BALCHEM CORP
Form 4
May 08, 2015

FORM 4

Check this box if no longer subject to Section 16. Form 4 or Form 5 obligations may continue. *See* Instruction 1(b).

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

STATEMENT OF CHANGES IN BENEFICIAL OWNERSHIP OF SECURITIES

Filed pursuant to Section 16(a) of the Securities Exchange Act of 1934, Section 17(a) of the Public Utility Holding Company Act of 1935 or Section 30(h) of the Investment Company Act of 1940

OMB APPROVAL
OMB Number: 3235-0287
Expires: January 31, 2005
Estimated average burden hours per response... 0.5

(Print or Type Responses)

1. Name and Address of Reporting Person *
ROSSI DINO A

(Last) (First) (Middle)

BALCHEM CORPORATION, 52 SUNRISE PARK ROAD

(Street)

NEW HAMPTON, NY 10958

(City) (State) (Zip)

2. Issuer Name **and** Ticker or Trading Symbol
BALCHEM CORP [BCPC]

3. Date of Earliest Transaction (Month/Day/Year)
05/07/2015

4. If Amendment, Date Original Filed(Month/Day/Year)

5. Relationship of Reporting Person(s) to Issuer

(Check all applicable)

__X__ Director _____ 10% Owner
_____ Officer (give title below) __X__ Other (specify below)
Executive Chairman

6. Individual or Joint/Group Filing(Check Applicable Line)
_X_ Form filed by One Reporting Person
___ Form filed by More than One Reporting Person

Table I - Non-Derivative Securities Acquired, Disposed of, or Beneficially Owned

1.Title of Security (Instr. 3)	2. Transaction Date (Month/Day/Year)	2A. Deemed Execution Date, if any (Month/Day/Year)	3. Transaction Code (Instr. 8)		4. Securities Acquired (A) or Disposed of (D) (Instr. 3, 4 and 5)			5. Amount of Securities Beneficially Owned Following Reported Transaction(s) (Instr. 3 and 4)	6. Ownership Form: Direct (D) or Indirect (I) (Instr. 4)	7. Nature of Indirect Beneficial Ownership (Instr. 4)
			Code	V	Amount	(A) or (D)	Price			
Common Stock	05/07/2015		M		1,200	A	$ 21.39	147,395	D	
Common Stock	05/07/2015		M		6,100	A	$ 32.21	153,495	D	
Common Stock	05/07/2015		S		7,300 (1)	D	$ 57.8754	146,195	D	
Common Stock	05/08/2015		M		7,300	A	$ 32.21	153,495	D	
Common Stock	05/08/2015		S		7,300 (1)	D	$ 57.5687	146,195	D	

Reminder: Report on a separate line for each class of securities beneficially owned directly or indirectly.

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SEC 1474 (9-02)

Table II - Derivative Securities Acquired, Disposed of, or Beneficially Owned
(*e.g.*, puts, calls, warrants, options, convertible securities)

1. Title of Derivative Security (Instr. 3)	2. Conversion or Exercise Price of Derivative Security	3. Transaction Date (Month/Day/Year)	3A. Deemed Execution Date, if any (Month/Day/Year)	4. Transaction Code (Instr. 8)		5. Number of Derivative Securities Acquired (A) or Disposed of (D) (Instr. 3, 4, and 5)		6. Date Exercisable and Expiration Date (Month/Day/Year)		7. Title and Amount of Underlying Securities (Instr. 3 and 4)		8. Price of Derivative Security (Instr. 5)	9. Nu Deriv Secur Bene Owne Follo Repo Trans (Instr
				Code	V	(A)	(D)	Date Exercisable	Expiration Date	Title	Amount or Number of Shares		

Reporting Owners

Reporting Owner Name / Address	Relationships			
	Director	10% Owner	Officer	Other
ROSSI DINO A BALCHEM CORPORATION 52 SUNRISE PARK ROAD NEW HAMPTON, NY 10958	X		Executive Chairman	

Signatures

/s/ Matthew Houston, Attorney in Fact	05/08/2015
**Signature of Reporting Person	Date

Explanation of Responses:

* If the form is filed by more than one reporting person, *see* Instruction 4(b)(v).

** Intentional misstatements or omissions of facts constitute Federal Criminal Violations. *See* 18 U.S.C. 1001 and 15 U.S.C. 78ff(a).

(1) Sale of shares pursuant to Rule 10b5-1.

