for responsive, yet controlled lending with credit approval requirements that are scaled to loan size. Within the scope of the credit policy, each prospective loan is reviewed in order to determine the appropriateness and the adequacy of the loan characteristics and the security or collateral prior to making a loan. We have established underwriting standards and loan origination procedures that require appropriate documentation, including

Table of Contents

financial data and credit reports. For loans secured by real property, we require property appraisals, title insurance or a title opinion, hazard insurance and flood insurance, in each case where appropriate.

Additionally, we have implemented procedures to timely identify loans that may become problematic in order to ensure the most beneficial resolution to the Company. Asset quality is monitored by our credit risk management department and evaluated based on quantitative and subjective factors such as the timeliness of contractual payments received. Additional factors that are considered, particularly with commercial loans over \$500,000, include the financial condition and liquidity of individual borrowers and guarantors, if any, and the value of our collateral. To facilitate the oversight of asset quality, loans are categorized based on the number of days past due and on an internal risk rating system, and both are discussed in more detail below.

Our internal risk rating system uses a series of grades which reflect our assessment of the credit quality of loans based on an analysis of the borrower's financial condition, liquidity and ability to meet contractual debt service requirements. Loans that are perceived to have acceptable risk are categorized as "Pass" loans. "Special mention" loans represent loans that have potential credit weaknesses that deserve close attention. Special mention loans include borrowers that have potential weaknesses or unwarranted risks that, unless corrected, may threaten the borrower's ability to meet debt service requirements. However, these borrowers are still believed to have the ability to respond to and resolve the financial issues that threaten their financial situation. Loans classified as "Substandard" have a well-defined credit weakness and are inadequately protected by the current paying capacity of the obligor or of the collateral pledged, if any. Although these loans are identified as potential problem loans, they may never become non-performing. Substandard loans have a distinct possibility of loss if the deficiencies are not corrected. "Doubtful" loans are loans that management believes that collection of payments in accordance with the terms of the loan agreement are highly questionable and improbable. Doubtful loans are deemed impaired and put on non-accrual status.

In the event of borrower default, we may seek recovery in compliance with state lending laws, the respective loan agreements, and credit monitoring and remediation procedures that may include modifying or restructuring a loan from its original terms, for economic or legal reasons, to provide a concession to the borrower from their original terms due to borrower financial difficulties in order to facilitate repayment. Such restructured loans are considered "troubled debt restructurings" or "TDRs" in accordance with ASC 310-40, Troubled Debt Restructurings by Creditors. Under this guidance, modifications to loans that fall within the scope of ASC 310-30 are not considered troubled debt restructurings, regardless of otherwise meeting the definition of a troubled debt restructuring. Assets that have been foreclosed on or acquired through deed-in-lieu of foreclosure are classified as OREO until sold, and are carried at the fair value of the collateral less estimated costs to sell, with any initial valuation adjustments charged to the ALL and any subsequent declines in carrying value charged to impairments on OREO.

Non-performing Assets

Non-performing assets consist of non-accrual loans, troubled debt restructurings on non-accrual, OREO and other repossessed assets. Non-accrual loans and troubled debt restructurings on non-accrual accounted for under ASC 310-30, as described below, may be excluded from our non-performing assets to the extent that the cash flows of the loan pools are still estimable. During the third quarter of 2014, we revised our definition of non-performing assets and non-performing loans to exclude accruing loans 90 days past due and accruing troubled debt restructurings to more accurately align the financial metrics related to non-performing assets and non-performing loans with our financial results. Prior period information has been modified for this revision. Interest income that would have been recorded had non-accrual loans performed in accordance with their original contract terms during 2018, 2017 and 2016 was \$1.4 million, \$1.5 million and \$2.6 million, respectively.

All loans accounted for under ASC 310-30 were classified as performing assets at December 31, 2018, as the future cash flows on the loan pools were considered estimable. While individual loans making up the pools may be accounted for on a cost recovery basis, the cash flows on the loan pools are considered estimable and, therefore, interest income, through accretion of the difference between the carrying value of the loans in the pool and the pool's expected future cash flows, is being recognized on all acquired loan pools accounted for under ASC 310-30.

Table of Contents

The following table sets forth the non-performing assets as of the dates presented:

| | December 31, 2018 | December 31, 2017 | December 31, 2016 | December 31, 2015 | December 31, 2014 |
|---|-------------------|-------------------|-------------------|-------------------|-------------------|
| Non-accrual loans: | | | | | |
| Commercial: | | | | | |
| Commercial and industrial | \$ 4,670 | \$ 3,747 | \$ 1,160 | \$ 942 | \$ 221 |
| Owner occupied commercial real estate | 6,658 | 3,336 | 2,054 | 954 | 385 |
| Food and agriculture | 768 | 2,003 | 297 | 1,904 | 130 |
| Energy | — | — | 6,517 | — | — |
| Total commercial | 12,096 | 9,086 | 10,028 | 3,800 | 736 |
| Commercial real estate non-owner occupied | 1,900 | 784 | 66 | 407 | 222 |
| Residential real estate | 6,979 | 3,846 | 3,875 | 3,617 | 2,845 |
| Consumer | 42 | 29 | 40 | 30 | 37 |
| Total non-accrual loans, excluding restructured loans | 21,017 | 13,745 | 14,009 | 7,854 | 3,840 |
| Restructured loans on non-accrual: | | | | | |
| Commercial: | | | | | |
| Commercial and industrial | 840 | 4,020 | 7,527 | 3,888 | 3,994 |
| Owner occupied commercial real estate | 273 | 143 | 2 | 319 | 458 |
| Food and agriculture | — | — | 1,608 | 81 | 365 |
| Energy | 742 | 1,645 | 6,128 | 12,009 | — |
| Total commercial | 1,855 | 5,808 | 15,265 | 16,297 | 4,817 |
| Commercial real estate non-owner occupied | — | — | — | 815 | — |
| Residential real estate | 1,584 | 1,336 | 1,301 | 679 | 1,966 |
| Consumer | — | 111 | 142 | 2 | 190 |
| Total restructured loans on non-accrual | 3,439 | 7,255 | 16,708 | 17,793 | 6,973 |
| Total non-performing loans | 24,456 | 21,000 | 30,717 | 25,647 | 10,813 |
| OREO | 10,596 | 10,491 | 15,662 | 20,814 | 29,120 |
| Other repossessed assets | — | — | — | 894 | 849 |
| Total non-performing assets | \$ 35,052 | \$ 31,491 | \$ 46,379 | \$ 47,355 | \$ 40,782 |
| Loans 90 days or more past due and still accruing interest | | | | | |
| | \$ 895 | \$ 150 | \$ — | \$ 166 | \$ 263 |
| Accruing restructured loans | \$ 5,944 | \$ 8,461 | \$ 5,766 | \$ 8,403 | \$ 19,275 |
| ALL | \$ 35,692 | \$ 31,264 | \$ 29,174 | \$ 27,119 | \$ 17,613 |
| Total non-performing loans to total loans | 0.60% | 0.66% | 1.07% | 0.99% | 0.50% |
| Loans 90 days or more past due and still accruing interest to total loans | | | | | |
| | 0.02% | 0.00% | 0.00% | 0.01% | 0.01% |

Edgar Filing: National Bank Holdings Corp - Form 10-K

| | | | | | |
|--|---------|---------|--------|---------|---------|
| Total non-performing assets to total loans and OREO | 0.85% | 0.99% | 1.61% | 1.81% | 1.86% |
| ALL to non-performing loans | 145.94% | 148.88% | 94.98% | 105.74% | 162.89% |

During 2018, total non-performing loans increased \$3.5 million, or 16.5%, from December 31, 2017 due to acquired Peoples loans, partially offset by paydowns during the period. During 2018, accruing TDRs decreased \$4.4 million.

OREO totaled \$10.6 million at December 31, 2018 and increased \$0.1 million from December 31, 2017. During 2018, a total of \$25.9 million of OREO was sold primarily driven by one large property that was previously an acquired 310-30 loan

Table of Contents

which was transferred to OREO during the second quarter of 2018. OREO sales during 2018 resulted in a net gain of \$0.5 million while OREO write-downs during 2018 were \$0.2 million. Total non-performing assets to total loans and OREO was 0.85% and 0.99% at December 31, 2018 and December 31, 2017, respectively.

The following table represents the carrying value of our accruing and non-accrual loans compared to the unpaid principal balance ("UPB") as of December 31, 2018:

| | Accruing Unpaid principal balance | Carrying value | Carrying value/ UPB | Non-accrual Unpaid principal balance | Carrying value | Carrying value/ UPB | Total Unpaid principal balance | Carrying value |
|---|--|-------------------|---------------------------|---|-------------------|---------------------------|---|-------------------|
| Originated: | | | | | | | | |
| Commercial: | | | | | | | | |
| Commercial and industrial Owner occupied commercial real estate | \$ 1,871,614 | \$ 1,871,949 | 100.1% | \$ 9,086 | \$ 5,272 | 58.0% | \$ 1,880,700 | \$ 1,885,972 |
| Food and agriculture | 334,945 | 334,459 | 99.9% | 3,034 | 2,799 | 92.3% | 337,979 | 337,258 |
| Energy | 217,192 | 216,581 | 99.7% | 722 | 713 | 98.8% | 217,914 | 217,627 |
| Total commercial real estate non-owner occupied | 48,847 | 48,462 | 99.2% | 5,366 | 742 | 13.8% | 54,213 | 49,464 |
| Residential real estate | 2,472,598 | 2,471,451 | 99.9% | 18,208 | 9,526 | 52.3% | 2,490,806 | 2,481,327 |
| Consumer | 407,909 | 406,916 | 99.8% | 550 | 515 | 93.6% | 408,459 | 407,444 |
| Total originated loans | 655,943 | 656,197 | 100.1% | 1,531 | 1,436 | 93.8% | 657,474 | 656,008 |
| Acquired: | 22,866 | 22,864 | 99.9% | 36 | 31 | 86.1% | 22,902 | 22,895 |
| Commercial: Commercial and industrial Owner occupied commercial real estate | 56,142 | 53,688 | 95.6% | 297 | 238 | 80.1% | 56,439 | 53,926 |
| Real estate non-owner occupied | 81,904 | 80,276 | 98.0% | 4,492 | 4,132 | 92.0% | 86,396 | 84,408 |
| Consumer | 4,897 | 4,807 | 98.2% | 83 | 55 | 65.6% | 4,980 | 4,862 |

Edgar Filing: National Bank Holdings Corp - Form 10-K

| | | | | | | | | | |
|----------------------|--------------|--------------|--------|-----------|-----------|--------|--------------|-------|--|
| Food and agriculture | | | | | | | | | |
| Total | | | | | | | | | |
| commercial | 142,943 | 138,771 | 97.1% | 4,872 | 4,425 | 90.8% | 147,815 | 14 | |
| Commercial | | | | | | | | | |
| real estate | 145,249 | 143,003 | 98.5% | 1,937 | 1,385 | 71.5% | 147,186 | 14 | |
| Residential | | | | | | | | | |
| real estate | 157,853 | 156,060 | 98.9% | 8,466 | 7,127 | 84.2% | 166,319 | 16 | |
| Consumer | 1,686 | 1,711 | 101.5% | 10 | 11 | 110.0% | 1,696 | 1, | |
| Total | | | | | | | | | |
| acquired | | | | | | | | | |
| loans | 447,731 | 439,545 | 98.2% | 15,285 | 12,948 | 84.7% | 463,016 | 45 | |
| ASC 310-30 | | | | | | | | | |
| loans: | | | | | | | | | |
| Commercial | 26,156 | 20,398 | 78.0% | — | — | 0.0% | 26,156 | 20 | |
| Commercial | | | | | | | | | |
| real estate | | | | | | | | | |
| non-owner | | | | | | | | | |
| occupied | 50,643 | 40,393 | 79.8% | — | — | 0.0% | 50,643 | 40 | |
| Residential | | | | | | | | | |
| real estate | 14,897 | 9,995 | 67.1% | — | — | 0.0% | 14,897 | 9,9 | |
| Consumer | 2,030 | 93 | 4.6% | — | — | 0.0% | 2,030 | 93 | |
| Total loans | | | | | | | | | |
| accounted for | | | | | | | | | |
| under ASC | | | | | | | | | |
| 310-30 | 93,726 | 70,879 | 75.6% | — | — | 0.0% | 93,726 | 70 | |
| Total loans | \$ 4,100,773 | \$ 4,067,852 | 99.2% | \$ 35,610 | \$ 24,456 | 68.7% | \$ 4,136,383 | \$ 4, | |

Past Due Loans

Past due status is monitored as an indicator of credit deterioration. Loans are considered past due or delinquent when the contractual principal or interest due in accordance with the terms of the loan agreement remains unpaid after the due date of the scheduled payment. Originated and acquired loans that are 90 days or more past due are put on non-accrual status unless the loan is well secured and in the process of collection.

Table of Contents

The table below shows the past due status of originated and acquired loans, based on contractual terms of the loans as of December 31, 2018 and 2017:

| | December 31, 2018 | December 31, 2017 |
|---|-------------------|-------------------|
| Loans 30-89 days past due and still accruing interest | \$ 4,610 | \$ 3,681 |
| Loans 90 days past due and still accruing interest | 895 | 150 |
| Non-accrual loans | 24,456 | 21,000 |
| Total past due and non-accrual loans | \$ 29,961 | \$ 24,831 |
| Total 90 days past due and still accruing interest and non-accrual loans to total originated and acquired loans | 0.63% | 0.69% |
| Total non-accrual loans to total originated and acquired loans | 0.61% | 0.69% |

Loans 30-89 days past due and still accruing interest increased \$0.9 million from December 31, 2017 to December 31, 2018 and loans 90 days or more past due and still accruing interest increased \$0.7 million from December 31, 2017 to December 31, 2018, for a collective increase in total past due loans of \$1.6 million. Non-accrual loans increased \$3.5 million at December 31, 2018, compared to December 31, 2017, further described within the Non-Performing Assets discussion of Management's Discussion and Analysis. There were no ASC 310-30 loan pools past due or on non-accrual at December 31, 2018 or 2017.

Allowance for Loan Losses

The ALL represents the amount that we believe is necessary to absorb probable losses inherent in the loan portfolio at the balance sheet date and involves a high degree of judgment and complexity. Determination of the ALL is based on an evaluation of the collectability of loans, the realizable value of underlying collateral, economic conditions, historical net loan losses, the estimated loss emergence period, estimated default rates, any declines in cash flow assumptions from acquisition, loan structures, growth factors and other elements that warrant recognition and, to the extent applicable, prior loss experience. The ALL is critical to the portrayal and understanding of our financial condition, liquidity and results of operations. The determination and application of the ALL accounting policy involves judgments, estimates, and uncertainties that are subject to change. Changes in these assumptions, estimates or the conditions surrounding them may have a material impact on our financial condition, liquidity or results of operations.

In accordance with the applicable guidance for business combinations, acquired loans were recorded at their acquisition date fair values, which were based on expected future cash flows and included an estimate for future loan losses; therefore, no ALL was recorded as of the acquisition date. Any estimated losses on acquired loans that arise after the acquisition date are reflected in a charge to the provision for loan losses in the consolidated statements of operations.

310-30 ALL

Loans accounted for under the accounting guidance provided in ASC 310-30 have been grouped into pools based on the predominant risk characteristics of purpose and/or type of loan. The timing and receipt of expected principal, interest and any other cash flows of these loans are periodically remeasured and the expected future cash flows of the collective pools are compared to the carrying value of the pools. To the extent that the expected future cash flows of each pool is less than the book value of the pool, an allowance for loan losses will be established through a charge to the provision for loan losses. If the remeasured expected future cash flows are greater than the book value of the pools, then the improvement in the expected future cash flows is accreted into interest income over the remaining expected life of the loan pool. During 2018 and 2017, these re-measurements resulted in overall increases in expected cash flows in certain loan pools, which, absent previous valuation allowances within the same pool, are reflected in increased accretion as well as an increased amount of accretable yield and are recognized over the expected remaining lives of the underlying loans as an adjustment to yield.

During 2018, loans accounted for under ASC 310-30 had provision of \$222 thousand. During 2017, loans accounted for under ASC 310-30 had recoupment of \$154 thousand.

Table of Contents

Originated and Acquired ALL

For all originated and acquired loans, the determination of the ALL follows a process to determine the appropriate level of ALL that is designed to account for changes in credit quality and other risk factors. This process provides an ALL consisting of a specific allowance component based on certain individually evaluated loans and a general allowance component based on estimates of reserves needed for all other loans, segmented based on similar risk characteristics.

Impaired loans less than \$250,000 are included in the general allowance population. Impaired loans over \$250,000 are subject to individual evaluation on a regular basis to determine the need, if any, to allocate a specific reserve to the impaired loan. Typically, these loans consist of commercial, commercial real estate and agriculture loans and exclude homogeneous loans such as residential real estate and consumer loans. Specific allowances are determined by collectively analyzing:

- the borrower’s resources, ability, and willingness to repay in accordance with the terms of the loan agreement;
- the likelihood of receiving financial support from any guarantors;
- the adequacy and present value of future cash flows, less disposal costs, of any collateral;
- the impact current economic conditions may have on the borrower's financial condition and liquidity or the value of the collateral.

In evaluating the loan portfolio for an appropriate ALL level, unimpaired loans are grouped into segments based on broad characteristics such as primary use and underlying collateral. We have identified four primary loan segments that are further stratified into eleven loan classes to provide more granularity in analyzing loss history and to allow for more definitive qualitative adjustments based upon specific factors affecting each loan class. Following are the loan classes within each of the four primary loan segments:

| | | | |
|---------------------------------------|---|-------------------------|----------------|
| Commercial | Non-owner occupied commercial real estate | Residential real estate | Consumer |
| Commercial and industrial | Construction | Senior lien | Total Consumer |
| Owner occupied commercial real estate | Acquisition and development | Junior lien | |
| Food and agriculture | Multifamily | | |
| Energy | Non-owner occupied | | |

Appropriate ALL levels are determined by segment and class utilizing risk ratings, loss history, peer loss history and qualitative adjustments. The qualitative adjustments consider the following risk factors:

economic/external conditions;
loan administration, loan structure and procedures;
risk tolerance/experience;
loan growth;
trends;
concentrations; and
other.

Management derives an estimated annual loss rate adjusted for an estimated loss emergence period based on historical loss data categorized by segment and class. The loss rates are applied at the loan segment and class level. Our historical loss history began in 2012, resulting in minimal losses in our originated portfolio. In order to address this lack of historical data, we incorporate not only our own historical loss rates since the beginning of 2012, but we also utilize peer historical loss data, including a historical average net charge-off ratio on each loan type, relying on the Uniform Bank Performance Reports compiled by the Federal Financial Institutions Examinations Council (“FFIEC”). We may also apply a long-term estimated loss rate to pass rated credits as necessary to account for inherent risks to the portfolio.

The collective resulting ALL for originated and acquired loans is calculated as the sum of the specific reserves and the general reserves. While these amounts are calculated by individual loan or segment and class, the entire ALL is available for any loan that, in our judgment, should be charged-off.

Table of Contents

During 2018, we recorded \$5.0 million of provision for loan losses for originated and acquired loans for general reserves on loan growth. For originated and acquired loans, the Company recorded charge-offs of \$2.1 million and were mostly offset by recoveries of \$1.4 million during the year ended December 31, 2018. Specific reserves on impaired loans totaled \$1.2 million at December 31, 2018.

During 2017, we recorded \$13.1 million of provision for loan losses for originated and acquired loans, which primarily reflects reserves to support loan growth and specific reserves on certain non-performing loans. Net charge-offs for originated and acquired loans during 2017 totaled \$10.9 million and were primarily due to two energy loans totaling \$7.5 million and one commercial and industrial loan totaling \$2.5 million. Specific reserves on impaired loans totaled \$1.5 million at December 31, 2017.

Total ALL

After considering the above mentioned factors, we believe that the ALL of \$35.7 million and \$31.3 million, at December 31, 2018 and 2017, respectively, is adequate to cover probable losses inherent in the loan portfolio. However, it is likely that future adjustments to the ALL will be necessary and any changes to the assumptions, circumstances or estimates used in determining the ALL could adversely affect the Company's results of operations, liquidity or financial condition.

The following table presents, by class stratification, the changes in the ALL during the periods listed.

| | As of and for the years ended December 31, 2018 | | | December 31, 2017 | | | December 31, 2016 |
|---|--|------------------------|-----------|-------------------------------------|------------------------|-----------|----------------------|
| | Originated and acquired loans | ASC 310-30 loans | Total | Originated and acquired loans | ASC 310-30 loans | Total | |
| Beginning allowance for loan losses | \$ 31,193 | \$ 71 | \$ 31,264 | \$ 28,949 | \$ 225 | \$ 29,174 | \$ 26,042 |
| Charge-offs: | | | | | | | |
| Commercial | (833) | (62) | (895) | (10,342) | — | (10,342) | (20,684) |
| Commercial real estate non-owner occupied | (11) | — | (11) | — | — | — | (280) |
| | (118) | — | (118) | (236) | — | (236) | (408) |

Edgar Filing: National Bank Holdings Corp - Form 10-K

| | | | | | | | |
|---|--------------|-----------|--------------|--------------|------------|--------------|--------------|
| Residential real estate | | | | | | | |
| Consumer | (1,134) | — | (1,134) | (737) | — | (737) | (771) |
| Total | | | | | | | |
| charge-offs | (2,096) | (62) | (2,158) | (11,315) | — | (11,315) | (22,143) |
| Recoveries | 1,389 | — | 1,389 | 433 | — | 433 | 594 |
| Net charge-offs | (707) | (62) | (769) | (10,882) | — | (10,882) | (21,549) |
| Provision (recoupment) | | | | | | | |
| for loan loss | 4,975 | 222 | 5,197 | 13,126 | (154) | 12,972 | 24,456 |
| Ending allowance for loan losses | \$ 35,461 | \$ 231 | \$ 35,692 | \$ 31,193 | \$ 71 | \$ 31,264 | \$ 28,949 |
| Ratio of net charge-offs to average total loans during the period, respectively | 0.02% | 0.07% | 0.02% | 0.38% | 0.00% | 0.36% | 0.85% |
| Ratio of ALL to total loans outstanding at period end, respectively | 0.88% | 0.33% | 0.87% | 1.02% | 0.06% | 0.98% | 1.07% |
| Ratio of ALL to total non-performing loans at period end, respectively | 145.00% | 0.00% | 145.94% | 148.54% | 0.00% | 148.88% | 94.24% |
| Total loans | \$ 4,021,429 | \$ 70,879 | \$ 4,092,308 | \$ 3,058,324 | \$ 120,623 | \$ 3,178,947 | \$ 2,715,069 |
| Average total loans outstanding during the period | \$ 3,728,817 | \$ 90,786 | \$ 3,819,603 | \$ 2,897,316 | \$ 132,130 | \$ 3,029,446 | \$ 2,530,464 |
| Non-performing loans | \$ 24,456 | \$ — | \$ 24,456 | \$ 21,000 | \$ — | \$ 21,000 | \$ 30,717 |

Table of Contents

| | As of and for the years ended | | | December 31, 2014 | | |
|---|-------------------------------------|------------------------|--------------|-------------------------------------|------------------------|--------------|
| | December 31, 2015 | | Total | December 31, 2014 | | Total |
| | Originated and acquired loans | ASC 310-30 loans | | Originated and acquired loans | ASC 310-30 loans | |
| Beginning allowance for loan losses | \$ 16,892 | \$ 721 | \$ 17,613 | \$ 11,241 | \$ 1,280 | \$ 12,521 |
| Charge-offs: | | | | | | |
| Commercial | (1,911) | — | (1,911) | (507) | (3) | (510) |
| Commercial real estate non-owner occupied | (222) | — | (222) | — | — | — |
| Residential real estate | (208) | — | (208) | (739) | — | (739) |
| Consumer | (1,196) | (10) | (1,206) | (783) | (36) | (819) |
| Total charge-offs | (3,537) | (10) | (3,547) | (2,029) | (39) | (2,068) |
| Recoveries | 609 | — | 609 | 951 | — | 951 |
| Net charge-offs | (2,928) | (10) | (2,938) | (1,078) | (39) | (1,117) |
| Provision (recoupment) for loan loss | 12,078 | 366 | 12,444 | 6,729 | (520) | 6,209 |
| Ending allowance for loan losses | \$ 26,042 | \$ 1,077 | \$ 27,119 | \$ 16,892 | \$ 721 | \$ 17,613 |
| Ratio of net charge-offs to average total loans during the period, respectively | 0.36% | 0.01% | 0.12% | 0.06% | 0.01% | 0.05% |
| Ratio of ALL to total loans outstanding at period end, respectively | 1.09% | 0.53% | 1.05% | 0.90% | 0.26% | 0.81% |
| Ratio of ALL to total non-performing loans at period end, respectively | 101.54% | 0.00% | 105.74% | 156.22% | 0.00% | 162.89% |
| Total loans | \$ 2,384,843 | \$ 202,830 | \$ 2,587,673 | \$ 1,882,764 | \$ 279,645 | \$ 2,162,409 |
| Average total loans outstanding during the period | 2,323,527 | \$ 209,268 | \$ 2,532,795 | 1,688,197 | \$ 361,806 | \$ 2,050,003 |
| Non-performing loans | \$ 25,647 | \$ — | \$ 25,647 | \$ 10,813 | \$ — | \$ 10,813 |

The following tables present the allocation of the ALL and the percentage of the total amount of loans in each loan category listed as of the dates presented:

December 31, 2018

Edgar Filing: National Bank Holdings Corp - Form 10-K

| | Total loans | % of total loans | Related ALL | ALL as a % of total ALL |
|---|--------------|------------------|----------------|----------------------------|
| Commercial | \$ 2,644,571 | 64.6% | \$ 27,137 | 76.1% |
| Commercial real estate non-owner occupied | 592,212 | 14.5% | 4,406 | 12.3% |
| Residential real estate | 830,815 | 20.3% | 3,800 | 10.6% |
| Consumer | 24,710 | 0.6% | 349 | 1.0% |
| Total | \$ 4,092,308 | 100.0% | \$ 35,692 | 100.0% |

December 31, 2017

| | Total loans | % of total loans | Related ALL | ALL as a % of total ALL |
|---|--------------|------------------|----------------|----------------------------|
| Commercial | \$ 1,874,605 | 59.0% | \$ 21,385 | 68.4% |
| Commercial real estate non-owner occupied | 563,049 | 17.7% | 5,609 | 17.9% |
| Residential real estate | 716,237 | 22.5% | 3,965 | 12.7% |
| Consumer | 25,056 | 0.8% | 305 | 1.0% |
| Total | \$ 3,178,947 | 100.0% | \$ 31,264 | 100.0% |

December 31, 2016

| | Total loans | % of total loans | Related ALL | ALL as a % of total ALL |
|---|--------------|------------------|----------------|----------------------------|
| Commercial | \$ 1,560,430 | 54.6% | \$ 18,821 | 64.6% |
| Commercial real estate non-owner occupied | 526,792 | 18.4% | 5,642 | 19.3% |
| Residential real estate | 744,885 | 26.0% | 4,387 | 15.0% |
| Consumer | 28,814 | 1.0% | 324 | 1.1% |
| Total | \$ 2,860,921 | 100.0% | \$ 29,174 | 100.0% |

Table of Contents

| | December 31, 2015 | | Related | ALL as a % |
|---|-------------------|------------------|-----------|--------------|
| | Total loans | % of total loans | ALL | of total ALL |
| Commercial | \$ 1,427,420 | 55.2% | \$ 17,261 | 63.6% |
| Commercial real estate non-owner occupied | 442,885 | 17.1% | 4,166 | 15.4% |
| Residential real estate | 684,002 | 26.4% | 5,281 | 19.5% |
| Consumer | 33,366 | 1.3% | 411 | 1.5% |
| Total | \$ 2,587,673 | 100.0% | \$ 27,119 | 100.0% |

| | December 31, 2014 | | Related | ALL as a % |
|---|-------------------|------------------|-----------|--------------|
| | Total loans | % of total loans | ALL | of total ALL |
| Commercial | \$ 1,092,885 | 50.6% | \$ 10,384 | 59.0% |
| Commercial real estate non-owner occupied | 401,636 | 18.6% | 3,042 | 17.3% |
| Residential real estate | 632,700 | 29.2% | 3,771 | 21.4% |
| Consumer | 35,188 | 1.6% | 416 | 2.4% |
| Total | \$ 2,162,409 | 100.0% | \$ 17,613 | 100.0% |

The ALL allocated to commercial loans increased to 76.1% at December 31, 2018 from 68.4% at December 31, 2017, due to the provision recorded during the period to support the increase in originated loans.

Other Assets

Significant components of other assets were as follows as of the dates indicated:

| | December 31, 2018 | December 31, 2017 | Increase (decrease) | |
|--|-------------------|-------------------|---------------------|----------|
| | | | Amount | % Change |
| Bank-owned life insurance | \$ 66,152 | \$ 64,387 | \$ 1,765 | 2.7% |
| Deferred tax asset | 28,351 | 35,630 | (7,279) | (20.4)% |
| Derivative assets | 21,498 | 13,105 | 8,393 | 64.0% |
| Accrued interest on loans | 16,917 | 11,784 | 5,133 | 43.6% |
| Accrued income taxes receivable | 2,300 | 3,992 | (1,692) | (42.4)% |
| Accrued interest on interest bearing bank deposits and investment securities | 2,399 | 2,471 | (72) | (2.9)% |
| Other miscellaneous assets | 21,623 | 7,879 | 13,744 | 174.4% |
| Total other assets | \$ 159,240 | \$ 139,248 | \$ 19,992 | 14.4% |

Other assets totaled \$159.2 million and \$139.2 million at December 31, 2018 and 2017, respectively, representing an increase of \$20.0 million, or 14.4%, year-over-year. Refer to note 20 of our consolidated financial statements for further discussion of the deferred tax assets. Derivative assets increased from 2017 due to changes in the rate environment, and accrued interest on loans increased from 2017 due to higher volumes of loans related to the Peoples acquisition. Refer to note 21 of our consolidated financial statements for further discussion of the derivative asset. Included in other miscellaneous assets at December 31, 2018 is \$10.0 million of restricted cash related to the Peoples acquisition for certain potential liabilities and an increase in prepaid assets of \$1.2 million.

Table of Contents

Other Liabilities

Significant components of other liabilities were as follows as of the dates indicated:

| | | | Increase (decrease) | |
|----------------------------------|-------------------|-------------------|---------------------|----------|
| | | | Amount | % Change |
| | December 31, 2018 | December 31, 2017 | | |
| Pending loan purchase settlement | \$ 8,979 | \$ 30,181 | \$ (21,202) | (70.2)% |
| Accrued expenses | 20,661 | 16,172 | 4,489 | 27.8% |
| Accrued interest payable | 7,015 | 5,776 | 1,239 | 21.5% |
| Derivative liabilities | 4,121 | 3,758 | 363 | 9.6% |
| Other miscellaneous liabilities | 37,556 | 15,346 | 22,210 | 144.7% |
| Participant interest in OREO | — | 688 | (688) | (100.0)% |
| Total other liabilities | \$ 78,332 | \$ 71,921 | \$ 6,411 | 8.9% |

Other liabilities totaled \$78.3 million and \$71.9 million at December 31, 2018 and 2017, respectively, representing an increase of \$6.4 million, or 8.9%, year-over-year. Pending loan purchase settlement decreased due to timing of loan settlements. Included in other miscellaneous liabilities is \$12.1 million of derivative collateral reserves, a \$10.0 million cash holdback liability related to the Peoples acquisition, and a \$4.1 million mortgage repurchase reserve. Refer to note 21 and note 22 of our consolidated financial statements for further discussion of the derivative liability and mortgage repurchase reserve, respectively.

Deposits

Deposits from banking clients serve as a primary funding source for our banking operations and our ability to gather and manage deposit levels is critical to our success. Deposits not only provide a low-cost funding source for our loans, but also provide a foundation for the client relationships that are critical to future loan growth.

The following table presents information regarding our deposit composition at December 31, 2018 and 2017:

| | | | | | Increase (decrease) | |
|--------------------------------------|-------------------|-------------------|------------|-------|---------------------|----------|
| | | | | | Amount | % Change |
| | December 31, 2018 | December 31, 2017 | | | | |
| Non-interest bearing demand deposits | \$ 1,072,029 | 23.6% | \$ 902,439 | 22.7% | \$ 169,590 | 18.8% |
| Interest bearing demand deposits | 688,255 | 15.2% | 474,607 | 11.9% | 213,648 | 45.0% |
| Savings accounts | 540,481 | 11.9% | 472,852 | 11.9% | 67,629 | 14.3% |
| Money market accounts | 1,154,327 | 25.5% | 1,011,611 | 25.4% | 142,716 | 14.1% |
| Total transaction deposits | 3,455,092 | 76.2% | 2,861,509 | 71.9% | 593,583 | 20.7% |

Edgar Filing: National Bank Holdings Corp - Form 10-K

| | | | | | | |
|---------------------------|--------------|--------|--------------|--------|------------|--------|
| Time deposits < \$100,000 | 616,391 | 13.6% | 637,789 | 16.0% | (21,398) | (3.4)% |
| Time deposits > \$100,000 | 464,138 | 10.2% | 480,261 | 12.1% | (16,123) | (3.4)% |
| Total time deposits | 1,080,529 | 23.8% | 1,118,050 | 28.1% | (37,521) | (3.4)% |
| Total deposits | \$ 4,535,621 | 100.0% | \$ 3,979,559 | 100.0% | \$ 556,062 | 14.0% |

The following table shows scheduled maturities of certificates of deposit with denominations greater than or equal to \$100,000 as of December 31, 2018:

| | December 31, 2018 |
|---------------------------------|-------------------|
| Three months or less | \$ 72,033 |
| Over 3 months through 6 months | 62,719 |
| Over 6 months through 12 months | 152,322 |
| Thereafter | 177,064 |
| Total time deposits > \$100,000 | \$ 464,138 |

Total deposits increased \$556.1 million, or 14.0% from the prior year, driven by the addition of \$729.9 million in total deposits from the Peoples acquisition on January 1, 2018 and transaction deposit growth. The mix of transaction deposits to total deposits improved to 76.2% at December 31, 2018, from 71.9% at December 31, 2017, due to the Peoples acquisition and our continued focus on developing long-term banking relationships.

Table of Contents

At December 31, 2018 and 2017, time deposits that were scheduled to mature within 12 months totaled \$685.4 million and \$684.6 million, respectively. Of the \$685.4 million in time deposits scheduled to mature within 12 months at December 31, 2018, \$287.1 million were in denominations of \$100,000 or more, and \$398.3 million were in denominations less than \$100,000. The aggregate amount of certificates of deposit in denominations that meet or exceed the FDIC insurance limit was \$137.3 million and \$140.7 million at December 31, 2018 and 2017, respectively. Note 12 to the consolidated financial statements provides a maturity schedule of time deposits outstanding at December 31, 2018.

Other Borrowings

As of December 31, 2018 and 2017, the Company sold securities under agreements to repurchase totaling \$66.0 million and \$130.5 million, respectively. In addition, as a member of the FHLB, the Bank has access to a line of credit and term financing from the FHLB with total available credit of \$1.1 billion. At December 31, 2018 and 2017, the Bank had \$67.3 million and \$129.1 million in term advances from the FHLB, respectively. The term advances have fixed rates between 1.55% - 2.33%, with maturity dates of 2019 - 2020. At December 31, 2018 and December 31, 2017 the Bank had \$234.3 million and \$0.0 million in line of credit advances from the FHLB, respectively. The Company utilized its FHLB line of credit during 2018 as a funding mechanism for originated loans.

Regulatory Capital

Our subsidiary bank and the holding company are subject to the regulatory capital adequacy requirements of the Federal Reserve Board and the FDIC, as applicable. Failure to meet the minimum capital requirements can initiate certain mandatory and possibly further discretionary actions by regulators that could have a material adverse effect on us. At December 31, 2018 and 2017, our subsidiary bank and the consolidated holding company exceeded all capital ratio requirements under prompt corrective action and other regulatory requirements, as further detailed in note 14 of our consolidated financial statements.

Results of Operations

Our net income depends largely on net interest income, which is the difference between interest income from interest earning assets and interest expense on interest bearing liabilities. Our results of operations are also affected by provisions for loan losses and non-interest income, such as service charges, bank card income, swap fee income, and gain on sale of mortgages, net. Our primary operating expenses, aside from interest expense, consist of salaries and benefits, occupancy costs, telecommunications and data processing, and marketing and business development. Any expenses related to the resolution of problem assets are also included in non-interest expense.

Overview of Results of Operations

Year ended 2018

We recorded net income of \$61.5 million, or \$1.95 per diluted share, during 2018, compared to net income of \$14.6 million, or \$0.53 per diluted share, during 2017. Net income during 2018 included \$8.0 million, or \$6.3 million after tax, in one-time expenses related to the acquisition of Peoples. Adjusted net income was \$67.8 million, or \$2.16 per diluted share. Net income during 2017 included a non-cash deferred tax asset re-measurement charge of \$18.5 million due to the enactment of the Act and \$3.2 million in one-time expenses primarily related to the acquisition of Peoples. Adjusted net income was \$35.0 million, or \$1.26 per diluted share. During 2018, fully taxable equivalent net interest income totaled \$201.9 million, representing an increase of \$49.8 million from 2017.

Provision for loan loss expense on originated and acquired loans was \$5.0 million for the year ended December 31, 2018, compared to \$13.1 million during 2017, a decrease of \$8.1 million. Net charge-offs on originated and acquired loans totaled 0.02% compared to 0.38% in the prior year.

Non-interest income totaled \$70.8 million during 2018, increasing \$31.6 million from 2017, due to increases in mortgage banking income of \$28.0 million, increases in service charges of \$3.5 million and an increase in bank card fees of \$2.5 million. These increases were partially offset by a decrease in other non-interest income of \$2.7 million.

Table of Contents

Non-interest expense totaled \$189.3 million during 2018, increasing \$52.7 million from 2017 primarily driven by the Peoples acquisition. Included in total non-interest expense for the year ended December 31, 2018 was \$8.0 million of acquisition costs, or \$6.3 million after tax.

Income tax expense totaled \$12.2 million during 2018 compared to \$21.3 million during 2017, a decrease of \$9.1 million. Included in income tax expense was \$1.3 million and \$4.2 million of tax benefits from stock compensation activity during 2018 and 2017, respectively. In addition, income tax expense during 2017 included an \$18.5 million non-cash, one-time charge related to the deferred tax asset re-measurement, due to the Act. Without these discrete items, tax expense would have been \$13.5 million, with an effective tax rate of 18.3%, at December 31, 2018 and \$7.1 million, with an effective tax rate of 19.7%, at December 31, 2017. The lower tax rate compared to the statutory rate reflects the continued success of our tax strategies and tax exempt income in relation to pre-tax income.

Years ended 2017 and 2016

We recorded net income of \$14.6 million, or \$0.53 per diluted share, during 2017, compared to net income of \$23.1 million, or \$0.79 per diluted share, during 2016. Net income during 2017 included a non-cash deferred tax asset re-measurement charge of \$18.5 million due to the enactment of the Act and \$3.2 million in non-recurring expenses primarily related to the acquisition of Peoples. Adjusting for these items, net income would have been \$35.0 million, or \$1.26 per diluted share. Fully taxable equivalent net interest income totaled \$152.2 million representing an increase of \$2.4 million from 2016.

Provision for loan loss expense on originated and acquired loans was \$13.1 million during 2017, compared to \$24.5 million during 2016, a decrease of \$11.4 million driven by a reduction in the provision for energy loans. Net charge-offs on originated and acquired loans totaled 0.38%, or 0.12% excluding the energy portfolio.

Non-interest income totaled \$39.2 million during 2017, decreasing \$0.8 million from 2016, due to decreases in OREO related income of \$1.8 million and gain on sale of mortgages, net of \$0.7 million. These decreases were partially offset by a combined increase in services charges and bank card fees of \$1.3 million and other non-interest income of \$0.4 million.

Non-interest expense totaled \$136.7 million during 2017, increasing \$0.7 million from 2016. The increase was largely due to \$3.2 million of non-recurring expenses primarily related to the Peoples acquisition, offset by decreases of \$1.9 million in occupancy and equipment, a \$0.5 million decrease in bank card expense and a \$0.5 million decrease in FDIC deposit insurance.

Net Interest Income

We regularly review net interest income metrics to provide us with indicators of how the various components of net interest income are performing. We regularly review: (i) our loan mix and the yield on loans; (ii) the investment portfolio and the related yields; (iii) our deposit mix and the cost of deposits; and (iv) net interest income simulations for various forecast periods.

The following tables present the components of net interest income for the periods indicated. The tables include: (i) the average daily balances of interest earning assets and interest bearing liabilities; (ii) the average daily balances of non-interest earning assets and non-interest bearing liabilities; (iii) the total amount of interest income earned on interest earning assets on a fully taxable equivalent basis; (iv) the total amount of interest expense incurred on interest bearing liabilities; (v) the resultant average yields and rates; (vi) net interest spread; and (vii) net interest margin, which represents the difference between interest income and interest expense, expressed as a percentage of interest earning assets. The effects of trade-date accounting of investment securities for which the cash had not settled are not considered interest earning assets and are excluded from this presentation for time frames prior to their cash settlement, as are the market value adjustments on the investment securities available-for-sale.

Table of Contents

The table below presents the components of net interest income on a fully taxable equivalent basis for the years ended December 31, 2018, 2017 and 2016:

| | For the year ended December 31, 2018 | | | For the year ended December 31, 2017 | | | For the year ended December 31, 2016 | | |
|--|---|------------|-----------------|---|------------|-----------------|---|------------|-----------------|
| | Average balance | Interest | Average rate | Average balance | Interest | Average rate | Average balance | Interest | Average rate |
| Net interest income | | | | | | | | | |
| Interest-earning assets | | | | | | | | | |
| Term loans | | | | | | | | | |
| (2)(3) | \$ 3,166,374 | \$ 142,461 | 4.50% | \$ 2,779,344 | \$ 112,817 | 4.06% | \$ 2,368,968 | \$ 89,873 | 3.77% |
| Other | 562,443 | 32,610 | 5.80% | 117,972 | 7,256 | 6.15% | 161,496 | 9,439 | 5.85% |
| Other | 90,786 | 19,155 | 21.10% | 132,130 | 22,505 | 17.03% | 170,330 | 33,256 | 19.46% |
| Held for sale | 73,644 | 3,380 | 4.59% | 8,231 | 523 | 6.35% | 15,179 | 830 | 5.47% |
| Investment securities | | | | | | | | | |
| Available-for-sale | 883,737 | 18,493 | 2.09% | 875,430 | 16,615 | 1.90% | 1,035,679 | 18,991 | 1.83% |
| Held-to-maturity | 258,809 | 7,252 | 2.80% | 296,093 | 8,226 | 2.78% | 382,366 | 10,674 | 2.79% |
| Securities | 18,093 | 1,096 | 6.06% | 15,249 | 839 | 5.50% | 14,975 | 748 | 4.99% |
| Other | | | | | | | | | |
| Interest-earning assets held under agreements to | 77,808 | 1,426 | 1.83% | 128,871 | 1,492 | 1.16% | 141,178 | 718 | 0.51% |
| Interest-earning assets | | | | | | | | | |
| (2)(3) | \$ 5,131,694 | \$ 225,873 | 4.40% | \$ 4,353,320 | \$ 170,273 | 3.91% | \$ 4,290,171 | \$ 164,529 | 3.83% |
| Due | 88,847 | | | 67,993 | | | 63,513 | | |
| Assets | 419,607 | | | 315,660 | | | 332,122 | | |
| Provision for | (32,616) | | | (31,732) | | | (33,853) | | |
| Assets | \$ 5,607,532 | | | \$ 4,705,241 | | | \$ 4,651,953 | | |
| Other | | | | | | | | | |
| Interest-bearing deposits: | | | | | | | | | |
| Demand, savings | | | | | | | | | |
| Money | | | | | | | | | |
| Deposits | \$ 2,418,326 | \$ 8,758 | 0.36% | \$ 1,895,852 | \$ 6,003 | 0.32% | \$ 1,865,225 | \$ 4,985 | 0.27% |

Edgar Filing: National Bank Holdings Corp - Form 10-K

| | | | | | | | | | |
|------------------|--------------|------------|-------|--------------|------------|-------|--------------|------------|-----|
| Deposits | 1,132,748 | 12,283 | 1.08% | 1,146,380 | 10,169 | 0.89% | 1,177,523 | 8,978 | 0.7 |
| Securities sold | | | | | | | | | |
| Agreements | | | | | | | | | |
| Purchase | 87,691 | 295 | 0.34% | 88,390 | 164 | 0.19% | 109,246 | 152 | 0.1 |
| Real Home | | | | | | | | | |
| Bank | | | | | | | | | |
| Loans | 133,932 | 2,618 | 1.95% | 113,433 | 1,779 | 1.57% | 45,773 | 693 | 1.5 |
| Interest | | | | | | | | | |
| On liabilities | \$ 3,772,697 | \$ 23,954 | 0.63% | \$ 3,244,055 | \$ 18,115 | 0.56% | \$ 3,197,767 | \$ 14,808 | 0.4 |
| On deposits | 1,082,158 | | | 873,265 | | | 818,901 | | |
| On liabilities | 90,257 | | | 41,205 | | | 51,587 | | |
| On liabilities | 4,945,112 | | | 4,158,525 | | | 4,068,255 | | |
| On holders' | | | | | | | | | |
| | 662,420 | | | 546,716 | | | 583,698 | | |
| On liabilities | | | | | | | | | |
| On shareholders' | \$ 5,607,532 | | | \$ 4,705,241 | | | \$ 4,651,953 | | |
| Interest | | | | | | | | | |
| On FTE(2) | | \$ 201,919 | | | \$ 152,158 | | | \$ 149,721 | |
| On rate | | | | | | | | | |
| On FTE(2) | | | 3.77% | | | 3.35% | | | 3.3 |
| Interest | | | | | | | | | |
| On assets | \$ 1,358,997 | | | \$ 1,109,265 | | | \$ 1,092,404 | | |
| Interest | | | | | | | | | |
| On FTE(2) | | | 3.93% | | | 3.50% | | | 3.4 |
| On | | | | | | | | | |
| On | 3,500,484 | | | 2,769,117 | | | 2,684,126 | | |
| On total | | | | | | | | | |
| On | 4,633,232 | | | 3,915,497 | | | 3,861,648 | | |
| On average | | | | | | | | | |
| On earning | | | | | | | | | |
| On average | | | | | | | | | |
| On bearing | | | | | | | | | |
| On | 136.02% | | | 134.19% | | | 134.16% | | |

- (1) Originated loans are net of deferred loan fees, less costs, which are included in interest income over the life of the loan.
- (2) Presented on a fully taxable equivalent basis using the statutory tax rate of 21% for 2018 and 35% for 2017 and 2016. The taxable equivalent adjustments included above are \$4,482, \$5,852 and \$4,081 for the years ended 2018, 2017 and 2016, respectively.
- (3) Loan fees included in interest income totaled \$6,027, \$5,208 and \$4,734 during 2018, 2017 and 2016, respectively.

Net interest income totaled \$197.4 million, \$146.3 million and \$145.6 million for the years ended 2018, 2017 and 2016, respectively. On a fully taxable equivalent basis, net interest income totaled \$201.9 million, \$152.2 million and \$149.7 million during 2018, 2017 and 2016, respectively, increasing \$49.8 million during 2018 and increasing \$2.4 million during 2017, when compared to prior periods. During 2018, the fully taxable equivalent net interest income benefitted from the Peoples acquisition, increasing yields on originated loans and the continued shift of earning assets

into the originated loan portfolio. These benefits were partially offset by lower levels of higher-yielding 310-30 loans and a 0.07% increase in the cost of interest bearing liabilities. During 2017, the fully taxable equivalent net interest income benefitted from the continued shift of earning assets into the originated loan portfolio partially offset by lower levels of higher-yielding 310-30 loans and a 0.10% increase in the cost of interest bearing liabilities.

Average loans comprised \$3.8 billion, or 74.4%, of total average interest earning assets during 2018, compared to \$3.0 billion, or 69.8%, during 2017 and \$2.7 billion, or 63.3%, during 2016. The increase in average loan balances was driven by an increase of \$444.5 million in acquired loans primarily driven from the Peoples acquisition and a \$387.0 million increase in originated loans. Originated loan yields were 4.50%, 4.06% and 3.79% during 2018, 2017 and 2016, respectively, benefiting from higher yields on variable rate loans, primarily driven by short-term market rate increases. The yield on the ASC 310-30

Table of Contents

loan portfolio was 21.1%, 17.03% and 19.52% during 2018, 2017 and 2016, respectively, increasing in 2018 due to accelerated accretion and decreasing in 2017 due to the continued resolution of the high yielding ASC 310-30 loan pools.

Average investment securities comprised 22.3%, 26.9% and 33.1% of total interest earning assets during 2018, 2017 and 2016, respectively. The decrease in the investment portfolio was a result of scheduled paydowns and reflects the re-mixing of the interest-earning assets as we have utilized the paydowns of the investment portfolio to fund loan originations. Short-term investments, comprised of the interest earning deposits and securities purchased under agreements to resell, were 1.5%, 3.0% and 3.3% of interest earning assets during 2018, 2017 and 2016, respectively.

Average balances of interest bearing liabilities increased \$528.6 million during 2018, compared to 2017, and increased \$46.3 million during 2017, compared to 2016. The Peoples acquisition added \$730 million in total deposits on January 1, 2018, coupled with transaction growth, partially offset by the sale of four banking centers in the second quarter of 2017. The increase during 2018 was driven by interest bearing demand, savings and money market deposits of \$522.5 million and Federal Home Loan Bank advances of \$20.5 million, partially offset by decreases in time deposits of \$13.6 million. The increase during 2017 was driven by increases in Federal Home Loan Bank advances of \$67.7 million and interest bearing demand, savings and money market deposits of \$30.6 million, partially offset by decreases in time deposits of \$31.1 million and securities sold under agreement to repurchase of \$20.9 million. Adjusting for banking center divestitures during the second quarter of 2017, interest bearing demand, savings and money market deposits increased \$56.5 million and \$109.0 million during 2017 and 2016, respectively, and time deposits increased \$5.7 million and decreased \$99.7 million during 2017 and 2016, respectively, when compared to prior periods. Total interest expense related to interest bearing liabilities was \$24.0 million, \$18.1 million and \$14.8 million during 2018, 2017 and 2016, respectively, at an average cost of 0.63%, 0.56% and 0.46% during 2018, 2017 and 2016, respectively. Additionally, the cost of deposits increased four basis points to 0.45% during 2018, compared to 0.41% during 2017 and 0.36% during 2016, due to increases in interest short-term interest rates.

Table of Contents

The following table summarizes the changes in net interest income on a taxable equivalent basis by major category of interest earning assets and interest bearing liabilities, identifying changes related to volume and changes related to rate for 2018, 2017 and 2016:

| | The year ended December 31, 2018 compared to the year ended December 31, 2017 Increase (decrease) due to | | | The year ended December 31, 2017 compared to the year ended December 31, 2016 Increase (decrease) due to | | |
|---|---|------------------|------------------|---|-----------------|-----------------|
| | Volume | Rate | Net | Volume | Rate | Net |
| Interest income: | | | | | | |
| Originated loans FTE(1)(2) | \$ 17,413 | \$ 12,231 | \$ 29,644 | \$ 17,274 | \$ 6,459 | \$ 23,733 |
| Acquired loans | 25,771 | (417) | 25,354 | (3,612) | 640 | (2,972) |
| ASC 310-30 loans | (8,723) | 5,373 | (3,350) | (6,506) | (4,245) | (10,751) |
| Loans held for sale | 3,002 | (145) | 2,857 | (441) | 134 | (307) |
| Investment securities available-for-sale | 174 | 1,704 | 1,878 | (3,041) | 665 | (2,376) |
| Investment securities held-to-maturity | (1,045) | 71 | (974) | (2,397) | (51) | (2,448) |
| Other securities | 172 | 85 | 257 | 15 | 76 | 91 |
| Interest earning deposits and securities purchased under agreements to resell | (936) | 870 | (66) | (142) | 916 | 774 |
| Total interest income | \$ 35,828 | \$ 19,772 | \$ 55,600 | \$ 1,150 | \$ 4,594 | \$ 5,744 |
| Interest expense: | | | | | | |
| Interest bearing demand, savings and money market deposits | \$ 1,892 | \$ 863 | \$ 2,755 | \$ 97 | \$ 921 | \$ 1,018 |
| Time deposits | (148) | 2,262 | 2,114 | (276) | 1,467 | 1,191 |
| Securities sold under agreements to repurchase | (2) | 133 | 131 | (39) | 51 | 12 |
| Federal Home Loan Bank advances | 401 | 438 | 839 | 1,061 | 25 | 1,086 |
| Total interest expense | 2,143 | 3,696 | 5,839 | 843 | 2,464 | 3,307 |
| Net change in net interest income | \$ 33,685 | \$ 16,076 | \$ 49,761 | \$ 307 | \$ 2,130 | \$ 2,437 |

- (1) Originated loans are net of deferred loan fees, less costs, which are included in interest income over the life of the loan.
- (2) Presented on a fully taxable equivalent basis using the statutory tax rate of 21% for 2018 and 35% for 2017 and 2016. The taxable equivalent adjustments included above are \$4,482, \$5,852 and \$4,081 for the years ended 2018, 2017 and 2016, respectively.