Note: File three copies of this Form, one of which must be manually signed. If space is insufficient, *see* Instruction 6 for procedure.
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Provision for loan losses

5,500

774

42

159

--

--

--

6,475

Other operating income

20,575

4,459

1,474

147

--

(137
)
(B)

--

26,518

Other operating expense

94,381

15,586

5,356

2,668

1,739

(C)

943

(C)

Explanation of Responses:

199

(C)

120,872

Income before provision for income taxes

47,599

4,758

3,149

1,328

(1,406
)

(855
)

(4
)

54,569

Provision for income taxes

16,055

1,569

952

457

(506
)
(D)

(308
)
(D)

(1
)
(D)

18,218

Net income
$
31,544

$
3,189

$
2,197

$
871

$
(900
)

$
(547
)

$
(3
)

$
36,351

Basic earnings per share
$
2.65

$
2.46

Diluted earning per share
$
2.58

$
2.40

Basic weighted average shares outstanding

11,906

2,030

364

402

1,726

(E)

819

(E)

299

(E)

14,750

Diluted weighted average shares outstanding

12,239

2,069

364

415

1,759

(E)

819

(E)

309

(E)

15,126

(A) Consists of net accretion of fair value adjustments related to the acquisitions of F&M Bank, SJFHC and NCW assuming acquired January 1, 2006.
(B) Reversal of effects of equity in earnings of San Juan Title Company not acquired in acquisition.
(C) Core deposit amortization assuming acquired January 1, 2006.
(D) Income tax effect of pro forma adjustments at 36%.
(E) Additional shares issued at an exchange rate of 0.85 to 1 for F&M, 2.2503 to 1 for SJFHC and 0.7438 to 1 for NCW.

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Explanation of Responses:

Note 6: CASH, DUE FROM BANKS AND CASH EQUIVALENTS

Cash, due from banks and cash equivalents consisted of the following (in thousands):

	December 31			
		2007		2006
Cash on hand and due from banks	$	98,120	$	68,317
Cash equivalents:				
Short-term cash investments		211		68
Federal funds sold		99		5,000
	$	98,430	$	73,385

For the purpose of reporting cash flows, cash and cash equivalents include cash on hand, amounts due from banks, overnight investments and short-term deposits with original maturities of less than 90 days.

Federal regulations require depository institutions to maintain certain minimum reserve balances. Included in cash and demand deposits were required reserves of $16.2 million and $10.8 million at December 31, 2007 and 2006, respectively.

Note 7: SECURITIES AT FAIR VALUE AND SECURITIES AVAILABLE FOR SALE

The amortized cost and estimated fair value of securities at fair value under SFAS Nos. 157 and 159 at December 31, 2007 are summarized as follows; see Note 9 for further discussion (dollars in thousands):

	Securities at Fair Value Under SFAS Nos. 157 and 159 December 31, 2007				
	Amortized cost	Unrealized holding gains	Unrealized holding losses	Estimated fair value	Percent of Total
U.S. Government and agency obligations	$ 29,857	$ 163	$ (5)	$ 30,015	14.8%
Municipal bonds:					
Taxable	2,010	33	--	2,043	1.0%
Tax exempt	7,099	92	(11)	7,180	3.5%
Total municipal bonds	9,109	125	(11)	9,223	4.5%
Corporate bonds	57,461	758	(2,094)	56,125	27.7%
Mortgage-backed or related securities:					
FHLMC certificates	32,818	--	(438)	32,380	16.0%
FHLMC collateralized mortgage obligations	8,600	11	(40)	8,571	4.2%
Total FHLMC mortgage-backed securities	41,418	11	(478)	40,951	20.2%
GNMA certificates	2,736	2	(6)	2,732	1.4%
GNMA collateralized mortgage obligations	--	--	--	--	--
	2,736	2	(6)	2,732	1.4%

Total GNMA mortgage-backed securities								
FNMA certificates		41,576		54		(253)		41,377	20.3%
FNMA collateralized mortgage obligations		15,192		--		(478)		14,714	7.3%
Total FNMA mortgage-backed securities		56,768		54		(731)		56,091	27.6%
Equity securities:									
FHLMC stock		1,023		761		(198)		1,586	0.8%
FNMA stock		5,893		196		--		6,089	3.0%
Other		14		37		--		51	--
	$	204,279	$	2,107	$	(3,523)	$	202,863	100.0%

Effective January 1, 2007, the Company adopted SFAS No. 157, Fair Value Measurements (SFAS No. 157) and SFAS No. 159, The Fair Value Option for Financial Assets and Financial Liabilities (SFAS No. 159), and elected to account for its portfolio of available for sale securities under that standard whereby changes in the securities' fair value are recognized in earnings. See Note 9 for further discussion.

Proceeds from sales of securities at fair value during the year ended December 31, 2007 were $76,462,000. Gross gains of $2,000 and gross losses of $1,506,000 were realized on those sales. Net unrealized holding gains of $2,691,000 were recognized on securities carried at fair value for the year ended December 31, 2007 and none for the years ended December 31, 2006 and 2005.