Below is a breakdown of deposits and the average rates paid during the periods indicated:

Edgar Filing: National Bank Holdings Corp - Form 10-K

| | For the three months ended | | | | For the years ended | | | |
|--------------------------------|----------------------------|-------------------------|--------------------|-------------------------|---------------------|-------------------------|--------------------|-------------------------|
| | December 31, 2018 | | December 31, 2017 | | December 31, 2018 | | December 31, 2017 | |
| | Average balance | Average rate paid | Average balance | Average rate paid | Average balance | Average rate paid | Average balance | Average rate paid |
| Non-interest bearing demand | \$ 1,104,411 | 0.00% | \$ 933,657 | 0.00% | \$ 1,082,158 | 0.00% | \$ 873,265 | 0.00% |
| Interest bearing demand | 671,362 | 0.13% | 443,106 | 0.12% | 677,252 | 0.13% | 424,408 | 0.10% |
| Money market accounts | 1,204,351 | 0.61% | 1,059,706 | 0.42% | 1,178,768 | 0.48% | 1,042,873 | 0.39% |
| Savings accounts | 539,914 | 0.46% | 454,494 | 0.40% | 562,306 | 0.40% | 428,571 | 0.35% |
| Time deposits | 1,099,205 | 1.22% | 1,128,069 | 0.95% | 1,132,748 | 1.08% | 1,146,380 | 0.89% |
| Total average deposits | \$ 4,619,243 | 0.52% | \$ 4,019,032 | 0.44% | \$ 4,633,232 | 0.45% | \$ 3,915,497 | 0.41% |

Table of Contents

Provision for Loan Losses

The provision for loan losses represents the amount of expense that is necessary to bring the ALL to a level that we deem appropriate to absorb probable losses inherent in the loan portfolio as of the balance sheet date. The ALL is in addition to the remaining purchase accounting marks of \$8.7 million on originated and acquired loans that were established at the time of acquisition. The Company recorded \$9.8 million of purchase accounting marks on January 1, 2018 related to the Peoples acquisition. Refer to note 4 of our consolidated financial statements for further discussion of the acquisition. The determination of the ALL, and the resultant provision for loan losses, is subjective and involves significant estimates and assumptions.

Below is a summary of the provision for loan losses recorded in the consolidated statements of operations for the periods indicated:

| | 2018 | 2017 | 2016 |
|---|----------|-----------|-----------|
| Provision (recoupment) for loans accounted for under ASC 310-30 | \$ 222 | \$ (154) | \$ (805) |
| Provision for loan losses on originated and acquired loans | 4,975 | 13,126 | 24,456 |
| Total provision for loan losses | \$ 5,197 | \$ 12,972 | \$ 23,651 |

Provision for loan loss expense on originated and acquired loans was \$5.2 million during 2018, compared to \$13.0 million during 2017 and \$23.7 million during 2016. To support loan growth, the Company recorded \$5.0 million of provision for loan losses on originated and acquired loans during 2018. Net charge-offs on the originated and acquired portfolios during 2018 totaled 0.02%. The originated and acquired allowance for loan losses was 0.88% of total originated and acquired loans at December 31, 2018 compared to 1.02% at December 31, 2017, and decreased as the acquired loans from the Peoples acquisition were recorded at fair value.

Provision for loan loss was \$13.1 million during 2017, compared to \$24.5 million during 2016, a decrease of \$11.4 million driven entirely by a reduction in the provision for energy loans. Net charge-offs on the originated and acquired portfolios during 2017 totaled 0.38%, or 0.12% excluding the energy portfolio, compared to 0.85% at December 31, 2016, or 0.10% excluding the energy portfolio. The originated and acquired allowance for loan losses was 1.02% of total originated and acquired loans at December 31, 2017 compared to 1.07% at December 31, 2016.

Edgar Filing: National Bank Holdings Corp - Form 10-K

During 2018, 2017 and 2016 we recorded provision of \$222 thousand, recoupments of \$154 thousand and recoupments of \$805 thousand, respectively, for loans accounted for under ASC 310-30 in connection with our re-measurements of expected cash flows. The decreases in expected future cash flows are reflected immediately in our financial statements through increased provisions for loan losses. Increases in expected future cash flows are reflected through an increase in accretable yield that is accreted to income in future periods once any previously recorded provision expense has been reversed.

Non-Interest Income

The table below details the components of non-interest income during 2018, 2017 and 2016, respectively:

| | For the years ended December 31, | | | 2018 vs 2017 | | 2017 vs 2016 | |
|----------------------------------|----------------------------------|-----------|-----------|--------------|----------|--------------|----------|
| | 2018 | 2017 | 2016 | Amount | % Change | Amount | % Change |
| Service charges | \$ 18,092 | \$ 14,634 | \$ 13,900 | \$ 3,458 | 23.6 % | \$ 734 | 5.3 % |
| Bank card fees | 14,489 | 12,026 | 11,429 | 2,463 | 20.5 % | 597 | 5.2 % |
| Mortgage banking income | 30,107 | 2,154 | 2,881 | 27,953 | >100% | (727) | (25.2)% |
| Bank-owned life insurance income | 1,791 | 1,871 | 1,861 | (80) | (4.3)% | 10 | 0.5 % |
| Other non-interest income | 5,379 | 8,082 | 7,708 | (2,703) | (33.4)% | 374 | 4.9 % |
| OREO related income | 917 | 438 | 2,248 | 479 | >100% | (1,810) | (80.5)% |
| Total non-interest income | \$ 70,775 | \$ 39,205 | \$ 40,027 | \$ 31,570 | 80.5 % | \$ (822) | (2.1)% |

Non-interest income totaled \$70.8 million, \$39.2 million and \$40.0 million during 2018, 2017 and 2016, respectively. Service charges represent various fees charged to clients for banking services, including fees such as non-sufficient (“NSF”) charges

Table of Contents

and service charges on deposit accounts. Service charges and bank card fees increased a combined \$5.9 million, or 22.2%, during 2018, compared to 2017 due to organic growth and the addition of the Peoples' client base. Mortgage banking income represents gains of mortgage loans held-for-sale and mark-to-market adjustments on mortgage banking derivatives. Gain on sale of mortgages increased \$28.0 million during 2018, compared to 2017, due to increased gain on sale of mortgages from the Peoples mortgage business.

OREO related income includes rental income and insurance proceeds received on OREO properties and write-ups to the fair-value of collateral that exceed the loan balance at the time of foreclosure. OREO related income increased \$0.5 million and decreased \$1.8 million during 2018 and 2017, when compared to prior periods.

Non-Interest Expense

The table below details non-interest expense for the periods presented:

| | For the years ended December 31, | | | 2018 vs 2017 | | 2017 vs 2016 | |
|--|----------------------------------|------------|------------|--------------|----------|--------------|----------|
| | 2018 | 2017 | 2016 | Amount | % Change | Amount | % Change |
| Salaries and benefits | \$ 114,939 | \$ 80,188 | \$ 79,765 | \$ 34,751 | 43.3 % | \$ 423 | 0.5 % |
| Occupancy and equipment | 28,493 | 20,994 | 22,904 | 7,499 | 35.7 % | (1,910) | (8.3)% |
| Telecommunications and data processing | 10,098 | 7,188 | 5,970 | 2,910 | 40.5 % | 1,218 | 20.4 % |
| Marketing and business development | 4,513 | 2,683 | 2,564 | 1,830 | 68.2 % | 119 | 4.6 % |
| FDIC deposit insurance | 2,475 | 2,762 | 3,236 | (287) | (10.4)% | (474) | (14.6)% |
| Bank card expenses | 5,453 | 3,986 | 4,440 | 1,467 | 36.8 % | (454) | (10.2)% |
| Professional fees | 6,059 | 3,330 | 3,496 | 2,729 | 82.0 % | (166) | (4.7)% |
| Other non-interest expense | 13,073 | 10,360 | 8,554 | 2,713 | 26.2 % | 1,806 | 21.1 % |
| Problem asset workout | 2,549 | 3,994 | 3,983 | (1,445) | (36.2)% | 11 | 0.3 % |
| Gain on OREO sales, net | (488) | (4,150) | (4,383) | 3,662 | (88.2)% | 233 | (5.3)% |
| Core deposit intangible asset amortization | 2,170 | 5,342 | 5,480 | (3,172) | (59.4)% | (138) | (2.5)% |
| Total non-interest expense | \$ 189,334 | \$ 136,677 | \$ 136,009 | \$ 52,657 | 38.5 % | \$ 668 | 0.5 % |

Non-interest expense totaled \$189.3 million, \$136.7 million and \$136.0 million during 2018, 2017 and 2016, respectively. The increase in 2018 was primarily driven by the Peoples acquisition. Included in non-interest expense for the years ended December 31, 2018 and 2017 are non-recurring acquisition costs totaling \$8.0 million, or \$6.3 million after tax, and \$2.7 million, or \$1.8 million after tax, respectively.

Occupancy and equipment expense decreased \$1.9 million during 2017, compared to 2016, primarily due to lower depreciation expense. Telecommunications and data processing expense increased \$1.2 million during 2017 compared to 2016, primarily due to \$0.7 million of acquisition-related costs. Other non-interest expense increased \$1.8 million from 2016 to 2017, primarily driven by increases in unfunded commitment reserves of \$1.1 million and acquisition-related costs of \$0.1 million.

Income taxes

Income taxes are accounted for in accordance with ASC Topic 740, Income Taxes. Under this guidance, deferred income taxes are determined based on the estimated future tax effects of differences between the financial statement and tax basis of assets and liabilities given the provisions of enacted tax laws. ASC Topic 740 requires the establishment of a valuation allowance against the net deferred tax asset unless it is more-likely-than-not that the tax benefit of the deferred tax asset will be realized. For purposes of projecting whether the deferred tax asset will be realized, we consider tax regulations of the jurisdictions in which we operate, estimates of future taxable income, and available tax planning strategies. If tax regulations, operating results, or the ability to implement tax planning strategies varies, adjustments to the carrying value of the deferred tax assets may be required. We believe that it is more likely than not that the results of future operations will generate sufficient taxable income to realize the deferred tax assets.

Income tax expense totaled \$12.2 million during 2018 compared to \$21.3 million during 2017, a decrease of \$9.1 million. Included in income tax expense was \$1.3 million and \$4.2 million of tax benefits from stock compensation activity during 2018 and 2017, respectively. Additionally, income tax expense during 2017 included an \$18.5 million non-cash, one-time charge related to the deferred tax asset re-measurement due to the Act. Adjusting for the above mentioned stock

Table of Contents

compensation activity and deferred tax assets re-measurement, the effective tax rate for 2018 would be 18.3% compared to an adjusted 2017 rate of 19.7%. The effective tax rate is lower compared to the prior year primarily due to the Act, which, among other items, reduced the federal corporate tax rate to 21% effective January 1, 2018. Income tax expense totaled \$2.9 million for 2016. The effective tax rate for 2016 was 11.3% and includes a \$2.1 million benefit related to the early adoption of ASU 2016-09. Prior to this adoption, the realized tax benefit from stock compensation awards vested would have been recorded directly to capital. Without this \$2.1 million benefit, tax expense would have been \$5.1 million, an effective tax rate of 19.7%. The yearly effective tax rates differ from the federal statutory tax rate was primarily due to interest income from tax-exempt lending, bank-owned life insurance income, and the relationship of these items to pre-tax income.

The Company has unvested stock-based compensation awards outstanding at December 31, 2018, including stock options, restricted stock and performance stock units. The strike prices for options range from \$18.09 to \$40.51, with a large portion of the awards having strike prices of \$20.00. The option awards and restricted stock awards vest over a range of a 1-3 year period. The performance stock units cliff vest over three years and the number of shares issued is determined by the final performance results. Depending on the movement in our stock price, these stock-based compensation awards may create either an excess tax benefit or tax deficiency depending on the relationship between the fair value at the time of vesting or exercise and the estimated fair value recorded at the time of grant. As of December 31, 2018, we had \$2.9 million of deferred tax assets related to stock-based compensation, \$2.3 million of which is associated with executive officers still employed by the Company.

ASC Topic 740 also requires the projected realization of tax benefits related to uncertain tax positions to be evaluated based upon the likelihood of successfully defending those positions. For tax positions meeting the more likely than not threshold, the amount recognized in the financial statements is the largest benefit that has greater than 50 percent likelihood of being realized upon ultimate settlement with the relevant tax authority. Interest and penalties on uncertain tax positions are recognized as a component of other non-interest expense. If our assessment of whether a tax position meets or no longer meets the more likely than not threshold were to change, adjustments to income tax benefits may be required. As of December 31, 2018 and 2017, we have not identified any uncertain tax positions.

As of December 31, 2018, our marginal tax rate (the rate we pay on each incremental dollar of earnings) was approximately 23%. However, our effective tax rate (income tax expense divided by income before income taxes) for a given period is driven largely by income and expense items that are non-taxable or non-deductible in the calculation of income tax expense.

Liquidity and Capital Resources

Liquidity is monitored and managed to ensure that sufficient funds are available to operate our business and pay our obligations to depositors and other creditors, while providing ample available funds for opportunistic and strategic investments. On-balance sheet liquidity is represented by our cash and cash equivalents and unencumbered investment securities, and is detailed in the table below as of December 31, 2018 and 2017:

| | December 31, 2018 | December 31, 2017 |
|---|-------------------|-------------------|
| Cash and due from banks | \$ 109,056 | \$ 193,297 |
| Cash segregated for Peoples acquisition | — | (36,189) |
| Unsegregated cash and due from banks | 109,056 | 157,108 |
| Interest bearing bank deposits | 500 | 64,067 |
| Unencumbered investment securities, at fair value | 573,637 | 637,048 |
| Total | \$ 683,193 | \$ 858,223 |

Total on-balance sheet liquidity decreased \$175.0 million from December 31, 2017 to December 31, 2018. The decrease was due to lower interest bearing bank deposits of \$63.6 million, lower unencumbered available-for-sale and held-to-maturity securities balances of \$63.4 million and unsegregated cash and due from banks of \$48.1 million.

Our primary sources of funds are deposits, securities sold under agreements to repurchase, prepayments and maturities of loans and investment securities, the sale of investment securities, funds provided from operations and FHLB borrowings. We anticipate having access to other third party funding sources, including the ability to raise funds through the issuance of shares of our common stock or other equity or equity-related securities, incurrence of debt, and federal funds purchased, that

Table of Contents

may also be a source of liquidity. We anticipate that these sources of liquidity will provide adequate funding and liquidity for at least a 12-month period.

Our primary uses of funds are loan originations, investment security purchases, withdrawals of deposits, settlement of repurchase agreements, capital expenditures, operating expenses, and share repurchases. For additional information regarding our operating, investing and financing cash flows, see our consolidated statements of cash flows in the accompanying consolidated financial statements.

Exclusive from the investing activities related to acquisitions, our primary investing activities are originations, pay-offs and pay downs of loans and purchases and sales of investment securities. At December 31, 2018, pledgeable investment securities represented our largest source of liquidity on the balance sheet. Our available-for-sale investment securities are carried at fair value and our held-to-maturity securities are carried at amortized cost. Our collective investment securities portfolio totaled \$1.1 billion at December 31, 2018, inclusive of pre-tax net unrealized losses of \$18.6 million on the available-for-sale securities portfolio. Additionally, our held-to-maturity securities portfolio had \$4.5 million of pre-tax net unrealized losses at December 31, 2018. The gross unrealized gains and losses are detailed in note 5 of our consolidated financial statements. As of December 31, 2018, our investment securities portfolio consisted primarily of mortgage-backed securities, all of which were issued or guaranteed by U.S. Government agencies or sponsored enterprises. The anticipated repayments and marketability of these securities offer substantial resources and flexibility to meet new loan demand, reinvest in the investment securities portfolio, or provide optionality for reductions in our deposit funding base.

At present, financing activities primarily consist of changes in deposits and repurchase agreements, and advances from the FHLB, in addition to the payment of dividends and the repurchase of our common stock. Maturing time deposits represent a potential use of funds. As of December 31, 2018, \$685.5 million of time deposits were scheduled to mature within 12 months. Based on the current interest rate environment, market conditions, and our consumer banking strategy focusing on both lower cost transaction accounts and term deposits, our strategy is to replace a significant portion of those maturing time deposits with transaction deposits and market-rate time deposits.

Through our relationship with the FHLB, we have pledged qualifying loans and investment securities allowing us to obtain additional liquidity through FHLB advances and lines of credit. FHLB advances and lines of credit available totaled \$1.1 billion of which \$301.7 million was used at December 31, 2018. We can obtain additional liquidity through FHLB advances if required. The Bank also has access to federal funds lines of credit with corresponding banks.

The Basel III Capital rules, effective January 1, 2015, changed the components of regulatory capital, changed the way in which risk ratings are assigned to various categories of bank assets, and defined a new Tier 1 common risk-based ratio. In addition, a capital conservation buffer requirement, designed to strengthen an institution's financial resilience during economic cycles through the restriction of capital distributions and other payments, became effective in 2016 with full phase in beginning January 1, 2019. When fully phased-in, the capital conservative buffer adds a 2.5%

capital requirement above existing regulatory minimum ratios. Under the Basel III requirements, at December 31, 2018 and 2017, the Company and the Bank met all capital adequacy requirements and the Bank had regulatory capital ratios in excess of the levels established for well-capitalized institutions. For more information on regulatory capital, see note 14 in our consolidated financial statements.

Our shareholders' equity is impacted by earnings, changes in unrealized gains and losses on securities, net of tax, stock-based compensation activity, share repurchases and the payment of dividends.

The Board of Directors has authorized multiple programs to repurchase shares of the Company's common stock from time to time either in open market or in privately negotiated transactions in accordance with applicable regulations of the SEC. We believe that our repurchases could serve to offset any future share issuances for future acquisitions.

On August 5, 2016, the Company announced that its Board of Directors authorized a new program to repurchase up to an additional \$50.0 million of the Company's common stock. The remaining authorization under this program as of December 31, 2018 was \$12.6 million. During 2018, we did not repurchase any shares of our common stock as part of a publicly announced program.

Table of Contents

On January 22, 2019, our Board of Directors declared a quarterly dividend of \$0.17 per common share, payable on March 15, 2019 to shareholders of record at the close of business on February 22, 2019.

Asset/Liability Management and Interest Rate Risk

Management and the Board of Directors are responsible for managing interest rate risk and employing risk management policies that monitor and limit this exposure. Interest rate risk is measured using net interest income simulations and market value of portfolio equity analyses. These analyses use various assumptions, including the nature and timing of interest rate changes, yield curve shape, prepayments on loans and securities, deposit decay rates, pricing decisions on loans and deposits, and reinvestment/replacement of asset and liability cash flows.

The principal objective of the Company's asset and liability management function is to evaluate the interest rate risk within the balance sheet and pursue a controlled assumption of interest rate risk while maximizing earnings and preserving adequate levels of liquidity and capital. The asset and liability management function is under the guidance of the Asset Liability Committee from direction of the Board of Directors. The Asset Liability Committee meets monthly to review, among other things, the sensitivity of the Company's assets and liabilities to interest rate changes, local and national market conditions and rates. The Asset Liability Committee also reviews the liquidity, capital, deposit mix, loan mix and investment positions of the Company.

Instantaneous parallel rate shift scenarios are modeled and utilized to evaluate risk and establish exposure limits for acceptable changes in net interest margin. These scenarios, known as rate shocks, simulate an instantaneous change in interest rates and use various assumptions, including, but not limited to, prepayments on loans and securities, deposit decay rates, pricing decisions on loans and deposits, reinvestment and replacement of asset and liability cash flows.

We also analyze the economic value of equity as a secondary measure of interest rate risk. This is a complementary measure to net interest income where the calculated value is the result of the market value of assets less the market value of liabilities. The economic value of equity is a longer term view of interest rate risk because it measures the present value of the future cash flows. The impact of changes in interest rates on this calculation is analyzed for the risk to our future earnings and is used in conjunction with the analyses on net interest income.

Our interest rate risk model indicated that the Company was asset sensitive in terms of interest rate sensitivity at December 31, 2018 and 2017. The table below illustrates the impact of an immediate and sustained 200 and 100 basis point increase and a 100 basis point decrease in interest rates on net interest income based on the interest rate risk model at December 31, 2018 and 2017:

| Hypothetical shift in interest rates (in bps) | % change in projected net interest income | |
|---|---|-------------------|
| | December 31, 2018 | December 31, 2017 |
| 200 | 5.86% | 6.93% |
| 100 | 2.98% | 4.82% |
| (100) | (4.84)% | (7.75)% |

Many assumptions are used to calculate the impact of interest rate fluctuations. Actual results may be significantly different than our projections due to several factors, including the timing and frequency of rate changes, market conditions and the shape of the yield curve. The computations of interest rate risk shown above do not include actions that management may undertake to manage the risks in response to anticipated changes in interest rates and actual results may also differ due to any actions taken in response to the changing rates.

As part of the asset/liability management strategy to manage primary market risk exposures expected to be in effect in future reporting periods, management has emphasized the origination of shorter duration loans as well as variable rate loans to limit the negative exposure to a rate increase. The strategy with respect to liabilities has been to emphasize transaction accounts, particularly non-interest or low interest bearing non-maturing deposit accounts which are less sensitive to changes in interest rates. Non-maturing deposit accounts totaled 76.2% of total deposits at December 31, 2018, compared to 71.9% at December

Table of Contents

31, 2017, when adjusted for banking center consolidations. We currently have no brokered time deposits and intend to continue to focus on our strategy of increasing non-interest or low-cost interest bearing non-maturing deposit accounts.

Off-Balance Sheet Activities

In the normal course of business, we are a party to various contractual obligations, commitments and other off-balance sheet activities that contain credit, market, and operational risk that are not required to be reflected in our consolidated financial statements. The most significant of these are the loan commitments that we enter into to meet the financing needs of clients, including commitments to extend credit, commercial and consumer lines of credit and standby letters of credit. As of December 31, 2018 and 2017, we had loan commitments totaling \$773.5 million and \$680.8 million, respectively, and standby letters of credit that totaled \$10.6 million and \$7.2 million, respectively. Unused commitments do not necessarily represent future credit exposure or cash requirements, as commitments often expire without being drawn upon. We do not anticipate any material losses arising from commitments or contingent liabilities, and we do not believe that there are any material commitments to extend credit that represent risks of an unusual nature.

Contractual Obligations

In addition to the financing commitments detailed above under “Off-Balance Sheet Activities,” in the normal course of business, we enter into contractual obligations that require future cash settlement. The following table summarizes the contractual cash obligations as of December 31, 2018 and the expected timing of those payments:

| | Within one year | After one but within three years | After three but within five years | After five years | Total |
|---------------------------------|--------------------|---|--|---------------------|------------|
| Federal Home Loan Bank advances | \$ 286,660 | \$ 15,000 | \$ — | \$ — | \$ 301,660 |
| Operating lease obligations | 3,092 | 6,072 | 5,099 | 10,163 | 24,426 |
| Purchase obligations | 9,750 | 11,018 | 4,125 | — | 24,893 |

Edgar Filing: National Bank Holdings Corp - Form 10-K

| | | | | | |
|---------------|------------|------------|-----------|-----------|--------------|
| Time deposits | 685,421 | 354,890 | 37,908 | 2,310 | 1,080,529 |
| Total | \$ 984,922 | \$ 386,980 | \$ 47,132 | \$ 12,473 | \$ 1,431,507 |

Impact of Inflation and Changing Prices

The primary impact of inflation on our operations is reflected in increasing operating costs and is reflected in non-interest expense. Unlike most industrial companies, virtually all of our assets and liabilities are monetary in nature. As a result, changes in interest rates have a more significant impact on our performance than do changes in the general rate of inflation and changes in prices. Interest rate changes do not necessarily move in the same direction, nor have the same magnitude, as changes in the prices of goods and services. Although not as critical to the banking industry as many other industries, inflationary factors may have some impact on our ability to grow, total assets, earnings, and capital levels. We do not expect inflation to be a significant factor in our financial results in the near future.

Item 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.

The information called for by this item is provided under the caption Asset/Liability Management and Interest Rate Risk in Part I, Item 2-Management's Discussion and Analysis of Financial Condition and Results of Operations and is incorporated herein by reference.

Table of Contents

Item 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA.

Report of Independent Registered Public Accounting Firm

To the Shareholders and Board of Directors
National Bank Holdings Corporation:

Opinion on the Consolidated Financial Statements

We have audited the accompanying consolidated statements of financial condition of National Bank Holdings Corporation and subsidiaries (the Company) as of December 31, 2018 and 2017, the related consolidated statements of operations, comprehensive income, shareholders' equity, and cash flows for each of the years in the three year period ended December 31, 2018, and the related notes (collectively, the consolidated financial statements). In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of the Company as of December 31, 2018 and 2017, and the results of its operations and its cash flows for each of the years in the three year period ended December 31, 2018, in conformity with U.S. generally accepted accounting principles.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States) (PCAOB), the Company's internal control over financial reporting as of December 31, 2018, based on criteria established in Internal Control – Integrated Framework (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission, and our report dated March 1, 2019 expressed an unqualified opinion on the effectiveness of the Company's internal control over financial reporting.

Basis for Opinion

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

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

We have served as the Company's auditor since 2010.