Note 7: SECURITIES AT FAIR VALUE AND SECURITIES AVAILABLE FOR SALE (continued)

Securities Available For Sale Under SFAS No. 115 December 31, 2006								
		Amortized cost		Gross unrealized gains		Gross unrealized losses		Estimated fair value	Percent of Total
U.S. Government and agency obligations	$	27,907	$	3	$	(615)	$	27,295	12.1%
Municipal bonds:									
Taxable		4,557		29		(31)		4,555	2.0%
Tax exempt		3,020		45		(21)		3,044	1.4%
Total municipal bonds		7,577		74		(52)		7,599	3.4%
Corporate bonds		37,542		71		(231)		37,382	16.5%
Mortgage-backed or related securities:									
FHLMC certificates		38,863		2		(1,453)		37,412	16.5%
FHLMC collateralized mortgage obligations		27,628		--		(775)		26,853	11.9%
Total FHLMC mortgage-backed securities		66,491		2		(2,228)		64,265	28.4%
FNMA certificates		43,888		--		(945)		42,943	19.0%
FNMA collateralized mortgage obligations		18,020		--		(875)		17,145	7.6%
Total FNMA mortgage-backed securities		61,908		--		(1,820)		60,088	26.6%
Other collateralized mortgage obligations		26,679		--		(865)		25,814	11.4%
Equity securities:									
FHLMC stock		1,022		1,539		(25)		2,536	1.1%
FNMA stock		1,003		69		--		1,072	0.5%
Other		60		42		--		102	0.0%
	$	230,189	$	1,800	$	(5,836)	$	226,153	100.0%

Proceeds from sales of securities during the year ended December 31, 2006 were $3,065,000. Gross gains of $65,000 and no gross losses were realized on those sales.

At December 31, 2007 and 2006, the Company's investment portfolio did not contain any securities of an issuer (other than the U.S. Government, its agencies and U.S. Government sponsored entities) which had an aggregate book value in excess of 10% of the Company's stockholders' equity at those dates.

The amortized cost and estimated fair value of securities at fair value at December 31, 2007 and securities available for sale at December 31, 2006, by contractual maturity, are shown below (in thousands). Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	Securities at Fair Value December 31, 2007		Securities Available For Sale December 31, 2006	
	Amortized Cost	Estimated Fair value	Amortized Cost	Estimated Fair value
Due in one year or less	$ 1,641	$ 1,648	$ 7,305	$ 7,266
Due after one year through five years	34,880	35,105	25,661	25,186
Due after five years through ten years	12,627	12,597	5,559	5,391
Due after ten years through twenty years	38,025	37,687	75,349	73,125
Due after twenty years	110,177	108,101	114,230	111,475
	197,350	195,138	228,104	222,443
Equity securities	6,929	7,725	2,085	3,710
	$ 204,279	$ 202,863	$ 230,189	$ 226,153

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Note 8: SECURITIES HELD TO MATURITY

The amortized cost and estimated fair value of securities held to maturity are summarized as follows (dollars in thousands):

	December 31, 2007								
	Percent of total		Amortized cost		Gross unrealized gains		Gross unrealized losses		Estimated fair value
Municipal bonds:									
Taxable	4.8%	$	2,565	$	35	$	--	$	2,600
Tax Exempt	79.8%		42,701		528		(27)		43,202
	84.6%		45,266		563		(27)		45,802
Corporate bonds	15.4%		8,250		669		--		8,919
	100.0%	$	53,516	$	1,232	$	(27)	$	54,721

	December 31, 2006								
	Percent of total		Amortized cost		Gross unrealized gains		Gross unrealized losses		Estimated fair value
Municipal bonds:									
Taxable	0.2%	$	99	$	1	$	--	$	100
Tax Exempt	83.1%		39,773		377		(86)		40,064
	83.3%		39,872		378		(86)		40,164
Corporate bonds	16.7%		8,000		844		--		8,844
Corporate bonds									
	100.0%	$	47,872	$	1,222	$	(86)	$	49,008

At December 31, 2007, an aging of unrealized losses and fair value of related held-to-maturity securities were as follows (in thousands):

	December 31, 2007											
	Less than 12 months				12 months or more				Total			
		Fair Value		Unrealized Losses		Fair Value		Unrealized Losses		Fair Value		Unrealized Losses
Municipal bonds	$	--	$	--	$	11,007	$	(27)	$	11,007	$	(27)

Management does not believe that any individual unrealized loss as of December 31, 2007 represents an other-than-temporary impairment. The decline in fair market value of these securities is generally due to changes in interest rates and changes in market-desired spreads subsequent to their purchase. There were 12 and 28 held-to-maturity securities with unrealized losses at December 31, 2007 and 2006, respectively.

The amortized cost and estimated fair value of securities held to maturity at December 31, 2007 and 2006, by contractual maturity, are shown below (in thousands). Expected maturities will differ from contractual maturities because borrowers may have the right to prepay obligations with or without call or prepayment penalties.