Kansas City, Missouri
March 1, 2019

74

Table of Contents

NATIONAL BANK HOLDINGS CORPORATION AND SUBSIDIARIES

Consolidated Statements of Financial Condition

December 31, 2018 and 2017

(In thousands, except share and per share data)

| | December 31, 2018 | December 31, 2017 |
|---|-------------------|-------------------|
| ASSETS | | |
| Cash and due from banks | \$ 109,056 | \$ 193,297 |
| Interest bearing bank deposits | 500 | 64,067 |
| Cash and cash equivalents | 109,556 | 257,364 |
| Investment securities available-for-sale (at fair value) | 791,102 | 855,345 |
| Investment securities held-to-maturity (fair value of \$230,926 and \$256,771 at December 31, 2018 and December 31, 2017, respectively) | 235,398 | 258,730 |
| Non-marketable securities | 27,555 | 15,030 |
| Loans | 4,092,308 | 3,178,947 |
| Allowance for loan losses | (35,692) | (31,264) |
| Loans, net | 4,056,616 | 3,147,683 |
| Loans held for sale | 48,120 | 4,629 |
| Other real estate owned | 10,596 | 10,491 |
| Premises and equipment, net | 109,986 | 93,708 |
| Goodwill | 115,027 | 59,630 |
| Intangible assets, net | 13,470 | 1,607 |
| Other assets | 159,240 | 139,248 |
| Total assets | \$ 5,676,666 | \$ 4,843,465 |
| LIABILITIES AND SHAREHOLDERS' EQUITY | | |
| Liabilities: | | |
| Deposits: | | |
| Non-interest bearing demand deposits | \$ 1,072,029 | \$ 902,439 |
| Interest bearing demand deposits | 688,255 | 474,607 |
| Savings and money market | 1,694,808 | 1,484,463 |
| Time deposits | 1,080,529 | 1,118,050 |
| Total deposits | 4,535,621 | 3,979,559 |
| Securities sold under agreements to repurchase | 66,047 | 130,463 |
| Federal Home Loan Bank advances | 301,660 | 129,115 |
| Other liabilities | 78,332 | 71,921 |
| Total liabilities | 4,981,660 | 4,311,058 |
| Shareholders' equity: | | |
| Common stock, par value \$0.01 per share: 400,000,000 shares authorized; 51,498,016 and 51,518,162 shares issued; 30,769,063 and 26,875,585 shares outstanding at December 31, 2018 and December 31, 2017, respectively | 515 | 515 |
| Additional paid-in capital | 1,014,399 | 970,668 |
| Retained earnings | 106,990 | 60,795 |

Edgar Filing: National Bank Holdings Corp - Form 10-K

| | | |
|--|--------------|--------------|
| Treasury stock of 20,582,459 and 24,479,020 shares at December 31, 2018 and December 31, 2017, respectively, at cost | (415,623) | (493,329) |
| Accumulated other comprehensive loss, net of tax | (11,275) | (6,242) |
| Total shareholders' equity | 695,006 | 532,407 |
| Total liabilities and shareholders' equity | \$ 5,676,666 | \$ 4,843,465 |

See accompanying notes to the consolidated financial statements.

75

Table of Contents

NATIONAL BANK HOLDINGS CORPORATION AND SUBSIDIARIES

Consolidated Statements of Operations

For the Years Ended December 31, 2018, 2017 and 2016

(In thousands, except share and per share data)

| | 2018 | 2017 | 2016 |
|--|------------|------------|------------|
| Interest and dividend income: | | | |
| Interest and fees on loans | \$ 193,124 | \$ 137,249 | \$ 129,317 |
| Interest and dividends on investment securities | 25,746 | 24,841 | 29,665 |
| Dividends on non-marketable securities | 1,096 | 839 | 748 |
| Interest on interest-bearing bank deposits | 1,425 | 1,492 | 718 |
| Total interest and dividend income | 221,391 | 164,421 | 160,448 |
| Interest expense: | | | |
| Interest on deposits | 21,041 | 16,172 | 13,963 |
| Interest on borrowings | 2,913 | 1,943 | 845 |
| Total interest expense | 23,954 | 18,115 | 14,808 |
| Net interest income before provision for loan losses | 197,437 | 146,306 | 145,640 |
| Provision for loan losses | 5,197 | 12,972 | 23,651 |
| Net interest income after provision for loan losses | 192,240 | 133,334 | 121,989 |
| Non-interest income: | | | |
| Service charges | 18,092 | 14,634 | 13,900 |
| Bank card fees | 14,489 | 12,026 | 11,429 |
| Mortgage banking income | 30,107 | 2,154 | 2,881 |
| Bank-owned life insurance income | 1,791 | 1,871 | 1,861 |
| Other non-interest income | 5,379 | 8,082 | 7,708 |
| OREO related income | 917 | 438 | 2,248 |
| Total non-interest income | 70,775 | 39,205 | 40,027 |
| Non-interest expense: | | | |
| Salaries and benefits | 114,939 | 80,188 | 79,765 |
| Occupancy and equipment | 28,493 | 20,994 | 22,904 |
| Telecommunications and data processing | 10,098 | 7,188 | 5,970 |
| Marketing and business development | 4,513 | 2,683 | 2,564 |
| FDIC deposit insurance | 2,475 | 2,762 | 3,236 |
| Bank card expenses | 5,453 | 3,986 | 4,440 |
| Professional fees | 6,059 | 3,330 | 3,496 |
| Other non-interest expense | 13,073 | 10,360 | 8,554 |
| Problem asset workout | 2,549 | 3,994 | 3,983 |
| Gain on OREO sales, net | (488) | (4,150) | (4,383) |
| Core deposit intangible asset amortization | 2,170 | 5,342 | 5,480 |
| Total non-interest expense | 189,334 | 136,677 | 136,009 |
| Income before income taxes | 73,681 | 35,862 | 26,007 |
| Income tax expense | 12,230 | 21,283 | 2,947 |
| Net income | \$ 61,451 | \$ 14,579 | \$ 23,060 |

Edgar Filing: National Bank Holdings Corp - Form 10-K

| | | | |
|---|------------|------------|------------|
| Income per share—basic | \$ 2.00 | \$ 0.54 | \$ 0.81 |
| Income per share—diluted | \$ 1.95 | \$ 0.53 | \$ 0.79 |
| Weighted average number of common shares outstanding: | | | |
| Basic | 30,748,234 | 26,928,763 | 28,313,061 |
| Diluted | 31,430,074 | 27,709,659 | 29,091,343 |

See accompanying notes to the consolidated financial statements.

Table of Contents

NATIONAL BANK HOLDINGS CORPORATION AND SUBSIDIARIES

Consolidated Statements of Comprehensive Income

For the Years Ended December 31, 2018, 2017 and 2016

(In thousands)

| | 2018 | 2017 | 2016 |
|---|-----------|-----------|-----------|
| Net income | \$ 61,451 | \$ 14,579 | \$ 23,060 |
| Other comprehensive loss, net of tax: | | | |
| Securities available-for-sale: | | | |
| Net unrealized (losses) gains arising during the period, net of tax (expense) benefit of (\$876), \$1,871 and (\$26) for the years ended December 31, 2018, 2017 and 2016, respectively | (2,243) | (3,128) | 42 |
| Less: amortization of net unrealized holding gains to income, net of tax benefit of \$361, \$828 and \$1,166 for the years ended December 31, 2018, 2017 and 2016, respectively | (1,311) | (1,352) | (1,899) |
| Other comprehensive loss | (3,554) | (4,480) | (1,857) |
| Comprehensive income | \$ 57,897 | \$ 10,099 | \$ 21,203 |

See accompanying notes to the consolidated financial statements.

Table of Contents

NATIONAL BANK HOLDINGS CORPORATION AND SUBSIDIARIES

Consolidated Statements of Changes in Shareholders' Equity

For the Years Ended 2018, 2017 and 2016

(In thousands, except share and per share data)

| | Common stock | Additional paid-in capital | Retained earnings | Treasury stock | Accumulated other comprehensive (loss), net | Total |
|---|-----------------|----------------------------------|----------------------|-------------------|--|------------|
| Balance, December 31, 2015 | \$ 513 | \$ 997,926 | \$ 38,670 | \$ (419,660) | \$ 95 | \$ 617,544 |
| Net income | — | — | 23,060 | — | — | 23,060 |
| Stock-based compensation | — | 3,492 | — | — | — | 3,492 |
| Issuance of stock under equity compensation plan, including gain on reissuance of treasury stock of \$96, net | 1 | (13,790) | — | 7,588 | — | (6,201) |
| Repurchase of 8,645,836 shares | — | — | — | (93,573) | — | (93,573) |
| Cash dividends declared (\$0.20 per share) | — | — | (6,276) | — | — | (6,276) |
| Warrant reclassification | — | (3,541) | — | 3,541 | — | — |
| Other comprehensive loss | — | — | — | — | (1,857) | (1,857) |
| Balance, December 31, 2016 | \$ 514 | \$ 984,087 | \$ 55,454 | \$ (502,104) | \$ (1,762) | \$ 536,189 |
| Net income | — | — | 14,579 | — | — | 14,579 |
| Stock-based compensation | — | 3,648 | — | — | — | 3,648 |
| Issuance of stock under purchase and equity compensation plans, including gain on reissuance of treasury stock of \$6,118, net | 1 | (15,134) | — | 6,842 | — | (8,291) |
| Cash dividends declared (\$0.34 per share) | — | — | (9,238) | — | — | (9,238) |
| Warrant exercise | — | (1,933) | — | 1,933 | — | — |
| Other comprehensive income | — | — | — | — | (4,480) | (4,480) |
| Balance, December 31, 2017 | \$ 515 | \$ 970,668 | \$ 60,795 | \$ (493,329) | \$ (6,242) | \$ 532,407 |
| Net income | — | — | 61,451 | — | — | 61,451 |
| Stock-based compensation | — | 4,420 | — | — | — | 4,420 |

| | | | | | | |
|--|--------|--------------|------------|--------------|-------------|------------|
| Issuance of stock under purchase and equity compensation plans, including gain on reissuance of treasury stock of \$7,998, net | — | (2,932) | — | 9,736 | — | 6,804 |
| Reissuance of treasury stock of 3,398,477 shares for acquisition of Peoples, Inc. | — | 42,243 | — | 67,970 | — | 110,213 |
| Cash dividends declared (\$0.54 per share) | — | — | (16,761) | — | — | (16,761) |
| Reclassification of certain tax effects from accumulated other comprehensive income(1) | — | — | 1,479 | — | (1,479) | — |
| Cumulative effect adjustment(2) | — | — | 26 | — | — | 26 |
| Other comprehensive loss | — | — | — | — | (3,554) | (3,554) |
| Balance, December 31, 2018 | \$ 515 | \$ 1,014,399 | \$ 106,990 | \$ (415,623) | \$ (11,275) | \$ 695,006 |

- (1) Related to the adoption of Accounting Standards Update No. 2018-02, Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income. Refer to note 2 – Recent Accounting Pronouncements of our consolidated financial statements for further details.
- (2) Related to the adoption of Accounting Standards Update No. 2017-12, Derivatives and Hedging: Targeted Improvements to Accounting for Hedging Activities. Refer to note 2 – Recent Accounting Pronouncements of our consolidated financial statements for further details.

See accompanying notes to the consolidated financial statements.

Table of Contents

NATIONAL BANK HOLDINGS CORPORATION AND SUBSIDIARIES

Consolidated Statements of Cash Flows

For the Years Ended December 31, 2018, 2017 and 2016

(In thousands)

| | 2018 | 2017 | 2016 |
|---|-------------|-----------|-----------|
| Cash flows from operating activities: | | | |
| Net income | \$ 61,451 | \$ 14,579 | \$ 23,060 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | | |
| Provision for loan losses | 5,197 | 12,972 | 23,651 |
| Depreciation and amortization | 11,522 | 12,889 | 14,203 |
| Current income tax receivable | 4,246 | 1,260 | 4,176 |
| Deferred income taxes | 9,092 | 17,180 | (176) |
| Net excess tax benefit on stock-based compensation | (1,286) | (4,225) | (2,078) |
| Discount accretion, net of premium amortization on securities | 2,911 | 2,581 | 3,067 |
| Loan accretion | (23,115) | (23,933) | (35,073) |
| Gain on sale of mortgages, net | (27,009) | (2,154) | (2,881) |
| Origination of loans held for sale, net of repayments | (1,005,850) | (85,959) | (114,397) |
| Proceeds from sales of loans held for sale | 1,030,906 | 101,935 | 101,098 |
| Bank-owned life insurance income | (1,791) | (1,871) | (1,861) |
| Impairment on mortgage servicing rights | 21 | — | — |
| Originations of mortgage servicing rights | (30) | — | — |
| Gain on the sale of other real estate owned, net | (488) | (4,150) | (4,383) |
| Impairment on other real estate owned | 230 | 766 | 298 |
| Loss on sale of fixed assets | (15) | (2,853) | (1,981) |
| Stock-based compensation | 4,420 | 3,648 | 3,492 |
| Acquisition-related costs | (7,957) | (2,691) | — |
| (Increase) decrease in other assets | (3,630) | 6,040 | (4,721) |
| Increase (decrease) in other liabilities | 14,749 | 12,125 | (9,430) |
| Net cash provided by (used in) operating activities | 73,574 | 58,139 | (3,936) |
| Cash flows from investing activities: | | | |
| Purchase of FHLB stock | (16,463) | (7,448) | (5,544) |
| Proceeds from redemption of FHLB stock | 12,062 | 6,877 | 7,670 |
| Purchase of FRB stock | (4,716) | — | — |
| Proceeds from redemption of FRB stock | 1,371 | — | 4,964 |
| Proceeds from maturities of investment securities held-to-maturity | 61,913 | 71,105 | 91,376 |
| Proceeds from maturities of investment securities available-for-sale | 216,077 | 224,336 | 275,448 |
| Proceeds from sales of investment securities available-for-sale | 33,637 | — | — |
| Proceeds from maturities of non-marketable securities | 67 | 490 | 490 |
| Purchase of investment securities held-to-maturity | (40,735) | — | — |
| Purchase of investment securities available-for-sale | (72,555) | (202,694) | (4,872) |
| Net increase in loans | (382,441) | (314,008) | (270,585) |

Edgar Filing: National Bank Holdings Corp - Form 10-K

| | | | |
|---|-------------|------------|------------|
| Purchases of premises and equipment, net | (6,277) | (5,617) | 690 |
| Purchase of bank-owned life insurance | — | — | (10,344) |
| Proceeds from sales of loans | 713 | 38,087 | 9,231 |
| Proceeds from sales of other real estate owned | 26,346 | 10,355 | 16,105 |
| Net cash activity from acquisition | 68,984 | — | — |
| Net cash (used in) provided by investing activities | (102,017) | (178,517) | 114,629 |
| Cash flows from financing activities: | | | |
| Net (decrease) increase in deposits | (173,849) | 113,796 | 27,972 |
| (Decrease) increase in repurchase agreements | (64,416) | 38,452 | (44,512) |
| Advances from FHLB | 889,416 | 263,129 | 218,629 |
| FHLB payoffs | (750,696) | (172,679) | (219,964) |
| Issuance of stock under purchase and equity compensation plans | (772) | (8,395) | (6,201) |
| Proceeds from exercise of stock options | 7,576 | 104 | — |
| Payment of dividends | (16,624) | (9,401) | (6,400) |
| Repurchase of shares | — | — | (93,573) |
| Net cash (used in) provided by financing activities | (109,365) | 225,006 | (124,049) |
| (Decrease) increase in cash, cash equivalents and restricted cash | (137,808) | 104,628 | (13,356) |
| Cash, cash equivalents and restricted cash at beginning of the year | 257,364 | 152,736 | 166,092 |
| Cash, cash equivalents and restricted cash at end of period | \$ 119,556 | \$ 257,364 | \$ 152,736 |
| Supplemental disclosure of cash flow information during the period: | | | |
| Cash paid for interest | \$ 22,714 | \$ 17,312 | \$ 14,154 |
| Net tax refunds | \$ 2,345 | \$ 127 | \$ 2,193 |
| Supplemental schedule of non-cash investing activities: | | | |
| Loans transferred to other real estate owned at fair value | \$ 24,940 | \$ 1,800 | \$ 6,868 |
| (Decrease) increase in loans purchased but not settled | \$ (21,202) | \$ 25,118 | \$ (4,873) |
| Loans transferred from loans held for sale to loans | \$ 1,038 | \$ 5,736 | \$ 5,285 |
| Treasury stock reissued for acquisition | \$ 110,213 | \$ — | \$ — |

See accompanying notes to the consolidated financial statements.

Table of Contents

NATIONAL BANK HOLDINGS CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2018, 2017 and 2016

Note 1 Basis of Presentation

National Bank Holdings Corporation ("NBHC" or the "Company") is a bank holding company that was incorporated in the State of Delaware in 2009. The Company is headquartered immediately south of Denver, in Greenwood Village, Colorado, and its primary operations are conducted through its wholly owned subsidiary, NBH Bank, (the "Bank"), a Colorado state-chartered bank and a member of the Federal Reserve System. The Company provides a variety of banking products to both commercial and consumer clients through a network of 104 banking centers as of December 31, 2018, located primarily in Colorado and the greater Kansas City region, and through online and mobile banking products and services. On January 1, 2018, the Company completed the acquisition of Peoples, Inc. Refer to note 4 – Acquisition Activities for further details.

The accompanying consolidated financial statements include the accounts of the Company and its wholly owned subsidiary, NBH Bank. The accompanying consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles ("GAAP") and where applicable, with general practices in the banking industry or guidelines prescribed by bank regulatory agencies. The consolidated financial statements reflect all adjustments which are, in the opinion of management, necessary for a fair statement of the results presented. All such adjustments are of a normal recurring nature. All significant intercompany balances and transactions have been eliminated in consolidation. Certain reclassifications of prior years' amounts are made whenever necessary to conform to current period presentation. All amounts are in thousands, except share data, or as otherwise noted.

Beginning in the first quarter 2018, loans previously referred to as "non 310-30 loans" are referred to as "originated and acquired loans," which include originated loans as well as acquired loans not accounted for under ASC 310-30. No amounts were reclassified resulting from this change in terminology.

The Company's significant accounting policies followed in the preparation of the consolidated financial statements are disclosed in note 2. GAAP requires management to make estimates that affect the reported amounts of assets, liabilities, revenues and expenses, and disclosures of contingent assets and liabilities. By their nature, estimates are based on judgment and available information. Management has made significant estimates in certain areas, such as the amount and timing of expected cash flows from assets, the valuation of other real estate owned ("OREO"), the fair value adjustments on assets acquired and liabilities assumed, the valuation of core deposit intangible assets, the valuation of investment securities for other-than-temporary impairment ("OTTI"), the valuation of stock-based compensation, the valuation of mortgage servicing rights, the fair values of financial instruments, the allowance for loan losses ("ALL"), and contingent liabilities. Because of the inherent uncertainties associated with any estimation process and future changes in market and economic conditions, it is possible that actual results could differ significantly from those estimates.

Note 2 Summary of Significant Accounting Policies

a) Acquisition activities—The Company accounts for business combinations under the acquisition method of accounting. Assets acquired and liabilities assumed are measured and recorded at fair value at the date of acquisition, including identifiable intangible assets. If the fair value of net assets acquired exceeds the fair value of consideration paid, a bargain purchase gain is recognized at the date of acquisition. Conversely, if the consideration paid exceeds the fair value of the net assets acquired, goodwill is recognized at the acquisition date. Fair values are subject to refinement for up to a maximum of one year after the closing date of an acquisition as information relative to closing date fair values becomes available. Adjustments recorded to the acquired assets and liabilities assumed are applied prospectively in accordance with Accounting Standards Codification (“ASC”) 805, Business Combinations. The determination of the fair value of loans acquired takes into account credit quality deterioration and probability of loss; therefore, the related ALL is not carried forward at the time of acquisition.

Identifiable intangible assets are recognized separately if they arise from contractual or other legal rights or if they are separable (i.e., capable of being sold, transferred, licensed, rented, or exchanged separately from the entity). Deposit liabilities and the related depositor relationship intangible assets, known as the core deposit intangible assets, may be

Table of Contents

exchanged in observable exchange transactions. As a result, the core deposit intangible asset is considered identifiable, because the separability criterion has been met.

b) Cash and cash equivalents—Cash and cash equivalents include cash, cash items, amounts due from other banks, amounts due from the Federal Reserve Bank of Kansas City, federal funds sold, and interest-bearing bank deposits. In addition, December 31, 2017 cash and cash equivalents included segregated cash held for the acquisition of Peoples, Inc.

c) Investment securities—Investment securities may be classified in three categories: trading, available-for-sale or held-to-maturity. Management determines the appropriate classification at the time of purchase and reevaluates the classification at each reporting period. Any sales of available-for-sale securities are for the purpose of executing the Company's asset/liability management strategy, reducing borrowings, funding loan growth, providing liquidity, or eliminating a perceived credit risk in a specific security. Held-to-maturity securities are carried at amortized cost and the available-for-sale securities are carried at estimated fair value. Unrealized gains or losses on securities available-for-sale are reported as accumulated other comprehensive income (loss) ("AOCI"), a component of shareholders' equity, net of income tax. Gains and losses realized upon sales of securities are calculated using the specific identification method. Premiums and discounts are amortized to interest income over the estimated lives of the securities. Prepayment experience is periodically evaluated and a determination made regarding the appropriate estimate of the future rates of prepayment. When a change in a bond's estimated remaining life is necessary, a corresponding adjustment is made in the related premium amortization or discount accretion. Purchases and sales of securities, including any corresponding gains or losses, are recognized on a trade-date basis and a receivable or payable is recognized for pending transaction settlements.

Management evaluates all investments for OTTI on a quarterly basis, and more frequently when economic or market conditions warrant such evaluation. Impairment is considered to be other-than-temporary if it is likely that all amounts contractually due will not be received for debt securities and when there is no positive evidence indicating that an investment's carrying amount is recoverable in the near term for equity securities. When impairment is considered other-than-temporary, the cost basis of the security is written down to fair value, with the impairment charge related to credit included in earnings, while the impairment charge related to all other factors is recognized in OCI. If the Company has the intent to sell the security or it is more likely than not that the Company will be required to sell the security, the entire amount of the OTTI is recorded in earnings. In evaluating whether the impairment is temporary or other than temporary, the Company considers, among other things, the severity and duration of the unrealized loss position; adverse conditions specifically related to the security; changes in expected future cash flows; downgrades in the rating of the security by a rating agency; the failure of the issuer to make scheduled interest or principal payments; whether the Company has the intent to sell the security; and whether it is more likely than not that the Company will be required to sell the security.

d) Non-marketable securities—Non-marketable securities include Federal Reserve Bank ("FRB") stock and Federal Home Loan Bank ("FHLB") stock. These securities have been acquired for debt facility or regulatory purposes and are carried at cost.

e) Loans receivable—Loans receivable include loans originated by the Company and loans that are acquired through acquisitions. Loans originated by the Company are carried at the principal amount outstanding, net of premiums, discounts, unearned income, and deferred loan fees and costs. Loan fees and certain costs of originating loans are deferred and the net amount is amortized over the contractual life of the related loans. Acquired loans are initially recorded at fair value and are accounted for under either ASC 310-30, Loans and Debt Securities Acquired with Deteriorated Credit Quality (see additional information below) or ASC Topic 310, Receivables. Non-refundable loan origination and commitment fees, net of direct costs of originating or acquiring loans, and fair value adjustments for acquired loans, are deferred and recognized over the remaining lives of the related loans in accordance with ASC 310-20.

Acquired loans are recorded at their estimated fair value at the time of acquisition and accounted for under either ASC 310-30 or ASC 310. Estimated fair values of acquired loans are based on a discounted cash flow methodology that considers various factors including the type of loan and related collateral, the expected timing of cash flows, classification status, fixed or variable interest rate, term of loan and whether or not the loan is amortizing, and a discount rate reflecting the Company's assessment of risk inherent in the cash flow estimates. Acquired 310-30 loans are grouped together according to similar characteristics such as type of loan, loan purpose, geography, risk rating and underlying collateral and are treated as distinct pools when applying various valuation techniques and, in certain circumstances, for the ongoing monitoring of the credit

Table of Contents

quality and performance of the pools. Each pool is accounted for as a single loan for which the integrity is maintained throughout the life of the asset. Discounts created when the loans are recorded at their estimated fair values at acquisition are accreted over the remaining term of the loan as an adjustment to the related loan's yield. Similar to originated loans described below, the accrual of interest income on acquired loans that are not accounted for under ASC 310-30 is discontinued when the collection of principal or interest, in whole or in part, is doubtful.

Interest income on acquired loans that are accounted for under ASC Topic 310 and interest income on loans originated by the Company is accrued and credited to income as it is earned using the interest method based on daily balances of the principal amount outstanding. However, interest is generally not accrued on loans 90 days or more past due, unless they are well secured and in the process of collection. Additionally, in certain situations, loans that are not contractually past due may be placed on non-accrual status due to the continued failure to adhere to contractual payment terms by the borrower coupled with other pertinent factors, such as insufficient collateral value or deficient primary and secondary sources of repayment. Accrued interest receivable is reversed when a loan is placed on non-accrual status and payments received generally reduce the carrying value of the loan. Interest is not accrued while a loan is on non-accrual status and interest income is generally recognized on a cash basis only after payment in full of the past due principal and collection of principal outstanding is reasonably assured. A loan may be placed back on accrual status if all contractual payments have been received, or sooner under certain conditions and collection of future principal and interest payments is no longer doubtful.

In the event of borrower default, the Company may seek recovery in compliance with state lending laws, the respective loan agreements, and credit monitoring and remediation procedures that may include modifying or restructuring a loan from its original terms, for economic or legal reasons, to provide a concession to the borrower from their original terms due to borrower financial difficulties in order to facilitate repayment. Such restructured loans are considered "troubled debt restructurings" and are identified in accordance with ASC 310-40, Troubled Debt Restructurings by Creditors. Under this guidance, modifications to loans that fall within the scope of ASC 310-30 are not considered troubled debt restructurings, regardless of otherwise meeting the definition of a troubled debt restructuring.

Loans receivable accounted for under ASC 310-30

The Company accounts for and evaluates acquired loans in accordance with the provisions of ASC 310-30, Loans and Debt Securities Acquired with Deteriorated Credit Quality. When loans exhibit evidence of credit deterioration since origination and it is probable at the date of acquisition that the Company will not collect all principal and interest payments in accordance with the terms of the loan agreement, the expected shortfall in future cash flows, as compared to the contractual amount due, is recognized as a non-accretable difference. Any excess of expected cash flows over the acquisition date fair value is known as the accretable yield, and is recognized as accretion income over the life of each pool. Contractual fees not expected to be collected are not included in ASC 310-30 contractual cash flows. Should fees be subsequently collected, the cash flows are accounted for as originated and acquired fee income in the period they are received. Loans that are accounted for under ASC 310-30 that meet the criteria for non-accrual of interest or are accounted for on the cost recovery method at the time of acquisition or subsequent to acquisition, may be considered performing, regardless of whether the client is contractually delinquent, if the timing and expected cash

flows on the loan pool in which the loan is included can be otherwise reasonably estimated and if collection of the new carrying value of such pool is expected.

The expected cash flows of individual loans accounted for under ASC 310-30 are periodically remeasured utilizing the same cash flow methodology used at the time of acquisition and subsequent decreases to the expected cash flows will generally result in a provision for loan losses charge in the Company's consolidated statements of operations. Any increases to the loan cash flow projections are recognized within the loan's respective loan pools on a prospective basis through an increase to the pool's accretion income over its remaining life once any previously recorded provision expense has been reversed. These cash flow evaluations are inherently subjective as they require material estimates, all of which may be susceptible to significant change.

f) Loans held for sale—The Company has elected to record loans originated and intended for sale in the secondary market at estimated fair value. The Company estimates fair value based on quoted market prices for similar loans in the secondary market. Gains or losses are recognized upon sale and are included as a component of gain on sale of mortgages, net in the consolidated statements of operations. Loans held for sale have primarily been fixed rate single-family residential mortgage loans under contract to be sold in the secondary market. In most cases, loans in this category are sold within 45 days. These

Table of Contents

loans are generally sold with the mortgage servicing rights released. Under limited circumstances, buyers may have recourse to return a purchased loan to the Company. Recourse conditions may include early payoff, early payment default, breach of representations or warranties, or documentation deficiencies.