	December 31, 2007		December 31, 2006	
	Amortized cost	Estimated fair value	Amortized cost	Estimated fair value
Due in one year or less	$ 507	$ 505	$ --	$ --
Due after one year through five years	9,012	9,139	4,055	4,081
Due after five years through ten years	12,717	12,857	12,235	12,259
Due after ten years through twenty years	14,844	15,015	15,830	15,977
Due after twenty years	16,436	17,205	15,752	16,691
	$ 53,516	$ 54,721	$ 47,872	$ 49,008

Note 9: FAIR VALUE ACCOUNTING AND MEASUREMENT

The Company elected early adoption of SFAS No. 159, The Fair Value Option for Financial Assets and Financial Liabilities, and SFAS No. 157, Fair Value Measurements, effective January 1, 2007. SFAS No. 159, which was issued in February 2007, generally permits the measurement of selected eligible financial instruments at fair value (FV) at specified election dates. Upon adoption of SFAS No. 159, the Company selected fair value measurement for all of our "available for sale" investment securities, FHLB advances and junior subordinated debentures, which had fair values of approximately $226.2 million, $176.8 million and $124.4 million, respectively, on January 1, 2007. The initial fair value measurement of these instruments resulted in a $3.5 million adjustment for the cumulative effect, net of tax, as a result of the change in accounting, which was recorded as a reduction in retained earnings as of January 1, 2007, and which under SFAS No. 159 has not been recognized in current earnings. While the adjustment to retained earnings is permanent, approximately $2.6 million of the amount was previously reported as accumulated other comprehensive loss at December 31, 2006, so the reduction in the January 1, 2007 opening stockholders' equity was $897,000 when SFAS No. 159 was adopted.

The following table details the financial instruments carried at fair value to the dates indicated (in thousands):

Cumulative Adjustment on Adoption of SFAS 159								
	January 1, 2007					December 31, 2007		
	Amortized Cost	Fair Market Valuation Adjustment	Fair Value	Related Taxes	Cumulative Effect of Adoption	Amortized Cost	Fair Market Valuation Adjustment	Fair Value
Assets:								
Securities available for sale reclassified to fair value	$ 230,189	$ (4,036)	$ 226,153	$ 1,413	$ (2,623)	$ 204,279	$ (1,416)	$ 202,863
Liabilities:								
Advances from FHLB	$ 177,430	$ (678)	$ 176,752	$ 244	$ 434	$ 167,073	$ (28)	$ 167,045
Junior subordinated debentures, net of unamortized deferred origination costs	122,287	2,079	124,366	(748)	(1,331)	122,884	(9,614)	113,270
	$ 299,717	$ 1,401	$ 301,118	$ (504)	$ (897)	$ 289,957	$ (9,642)	$ 280,315
Total adjustment					$ (3,520)		$ (11,057)	
Less transfer from accumulated other comprehensive loss to retained					(2,623)			

earnings		
Cumulative reduction of opening stockholders' equity at January 1, 2007 upon adoption of SFAS No. 159	$	(897)

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Note 9: FAIR VALUE ACCOUNTING AND MEASUREMENT (continued)

SFAS No. 157 defines fair value, establishes a consistent framework for measuring fair value and expands disclosure requirements about fair value measurements. SFAS No. 157, among other things, requires the Company to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. Observable inputs reflect market data obtained from independent sources, while unobservable inputs reflect the Company's market assumptions. These two types of inputs create the following fair value hierarchy:

- Level 1 – Quoted prices for identical instruments in active markets
- Level 2 – Quoted prices for similar instruments in active markets; quoted prices for identical or similar instruments in markets that are not active; and model-derived valuations whose inputs are observable or whose significant value drivers are observable.
- Level 3 – Instruments whose significant value drivers are unobservable.

The Company holds fixed and variable rate interest bearing securities, investments in marketable equity securities and certain other financial instruments, which are carried at fair value. Fair value is determined based upon quoted prices when available or through the use of alternative approaches, such as matrix or model pricing, when market quotes are not readily accessible or available.

The Company also carries its FHLB advances and junior subordinated debentures at fair value. In determining the fair value of its obligations, various factors are considered including: price activity for equivalent or similar instruments, discounting the expected cash flows using market interest rates and its credit standing.

Fair values are determined as follows:

- Securities at fair value are priced using matrix pricing based on the securities' relationship to other benchmark quoted prices and under the provisions of SFAS No. 157 are considered a Level 2 input method.
- Advances from FHLB are priced using discounted cash flows to the date of maturity based on the FHLB of Seattle's current rate sheet for member bank advances on the date of valuation and is considered a Level 2 input method.
- Junior subordinated debentures are priced using discounted cash flows to maturity or the next available redemption date as appropriate on the date of valuation based on recent issuances or quotes from brokers for comparable bank holding companies and are considered a Level 2 input method.

The following table outlines the net change in fair values recorded at the dates indicated (in thousands):

	Years Ended December 31		
	2007	2006	2005
Assets:			
Securities available for sale reclassified as carried at fair value	$ 1,187	$ N/A	$ N/A
Liabilities			
Advances from FHLB	(651)	--	--
Junior subordinated debentures net of unamortized deferred issuance costs	11,038	--	--

Net change in fair value	$	11,574	$	N/A	$	N/A

The Company has elected to continue to recognize the interest income and dividends from the securities reclassified to fair value as a component of interest income as was done in prior years when they were classified as available for sale. Interest expense related to the FHLB advances and junior subordinated debentures continues to be measured based on contractual interest rate and reported in interest expense. The change in fair market value of these financial instruments has been recorded as a component of other operating income.

The significant changes in fair value during the period for junior subordinated debentures are not the result of any instrument-specific credit risk, but rather of market changes in the pricing of this type of debt. Increases in market rate spreads significantly above some of the Company's debt rate spreads contributed to the positive fair value adjustments. These same market rate increases also resulted in calculating the fair value adjustments out to maturity dates, instead of to call dates, on some debt.

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Note 10: ADDITIONAL INFORMATION REGARDING INTEREST INCOME FROM SECURITIES AND CASH EQUIVALENTS

The following table sets forth the composition of income from securities and cash equivalents for the periods indicated (in thousands):

	Years Ended December 31		
	2007	2006	2005
Taxable interest income	$ 5,903	$ 5,375	$ 9,244
Tax-exempt interest income	2,075	1,930	2,045
Other stock—dividend income	142	157	166
FHLB stock—dividend income (reversal)	222	36	(29)
Total income from securities and cash equivalents	$ 8,342	$ 7,498	$ 11,426

Note 11: LOANS RECEIVABLE

Loans receivable at December 31, 2007 and 2006 are summarized as follows (dollars in thousands) (includes loans held for sale):

	December 31, 2007		December 31, 2006	
	Amount	Percent	Amount	Percent
Loans:				
Commercial real estate	$ 882,523	23.2%	$ 596,488	20.1%
Multifamily real estate	165,886	4.4	147,311	5.0
Commercial construction	74,123	1.9	98,224	3.3
Multifamily construction	35,318	0.9	39,908	1.3
One- to four-family construction	613,779	16.1	570,501	19.2
Land and land development	497,962	13.1	402,665	13.6
Commercial business	696,350	18.3	467,745	15.8
Agricultural business, including secured by farmland	186,305	4.9	163,518	5.5
One- to four-family real estate	463,954	12.2	361,625	12.2
Consumer	93,183	2.4	50,826	1.7
Consumer secured by one- to four family	100,234	2.6	67,179	2.3
Total consumer	193,417	5.0	118,005	4.0
Total loans outstanding	3,809,617	100.0%	2,965,990	100.0%
Less allowance for loan losses	(45,827)		(35,535)	

Total net loans at end of period	$	3,763,790	$	2,930,455

Loan amounts are net of net unearned, unamortized loan fees of $6,917,000 and $9,507,000 at December 31, 2007 and 2006, respectively.

Loans receivable includes $315,000 and $593,000 of loans at December 31, 2007 and 2006, respectively, that were more than 90 days delinquent and still on accrual of interest.

Loans serviced for others totaled $361,519,000 and $361,126,000 at December 31, 2007 and 2006, respectively. Custodial accounts maintained in connection with this servicing totaled $3,077,000 and $3,427,000 at December 31, 2007 and 2006, respectively.

The Company's outstanding loan commitments totaled $1,134,457,000 and $1,072,983,000 at December 31, 2007 and 2006, respectively. In addition, the Company had outstanding commitments to sell loans of $20,645,000 and $22,292,000 at December 31, 2007 and 2006, respectively.

A substantial portion of the loans are to borrowers in the states of Washington, Oregon and Idaho. Accordingly, their ultimate collectibility is particularly susceptible to, among other things, changes in market and economic conditions within these states.

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The Company's loans by geographic concentration at December 31, 2007 were as follows (in thousands):

	Washington	Oregon	Idaho	Other	Total
Loans:					
Commercial real estate	$ 684,863	$ 119,259	$ 46,281	$ 32,120	$ 882,523
Multifamily real estate	127,664	11,419	4,762	22,041	165,886
Construction and land	575,571	504,125	140,276	1,210	1,221,182
Commercial business	519,556	82,873	80,001	13,920	696,350
Agricultural business, including secured by farmland	69,197	53,068	63,842	198	186,305
One-to four-family real estate	407,995	27,189	19,835	8,935	463,954
Consumer	65,102	21,252	4,069	2,760	93,183
Consumer secured by one- to four-family real estate	77,244	14,248	6,493	2,249	100,234
Total consumer	142,346	35,500	10,562	5,009	193,417
	$ 2,527,192	$ 833,433	$ 365,559	$ 83,433	$ 3,809,617
Percent of total loans	66.3%	21.9%	9.6%	2.2%	100.0%

The Company's loans to directors, executive officers and related entities are on substantially the same terms and underwriting as those prevailing at the time for comparable transactions with unrelated persons and do not involve more than normal risk of collectibility. Such loans had the following balances and activity during the years ended December 31, 2007 and 2006 (in thousands):