The Company enters into commitments to originate residential mortgage loans whereby the interest rate on the loan is determined prior to funding (i.e. interest rate lock commitments). Such interest rate lock commitments on mortgage loans to be sold in the secondary market are considered to be derivatives. To protect against the price risk inherent in residential mortgage loan commitments, the Company utilizes both "best efforts" and "mandatory delivery" forward loan sale commitments to mitigate the risk of potential increases or decreases in the values of loans that would result from the change in market rates for such loans. The Company manages the interest rate risk on interest rate lock commitments by entering into forward sale contracts of mortgage backed securities. Such contracts are accounted for as derivatives and are recorded at fair value as derivative assets or liabilities. They are carried on the consolidated statements of financial condition within other assets or other liabilities and changes in fair value are recorded as a component of gain on sale of mortgages, net in the consolidated statements of operations. The gross gains on loan sales are recognized based on new loan commitments with adjustment for price and pair-off activity. Commission expenses on loans held for sale are recognized based on loans closed.

g) Allowance for loan losses—The allowance for loan losses represents management’s estimate of probable credit losses inherent in loans, including acquired loans to the extent necessary, as of the balance sheet date. The determination of the ALL takes into consideration, among other matters, the estimated fair value of the underlying collateral, economic conditions, historical net loan losses, the estimated loss emergence period, estimated default rates, any declines in cash flow assumptions from acquisition, loan structures, growth factors and other elements that warrant recognition. In addition, various regulatory agencies, as an integral part of the examination process, periodically review the ALL. Such agencies may require the Company to recognize additions to the ALL or increases to adversely graded classified loans based on their judgments about information available to them at the time of their examinations.

The Company uses an internal risk rating system to indicate credit quality in the loan portfolio. The risk rating system is applied to all loans and uses a series of grades, which reflect management’s assessment of the risk attributable to loans based on an analysis of the borrower’s financial condition and ability to meet contractual debt service requirements. Loans that management perceives to have acceptable risk are categorized as “Pass” loans. The “Special Mention” loans represent loans that have potential credit weaknesses that deserve management’s close attention. Special mention loans include borrowers that have potential weaknesses or unwarranted risks that, unless corrected, may threaten the borrower’s ability to meet debt requirements. However, these borrowers are still believed to have the ability to respond to and resolve the financial issues that threaten their financial situation. Loans classified as “Substandard” are inadequately protected by the current sound worth and paying capacity of the obligor or of the collateral pledged, if any. Substandard loans have a distinct possibility of loss if the deficiencies are not corrected. “Doubtful” loans are loans that management believes the collection of payments in accordance with the terms of the loan agreement is highly questionable and improbable. Loans accounted for under ASC 310-30, despite being 90 days or more past due or internally adversely classified, may be classified as performing upon and subsequent to acquisition, regardless of whether the client is contractually delinquent, if the timing and expected cash flows on the loan pool can be reasonably estimated and if collection of the carrying value of the loan pool loans is reasonably expected. Interest accrual is discontinued on doubtful loans and certain substandard loans that are excluded from ASC 310-30, as is more fully discussed in note 7.

The Company routinely evaluates adversely risk-rated credits for impairment. Impairment, if any, is typically measured for each loan based on a thorough analysis of the most probable source of repayment, including the present value of the loan's expected future cash flows, the loan's estimated fair value, or the estimated fair value of the underlying collateral less costs of disposition for collateral dependent loans. General allowances are established for loans with similar characteristics. In this process, general allowance factors are based on an analysis of historical loss and recovery experience, if any, related to originated and acquired loans, as well as certain industry experience, with adjustments made for qualitative or environmental factors that are likely to cause estimated credit losses to differ from historical experience. To the extent that the data supporting such factors has limitations, management's judgment and experience play a key role in determining the allowance estimates.

Additions to the ALL are made by provisions for loan losses that are charged to operations. The allowance is decreased by charge-offs due to losses and is increased by provisions for loan losses and recoveries. When it is determined that specific

Table of Contents

loans, or portions thereof, are uncollectible, these amounts are charged off against the ALL. If repayment of the loan is collateral dependent, the fair value of the collateral, less cost to sell, is used to determine charge-off amounts.

The Company maintains an ALL for loans accounted for under ASC 310-30 as a result of impairment to loan pools arising from the periodic re-measurement of these loans. Any impairment in the individual pool is generally recognized in the current period as provision for loan losses. Any improvement in the estimated cash flows, is generally not recognized immediately, but is instead reflected as an adjustment to the related loan pools yield on a prospective basis once any previously recorded impairment has been recaptured.

h) Premises and equipment—With the exception of premises and equipment acquired through business combinations, which are initially measured and recorded at fair value, purchased land is stated at cost, and buildings and equipment are carried at cost, including capitalized interest when appropriate, less accumulated depreciation. Depreciation is computed using the straight-line method over the estimated useful life of the asset. The Company generally assigns depreciable lives of 39 years for buildings, 7 to 15 years for building improvements, and 3 to 7 years for equipment. Leasehold improvements are amortized over the shorter of their estimated useful lives or remaining lease terms. Maintenance and repairs are charged to non-interest expense as incurred. The Company reviews premises and equipment whenever events or changes in circumstances indicate that the carrying amount of the asset may not be recoverable. An impairment loss is recognized when the sum of the undiscounted future net cash flows expected to result from the use of the asset and its eventual disposal is less than its carrying amount. In the case of a property that is subject to an operating lease that the Company no longer expects to use, a liability is recorded at the cease-use date equal to the remaining lease rentals, adjusted for the effects of any prepaid or deferred items recognized under the lease, and reduced by estimated sublease rentals that could be reasonably obtained for the property, even if the entity does not intend to enter into a sublease. A ratable portion of the sublease allocation is then expensed until the property is subleased. Property and equipment that meet the held-for-sale criteria is recorded at the lower of its carrying amount or fair value less cost to sell and depreciation is ceased.

i) Goodwill and intangible assets—Goodwill is established and recorded if the consideration given during an acquisition transaction exceeds the fair value of the net assets received. Goodwill has an indefinite useful life and is not amortized, but is evaluated annually for potential impairment, or when events or circumstances indicate that it is more likely than not that the fair value of the reporting unit is less than its carrying amount. Such events or circumstances may include deterioration in general economic conditions, deterioration in industry or market conditions, an increased competitive environment, a decline in market-dependent multiples or metrics, declining financial performance, entity-specific events or circumstances or a sustained decrease in share price (either in absolute terms or relative to peers). If the Company determines, based upon the qualitative assessment, that it is more likely than not that the fair value of the reporting unit is greater than the carrying amount no additional procedures are performed; however, if the Company determines that it is more likely than not that the fair value of the reporting unit is less than the carrying amount the Company will compare the fair value of the reporting unit to its carrying amount. Any excess of the carrying amount over fair value would indicate a potential impairment and the Company would proceed to perform an additional test to determine whether goodwill has been impaired and calculate the amount of that impairment.

Intangible assets that have finite useful lives, such as core deposit intangibles, are amortized over their estimated useful lives. The Company's core deposit intangible assets represent the value of the anticipated future cost savings that will result from the acquired core deposit relationships versus an alternative source of funding.

Judgment may be used in assessing goodwill and intangible assets for impairment. Estimates of fair value are based on projections of revenues, operating costs and cash flows of the reporting unit considering historical and anticipated future results, general economic and market conditions, as well as the impact of planned business or operational strategies. The valuations use a combination of present value techniques to measure fair value considering market factors. Additionally, judgment is used in determining the useful lives of finite-lived intangible assets. Adverse changes in the economic environment, operations of the reporting unit, or changes in judgments and projections could result in a significantly different estimate of the fair value of the reporting unit and could result in an impairment of goodwill and/or intangible assets.

j) Mortgage Servicing– Mortgage servicing rights (“MSRs”) associated with loans originated and sold, where servicing is retained, are initially capitalized at fair value and included in intangible assets, net on the consolidated statements of financial condition. For subsequent measurement purposes, the Company measures servicing assets based on the lower of cost or

Table of Contents

market using the amortization method. The values of these capitalized servicing rights are amortized as an offset to the loan servicing income earned in relation to the servicing revenue expected to be earned. The carrying values of these rights are reviewed quarterly for impairment based on the fair value of those assets. For purposes of impairment evaluation and measurement, management stratifies MSR's based on the predominant risk characteristics of the underlying loans, including loan type and loan term. If, by individual stratum, the carrying amount of these MSR's exceeds fair value, a valuation allowance is established and the impairment is recognized in mortgage banking income. If the fair value of impaired MSR's subsequently increases, management recognizes the increase in fair value in current period mortgage banking income and, through a reduction in the valuation allowance, adjusts the carrying value of the MSR's to a level not in excess of amortized cost.

k) Reserve for Mortgage Loan Repurchase Losses—The Company sells mortgage loans to various third parties, including government-sponsored entities, under contractual provisions that include various representations and warranties that typically cover ownership of the loan, compliance with loan criteria set forth in the applicable agreement, validity of the lien securing the loan, absence of delinquent taxes or liens against the property securing the loan, and similar matters. The Company may be required to repurchase the mortgage loans with identified defects, indemnify the investor or insurer, or reimburse the investor for credit loss incurred on the loan (collectively “repurchase”) in the event of a material breach of such contractual representations or warranties. Risk associated with potential repurchases or other forms of settlement is managed through underwriting and quality assurance practices.

The Company establishes mortgage repurchase reserves related to various representations and warranties that reflect management’s estimate of losses based on a combination of factors. Such factors incorporate actual and historic loss history, delinquency trends in the portfolio and economic conditions. The Company establishes a reserve at the time loans are sold and updates the reserve estimate quarterly during the estimated loan life. The repurchase reserve is included in other liabilities on the consolidated statements of financial condition.

l) Other real estate owned—OREO consists of property that has been foreclosed on or repossessed by deed in lieu of foreclosure. The assets are initially recorded at the fair value of the collateral less estimated costs to sell, with any initial valuation adjustments charged to the ALL. Subsequent downward valuation adjustments, if any, in addition to gains and losses realized on sales and net operating expenses, are recorded in non-interest expense, while any subsequent write-ups are recorded in non-interest income. Costs associated with maintaining property, such as utilities and maintenance, are charged to expense in the period in which they occur, while costs relating to the development and improvement of property are capitalized to the extent the balance does not exceed fair value. All OREO acquired through acquisition is recorded at fair value, less cost to sell, at the date of acquisition.

m) Bank-owned life insurance—The Company purchased or acquired bank-owned life insurance ("BOLI") policies on certain associates of the Company. The Company is the owner and beneficiary of these policies. The BOLI is carried at net realizable value with changes in net realizable value recorded in non-interest income.

n) Securities purchased under agreements to resell and securities sold under agreements to repurchase—The Company periodically enters into purchases or sales of securities under agreements to resell or repurchase as of a specified future date. The securities purchased under agreements to resell are accounted for as collateralized financing transactions and are reflected as an asset in the consolidated statements of financial condition. The securities pledged by the counterparties are held by a third party custodian and valued daily. The Company may require additional collateral to ensure full collateralization for these transactions. The repurchase agreements are considered financing agreements and the obligation to repurchase assets sold is reflected as a liability in the consolidated statements of financial condition of the Company. The repurchase agreements are collateralized by debt securities that are under the control of the Company.

o) Stock-based compensation—The Company accounts for stock-based compensation in accordance with ASC Topic 718, Compensation—Stock Compensation as amended by ASU 2016-09, Improvements to Employee Share-Based Payment Accounting. The Company grants stock-based awards including stock options, restricted stock and performance stock units. Stock option grants are for a fixed number of common shares and are issued at exercise prices which are not less than the fair value of a share of stock at the date of grant. The options vest over a time period stated in each option agreement and may be subject to other performance vesting conditions, which require the related compensation expense to be recorded ratably over the requisite service period starting when such conditions become probable. Restricted stock is granted for a fixed number of

Table of Contents

shares, the transferability of which is restricted until such shares become vested according to the terms in the award agreement. Restricted shares may have multiple vesting qualifications, which can include time vesting of a set portion of the restricted shares and performance criterion, such as market criteria that are tied to specified market conditions of the Company's common stock price and performance targets tied to the Company's earnings per share.

The fair value of stock options is measured using a Black-Scholes model. The fair value of time-based restricted stock awards and performance stock units with performance based vesting criteria is based on the Company's stock price on the date of grant. The fair value of performance stock units with market-based vesting criteria is measured using a Monte Carlo simulation model. Compensation expense for the portion of the awards that contain performance and service vesting conditions is recognized over the requisite service period based on the fair value of the awards on the grant date. Compensation expense for the portion of the awards that contain a market vesting condition is recognized over the derived service period based on the fair value of the awards on the grant date. The amortization of stock-based compensation reflects any estimated forfeitures, and the expense realized in subsequent periods may be adjusted to reflect the actual forfeitures realized. The outstanding stock options primarily carry a maximum contractual term of ten years. To the extent that any award is forfeited, surrendered, terminated, expires, or lapses without being vested or exercised, the shares of stock subject to such award not delivered as a result thereof are again made available for awards under the Plan.

All excess tax benefits and tax deficiencies (including tax benefits of dividends on share-based payment awards) are recognized in the consolidated statements of operations as a component of income tax expense or benefit and are classified as an operating activity within the Company's consolidated statements of cash flows. The tax effects of exercised, expired or vested awards are treated as discrete items in the reporting period in which they occur and may result in increased volatility in our effective tax rate. Cash paid by the Company when directly withholding shares for tax withholding purposes is classified as a financing activity in the consolidated statements of cash flows.

Prior to the Company's adoption of ASU 2016-09 during 2016, excess tax benefits were recognized in additional paid-in capital and tax deficiencies were recognized either as an offset to accumulated excess tax benefits, if any, or in the consolidated statements of operations. Excess tax benefits were not recognized until the deduction reduced taxes payable.

p) Warrants—The Company issued warrants to certain lead investors in 2009 and 2010. During 2015, the outstanding warrant contracts were modified and recorded at fair value as of the modification date using a Black-Scholes model with the change in fair value reported in the statement of operations as non-interest expense. The awards were classified as equity in the Company's consolidated statements of financial condition. Prior to the modification, the exercise price and the number of warrants were subject to certain down-round provisions, whereby certain subsequent equity issuances at a price below the existing exercise price would result in a downward adjustment to the exercise price and an increase in the number of warrants, and as a result, the warrants were historically classified as a liability in the Company's consolidated statements of financial condition with changes in the fair value each period reported in the statements of operations as non-interest expense.

During the first quarter of 2017, the remaining issued warrants were exercised in a non-cash transaction. Refer to the consolidated statements of changes in shareholders' equity for additional details.

q) Income taxes—The Company and its subsidiaries file U.S. federal and certain state income tax returns on a consolidated basis. Additionally, the Company and its subsidiaries file separate state income tax returns with various state jurisdictions. The provision for income taxes includes the income tax balances of the Company and all of its subsidiaries.

Deferred tax assets and liabilities are recognized for temporary differences between the financial reporting basis and the tax basis of the Company's assets and liabilities at enacted tax rates expected to be in effect when such amounts are realized or settled. Deferred tax assets and liabilities are adjusted for the effects of changes in tax rates in the period of change. The Company establishes a valuation allowance when management believes, based on the weight of available evidence, it is more likely than not that some portion of the deferred tax assets will not be realized.

The Company recognizes and measures income tax benefits based upon a two-step model: 1) a tax position must be more likely than not to be sustained based solely on its technical merits in order to be recognized; and 2) the benefit is measured as the largest dollar amount of that position that is more likely than not to be sustained upon settlement. The difference between

Table of Contents

the benefit recognized for a position in this model and the tax benefit claimed on a tax return is treated as an unrecognized tax benefit. The Company recognizes income tax related interest and penalties in other non-interest expense.

r) Income per share—The Company applies the two-class method of computing income per share as certain of the Company's restricted shares are entitled to non-forfeitable dividends and are therefore considered to be a class of participating securities. The two-class method allocates income according to dividends declared and participation rights in undistributed income. Basic income per share is computed by dividing income allocated to common shareholders by the weighted average number of common shares outstanding during each period. Diluted income per common share is computed by dividing income allocated to common shareholders by the weighted average common shares outstanding during the period, plus amounts representing the dilutive effect of stock options outstanding, certain unvested restricted shares, warrants to issue common stock, or other contracts to issue common shares (“common stock equivalents”) using the treasury stock method. Common stock equivalents are excluded from the computation of diluted earnings per common share in periods in which they have an anti-dilutive effect.

s) Interest Rate Swap Derivatives—The Company carries all derivatives on the statement of financial condition at fair value. All derivative instruments are recognized as either assets or liabilities depending on the rights or obligations under the contracts. All gains and losses on the derivatives due to changes in fair value are recognized in earnings each period.

The Company offers interest rate swap products to certain of its clients to manage potential changes in interest rates. Each contract between the Company and a client is offset with a contract between the Company and an institutional counterparty, thus minimizing the Company's exposure to rate changes. The Company's portfolio consists of a “matched book,” and as such, changes in fair value of the swap pairs will largely offset in earnings. In accordance with applicable accounting guidance, if certain conditions are met, a derivative may be designated as (1) a hedge of the exposure to changes in the fair value of a recognized asset or liability, or of an unrecognized firm commitment, that are attributable to a particular risk (referred to as a fair value hedge) or (2) a hedge of the exposure to variability in the cash flows of a recognized asset or liability, or of a forecasted transaction, that is attributable to a particular risk (referred to as a cash flow hedge). The Company documents all hedging relationships at the inception of each hedging relationship and uses industry accepted methodologies and ranges to determine the effectiveness of each hedge. The fair value of the hedged item is calculated using the estimated future cash flows of the hedged item and applying discount rates equal to the market interest rate for the hedged item at the inception of the hedging relationship (inception benchmark interest rate plus an inception credit spread), adjusted for changes in the designated benchmark interest rate thereafter.

t) Treasury stock —When the Company acquires treasury stock, the sum of the consideration paid and direct transaction costs after tax is recognized as a deduction from equity. The cost basis for the reissuance of treasury stock is determined using a first-in, first-out basis. To the extent that the reissuance price is more than the cost basis (gain), the excess is recorded as an increase to additional paid-in capital in the consolidated statements of financial condition. If the reissuance price is less than the cost basis (loss), the difference is recorded to additional paid-in capital to the extent there is a cumulative treasury stock paid-in capital balance. Any loss in excess of the cumulative treasury stock

paid-in capital balance is charged to retained earnings.

Note 3 Recent Accounting Pronouncements

Revenue from Contracts with Customers—In May 2014, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) 2014-09, Revenue from Contracts with Customers. This update supersedes revenue recognition requirements in ASC Topic 605, Revenue Recognition, including most industry-specific revenue recognition guidance in the FASB Accounting Standards Codification. The new guidance stipulates that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The guidance provides specific steps that entities should apply in order to achieve this principle.

The new guidance does not apply to revenue associated with financial assets and liabilities including loans, leases, securities, and derivatives that are accounted for under other GAAP. Accordingly, the majority of the Company’s revenues are not affected. The Company adopted ASU 2014-09 on January 1, 2018 utilizing the modified retrospective approach. Additionally, the Company has determined certain service charges, bank card fees and real estate sales are within the scope of

Table of Contents

the ASU, but has not identified changes to the timing or amount of revenue recognition. Accounting policies and procedures did not change materially as the principles of revenue recognition from the ASU are largely consistent with existing guidance and current practices applied by the Company. Refer to note 15 of our consolidated financial statements for required disclosures under the new standard.

Leases—In February 2016, the FASB issued ASU 2016-02, Leases. The guidance in ASU 2016-02 supersedes the lease recognition requirements in ASC Topic 840, Leases. The new standard establishes a right-of-use (“ROU”) model that requires a lessee to record a ROU asset and lease liability on the balance sheet for all leases with terms longer than 12 months. Leases will be classified as either finance or operating, with classification affecting the pattern of expense recognition in the income statements. ASU 2016-02 becomes effective for the Company on January 1, 2019 and initially required a transition using a modified retrospective approach for leases existing at, or entered into after, the beginning of the earliest comparative period presented in the financial statements. In July 2018, the Financial Accounting Standards Board issued ASU 2018-11 which, among other things, provides an additional transition method that allows entities to not apply the guidance in ASU 2016-02 in the comparative periods presented in the financial statements and instead recognize a cumulative-effect adjustment to the opening balance of retained earnings in the period of adoption. We expect to elect to apply certain practical expedients provided under ASU 2016-02 whereby we will not reassess (i) whether any expired or existing contracts are or contain leases, (ii) the lease classification for any expired or existing leases and (iii) initial direct costs for any existing leases. We also do not expect to apply the recognition requirements of ASU 2016-02 to any short-term leases (as defined by related accounting guidance). We plan to utilize the modified-retrospective transition approach prescribed by ASU 2018-11. Upon adoption of ASU 2016-02 and ASU 2018-11 on January 1, 2019, we expect to recognize right-of-use assets and related lease liabilities totaling \$32.6 million with a cumulative-effect adjustment to beginning retained earnings of \$0.3 million.

Financial Instruments - Credit Losses—In June 2016, the FASB issued ASU 2016-13, Measurement of Credit Losses on Financial Instruments. This update replaces the current incurred loss methodology for recognizing credit losses with a current expected credit loss model, which requires the measurement of all expected credit losses for financial assets held at the reporting date based on historical experience, current conditions, and reasonable and supportable forecasts. This amendment broadens the information that an entity must consider in developing its expected credit loss estimates. Additionally, the update amends the accounting for credit losses for available-for-sale debt securities and purchased financial assets with a more-than-insignificant amount of credit deterioration since origination. This update requires enhanced disclosures to help investors and other financial statement users better understand significant estimates and judgments used in estimating credit losses, as well as the credit quality and underwriting standards of a company’s loan portfolio. ASU 2016-13 becomes effective for us on January 1, 2020. We have formed a cross-functional working group, including our credit, finance, risk management, and enterprise technology departments, to address the adoption and implementation of ASU 2016-13. We are currently working through our implementation plan and are in the process of implementing a third-party vendor solution to assist us in the application of ASU 2016-13. The adoption of ASU 2016-13 could result in an increase in the allowance for loan losses as a result of changing from an “incurred loss” model, which encompasses allowances for current known and inherent losses within the portfolio, to an “expected loss” model, which encompasses allowances for losses expected to be incurred over the life of the portfolio. We are currently evaluating the potential impact of ASU 2016-13 on our financial statements.

Statement of Cash Flows - Restricted Cash—In November 2016, the FASB issued ASU 2016-18, Restricted Cash (a consensus of the FASB Emerging Issues Task Force), which addresses classification and presentation of changes in restricted cash on the statement of cash flows. The standard requires an entity’s reconciliation of the beginning-of-period and end-of-period total amounts shown on the statement of cash flows to include in cash and cash equivalents amounts general described as restricted cash and restricted cash equivalents. The ASU does not define restricted cash or restricted cash equivalents, but an entity will need to disclose the nature of the restrictions. The ASU is effective for public business entities for annual and interim periods in fiscal years beginning after December 15, 2017. Early adoption is permitted, including adoption in an interim period. If an entity early adopts the amendments in an interim period, any adjustments should be reflected as of the beginning of the fiscal year that includes that interim period. Entities should apply this ASU using a retrospective transition method to each period presented. The Company adopted ASU 2016-18 on January 1, 2018 with no material impact to the consolidated financial statements.

Derivatives and Hedging - Targeted Improvements to Accounting for Hedging Activities—In August 2017, the FASB issued ASU 2017-12, Derivatives and Hedging: Targeted Improvements to Accounting for Hedging Activities. The purpose of this

Table of Contents

updated guidance is to better align a company's financial reporting for hedging activities with the economic objectives of those activities. ASU 2017-12 is effective for public business entities for annual and interim periods in fiscal years beginning after December 15, 2018. Early adoption is permitted, including in an interim period. ASU 2017-12 requires a modified retrospective transition method in which the Company will recognize the cumulative effect of the change on the opening balance of each affected component of equity in the consolidated statements of financial condition as of the date of adoption. The Company adopted ASU 2017-12 during the first quarter of 2018 and recorded a cumulative effect adjustment of \$26 thousand within equity in the consolidated statements of financial condition.

Reclassification of Certain Tax Effects—In February 2018, the FASB issued ASU 2018-02, *Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income*. This update allows a reclassification from accumulated other comprehensive income ("AOCI") to retained earnings for stranded tax effects resulting from the Tax Cuts and Jobs Act. The amendments eliminate the stranded tax effects that were created as a result of the reduction of historical U.S. federal corporate income tax rate to the newly enacted U.S. federal corporate income tax rate. The update is effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2018, with early adoption permitted, and is to be applied either in the period of adoption or retrospectively to each period in which the effect of the change in the U.S. federal corporate income tax rate in the Tax Cuts and Jobs Act is recognized. The Company early adopted ASU 2018-02 in the first quarter of 2018, resulting in a \$1.5 million reclassification from accumulated other comprehensive loss to retained earnings on the consolidated statements of financial condition and the consolidated statements of changes in shareholders' equity.

Other Pronouncements—The Company early adopted ASU 2018-15, *Intangibles – Goodwill and Other – Internal-Use Software: Customer's Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement That is a Service Contract* (Subtopic 350-40) on a prospective basis with no material impact on its financial statements. The Company also adopted ASU 2018-07, *Compensation – Stock Compensation (Topic 718): Improvements to Nonemployee Share-Based Payment Accounting*; ASU 2016-01, *Financial Instruments - Recognition and Measurement of Financial Assets and Financial Liabilities* (Topic 825); ASU 2016-18, *Restricted Cash* (a consensus of the FASB Emerging Issues Task Force); ASU 2016-15, *Statement of Cash Flows: Classification of Certain Cash Receipts and Cash Payments* and ASU 2017-05, *Other Income – Gains and Losses from the Derecognition of Nonfinancial Assets* (Subtopic 610-20) with no material impact on its financial statements.

The Company reviewed ASU 2017-04, *Intangibles - Goodwill and Other (Topic 350): Simplifying the Test for Goodwill Impairment* and ASU 2018-13, *Fair Value Measurement (Topic 820): Disclosure Framework-Changes to the Disclosure Requirements for Fair Value Measurement* and does not expect the adoption of these pronouncements to have a material impact on its financial statements.