	Years Ended December 31	
	2007	2006
Balance at beginning of year	$ 6,884	$ 7,639
New loans or advances	10,613	10,522
Repayments and adjustments	(11,423)	(11,277)
Charge-offs	--	--
Net change due to addition/retirement of Directors/Officers	1,878	--
Balance, end of period	$ 7,952	$ 6,884

The amount of impaired loans and the related allocated reserve for loan losses were as follows (in thousands):

	December 31, 2007		December 31, 2006	
	Loan amount	Allocated reserves	Loan amount	Allocated reserves
Impaired loans:				
Non-accrual	$ 42,068	$ 3,189	$ 13,463	$ 2,650
Accrual	2,750	53	--	--
	$ 44,818	$ 3,242	$ 13,463	$ 2,650

As of December 31, 2007, the Company had additional commitments to advance funds up to an amount of $618,000 related to impaired loans.

The average balance of impaired loans and the related interest income recognized were as follows (in thousands):

	Years Ended December 31					
		2007		2006		2005
Average balance of impaired loans	$	22,663	$	10,546	$	14,033
Interest income recognized	$	28	$	--	$	--

For the years ended December 31, 2007, 2006 and 2005, additional interest income of $2,491,000, $1,287,000 and $1,125,000, respectively, would have been recorded had non-accrual loans been current.

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The Company originates both adjustable- and fixed-rate loans. At December 31, 2007 and 2006, the maturity and repricing composition of those loans, less undisbursed amounts and deferred fees, were as follows (in thousands):

	December 31	
	2007	2006
Fixed-rate (term to maturity):		
Due in one year or less	$ 158,536	$ 89,883
Due after one year through three years	181,459	123,263
Due after three years through five years	193,099	127,725
Due after five years through ten years	174,191	106,688
Due after ten years	351,413	301,784
	$ 1,058,698	$ 749,343
Adjustable-rate (term to rate adjustment):		
Due in one year or less	$ 1,947,094	$ 1,683,716
Due after one year through three years	421,184	271,401
Due after three years through five years	351,813	243,555
Due after five years through ten years	29,740	17,542
Due after ten years	1,088	433
	2,750,919	2,216,647
	$ 3,809,617	$ 2,965,990

The adjustable-rate loans have interest rate adjustment limitations and are generally indexed to various prime (The Wall Street Journal) or LIBOR rates, or One to Five Year Constant Maturity Treasury Indices. Future market factors may affect the correlation of the interest rate adjustment with the rates the Banks pay on the short-term deposits that primarily have been utilized to fund these loans.

Banner Bank has invested, as of December 31, 2007, $3,951,000 in four limited partnerships, Homestead Equity Fund (HEF), II, III IV and Homestead Western Communities Fund (HWCF) that develop low income housing projects. Banner Bank's partnership interests commit it to invest up to $11,000,000 in the partnerships. In connection with HEF II and HWCF project developments, the Bank also made commercial loans to the partnerships that have outstanding balances of $459,000 and $5,719,000 respectively at December 31, 2007. Banner Bank is committed on these loans to advance up to a combined amount of $14,445,000. The loans are secured by notes from the limited partners, which includes Banner Bank, to make capital contributions to the partnership.

Note 12: ALLOWANCE FOR LOAN LOSSES

An analysis of the changes in the allowance for loan losses is as follows (dollars in thousands):

	Years Ended December 31		
	2007	2006	2005
Balance, beginning of period	$ 35,535	$ 30,898	$ 29,610
Allowance added through business combinations	7,276		
Provision	5,900	5,500	4,903
Recoveries of loans previously charged off:			
Secured by real estate:			
One- to four-family	338	77	--
Commercial	--	75	187
Multifamily	--	--	6
Construction and land	62	507	259
Commercial business	678	1,112	713
Agricultural business	275	72	70
Consumer	138	55	91
	1,491	1,898	1,326
Loans charged off:			
Secured by real estate:			
One- to four-family	(385)	(62)	(135)
Commercial	--	--	(521)
Multifamily	--	--	(8)
Construction and land	(1,344)	--	(218)
Commercial business	(1,081)	(1,632)	(1,692)
Agricultural business	(650)	(759)	(1,886)
Consumer	(915)	(308)	(481)
	(4,375)	(2,761)	(4,941)
Net charge-offs	(2,884)	(863)	(3,615)
Balance, end of period	$ 45,827	$ 35,535	$ 30,898
Ratio of allowance to net loans before allowance for loan losses	1.20%	1.20%	1.27%
Ratio of net loan charge-offs to the average net book value of loans outstanding during the period	0.08%	0.03%	0.16%

The following is a schedule of the Company’s allocation of the allowance for loan losses (dollars in thousands):

	December 31		
	2007	2006	2005
Specific or allocated loss allowance:			
Secured by real estate:			
One- to four-family	$ 1,987	$ 1,420	$ 860