Note 4 Acquisition Activities

On January 1, 2018, the Company completed its acquisition of Peoples, Inc. (“Peoples”), the bank holding company of Colorado-based Peoples National Bank and Kansas-based Peoples Bank. Immediately following the completion of the acquisition, Peoples National Bank and Peoples Bank merged into NBH Bank. Pursuant to the merger agreement executed in June 2017, the Company paid \$36.2 million of cash consideration and 3,398,477 shares of the Company’s Class A common stock in exchange for all of the outstanding common stock of Peoples. Included in the cash consideration is \$10.0 million of restricted cash placed in escrow for certain potential liabilities for which the Company is indemnified pursuant to the merger agreement. The restricted cash is included in other assets in the Company’s consolidated statements of financial condition at December 31, 2018. The transaction has a value of \$146.4 million in the aggregate, based on the Company’s closing price of \$32.43 on the acquisition date. Acquisition-related costs of \$8.0 million were included in the Company’s consolidated statements of operations for the year ended December 31, 2018. The financial results of Peoples are included in the financial results of the Company subsequent to the acquisition date.

The Company determined that this acquisition constitutes a business combination as defined in ASC Topic 805, Business Combinations. Accordingly, as of the date of the acquisition, the Company recorded the assets acquired and liabilities assumed at fair value. The Company determined fair values in accordance with the guidance provided in ASC Topic 820, Fair Value Measurements and Disclosures. Fair value is established by discounting the expected future cash flows with a market discount rate for like maturities and risk instruments. The estimation of expected future cash flows, market conditions and other future events and actual results could differ materially. The determination of the fair values of fixed assets, loans,

Table of Contents

OREO, core deposit intangible, mortgage servicing rights and mortgage repurchase reserve involves a high degree of judgment and complexity.

The table below summarizes the net assets acquired (at fair value) and consideration transferred in connection with the Peoples acquisition:

| | |
|---|------------|
| Assets: | |
| Cash and due from banks | \$ 105,173 |
| Investment securities available-for-sale | 118,512 |
| Non-marketable securities | 4,796 |
| Loans | 542,707 |
| Loans held for sale | 54,260 |
| Other real estate owned | 1,253 |
| Premises and equipment | 18,584 |
| Core deposit intangible asset | 10,477 |
| Mortgage servicing rights | 4,301 |
| Other assets | 15,361 |
| Total assets acquired | \$ 875,424 |
| Liabilities: | |
| Total deposits | 729,911 |
| FHLB borrowings | 33,825 |
| Other liabilities | 20,683 |
| Total liabilities assumed | \$ 784,419 |
| Identifiable net assets acquired | \$ 91,005 |
| Consideration: | |
| NBHC common stock paid at January 1, 2018, closing price of \$32.43 | \$ 110,213 |
| Cash | 36,189 |
| Total | \$ 146,402 |
| Estimated goodwill created | \$ 55,397 |

In connection with the Peoples acquisition, the Company recorded \$55.4 million of goodwill, a \$10.5 million core deposit intangible asset, a \$4.3 million mortgage servicing rights intangible asset and a \$4.0 million mortgage repurchase reserve, included in other liabilities. The core deposit intangible will be amortized straight-line over ten years and the mortgage servicing rights intangible is amortized in proportion to and over the period of the estimated net servicing income. The FHLB borrowings of \$33.8 million were paid off during the first quarter of 2018. The goodwill associated with this transaction is not tax deductible.

At the date of acquisition, the gross contractual amounts receivable, inclusive of all principal and interest, was \$713.6 million. The Company's best estimate of the contractual principal cash flows for loans not expected to be collected was \$2.1 million.

The following unaudited pro forma information combines the historical results of Peoples and the Company. In accordance with the merger agreement, the Peoples national mortgage business was wound down prior to acquisition. Accordingly, the pro forma information excludes the results of the Peoples national mortgage business for prior periods presented. The pro forma financial information does not include the potential impacts of possible business model changes, current market conditions, revenue enhancements, expense efficiencies, or other factors.

If the Peoples acquisition had been completed on January 1, 2017, pro forma total revenue for the Company would have been approximately \$268.2 million and \$266.5 million for the years ended December 31, 2018 and 2017, respectively. Pro forma net income for the Company would have been approximately \$67.8 million and \$16.6 million for the years ended December

Table of Contents

31, 2018 and 2017, respectively. Pro forma basic and dilutive earnings per share for the Company would have been \$2.20 and \$2.16 for the years ended December 31, 2018, respectively, and \$0.55 and \$0.53 for the years ended December 31, 2017, respectively.

For the year ended December 31, 2018, the pro forma information reflects adjustments made to exclude acquisition-related expenses of the Company of \$8.0 million. For the year ended December 31, 2017, the pro-forma information reflects adjustments made to exclude acquisition-related expenses of the Company of \$2.7 million and include estimated amortization and accretion of purchase discounts and premiums of \$0.7 million in addition to estimated amortization of acquired identifiable intangibles of \$1.0 million. The pro forma information is theoretical in nature and not necessarily indicative of future consolidated results of operations of the Company or the consolidated results of operations which would have resulted had the Company acquired Peoples during the periods presented.

The Company has determined that it is impractical to report the amounts of revenue and earnings of legacy Peoples since the acquisition date. Peoples operations were completely integrated shortly after the acquisition date. Accordingly, reliable and separate complete revenue and earnings information is no longer available. In addition, such amounts would require significant estimates related to the proper allocation of merger cost savings that cannot be objectively made.

Note 5 Investment Securities

The Company's investment securities portfolio is comprised of available-for-sale and held-to-maturity investment securities. These investment securities totaled \$1.0 billion at December 31, 2018 and included \$0.8 billion of available-for-sale securities and \$0.2 billion of held-to-maturity securities. At December 31, 2017, investment securities totaled \$1.1 billion and included \$0.8 billion of available-for-sale securities and \$0.3 billion of held-to-maturity securities.

Available-for-sale

At December 31, 2018 and 2017, the Company held \$791.1 million and \$855.3 million of available-for-sale investment securities, respectively. Available-for-sale securities are summarized as follows as of the dates indicated:

| December 31, 2018 | | | |
|-------------------|---------------------------|----------------------------|------------|
| Amortized cost | Gross unrealized gains | Gross unrealized losses | Fair value |

Mortgage-backed securities (“MBS”):

| | | | | |
|--|------------|----------|-------------|------------|
| Residential mortgage pass-through securities issued or guaranteed by U.S. Government agencies or sponsored enterprises | \$ 147,283 | \$ 1,232 | \$ (1,873) | \$ 146,642 |
| Other residential MBS issued or guaranteed by U.S. Government agencies or sponsored enterprises | 661,354 | 1,056 | (19,029) | 643,381 |
| Municipal securities | 619 | — | (9) | 610 |
| Other securities | 469 | — | — | 469 |
| Total investment securities available-for-sale | \$ 809,725 | \$ 2,288 | \$ (20,911) | \$ 791,102 |

Table of Contents

| | December 31, 2017 | | | Fair value |
|--|-------------------|------------------------|-------------------------|------------|
| | Amortized cost | Gross unrealized gains | Gross unrealized losses | |
| Mortgage-backed securities: | | | | |
| Residential mortgage pass-through securities issued or guaranteed by U.S. Government agencies or sponsored enterprises | \$ 167,269 | \$ 2,371 | \$ (992) | \$ 168,648 |
| Other residential MBS issued or guaranteed by U.S. Government agencies or sponsored enterprises | 702,107 | 351 | (17,228) | 685,230 |
| Municipal securities | 1,054 | — | (6) | 1,048 |
| Other securities | 419 | — | — | 419 |
| Total investment securities available-for-sale | \$ 870,849 | \$ 2,722 | \$ (18,226) | \$ 855,345 |

At December 31, 2018 and 2017, mortgage-backed securities represented primarily all of the Company's available-for-sale investment portfolio and all mortgage-backed securities were backed by government sponsored enterprises ("GSE") collateral such as FHLMC, FNMA and GNMA.

The tables below summarize the available-for-sale securities with unrealized losses as of the dates shown, along with the length of the impairment period:

| | December 31, 2018 | | | | Total Fair value | Unrealized losses |
|--|--------------------------------|-------------------|------------------------------|-------------------|------------------|-------------------|
| | Less than 12 months Fair value | Unrealized losses | 12 months or more Fair value | Unrealized losses | | |
| Mortgage-backed securities: | | | | | | |
| Residential mortgage pass-through securities issued or guaranteed by U.S. Government agencies or sponsored enterprises | \$ 30,853 | \$ (392) | \$ 69,169 | \$ (1,481) | \$ 100,022 | \$ (1,873) |
| Other residential MBS issued or guaranteed by U.S. Government agencies or sponsored enterprises | 127,767 | (1,150) | 454,662 | (17,879) | 582,429 | (19,029) |
| Municipal securities | 441 | (9) | — | — | 441 | (9) |
| Total | \$ 159,061 | \$ (1,551) | \$ 523,831 | \$ (19,360) | \$ 682,892 | \$ (20,911) |

| | December 31, 2017 | | | | Total Fair value | Unrealized losses |
|--|--------------------------------------|----------------------|------------------------------------|----------------------|------------------------|----------------------|
| | Less than 12 months Fair value | Unrealized losses | 12 months or more Fair value | Unrealized losses | | |
| Mortgage-backed securities: | | | | | | |
| Residential mortgage pass-through securities issued or guaranteed by U.S. Government agencies or sponsored enterprises | \$ 62,178 | \$ (408) | \$ 36,086 | \$ (584) | \$ 98,264 | \$ (992) |
| Other residential MBS issued or guaranteed by U.S. Government agencies or sponsored enterprises | 162,346 | (830) | 412,967 | (16,398) | 575,313 | (17,228) |
| Municipal securities | 514 | (6) | — | — | 514 | (6) |
| Total | \$ 225,038 | \$ (1,244) | \$ 449,053 | \$ (16,982) | \$ 674,091 | \$ (18,226) |

The unrealized losses in the Company's investment portfolio at December 31, 2018 were caused by changes in interest rates. The portfolio included 211 securities, having an aggregate fair value of \$682.9 million, which were in an unrealized loss position at December 31, 2018, compared to 87 securities, with an aggregate fair value of \$674.1 million at December 31, 2017.

Management evaluated all of the available for sale securities in an unrealized loss position at December 31, 2018 and December 31, 2017 and concluded no OTTI existed. During the year ended December 31, 2018, the Company recorded a

Table of Contents

\$0.2 million recovery included in other non-interest expense related to one security with an aggregate fair value of \$0.3 million which had previously incurred OTTI of \$0.2 million during the year ended December 31, 2017. The unrealized losses on the remaining securities in an unrealized loss position were caused by changes in interest rates. The Company has no intention to sell these securities before recovery of their amortized cost and believes it will not be required to sell the securities before the recovery of their amortized cost.

Certain securities are pledged as collateral for public deposits, securities sold under agreements to repurchase and to secure borrowing capacity at the Federal Reserve Bank, and FHLB, if needed. The fair value of available-for-sale investment securities pledged as collateral totaled \$318.1 million and \$334.6 million at December 31, 2018 and 2017, respectively. Certain investment securities may also be pledged as collateral for the line of credit at the FHLB; at December 31, 2018 or December 31, 2017, no securities were pledged for this purpose.

Mortgage-backed securities do not have a single maturity date and actual maturities may differ from contractual maturities depending on the repayment characteristics and experience of the underlying financial instruments. The estimated weighted average life of the available-for-sale mortgage-backed securities portfolio was 3.2 years and 3.4 years at December 31, 2018 and 2017, respectively. This estimate is based on assumptions and actual results may differ. At December 31, 2018 and 2017, the duration of the total available-for-sale investment portfolio was 3.0 years and 3.1 years, respectively.

As of December 31, 2018, municipal securities with an amortized cost and fair value of \$0.2 million were due after one year through five years, while municipal securities with an amortized cost and fair value of \$0.4 million were due after five years through ten years. Other securities of \$0.5 million as of December 31, 2018, have no stated contractual maturity date.

Held-to-maturity

At December 31, 2018 and 2017, the Company held \$235.4 million and \$258.7 million of held-to-maturity investment securities, respectively. Held-to-maturity investment securities are summarized as follows as of the dates indicated:

| | December 31, 2018 | | | |
|--|-------------------|------------------------|-------------------------|------------|
| | Amortized cost | Gross unrealized gains | Gross unrealized losses | Fair value |
| Mortgage-backed securities: | | | | |
| Residential mortgage pass-through securities issued or guaranteed by U.S. Government agencies or sponsored | \$ 157,115 | \$ 2 | \$ (2,705) | \$ 154,412 |

enterprises

Other residential MBS issued or guaranteed by U.S.

Government agencies or sponsored enterprises

Total investment securities held-to-maturity

| | | | |
|------------|------|------------|------------|
| 78,283 | — | (1,769) | 76,514 |
| \$ 235,398 | \$ 2 | \$ (4,474) | \$ 230,926 |

December 31, 2017

| Amortized cost | Gross unrealized gains | Gross unrealized losses | Fair value |
|-------------------|------------------------------|-------------------------------|------------|
|-------------------|------------------------------|-------------------------------|------------|

Mortgage-backed securities:

Residential mortgage pass-through securities issued or
guaranteed by U.S. Government agencies or sponsored
enterprises

| | | | |
|------------|--------|----------|------------|
| \$ 204,352 | \$ 151 | \$ (455) | \$ 204,048 |
|------------|--------|----------|------------|

Other residential MBS issued or guaranteed by U.S.

Government agencies or sponsored enterprises

Total investment securities held-to-maturity

| | | | |
|------------|--------|------------|------------|
| 54,378 | — | (1,655) | 52,723 |
| \$ 258,730 | \$ 151 | \$ (2,110) | \$ 256,771 |

Table of Contents

The tables below summarize the held-to-maturity securities with unrealized losses as of the dates shown, along with the length of the impairment period:

| | December 31, 2018 | | 12 months or more | | Total Fair value | Unrealized losses |
|--|--------------------------------------|----------------------|-------------------|----------------------|------------------------|----------------------|
| | Less than 12 months Fair value | Unrealized losses | Fair value | Unrealized losses | | |
| Mortgage-backed securities: | | | | | | |
| Residential mortgage pass-through securities issued or guaranteed by U.S. Government agencies or sponsored enterprises | \$ 26,660 | \$ (381) | \$ 126,475 | \$ (2,324) | \$ 153,135 | \$ (2,705) |
| Other residential MBS issued or guaranteed by U.S. Government agencies or sponsored enterprises | 35,235 | (79) | 41,279 | (1,690) | 76,514 | (1,769) |
| Total | \$ 61,895 | \$ (460) | \$ 167,754 | \$ (4,014) | \$ 229,649 | \$ (4,474) |

| | December 31, 2017 | | 12 months or more | | Total Fair value | Unrealized losses |
|--|--------------------------------------|----------------------|-------------------|----------------------|------------------------|----------------------|
| | Less than 12 months Fair value | Unrealized losses | Fair value | Unrealized losses | | |
| Mortgage-backed securities: | | | | | | |
| Residential mortgage pass-through securities issued or guaranteed by U.S. Government agencies or sponsored enterprises | \$ 149,182 | \$ (220) | \$ 17,506 | \$ (235) | \$ 166,688 | \$ (455) |
| Other residential MBS issued or guaranteed by U.S. Government agencies or sponsored enterprises | 6,460 | (65) | 46,264 | (1,590) | 52,724 | (1,655) |
| Total | \$ 155,642 | \$ (285) | \$ 63,770 | \$ (1,825) | \$ 219,412 | \$ (2,110) |

The held-to-maturity portfolio included 49 securities, having an aggregate fair value of \$229.6 million, which were in an unrealized loss position at December 31, 2018, compared to 36 securities, with a fair value of \$219.4 million, at December 31, 2017.

The unrealized losses in the Company's investments at December 31, 2018 and December 31, 2017 were caused by changes in interest rates. Management evaluated all of the held-to-maturity securities in an unrealized loss position and concluded that no OTTI existed at December 31, 2018 or December 31, 2017. The Company has no intention to sell these securities before the recovery of their amortized cost and believes it will not be required to sell the securities before the recovery of their amortized cost.

The carrying value of held-to-maturity investment securities pledged as collateral totaled \$133.1 million and \$142.0 million at December 31, 2018 and 2017, respectively.

Actual maturities of mortgage-backed securities may differ from scheduled maturities depending on the repayment characteristics and experience of the underlying financial instruments. The estimated weighted average expected life of the held-to-maturity mortgage-backed securities portfolio as of December 31, 2018 and 2017 was 2.8 years and 3.1 years, respectively. This estimate is based on assumptions and actual results may differ. The duration of the total held-to-maturity investment portfolio was 2.5 years and 2.8 years as of December 31, 2018 and 2017, respectively.

Note 6 Non-marketable Securities

Non-marketable securities include Federal Reserve Bank stock and FHLB stock. At December 31, 2018, the Company held \$13.9 million of Federal Reserve Bank stock and \$13.6 million of FHLB stock for regulatory or debt facility purposes. At December 31, 2017, the Company held \$9.2 million of Federal Reserve Bank stock and \$5.8 million of FHLB stock.

Table of Contents

These are restricted securities which, lacking a market, are carried at cost. There have been no identified events or changes in circumstances that may have an adverse effect on the investments carried at cost. Management evaluated all of the non-marketable securities and concluded that no OTTI existed at December 31, 2018 or December 31, 2017.

Note 7 Loans

The loan portfolio is comprised of loans originated by the Company and loans that were acquired in connection with the Company's acquisitions. Beginning in the first quarter 2018, loans previously referred to as "non 310-30 loans" are referred to as "originated and acquired loans," which include originated loans as well as acquired loans not accounted for under ASC 310-30. No amounts were reclassified resulting from this change in terminology.

The tables below show the loan portfolio composition including carrying value by segment of originated and acquired loans and loans accounted for under ASC 310-30, Receivables—Loans and Debt Securities Acquired with Deteriorated Credit Quality, as of the dates shown. The carrying value of originated and acquired loans is net of discounts, fees, costs and fair value marks of \$10.2 million and \$4.3 million at December 31, 2018 and 2017, respectively.

| | December 31, 2018 | | | |
|---|--|------------------------|--------------|------------|
| | Originated and acquired loans | ASC 310-30 loans | Total loans | % of total |
| Commercial | \$ 2,624,173 | \$ 20,398 | \$ 2,644,571 | 64.6% |
| Commercial real estate non-owner occupied | 551,819 | 40,393 | 592,212 | 14.5% |
| Residential real estate | 820,820 | 9,995 | 830,815 | 20.3% |
| Consumer | 24,617 | 93 | 24,710 | 0.6% |
| Total | \$ 4,021,429 | \$ 70,879 | \$ 4,092,308 | 100.0% |

| | December 31, 2017 | | | |
|---|--|------------------------|--------------|------------|
| | Originated and acquired loans | ASC 310-30 loans | Total loans | % of total |
| Commercial | \$ 1,845,130 | \$ 29,475 | \$ 1,874,605 | 59.0% |
| Commercial real estate non-owner occupied | 485,141 | 77,908 | 563,049 | 17.7% |
| Residential real estate | 703,478 | 12,759 | 716,237 | 22.5% |
| Consumer | 24,575 | 481 | 25,056 | 0.8% |
| Total | \$ 3,058,324 | \$ 120,623 | \$ 3,178,947 | 100.0% |

Table of Contents

Delinquency for originated and acquired loans is shown in the following tables at December 31, 2018 and 2017:

| | December 31, 2018 | | Non-accrual loans | Total past due and non-accrual | Current | Total loans |
|--|--|---|----------------------|--------------------------------------|--------------|--------------|
| | 30-89 days past due and accruing | Greater than 90 days past due and accruing | | | | |
| Originated and acquired loans: | | | | | | |
| Commercial: | | | | | | |
| Commercial and industrial | \$ 495 | \$ 74 | \$ 5,510 | \$ 6,079 | \$ 1,925,068 | \$ 1,931,147 |
| Owner occupied commercial real estate | 893 | — | 6,931 | 7,824 | 413,842 | 421,666 |
| Food and agriculture | 141 | 125 | 768 | 1,034 | 221,122 | 222,156 |
| Energy | — | — | 742 | 742 | 48,462 | 49,204 |
| Total commercial | 1,529 | 199 | 13,951 | 15,679 | 2,608,494 | 2,624,173 |
| Commercial real estate non-owner occupied: | | | | | | |
| Construction | — | — | 1,208 | 1,208 | 93,646 | 94,854 |
| Acquisition/development | — | — | 121 | 121 | 19,529 | 19,650 |
| Multifamily | — | — | — | — | 56,685 | 56,685 |
| Non-owner occupied | 328 | 132 | 572 | 1,032 | 379,598 | 380,630 |
| Total commercial real estate | 328 | 132 | 1,901 | 2,361 | 549,458 | 551,819 |
| Residential real estate: | | | | | | |
| Senior lien | 2,106 | 548 | 7,790 | 10,444 | 712,592 | 723,036 |
| Junior lien | 556 | — | 772 | 1,328 | 96,456 | 97,784 |
| Total residential real estate | 2,662 | 548 | 8,562 | 11,772 | 809,048 | 820,820 |
| Consumer | 91 | 16 | 42 | 149 | 24,468 | 24,617 |
| Total originated and acquired loans | \$ 4,610 | \$ 895 | \$ 24,456 | \$ 29,961 | \$ 3,991,468 | \$ 4,021,429 |

| | December 31, 2017 | | Non-accrual loans | Total past due and |
|--|----------------------------------|---|----------------------|-----------------------|
| | 30-89 days past due and | Greater than 90 days past due and | | |

Edgar Filing: National Bank Holdings Corp - Form 10-K

| | accruing | accruing | loans | non-accrual | Current | Total loans |
|--|----------|----------|-----------|-------------|--------------|--------------|
| Originated and acquired loans: | | | | | | |
| Commercial: | | | | | | |
| Commercial and industrial | \$ 671 | \$ 150 | \$ 7,767 | \$ 8,588 | \$ 1,367,434 | \$ 1,376,022 |
| Owner occupied commercial real estate | — | — | 3,479 | 3,479 | 269,274 | 272,753 |
| Food and agriculture | 537 | — | 2,003 | 2,540 | 136,355 | 138,895 |
| Energy | — | — | 1,645 | 1,645 | 55,815 | 57,460 |
| Total commercial | 1,208 | 150 | 14,894 | 16,252 | 1,828,878 | 1,845,130 |
| Commercial real estate non-owner occupied: | | | | | | |
| Construction | — | — | 179 | 179 | 107,502 | 107,681 |
| Acquisition/development | 1,097 | — | — | 1,097 | 13,318 | 14,415 |
| Multifamily | — | — | — | — | 26,947 | 26,947 |
| Non-owner occupied | 56 | — | 605 | 661 | 335,437 | 336,098 |
| Total commercial real estate | 1,153 | — | 784 | 1,937 | 483,204 | 485,141 |
| Residential real estate: | | | | | | |
| Senior lien | 841 | — | 4,723 | 5,564 | 640,918 | 646,482 |
| Junior lien | 316 | — | 459 | 775 | 56,221 | 56,996 |
| Total residential real estate | 1,157 | — | 5,182 | 6,339 | 697,139 | 703,478 |
| Consumer | 163 | — | 140 | 303 | 24,272 | 24,575 |
| Total originated and acquired loans | \$ 3,681 | \$ 150 | \$ 21,000 | \$ 24,831 | \$ 3,033,493 | \$ 3,058,324 |

Loans are considered past due or delinquent when the contractual principal or interest due in accordance with the terms of the loan agreement remains unpaid after the due date of the scheduled payment. Pooled loans accounted for under ASC 310-30 that are 90 days or more past due and still accreting are generally considered to be performing and therefore are not included in the tables above. Non-accrual loans include non-accrual loans and troubled debt restructurings on non-accrual status. Non-accrual originated and acquired loans totaled \$24.5 million at December 31, 2018, increasing \$3.5 million, or 16.5% from December 31, 2017.

Table of Contents

Credit exposure for all loans as determined by the Company's internal risk rating system was as follows at December 31, 2018 and 2017, respectively:

| | December 31, 2018 | | | | |
|---|-------------------|--------------------|-------------|----------|--------------|
| | Pass | Special mention | Substandard | Doubtful | Total |
| Originated and acquired loans: | | | | | |
| Commercial: | | | | | |
| Commercial and industrial | \$ 1,890,710 | \$ 16,531 | \$ 22,919 | \$ 987 | \$ 1,931,147 |
| Owner occupied commercial real estate | 393,404 | 16,349 | 11,828 | 85 | 421,666 |
| Food and agriculture | 220,004 | 1,260 | 847 | 45 | 222,156 |
| Energy | 48,462 | — | 742 | — | 49,204 |
| Total commercial | 2,552,580 | 34,140 | 36,336 | 1,117 | 2,624,173 |
| Commercial real estate non-owner occupied: | | | | | |
| Construction | 92,731 | 915 | 1,208 | — | 94,854 |
| Acquisition/development | 19,529 | — | 121 | — | 19,650 |
| Multifamily | 56,685 | — | — | — | 56,685 |
| Non-owner occupied | 355,776 | 23,243 | 1,611 | — | 380,630 |
| Total commercial real estate | 524,721 | 24,158 | 2,940 | — | 551,819 |
| Residential real estate: | | | | | |
| Senior lien | 710,972 | 3,571 | 8,493 | — | 723,036 |
| Junior lien | 96,456 | 415 | 913 | — | 97,784 |
| Total residential real estate | 807,428 | 3,986 | 9,406 | — | 820,820 |
| Consumer | 24,575 | — | 42 | — | 24,617 |
| Total originated and acquired loans | \$ 3,909,304 | \$ 62,284 | \$ 48,724 | \$ 1,117 | \$ 4,021,429 |
| Loans accounted for under ASC 310-30: | | | | | |
| Commercial | \$ 17,579 | \$ 537 | \$ 2,282 | \$ — | \$ 20,398 |
| Commercial real estate non-owner occupied | 39,322 | 246 | 825 | — | 40,393 |
| Residential real estate | 7,484 | 908 | 1,598 | — | 9,990 |
| Consumer | — | — | 98 | — | 98 |
| Total loans accounted for under ASC 310-30 | \$ 64,385 | \$ 1,691 | \$ 4,803 | \$ — | \$ 70,879 |
| Total loans | \$ 3,973,689 | \$ 63,975 | \$ 53,527 | \$ 1,117 | \$ 4,092,308 |

| | December 31, 2017 | | | | |
|--------------------------------|-------------------|--------------------|-------------|----------|-------|
| | Pass | Special mention | Substandard | Doubtful | Total |
| Originated and acquired loans: | | | | | |
| Commercial: | | | | | |

Edgar Filing: National Bank Holdings Corp - Form 10-K

| | | | | | |
|--|--------------|-----------|-----------|----------|--------------|
| Commercial and industrial | \$ 1,349,116 | \$ 10,829 | \$ 14,824 | \$ 1,253 | \$ 1,376,022 |
| Owner occupied commercial real estate | 250,224 | 17,030 | 5,424 | 75 | 272,753 |
| Food and agriculture | 118,068 | 18,824 | 1,870 | 133 | 138,895 |
| Energy | 55,814 | — | 1,646 | — | 57,460 |
| Total commercial | 1,773,222 | 46,683 | 23,764 | 1,461 | 1,845,130 |
| Commercial real estate non-owner occupied: | | | | | |
| Construction | 107,502 | — | 179 | — | 107,681 |
| Acquisition/development | 14,415 | — | — | — | 14,415 |
| Multifamily | 24,817 | — | 2,130 | — | 26,947 |
| Non-owner occupied | 333,225 | 1,396 | 1,477 | — | 336,098 |
| Total commercial real estate | 479,959 | 1,396 | 3,786 | — | 485,141 |
| Residential real estate: | | | | | |
| Senior lien | 641,294 | 91 | 5,097 | — | 646,482 |
| Junior lien | 56,172 | — | 824 | — | 56,996 |
| Total residential real estate | 697,466 | 91 | 5,921 | — | 703,478 |
| Consumer | 24,432 | 1 | 142 | — | 24,575 |
| Total originated and acquired loans | \$ 2,975,079 | \$ 48,171 | \$ 33,613 | \$ 1,461 | \$ 3,058,324 |
| Loans accounted for under ASC 310-30: | | | | | |
| Commercial | \$ 23,954 | \$ 1,070 | \$ 4,451 | \$ — | \$ 29,475 |
| Commercial real estate non-owner occupied | 50,537 | 883 | 26,488 | — | 77,908 |
| Residential real estate | 10,072 | 1,055 | 1,632 | — | 12,759 |
| Consumer | 327 | 9 | 145 | — | 481 |
| Total loans accounted for under ASC 310-30 | \$ 84,890 | \$ 3,017 | \$ 32,716 | \$ — | \$ 120,623 |
| Total loans | \$ 3,059,969 | \$ 51,188 | \$ 66,329 | \$ 1,461 | \$ 3,178,947 |

Table of Contents

Impaired Loans

Loans are considered to be impaired when it is probable that the Company will not be able to collect all amounts due in accordance with the contractual terms of the loan agreement. Impaired loans are comprised of originated and acquired loans on non-accrual status, loans in bankruptcy, and troubled debt restructurings (“TDRs”) described below. If a specific allowance is warranted based on the borrower’s overall financial condition, the specific allowance is calculated based on discounted cash flows using the loan’s initial contractual effective interest rate or the fair value of the collateral less selling costs for collateral dependent loans.

At December 31, 2018 and 2017, the Company’s recorded investment in impaired loans were \$31.1 million and \$30.9 million, respectively, of which \$4.1 million and \$8.5 million, respectively, were accruing TDRs. Impaired loans at December 31, 2018 were primarily comprised of six relationships totaling \$12.1 million. Impaired loans had a collective related allowance for loan losses allocated to them of \$1.2 million and \$1.5 million at December 31, 2018 and 2017, respectively.

Table of Contents

Additional information regarding impaired loans at December 31, 2018 and 2017 is set forth in the table below:

| | December 31, 2018 | | | December 31, 2017 | | |
|---|--------------------------|---------------------|-------------------------------------|--------------------------|---------------------|-------------------------------------|
| | Unpaid principal balance | Recorded investment | Allowance for loan losses allocated | Unpaid principal balance | Recorded investment | Allowance for loan losses allocated |
| With no related allowance recorded: | | | | | | |
| Commercial: | | | | | | |
| Commercial and industrial | \$ 4,374 | \$ 3,029 | \$ — | \$ 6,481 | \$ 5,055 | \$ — |
| Owner occupied commercial real estate | 7,130 | 6,609 | — | 4,186 | 3,934 | — |
| Food and agriculture | 1,468 | 1,260 | — | 1,502 | 1,245 | — |
| Energy | 5,366 | 742 | — | 8,661 | 3,861 | — |
| Total commercial | 18,338 | 11,640 | — | 20,830 | 14,095 | — |
| Commercial real estate non-owner occupied: | | | | | | |
| Construction | 1,435 | 1,208 | — | 215 | 179 | — |
| Acquisition/development | 378 | 121 | — | — | — | — |
| Multifamily | — | — | — | 29 | 29 | — |
| Non-owner occupied | 641 | 547 | — | 901 | 853 | — |
| Total commercial real estate | 2,454 | 1,876 | — | 1,145 | 1,061 | — |
| Residential real estate: | | | | | | |
| Senior lien | 4,229 | 3,814 | — | 333 | 309 | — |
| Junior lien | 409 | 341 | — | — | — | — |
| Total residential real estate | 4,638 | 4,155 | — | 333 | 309 | — |
| Consumer | 46 | 42 | — | — | — | — |
| Total impaired loans with no related allowance recorded | \$ 25,476 | \$ 17,713 | \$ — | \$ 22,308 | \$ 15,465 | \$ — |
| With a related allowance recorded: | | | | | | |
| Commercial: | | | | | | |
| Commercial and industrial | \$ 7,252 | \$ 4,627 | \$ 996 | \$ 7,919 | \$ 5,339 | \$ 1,329 |
| Owner occupied commercial real estate | 1,362 | 1,169 | 90 | 873 | 713 | 4 |
| Food and agriculture | 883 | 845 | 46 | 2,122 | 2,083 | 133 |
| Energy | — | — | — | — | — | — |
| Total commercial | 9,497 | 6,641 | 1,132 | 10,914 | 8,135 | 1,466 |
| Commercial real estate non-owner occupied: | | | | | | |
| Construction | — | — | — | — | — | — |
| Acquisition/development | — | — | — | — | — | — |
| Multifamily | — | — | — | — | — | — |
| Non-owner occupied | 313 | 254 | 2 | 207 | 200 | 1 |
| Total commercial real estate | 313 | 254 | 2 | 207 | 200 | 1 |
| Residential real estate: | | | | | | |
| Senior lien | 6,032 | 5,178 | 27 | 6,481 | 5,753 | 24 |

Edgar Filing: National Bank Holdings Corp - Form 10-K

| | | | | | | |
|--|-----------|-----------|----------|-----------|-----------|----------|
| Junior lien | 1,408 | 1,293 | 8 | 1,295 | 1,179 | 8 |
| Total residential real estate | 7,440 | 6,471 | 35 | 7,776 | 6,932 | 32 |
| Consumer | — | — | — | 146 | 141 | 1 |
| Total impaired loans with a related allowance recorded | \$ 17,250 | \$ 13,366 | \$ 1,169 | \$ 19,043 | \$ 15,408 | \$ 1,500 |
| Total impaired loans | \$ 42,726 | \$ 31,079 | \$ 1,169 | \$ 41,351 | \$ 30,873 | \$ 1,500 |

Table of Contents

The table below shows additional information regarding the average recorded investment and interest income recognized on impaired loans for the periods presented:

| | For the years ended | | December 31, 2017 | | December 31, 2016 | |
|---|-----------------------------|----------------------------|-----------------------------|----------------------------|-----------------------------|----------------------------|
| | Average recorded investment | Interest income recognized | Average recorded investment | Interest income recognized | Average recorded investment | Interest income recognized |
| With no related allowance recorded: | | | | | | |
| Commercial: | | | | | | |
| Commercial and industrial | \$ 3,248 | \$ 168 | \$ 5,609 | \$ 152 | \$ 7,909 | \$ 252 |
| Owner occupied commercial real estate | 6,799 | 38 | 4,155 | 80 | 3,249 | 92 |
| Food and agriculture | 1,259 | 98 | 1,422 | 244 | 1,830 | — |
| Energy | 884 | — | 8,004 | 156 | 12,565 | — |
| Total Commercial | 12,190 | 304 | 19,190 | 632 | 25,553 | 344 |
| Commercial real estate non-owner occupied: | | | | | | |
| Construction | 1,208 | — | — | — | — | — |
| Acquisition/development | 606 | — | — | — | — | — |
| Multifamily | — | — | — | — | — | — |
| Non-owner occupied | 573 | — | 878 | 22 | 368 | 22 |
| Total commercial real estate | 2,387 | — | 878 | 22 | 368 | 22 |
| Residential real estate: | | | | | | |
| Senior lien | 3,904 | — | 326 | — | 1,466 | 19 |
| Junior lien | 355 | 2 | — | — | 54 | 2 |
| Total residential real estate | 4,259 | 2 | 326 | — | 1,520 | 21 |
| Consumer | 12 | — | — | — | 4 | — |
| Total impaired loans with no related allowance recorded | \$ 18,848 | \$ 306 | \$ 20,394 | \$ 654 | \$ 27,445 | \$ 387 |
| With a related allowance recorded: | | | | | | |
| Commercial: | | | | | | |
| Commercial and industrial | \$ 4,677 | \$ — | \$ 7,331 | \$ — | \$ 3,545 | \$ 198 |
| Owner occupied commercial real estate | 1,220 | 19 | 747 | 20 | 703 | 20 |
| Food and agriculture | 862 | 5 | 2,092 | 5 | 162 | 5 |
| Energy | — | — | — | — | 10,008 | — |
| Total Commercial | 6,759 | 23 | 10,170 | 25 | 14,418 | 223 |
| Commercial real estate non-owner occupied: | | | | | | |
| Construction | — | — | 188 | — | — | — |
| Acquisition/development | — | — | — | — | — | — |
| Multifamily | — | — | 30 | 1 | 34 | 2 |
| Non-owner occupied | 288 | 16 | 213 | 9 | 268 | 13 |
| Total commercial real estate | 288 | 16 | 431 | 10 | 302 | 15 |
| Residential real estate: | | | | | | |
| Senior lien | 5,412 | 57 | 5,986 | 67 | 5,200 | 88 |
| Junior lien | 1,331 | 43 | 1,225 | 42 | 1,600 | 56 |

Edgar Filing: National Bank Holdings Corp - Form 10-K

| | | | | | | |
|--|-----------|--------|-----------|--------|-----------|--------|
| Total residential real estate | 6,743 | 100 | 7,211 | 109 | 6,800 | 144 |
| Consumer | 36 | — | 163 | — | 196 | — |
| Total impaired loans with a related allowance recorded | \$ 13,826 | \$ 140 | \$ 17,975 | \$ 144 | \$ 21,716 | \$ 382 |
| Total impaired loans | \$ 32,674 | \$ 446 | \$ 38,369 | \$ 798 | \$ 49,161 | \$ 769 |

Interest income recognized on impaired loans noted in the tables above, primarily represents interest earned on accruing TDRs. Interest income recognized on impaired loans during the years ended December 31, 2018, 2017 and 2016 was \$0.4 million, \$0.8 million and \$0.8 million, respectively.

Troubled debt restructurings

The Company's policy is to review each prospective credit to determine the appropriateness and the adequacy of security or collateral prior to making a loan. In the event of borrower default, the Company seeks recovery in compliance with lending laws, the respective loan agreements, and credit monitoring and remediation procedures that may include restructuring a loan

Table of Contents

to provide a concession by the Company to the borrower from their original terms due to borrower financial difficulties in order to facilitate repayment. Additionally, if a borrower's repayment obligation has been discharged by a court, and that debt has not been reaffirmed by the borrower, regardless of past due status, the loan is considered to be a TDR.

During 2018, the Company restructured ten loans with a recorded investment of \$0.8 million at December 31, 2018 to facilitate repayment. All of the loan modifications were a reduction of the principal payment, a reduction in interest rate, or an extension of term. Loan modifications to loans accounted for under ASC 310-30 are not considered TDRs. The tables below provide additional information related to accruing TDRs at December 31, 2018 and 2017:

| | December 31, 2018 | | | Unfunded |
|---|-------------------|--------------|-----------|--------------|
| | Recorded | Average | Unpaid | commitments |
| | investment | year-to-date | principal | to fund TDRs |
| | recorded | recorded | balance | |
| Commercial | \$ 2,730 | \$ 2,827 | \$ 3,155 | \$ — |
| Commercial real estate non-owner occupied | 229 | 260 | 280 | — |
| Residential real estate | 1,114 | 1,163 | 1,121 | 12 |
| Consumer | — | — | — | — |
| Total | \$ 4,073 | \$ 4,250 | \$ 4,556 | \$ 12 |

| | December 31, 2017 | | | Unfunded |
|---|-------------------|--------------|-----------|--------------|
| | Recorded | Average | Unpaid | commitments |
| | investment | year-to-date | principal | to fund TDRs |
| | recorded | recorded | balance | |
| Commercial | \$ 6,595 | \$ 7,308 | \$ 7,171 | \$ 2,041 |
| Commercial real estate non-owner occupied | 455 | 489 | 500 | — |
| Residential real estate | 1,409 | 1,461 | 1,420 | 2 |
| Consumer | 1 | 3 | 1 | — |
| Total | \$ 8,460 | \$ 9,261 | \$ 9,092 | \$ 2,043 |

The following table summarizes the Company's carrying value of non-accrual TDRs as of December 31, 2017 and 2016:

| | December 31, 2018 | December 31, 2017 |
|---|-------------------|-------------------|
| Commercial | \$ 1,854 | \$ 5,808 |
| Commercial real estate non-owner occupied | — | — |

Edgar Filing: National Bank Holdings Corp - Form 10-K

| | | |
|-------------------------|----------|----------|
| Residential real estate | 1,584 | 1,336 |
| Consumer | — | 111 |
| Total non-accruing TDRs | \$ 3,438 | \$ 7,255 |

Accrual of interest is resumed on loans that were previously on non-accrual only after the loan has performed sufficiently. The Company had one TDR that was modified within the past twelve months and had defaulted on its restructured terms. The defaulted TDR was a residential loan totaling \$0.1 million. For purposes of this disclosure, the Company considers “default” to mean 90 days or more past due on principal or interest. Non-accruing TDRs decreased \$3.8 million from December 31, 2017 due to paydowns. The allowance for loan losses related to troubled debt restructurings on non-accrual status is determined by individual evaluation, including collateral adequacy, using the same process as loans on non-accrual status which are not classified as TDRs.

During 2017, the Company had three TDRs that had been modified within the prior twelve months that defaulted on their restructured terms.

Loans accounted for under ASC 310-30

Loan pools accounted for under ASC Topic 310-30 are periodically remeasured to determine expected future cash flows. In determining the expected cash flows, the timing of cash flows and prepayment assumptions for smaller homogeneous loans are based on statistical models that take into account factors such as the loan interest rate, credit profile of the borrowers, the years in which the loans were originated, and whether the loans are fixed or variable rate loans. Prepayments may be assumed

Table of Contents

on loans if circumstances specific to that loan warrant a prepayment assumption. The re-measurement of loans accounted for under ASC 310-30 resulted in the following changes in the carrying amount of accretable yield during 2018 and 2017:

| | December 31, 2018 | December 31, 2017 |
|---|-------------------|-------------------|
| Accretable yield beginning balance | \$ 46,568 | \$ 60,476 |
| Reclassification from non-accretable difference | 10,751 | 11,398 |
| Reclassification to non-accretable difference | (2,263) | (2,801) |
| Accretion | (19,155) | (22,505) |
| Accretable yield ending balance | \$ 35,901 | \$ 46,568 |

Below is the composition of the net book value for loans accounted for under ASC 310-30 at December 31, 2018 and 2017:

| | December 31, 2018 | December 31, 2017 |
|--------------------------------------|-------------------|-------------------|
| Contractual cash flows | \$ 420,994 | \$ 489,892 |
| Non-accretable difference | (314,214) | (322,701) |
| Accretable yield | (35,901) | (46,568) |
| Loans accounted for under ASC 310-30 | \$ 70,879 | \$ 120,623 |

Note 8 Allowance for Loan Losses

The tables below detail the Company's allowance for loan losses and recorded investment in loans as of and for the years ended December 31, 2018 and 2017:

| | Year ended December 31, 2018 | | | | Total |
|-------------------|------------------------------|---|-------------------------|----------|-----------|
| | Commercial | Non-owner occupied commercial real estate | Residential real estate | Consumer | |
| Beginning balance | \$ 21,385 | \$ 5,609 | \$ 3,965 | \$ 305 | \$ 31,264 |
| | 21,340 | 5,583 | 3,965 | 305 | 31,193 |

Edgar Filing: National Bank Holdings Corp - Form 10-K

| | | | | | |
|---|--------------|------------|------------|-----------|--------------|
| Originated and acquired beginning balance | | | | | |
| Charge-offs | (833) | (11) | (118) | (1,134) | (2,096) |
| Recoveries | 1,171 | — | 14 | 204 | 1,389 |
| Provision | 5,268 | (1,166) | (101) | 974 | 4,975 |
| Originated and acquired ending balance | 26,946 | 4,406 | 3,760 | 349 | 35,461 |
| ASC 310-30 beginning balance | 45 | 26 | — | — | 71 |
| Charge-offs | (62) | — | — | — | (62) |
| Recoveries | — | — | — | — | — |
| Provision (recoupment) | 208 | (26) | 40 | — | 222 |
| ASC 310-30 ending balance | 191 | — | 40 | — | 231 |
| Ending balance | \$ 27,137 | \$ 4,406 | \$ 3,800 | \$ 349 | \$ 35,692 |
| Ending allowance balance attributable to: | | | | | |
| Originated and acquired loans individually evaluated for impairment | \$ 1,132 | \$ 2 | \$ 35 | \$ — | \$ 1,169 |
| Originated and acquired loans collectively evaluated for impairment | 25,814 | 4,404 | 3,725 | 349 | 34,292 |
| ASC 310-30 loans | 191 | — | 40 | — | 231 |
| Total ending allowance balance | \$ 27,137 | \$ 4,406 | \$ 3,800 | \$ 349 | \$ 35,692 |
| Loans: | | | | | |
| Originated and acquired loans individually evaluated for impairment | \$ 18,282 | \$ 2,129 | \$ 5,169 | \$ 5,499 | \$ 31,079 |
| Originated and acquired loans collectively evaluated for impairment | 2,605,891 | 549,690 | 815,651 | 19,118 | 3,990,350 |
| ASC 310-30 loans | 20,398 | 40,393 | 9,995 | 93 | 70,879 |
| Total loans | \$ 2,644,571 | \$ 592,212 | \$ 830,815 | \$ 24,710 | \$ 4,092,308 |

Table of Contents

| | Year ended December 31, 2017 | | | | |
|--|------------------------------|--|----------------------------|-----------|--------------|
| | Commercial | Non-owner occupied commercial real estate | Residential real estate | Consumer | Total |
| Beginning balance | \$ 18,821 | \$ 5,642 | \$ 4,387 | \$ 324 | \$ 29,174 |
| Originated and acquired beginning balance | 18,821 | 5,422 | 4,387 | 319 | 28,949 |
| Charge-offs | (10,342) | — | (236) | (737) | (11,315) |
| Recoveries | 99 | 20 | 129 | 185 | 433 |
| Provision (recoupment) | 12,762 | 141 | (315) | 538 | 13,126 |
| Originated and acquired ending balance | 21,340 | 5,583 | 3,965 | 305 | 31,193 |
| ASC 310-30 beginning balance | — | 220 | — | 5 | 225 |
| Charge-offs | — | — | — | — | — |
| Recoveries | — | — | — | — | — |
| Provision (recoupment) | 45 | (194) | — | (5) | (154) |
| ASC 310-30 ending balance | 45 | 26 | — | — | 71 |
| Ending balance | \$ 21,385 | \$ 5,609 | \$ 3,965 | \$ 305 | \$ 31,264 |
| Ending allowance balance attributable to: | | | | | |
| Originated and acquired loans individually evaluated for impairment | \$ 1,466 | \$ 2 | \$ 32 | \$ 1 | \$ 1,501 |
| Originated and acquired loans collectively evaluated for impairment | 19,874 | 5,581 | 3,933 | 304 | 29,692 |
| ASC 310-30 loans | 45 | 26 | — | — | 71 |
| Total ending allowance balance | \$ 21,385 | \$ 5,609 | \$ 3,965 | \$ 305 | \$ 31,264 |
| Loans: | | | | | |
| Originated and acquired loans individually evaluated for impairment | \$ 22,232 | \$ 1,260 | \$ 7,240 | \$ 141 | \$ 30,873 |
| Originated and acquired loans collectively evaluated for impairment | 1,822,898 | 483,881 | 696,238 | 24,434 | 3,027,451 |
| ASC 310-30 loans | 29,475 | 77,908 | 12,759 | 481 | 120,623 |
| Total loans | \$ 1,874,605 | \$ 563,049 | \$ 716,237 | \$ 25,056 | \$ 3,178,947 |

In evaluating the loan portfolio for an appropriate ALL level, non-impaired originated and acquired loans were grouped into segments based on broad characteristics such as primary use and underlying collateral. Within the segments, the portfolio was further disaggregated into classes of loans with similar attributes and risk characteristics for purposes of applying loss ratios and determining applicable subjective adjustments to the ALL. The application of subjective adjustments was based upon qualitative risk factors, including economic trends and conditions, industry conditions, asset quality, loss trends, lending management, portfolio growth and loan review/internal audit results.

Net charge-offs on originated and acquired loans during the year ended December 31, 2018 were \$0.7 million. Management's evaluation of credit quality resulted in provision for originated and acquired loan losses of \$5.0 million during the year ended December 31, 2018. One large recovery of \$1.1 million in 2018 resulted in lower provision.

During 2018 and 2017, the Company re-estimated the expected cash flows of the loan pools accounted for under ASC 310-30. The re-measurement in 2018 resulted in provision of \$222 thousand primarily driven by the commercial segment. The re-measurement in 2017 resulted in a net recoupment of \$154 thousand, due to a \$194 thousand recoupment in the non-owner occupied commercial real estate segment.

Table of Contents

Note 9 Premises and Equipment

Premises and equipment consisted of the following at December 31, 2018 and 2017:

| | December 31, 2018 | December 31, 2017 |
|---|-------------------|-------------------|
| Land | \$ 32,058 | \$ 28,698 |
| Buildings and improvements | 88,955 | 73,703 |
| Equipment | 52,354 | 46,091 |
| Total premises and equipment, at cost | 173,367 | 148,492 |
| Less: accumulated depreciation and amortization | (63,381) | (54,784) |
| Premises and equipment, net | \$ 109,986 | \$ 93,708 |

The Company incurred \$8.6 million, \$7.6 million and \$8.7 million of depreciation expense during 2018, 2017 and 2016, respectively, as a component of occupancy and equipment expense in the consolidated statements of operations. The Company disposed of \$1.7 million, \$2.3 million and \$3.5 million of premises and equipment, net, during 2018, 2017 and 2016, respectively. During 2018, the Company consolidated one banking center acquired from Peoples that was valued at fair value less cost to sell at the date of acquisition. The banking center totaled \$4.6 million and is classified as held-for-sale at December 31, 2018.

During 2018, the Company consolidated one banking center. During 2017, the Company consolidated two banking centers and completed the divestiture of four banking centers, resulting in a gain of \$2.9 million included in non-interest income in the consolidated statements of operations.

Space in certain facilities is leased under operating leases. Below is a summary of future minimum lease payments as of December 31, 2018:

| Years ending December 31, | Amount |
|---------------------------|-----------|
| 2019 | \$ 3,092 |
| 2020 | 2,981 |
| 2021 | 3,091 |
| 2022 | 3,052 |
| 2023 | 2,047 |
| Thereafter | 10,163 |
| Total | \$ 24,426 |

Note 10 Other Real Estate Owned

A summary of the activity in the OREO balances during 2018 and 2017 is as follows:

| | For the years ended | |
|--|---------------------|-----------|
| | December 31, | |
| | 2018 | 2017 |
| Beginning balance | \$ 10,491 | \$ 15,662 |
| Acquired through acquisition | 1,253 | — |
| Transfers from loan portfolio, at fair value | 24,940 | 1,800 |
| Impairments | (230) | (766) |
| Sales | (25,858) | (6,205) |
| Ending balance | \$ 10,596 | \$ 10,491 |

OREO totaled \$10.6 million at December 31, 2018 and increased \$0.1 million from December 31, 2017. During 2018, the Company sold \$25.9 million of OREO primarily driven by one large property that was previously an acquired 310-30 loan, which was transferred to OREO during the second quarter of 2018. OREO net gains of \$0.5 million and \$4.2 million were included in the consolidated statement of operations for the years ended December 31, 2018 and 2017, respectively.

Table of Contents

Note 11 Goodwill and Intangible Assets

Goodwill and core deposit intangible

In connection with all of our acquisitions, the Company recorded goodwill of \$115.0 million and core deposit intangible assets of \$48.8 million. In connection with the acquisition of Peoples in January of 2018, the Company recorded goodwill of \$55.4 million and core deposit intangible assets of \$10.5 million. The goodwill is measured as the excess of the fair value of consideration paid over the fair value of net assets acquired. No goodwill impairment was recorded during the years ended December 31, 2018 or December 31, 2017.

The gross carrying amount of the core deposit intangibles and the associated accumulated amortization at December 31, 2018 and December 31, 2017, are presented as follows:

| | December 31, 2018 | | | December 31, 2017 | | |
|-------------------------|-----------------------|--------------------------|---------------------|-----------------------|--------------------------|---------------------|
| | Gross carrying amount | Accumulated amortization | Net carrying amount | Gross carrying amount | Accumulated amortization | Net carrying amount |
| Core deposit intangible | \$ 48,834 | \$ 38,920 | \$ 9,914 | \$ 38,357 | \$ 36,750 | \$ 1,607 |

The accumulated amortization of the core deposit intangible assets was \$38.9 million and \$36.8 million at December 31, 2018 and 2017, respectively. At December 31, 2018, the core deposit intangible for the Bank Midwest, Hillcrest Bank, Bank of Choice and Community Banks of Colorado acquisitions were fully amortized.

The Company is amortizing the core deposit intangibles from acquisitions on a straight line basis over 7-10 years from the date of the respective acquisitions, which represents the expected useful life of the assets. The Company recognized core deposit intangible amortization expense of \$2.2 million, \$5.3 million and \$5.5 million during 2018, 2017 and 2016, respectively.

The following table shows the estimated future amortization expense for the core deposit intangibles as of December 31, 2018:

| Years ending December 31, | Amount |
|---------------------------|--------|
|---------------------------|--------|

| | |
|------|----------|
| 2019 | \$ 1,183 |
| 2020 | 1,183 |
| 2021 | 1,183 |
| 2022 | 1,127 |
| 2023 | 1,048 |

Mortgage servicing rights

In connection with the acquisition of Peoples, the Company recorded mortgage servicing rights of \$4.3 million. Mortgage servicing rights represent rights to service loans originated by the Company and sold to government sponsored enterprises including FHLMC, FNMA, GNMA and FHLB. Mortgage loans serviced for others were \$389.0 million at December 31, 2018 and \$0.0 million at December 31, 2017.