Commercial	3,771	5,129	4,566
Multifamily	934	886	839
Construction and land	7,569	11,717	7,223
Commercial business	19,026	10,513	9,741
Agricultural business	1,419	2,417	3,502
Consumer	3,468	903	561
Total allocated	38,174	32,985	27,292
Estimated allowance for undisbursed commitments	330	513	156
Unallocated	7,323	2,037	3,450
Total allowance for loan losses	$ 45,827	$ 35,535	$ 30,898
Ratio of allowance for loan losses to non-performing loans	108%	253%	296%

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Note 13: PROPERTY AND EQUIPMENT

Land, buildings and equipment owned by the Company and its subsidiaries at December 31, 2007 and 2006 are summarized as follows (in thousands):

	December 31			
		2007		2006
Buildings and leasehold improvements	$	77,481	$	47,412
Furniture and equipment		46,855		31,688
		124,336		79,100
Less accumulated depreciation		(44,764)		(29,474)
		79,572		49,626
Land		18,526		8,377
	$	98,098	$	58,003

The Banks' depreciation expense related to property and equipment was $8,233,000, $6,081,000 and $4,946,000 for the years ended December 31, 2007, 2006 and 2005, respectively.

The Banks' rental expense was $5,834,000, $4,644,000, and $4,057,000 for the years ended December 31, 2007, 2006 and 2005, respectively.

The Banks' obligation under long-term property leases over the next five years is as follows: 2008, $6,358,000; 2009, $5,536,000; 2010, $4,337,000; 2011, $4,114,000; 2012, $3,971,000; and thereafter, $18,365,000.

At December 31, 2007, the Banks had entered into various contractual obligations, generally related to the construction or remodel of various premises. Total commitments related to those contractual obligations were $2.4 million, with $1.9 million remaining unpaid against those commitments at December 31, 2007.

Note 14: DEPOSITS

Deposits consist of the following at December 31, 2007 and 2006 (dollars in thousands):

		December 31 2007	Percent of Total		December 31 2006	Percent of Total
Demand, NOW and money market accounts, including non-interest-bearing deposits at December 31, 2007 and 2006 of $484,251 and $332,372, respectively, 0% to 5.26%	$	1,163,290	32.2%	$	873,161	31.2%
Regular savings, 0% to 6.50%		609,073	16.8		364,957	13.1
Certificate accounts:						
0.00% to 2.00%		3,887	0.1		33	--
2.01% to 4.00%		197,832	5.4		144,439	5.2

4.01% to 6.00%		1,644,006	45.4		1,405,363	50.3
6.01% to 8.01% for 2007; to 7.79% for 2006		2,505	0.1		6,639	0.2
		1,848,230	51.0		1,556,474	55.7
	$	3,620,593	100.0%	$	2,794,592	100.0%

Deposits at December 31, 2007 and 2006 included public funds of $338,132,000 and $257,369,000, respectively. Securities with a carrying value of $42,462,000 and $33,348,000 were pledged as collateral on these deposits at December 31, 2007 and 2006, respectively, which exceeded the minimum collateral requirements established by state regulations.

Deposits at December 31, 2007 and 2006 included deposits from the Company's directors, executive officers and related entities totaling $8,065,000 and $6,155,000, respectively.

Scheduled maturities of certificate accounts at December 31, 2007 and 2006 are as follows (in thousands):

	December 31	
	2007	2006
Due in one year or less	$ 1,610,247	$ 1,351,922
Due after one year through two years	153,704	109,890
Due after two years through three years	34,147	42,416
Due after three years through four years	24,285	16,406
Due after four years through five years	18,058	23,294
Due after five years	7,789	12,546
	$ 1,848,230	$ 1,556,474

Included in deposits are certificate accounts in excess of $100,000 of $1,078,056,000 and $895,215,000 at December 31, 2007 and 2006, respectively. Interest on deposit accounts in excess of $100,000 totaled $49,269,000 for the year ended December 31, 2007 and $39,352,000 for the year ended December 31, 2006.

The following table sets forth the deposit activities of the Banks for the periods indicated (in thousands):

	Years Ended December 31		
	2007	2006	2005
Beginning balance	$ 2,794,592	$ 2,323,313	$ 1,925,909
Acquisitions	559,842	--	--
Net increase before interest credited	136,739	381,292	345,151
Interest credited	129,420	89,987	52,253
Net increase in deposits	826,001	471,279	397,404
Ending balance	$ 3,620,593	$ 2,794,592	$ 2,323,313

Deposit interest expense by type for the years ended December 31, 2007, 2006 and 2005 was as follows (in thousands):

	Years Ended December 31		
	2007	2006	2005
Certificates	$ 87,709	$ 62,314	$ 37,137
Demand, NOW and money market accounts	20,263	18,485	11,642
Regular savings	21,448	9,188	3,474
	$ 129,420	$ 89,987	$ 52,253