105

Table of Contents

Below are the changes in the mortgage servicing rights for the period presented:

| | For the years ended December 31, 2018 |
|---|---|
| Beginning balance | \$ — |
| Acquired through acquisition | 4,301 |
| Originations | 30 |
| Impairment | (21) |
| Amortization | (754) |
| Ending balance | \$ 3,556 |
| Fair value of mortgage servicing rights | \$ 3,884 |

The fair value of mortgage servicing rights was determined based upon a discounted cash flow analysis. The cash flow analysis included assumptions for discount rates and prepayment speeds. Discount rates ranged from 9.5% to 10.5% and the constant prepayment speed ranged from 12.2% to 17.2% for the December 31, 2018 valuation. Included in mortgage banking income in the consolidated statements of operations were service fees of \$1.1 million for the year ended December 31, 2018.

Mortgage servicing rights are evaluated for impairment and recognized to the extent fair value is less than the carrying amount. The Company evaluates impairment by type (FHLMC, FNMA, GNMA and FHLB) and interest rate. The Company is amortizing the mortgage servicing rights in proportion to and over the period of the estimated net servicing income of the underlying loans. The Company recognized mortgage servicing rights amortization expense of \$0.8 million and \$0.0 million during the years ended December 31, 2018 and 2017, respectively.

The following table shows the estimated future amortization expense for the mortgage servicing rights as of December 31, 2018:

| Years ending December 31, | Amount |
|---------------------------|--------|
| 2019 | \$ 604 |
| 2020 | 501 |
| 2021 | 416 |
| 2022 | 346 |
| 2023 | 287 |

Note 12 Deposits

Total deposits were \$4.5 billion and \$4.0 billion at December 31, 2018 and 2017, respectively. Time deposits were \$1.1 billion and \$1.1 billion at December 31, 2018 and 2017, respectively. The following table summarizes the Company's time deposits by remaining contractual maturity:

| Years ending December 31, | Amount |
|---------------------------|--------------|
| 2019 | \$ 685,421 |
| 2020 | 316,113 |
| 2021 | 38,778 |
| 2022 | 32,989 |
| 2023 | 4,919 |
| Thereafter | 2,309 |
| Total time deposits | \$ 1,080,529 |

Table of Contents

The Company incurred interest expense on deposits as follows during the periods indicated:

| | For the years ended December 31, | | |
|----------------------------------|----------------------------------|-----------|-----------|
| | 2018 | 2017 | 2016 |
| Interest bearing demand deposits | \$ 887 | \$ 445 | \$ 369 |
| Money market accounts | 5,622 | 4,077 | 3,600 |
| Savings accounts | 2,249 | 1,481 | 1,016 |
| Time deposits | 12,283 | 10,169 | 8,978 |
| Total | \$ 21,041 | \$ 16,172 | \$ 13,963 |

The Federal Reserve System requires cash balances to be maintained at the Federal Reserve Bank based on certain deposit levels. There was no minimum reserve requirement for the Bank at December 31, 2018.

Note 13 Borrowings

The following table sets forth selected information regarding repurchase agreements during 2018, 2017 and 2016:

| | As of and for the years ended December 31, | | |
|---|--|------------|------------|
| | 2018 | 2017 | 2016 |
| Maximum amount of outstanding agreements at any month end during the period | \$ 142,292 | \$ 130,463 | \$ 154,404 |
| Average amount outstanding during the period | \$ 87,691 | \$ 88,390 | \$ 109,246 |
| Weighted average interest rate for the period | 0.34% | 0.19% | 0.14% |

As of December 31, 2018, 2017 and 2016, the Company had pledged mortgage-backed securities with a fair value of approximately \$73.9 million, \$136.1 million and \$99.1 million, respectively, for securities sold under agreements to repurchase. Additionally, there was \$5.9 million, \$5.7 million and \$7.0 million of excess collateral pledged for repurchase agreements at December 31, 2018, 2017 and 2016, respectively.

The vast majority of the Company's repurchase agreements are overnight transactions with clients that mature the day after the transaction. During 2018, 2017 and 2016, the overnight agreements had a weighted average interest rate of 0.34%, 0.19% and 0.14%, respectively. At December 31, 2018, 2017 and 2016, none of the Company's repurchase agreements were for periods longer than one day. The repurchase agreements are subject to a master netting arrangement; however, the Company has not offset any of the amounts shown in the consolidated financial statements.

As a member of the FHLB, the Bank has access to a line of credit and term financing from the FHLB with total available credit of \$1.1 billion at December 31, 2018. At December 31, 2018, 2017 and 2016, the Bank had \$234.3 million, \$0.0 million and \$0.0 million in line of credit advances from the FHLB, respectively, that mature within a day. At December 31, 2018, 2017 and 2016, the Bank had \$67.3 million, \$129.1 million and \$25.0 million in term advances from the FHLB, respectively. The term advances have fixed interest rates between 1.55% - 2.33% with maturity dates of 2019 - 2020. The Bank had investment securities pledged as collateral for FHLB advances in the amount of \$16.0 million, \$28.1 million and \$28.8 million at December 31, 2018, 2017 and 2016, respectively. Loans pledged were \$1.6 billion at December 31, 2018 and \$1.2 billion at December 31, 2017. Interest expense related to FHLB advances totaled \$2.6 million, \$1.8 million and \$0.7 million for the years ended December 31, 2018, 2017 and 2016, respectively.

Note 14 Regulatory Capital

As a bank holding company, the Company is subject to regulatory capital adequacy requirements implemented by the Federal Reserve. The federal banking agencies have risk-based capital adequacy regulations intended to provide a measure of capital adequacy that reflects the degree of risk associated with a banking organization's operations. Under these regulations, assets are assigned to one of several risk categories, and nominal dollar amounts of assets and credit equivalent amounts of off-balance-sheet items are multiplied by a risk adjustment percentage for the category.

The Basel III rules, effective January 1, 2015, changed the components of regulatory capital, changed the way in which risk ratings are assigned to various categories of bank assets and defined a new Tier 1 common risk-based ratio. In addition, a capital conservative buffer requirement, designed to strengthen an institution's financial resilience during economic cycles

Table of Contents

through the restriction of capital distributions and other payments, became effective in 2017, with full phase-in beginning January 1, 2019. When fully phased-in, the capital conservation buffer adds a 2.5% capital requirement above existing regulatory minimum ratios.

Under the Basel III requirements, at December 31, 2018 and 2017, the Company and the Bank met all capital requirements and the Bank had regulatory capital ratios in excess of the levels established for well-capitalized institutions, as detailed in the tables below.

| | December 31, 2018 | | | | | |
|--|-------------------|------------|---|------------|---|------------|
| | Actual | | Required to be well capitalized under prompt corrective action provisions | | Required to be considered adequately capitalized(1) | |
| | Ratio | Amount | Ratio | Amount | Ratio | Amount |
| Tier 1 leverage ratio: | | | | | | |
| Consolidated | 10.5% | \$ 580,504 | N/A | N/A | 4.0% | \$ 220,988 |
| NBH Bank | 9.0% | 498,283 | 5.0% | \$ 275,703 | 4.0% | 220,563 |
| Common equity tier 1 risk-based capital: | | | | | | |
| Consolidated | 12.9% | \$ 580,504 | N/A | N/A | 7.0% | \$ 386,728 |
| NBH Bank | 11.1% | 498,283 | 6.5% | \$ 358,414 | 7.0% | 385,984 |
| Tier 1 risk-based capital ratio: | | | | | | |
| Consolidated | 12.9% | \$ 580,504 | N/A | N/A | 8.5% | \$ 382,306 |
| NBH Bank | 11.1% | 498,283 | 8.0% | \$ 358,938 | 8.5% | 381,372 |
| Total risk-based capital ratio: | | | | | | |
| Consolidated | 13.8% | \$ 620,275 | N/A | N/A | 10.5% | \$ 472,261 |
| NBH Bank | 12.0% | 538,054 | 10.0% | \$ 448,672 | 10.5% | 471,106 |

| | December 31, 2017 | | | | | |
|--|-------------------|------------|---|------------|---|------------|
| | Actual | | Required to be well capitalized under prompt corrective action provisions | | Required to be considered adequately capitalized(1) | |
| | Ratio | Amount | Ratio | Amount | Ratio | Amount |
| Tier 1 leverage ratio: | | | | | | |
| Consolidated | 9.8% | \$ 470,877 | N/A | N/A | 4.0% | \$ 191,559 |
| NBH Bank | 8.1% | 382,918 | 5.0% | \$ 237,772 | 4.0% | 190,217 |
| Common equity tier 1 risk-based capital: | | | | | | |
| Consolidated | 12.9% | \$ 470,877 | N/A | N/A | 7.0% | \$ 335,228 |
| NBH Bank | 10.6% | 382,918 | 6.5% | \$ 309,103 | 7.0% | 332,881 |
| Tier 1 risk-based capital ratio: | | | | | | |

Edgar Filing: National Bank Holdings Corp - Form 10-K

| | | | | | | |
|---------------------------------|-------|------------|-------|------------|-------|------------|
| Consolidated | 12.9% | \$ 470,877 | N/A | N/A | 8.5% | \$ 309,400 |
| NBH Bank | 10.6% | 382,918 | 8.0% | \$ 289,022 | 8.5% | 307,086 |
| Total risk-based capital ratio: | | | | | | |
| Consolidated | 13.8% | \$ 502,917 | N/A | N/A | 10.5% | \$ 382,200 |
| NBH Bank | 11.5% | 414,958 | 10.0% | \$ 361,277 | 10.5% | 379,341 |

(1) As of the fully phased-in date of January 1, 2019, including the capital conservation buffer.

Note 15 Revenue from Contracts with Clients

On January 1, 2018, the Company adopted ASU No. 2014-09 “Revenue from Contracts with Customers” (Topic 606) and all subsequent ASUs that modified Topic 606. As stated in Note 3, Recent Accounting Pronouncements, the implementation of the new standard did not have a material impact on the measurement or recognition of revenue; as such, a cumulative effect adjustment to opening retained earnings was not deemed necessary. Results for reporting periods beginning after January 1, 2018 are presented under Topic 606, while prior period amounts were not adjusted and continue to be reported in accordance with our historic accounting under Topic 605.

Topic 606 does not apply to revenue associated with financial instruments, including revenue from loans and securities. In addition, certain noninterest income streams such as fees associated with mortgage servicing rights, financial guarantees, and

Table of Contents

derivatives are also not in scope of the new guidance. Topic 606 is applicable to non-interest revenue streams such as deposit related fees, interchange fees, and merchant income. However, the recognition of these revenue streams did not change significantly upon adoption of Topic 606. Substantially all of the Company's revenue is generated from contracts with clients. Noninterest revenue streams in-scope of Topic 606 are discussed below.

Service Charges and other fees

Service charge fees are primarily comprised of monthly service fees, check orders, and other deposit account related fees. Other fees include revenue from processing wire transfers, bill pay service, cashier's checks, and other services. The Company's performance obligation for account analysis fees and monthly service fees is generally satisfied, and the related revenue recognized, over the period in which the service is provided. Check orders and other deposit account related fees are largely transactional based, and therefore, the Company's performance obligation is satisfied, and related revenue recognized, at a point in time. Payment for service charges on deposit accounts is primarily received immediately or in the following month through a direct charge to clients' accounts.

Bank card fees

Bank card fees are primarily comprised of debit card income, ATM fees, merchant services income, and other fees. Debit card income is primarily comprised of interchange fees earned whenever the Company's debit cards are processed through card payment networks such as Visa. ATM fees are primarily generated when a Company cardholder uses a non-Company ATM or a non-Company cardholder uses a Company ATM. Merchant services income mainly represents fees charged to merchants to process their debit card transactions. The Company's performance obligation for bank card fees are largely satisfied, and related revenue recognized, when the services are rendered or upon completion. Payment is typically received immediately or in the following month.

Loss (gain) on OREO Sales, net

Loss (gain) on OREO Sales, net is recognized when the Company meets its performance obligation to transfer title to the buyer. The gain or loss is measured as the excess of the proceeds received compared to the OREO carrying value. Sales proceeds are received in cash at the time of transfer.

The following table presents non-interest income, segregated by revenue streams in-scope and out-of-scope of Topic 606, and non-interest expense in-scope of Topic 606 for the years ended December 31, 2018 and 2017.

| | For the years ended December 31, | | |
|---|----------------------------------|-----------|-----------|
| | 2018 | 2017 | 2016 |
| Non-interest income | | | |
| In-scope of Topic 606: | | | |
| Service Charges and other fees | \$ 20,408 | \$ 19,070 | \$ 15,961 |
| Bank card fees | 14,489 | 12,026 | 11,429 |
| Gain on banking center divestiture | — | 2,942 | — |
| Non-interest income (in-scope of Topic 606) | 34,897 | 34,038 | 27,390 |
| Non-interest income (out-of-scope of Topic 606) | 35,878 | 5,167 | 12,637 |
| Total non-interest income | \$ 70,775 | \$ 39,205 | \$ 40,027 |
| Non-interest expense | | | |
| In-scope of Topic 606: | | | |
| (Gain) loss on OREO sales, net | (488) | (4,150) | (4,383) |
| Total revenue in-scope of Topic 606 | \$ 34,409 | \$ 29,888 | \$ 23,007 |

Contract Balances

A contract asset balance occurs when an entity performs a service for a client before the client pays consideration (resulting in a contract receivable) or before payment is due (resulting in a contract asset). A contract liability balance is an entity's obligation to transfer a service to a client for which the entity has already received payment (or payment is due) from the client. The Company's noninterest revenue streams are largely based on transactional activity or standard month-end revenue accruals. Consideration is often received immediately or shortly after the Company satisfies its performance obligation and

Table of Contents

revenue is recognized. The Company does not typically enter into long-term revenue contracts with clients, and therefore, does not experience significant contract balances. As of December 31, 2018 and December 31, 2017, the Company did not have any contract balances.

Contract Acquisition Costs

In connection with the adoption of Topic 606, an entity is required to capitalize, and subsequently amortize into expense, certain incremental costs of obtaining a contract with a client if these costs are expected to be recovered. The incremental costs of obtaining a contract are those costs that an entity incurs to obtain a contract with a client that it would not have incurred if the contract had not been obtained (for example, sales commission). The Company utilizes the practical expedient which allows entities to immediately expense contract acquisition costs when the asset that would have resulted from capitalizing these costs would have been amortized in one year or less. Upon adoption of Topic 606, the Company did not capitalize any contract acquisition cost.

Note 16 Stock-based Compensation and Benefits

The Company provides stock-based compensation in accordance with shareholder-approved plans. During the second quarter of 2014, shareholders approved the 2014 Omnibus Incentive Plan (the "2014 Plan"). The 2014 Plan replaces the NBH Holdings Corp. 2009 Equity Incentive Plan (the "Prior Plan"), pursuant to which the Company granted equity awards prior to the approval of the 2014 Plan. Pursuant to the 2014 Plan, the Compensation Committee of the Board of Directors has the authority to grant, from time to time, awards of stock options, stock appreciation rights, restricted stock, restricted stock units, performance units, other stock-based awards, or any combination thereof to eligible persons.

As of December 31, 2018, the aggregate number of Class A common stock available for issuance under the 2014 Plan is 5,254,682 shares. Any shares that are subject to stock options or stock appreciation rights under the 2014 Plan will be counted against the amount available for issuance as one share for every one share granted, and any shares that are subject to awards under the 2014 Plan other than stock options or stock appreciation rights will be counted against the amount available for issuance as 3.25 shares for every one share granted. The 2014 Plan provides for recycling of shares from both the Prior Plan and the 2014 Plan, the terms of which are further described in the Company's Proxy Statement for its 2014 Annual Meeting of Shareholders. Upon an option exercise, it is the Company's policy to issue shares from treasury stock.

To date, the Company has issued stock options, restricted stock and performance stock units under the plans. The Compensation Committee sets the option exercise price at the time of grant, but in no case is the exercise price less than the fair market value of a share of stock at the date of grant.

Stock options

The Company issued stock options during 2018, 2017 and 2016, which are primarily time-vesting with 1/3 vesting on each of the first, second and third anniversary of the date of grant or date of hire.

The expense associated with the awarded stock options was measured at fair value using a Black-Scholes option-pricing model. The outstanding option awards vest or have vested on a graded basis over 1-4 years of continuous service and have 7-10 year contractual terms.

110

Table of Contents

Below are the weighted average assumptions used in the Black-Scholes option pricing model to determine fair value of the Company's stock options granted in 2018, 2017 and 2016:

| | 2018 | 2017 | 2016 |
|--|---------|---------|---------|
| Weighted average fair value | \$ 7.43 | \$ 7.84 | \$ 4.24 |
| Weighted average risk-free interest rate (1) | 2.69% | 2.14% | 1.47% |
| Expected volatility (2) | 20.75% | 21.61% | 22.47% |
| Expected term (years) (3) | 6.10 | 6.09 | 6.09 |
| Dividend yield (4) | 1.13% | 0.83% | 1.02% |

- (1) The risk-free rate for the expected term of the options was based on the U.S. Treasury yield curve at the date of grant and based on the expected term.
- (2) Expected volatility was calculated using a time-based weighted migration of the Company's own stock price volatility coupled with those of a peer group of eight comparable publicly traded companies for a period commensurate with the expected term of the options.
- (3) The expected term was estimated to be the average of the contractual vesting term and time to expiration.
- (4) The dividend yield was assumed to be \$0.05 per share per quarter through the third quarter of 2016, \$0.07 per share per quarter through the first quarter of 2017, \$0.09 per share per quarter through the first quarter of 2018, \$0.14 per share per quarter through the third quarter of 2018 and \$0.17 per share per quarter through the fourth quarter of 2018 in accordance with the Company's dividend policy at the time of grant.

The Company issued stock options in accordance with the 2014 Plan during 2018. The following table summarizes stock option activity for 2018:

| | Options | Weighted average exercise price | Weighted average contractual term in years | Aggregate intrinsic value |
|--|-----------|---------------------------------|--|---------------------------|
| Outstanding at December 31, 2017 | 1,598,318 | \$ 20.62 | 4.07 | \$ 19,017 |
| Granted | 158,316 | 32.99 | | |
| Exercised | (473,363) | 19.88 | | |
| Forfeited | (18,395) | 28.76 | | |
| Outstanding at December 31, 2018 | 1,264,876 | \$ 22.33 | 3.92 | \$ 11,387 |
| Options exercisable at December 31, 2018 | 1,011,744 | 20.18 | 2.74 | 10,903 |
| Options vested and expected to vest | 1,241,729 | 22.14 | 3.82 | 11,376 |

Stock option expense is a component of salaries and benefits in the consolidated statements of operations and totaled \$0.8 million, \$0.7 million and \$0.7 million for 2018, 2017 and 2016, respectively. At December 31, 2018, there was \$0.7 million of total unrecognized compensation cost related to non-vested stock options granted under the plans. The

cost is expected to be recognized over a weighted average period of 2.1 years.

Table of Contents

The following table summarizes the Company's outstanding stock options:

| Range of exercise price | Options outstanding | | | Options exercisable | |
|-------------------------|---------------------|---|---------------------------------|---------------------|---------------------------------|
| | Number outstanding | Weighted average remaining contractual life (years) | Weighted average exercise price | Number exercisable | Weighted average exercise price |
| \$ 18.00- 18.99 | 75,863 | 4.90 | \$ 18.60 | 75,863 | \$ 18.60 |
| \$ 19.00- 19.99 | 197,339 | 6.80 | \$ 19.39 | 155,231 | \$ 19.34 |
| \$ 20.00- 20.99 | 752,786 | 1.51 | \$ 20.01 | 752,440 | \$ 20.01 |
| and | | | | | |
| \$ 21.00above | 238,888 | 8.80 | \$ 33.27 | 28,210 | \$ 33.59 |

Restricted stock awards

The Company issued time-based restricted stock awards during 2018, 2017 and 2016. The restricted stock awards vest over a range of a 1 – 3 year period. Restricted stock with time-based vesting was valued at the fair value of the shares on the date of grant as they are assumed to be held beyond the vesting period.

No market-based stock awards were granted during 2018 or 2017. The market-based performance condition has been met for market-based stock awards granted during 2016, and the total unrecognized compensation cost related to non-vested market-based stock awards is expected to be recognized over a weighted average period of approximately 0.2 years.

Performance stock units

During the years ended December 31, 2018, 2017 and 2016, the Company granted 77,125, 49,758, and 91,342 performance stock units in accordance with the 2014 Plan, respectively. These performance stock units granted represent initial target awards and do not reflect potential increases or decreases resulting from the final performance results, which are to be determined at the end of the three-year performance period (vesting date). The actual number of shares to be awarded at the end of the performance period will range from 0% - 150% of the initial target awards. 60% of the award is based on the Company's cumulative earnings per share (EPS target) during the performance period, and 40% of the award is based on the Company's cumulative total shareholder return (TSR target), or TSR, during the performance period. On the vesting date, the Company's TSR will be compared to the respective TSRs of the companies comprising the KBW Regional Index at the grant date to determine the shares awarded. The fair value of the EPS target portion of the award was determined based on the closing stock price of the Company's common

stock on the grant date. The fair value of the TSR target portion of the award was determined using a Monte Carlo Simulation at the grant date. The weighted-average grant date fair value per unit for awards granted during 2018 of the EPS target portion and the TSR target portion was \$32.65 and \$27.51, respectively.

The following table summarizes restricted stock and performance stock unit activity during 2018 and 2017:

| | Restricted stock shares | Weighted average grant- date fair value | Performance stock units | Weighted average grant- date fair value |
|-------------------------------|----------------------------|---|----------------------------|---|
| Unvested at December 31, 2016 | 499,271 | \$ 15.82 | 85,295 | \$ 18.22 |
| Granted | 66,471 | 33.43 | 49,758 | 33.22 |
| Vested | (380,956) | 15.40 | — | — |
| Forfeited | (21,229) | 18.73 | (9,971) | 21.78 |
| Unvested at December 31, 2017 | 163,557 | \$ 22.60 | 125,082 | \$ 23.90 |
| Granted | 92,133 | 33.69 | 77,125 | 30.38 |
| Vested | (94,775) | 23.71 | — | — |
| Forfeited | (14,421) | 29.37 | (10,158) | 25.90 |
| Unvested at December 31, 2018 | 146,494 | \$ 28.19 | 192,049 | \$ 26.40 |

As of December 31, 2018, the total unrecognized compensation cost related to the non-vested restricted stock awards and performance stock units totaled \$2.0 million and \$2.5 million, respectively, and is expected to be recognized over a weighted

Table of Contents

average period of approximately 2.0 years and 1.8 years, respectively. Expense related to non-vested restricted stock awards totaled \$2.1 million, \$2.2 million and \$2.4 million during 2018, 2017 and 2016, respectively. Expense related to non-vested performance stock units totaled \$1.5 million, \$0.8 million and \$0.4 million during 2018, 2017 and 2016, respectively. Expense related to non-vested restricted stock awards and units is a component of salaries and benefits in the Company's consolidated statements of operations.

Employee Stock Purchase Plan

The 2014 Employee Stock Purchase Plan ("ESPP") is intended to be a qualified plan within the meaning of Section 423 of the Internal Revenue Code of 1986 and allows eligible employees to purchase shares of common stock through payroll deductions up to a limit of \$25,000 per calendar year and 2,000 shares per offering period. The price an employee pays for shares is 90.0% of the fair market value of Company common stock on the last day of the offering period. The offering periods are the six-month periods commencing on March 1 and September 1 of each year and ending on August 31 and February 28 (or February 29 in the case of a leap year) of each year. There are no vesting or other restrictions on the stock purchased by employees under the ESPP. Under the ESPP, the total number of shares of common stock reserved for issuance totaled 400,000 shares, of which 342,644 were available for issuance.

Under the ESPP, employees purchased 12,515 shares and 11,178 shares during 2018 and 2017, respectively.

Note 17 Warrants

During 2017 and 2016, 250,750 and 475,000 warrants were exercised in a non-cash transaction, respectively, representing the remaining outstanding warrants. The warrants were granted to certain lead shareholders of the Company at the time of the Company's initial capital raise (2009-2010), all with an exercise price of \$20.00 per share. Refer to the consolidated statements of changes in shareholders' equity for additional detail.

During 2015, the Company modified its remaining warrant agreements resulting in the reclassification of \$3.1 million to additional paid-in capital included in the consolidated statements of financial condition at December 31, 2015. Refer to the consolidated statements of changes in shareholders' equity for additional detail.

Note 18 Common Stock

The Company had 30,769,063 and 26,875,585 shares of Class A common stock outstanding at December 31, 2018 and 2017, respectively. Additionally, the Company had 146,494 and 163,557 shares outstanding at December 31, 2018 and 2017, respectively, of restricted Class A common stock issued but not yet vested under the 2014 Omnibus Incentive Plan and the Prior Plan that are not included in shares outstanding until such time that they are vested; however, these shares do have voting and certain dividend rights during the vesting period.

On August 5, 2016, the Board of Directors authorized a share repurchase program for up to \$50.0 million from time to time in either the open market or through privately negotiated transactions. The remaining authorization under this program at December 31, 2018 was \$12.6 million.

Note 19 Earnings Per Share

The Company calculates earnings per share under the two-class method, as certain non-vested share awards contain non-forfeitable rights to dividends. As such, these awards are considered securities that participate in the earnings of the Company. Non-vested shares are discussed further in note 17.

The Company had 30,769,063 and 26,875,585 shares of Class A common stock outstanding as of December 31, 2018 and 2017, respectively, exclusive of issued non-vested restricted shares. Certain stock options and non-vested restricted shares are potentially dilutive securities, but are not included in the calculation of diluted income per share because to do so would have been anti-dilutive for 2018, 2017 and 2016.

Table of Contents

The following table illustrates the computation of basic and diluted income per share for 2018, 2017 and 2016:

| | For the years ended December 31, | | |
|---|----------------------------------|------------|------------|
| | 2018 | 2017 | 2016 |
| Net income | \$ 61,451 | \$ 14,579 | \$ 23,060 |
| Less: income allocated to participating securities | (70) | (56) | (52) |
| Income allocated to common shareholders | \$ 61,381 | \$ 14,523 | \$ 23,008 |
| Weighted average shares outstanding for basic earnings per common share | 30,748,234 | 26,928,763 | 28,313,061 |
| Dilutive effect of equity awards | 681,840 | 772,392 | 704,831 |
| Dilutive effect of warrants | — | 8,504 | 73,451 |
| Weighted average shares outstanding for diluted earnings per common share | 31,430,074 | 27,709,659 | 29,091,343 |
| Basic earnings per share | \$ 2.00 | \$ 0.54 | \$ 0.81 |
| Diluted earnings per share | \$ 1.95 | \$ 0.53 | |