Note 15: ADVANCES FROM FEDERAL HOME LOAN BANK OF SEATTLE

The Banks have entered into borrowing arrangements with the FHLB of Seattle to borrow funds under a short-term floating rate cash management advance program and fixed-term loan agreements. All borrowings are secured by

stock of, and cash held by, the FHLB of Seattle. Additionally, specific securities with a recorded fair value of $5,815,000 at December 31, 2007 are pledged as security for the loans along with a blanket pledge of qualifying loans receivable. At December 31, 2007, FHLB advances were scheduled to mature as follows (dollars in thousands):

	Adjustable-rate advances			Fixed-rate advances			Total advances		
	Rate*		Amount	Rate*		Amount	Rate*		Amount
Due in one year or less	4.35%	$	128,835	3.24%	$	17,000	4.22%	$	145,835
Due after one year through two years	--		--	4.03		18,000	4.03		18,000
Due after two years through three years				4.03		3,000	4.03		3,000
Due after five years				5.94		238	5.94		238
Total FHLB advances, at par	4.35%	$	128,835	3.69%	$	38,238	4.20%	$	167,073
Fair value adjustment									(28)
Total FHLB advances, carried at fair value								$	167,045

- Weighted average interest rate

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The maximum, average outstanding and year-end balances and average interest rates on advances from the FHLB were as follows for the years ended December 31, 2007, 2006 and 2005 (dollars in thousands):

	Years Ended December 31					
		2007		2006		2005
Maximum outstanding at any month end	$	209,172	$	388,930	$	594,958
Average outstanding		87,957		295,228		522,624
Year-end outstanding		167,045		177,430		265,030
Weighted average interest rates:						
Annual		4.74%		4.86%		4.19%
End of period		4.20%		5.01%		4.13%
Interest expense during the period	$	4,168	$	14,354	$	21,906

As of December 31, 2007, Banner Bank and Islanders Bank have each established a borrowing line with the FHLB to borrow up to the lesser of 35% of their total assets or adjusted qualifying collateral. This would provide a maximum total credit line of $781,384,000 and $22,581,000 for Banner Bank and Islanders Bank, respectively, at December 31, 2007.

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Note 16: OTHER BORROWINGS

Other borrowings consist of retail repurchase agreements, wholesale repurchase agreements and other short-term borrowings.

Retail Repurchase Agreements and Other Short-term Borrowings: At December 31, 2007, retail repurchase agreements carry interest rates ranging from 2.23% to 5.00%, payable at maturity, and are secured by the pledge of certain mortgage-backed and agency securities with a carrying value of $96,218,000. The Bank has the right to pledge or sell these securities, but they must replace them with substantially the same security.

A summary of retail repurchase agreements at December 31, 2007 and 2006 by the period remaining to maturity is as follows (dollars in thousands):

	December 31					
	2007			2006		
	Weighted average rate		Balance	Weighted average rate		Balance
Retail repurchase agreements:						
Due in one year or less	3.33%	$	91,296	3.66%	$	76,397
Due after one year through two years	--		--	--		--
Due after five years	5.00		428	5.00		428
	3.34%	$	91,724	3.67%	$	76,825
Other short-term borrowings:						
Due in one year or less	--%	$	--	--%	$	--
Total retail repurchase agreements and other	3.34 %	$	91,724	3.67 %	$	76,825

short-term borrowings

The maximum, average outstanding and year-end balances and average interest rates on retail repurchase agreements and other short-term borrowings, such as Fed Funds, were as follows for the years ended December 31, 2007, 2006 and 2005, respectively (dollars in thousands):

	Years Ended December 31		
	2007	2006	2005
Maximum outstanding at any month end	$ 91,724	$ 92,853	$ 78,166
Average outstanding	73,646	72,475	44,142
Year-end outstanding	91,724	76,825	78,166
Weighted average interest rates:			
Annual	3.64%	3.58%	2.20%
End of period	3.35%	3.67%	5.30%
Interest expense during the period	$ 2,690	$ 2,594	$ 971

Wholesale Repurchase Agreements: The table below outlines the wholesale repurchase agreements as of December 31, 2007 and 2006. The broker holds the security while the Bank continues to receive the principal and interest payments from the security. Upon maturity of the agreement, the pledged securities will be returned to the Bank.

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A summary of wholesale repurchase agreements at December 31, 2007 and 2006 by the period remaining to maturity is as follows (dollars in thousands):

	December 31					
	2007			2006		
	Weighted average rate		Balance	Weighted average rate		Balance
Wholesale repurchase agreements:						
Due in one year or less	--%	$	--	5.38%	$	26,359

The maximum, average outstanding and year-end balances and average interest rates on wholesale repurchase agreements were as follows for the years ended December 31, 2007, 2006 and 2005 (dollars in thousands):

	Years Ended December 31					
		2007		2006		2005
Maximum outstanding at any month end	$	25,921	$	27,699	$	28,669
Average outstanding		8,794		22,138		24,197
Year-end outstanding		--		26,359		18,683
Weighted average interest rates:						
Annual		5.96%		5.19%		3.28%
End of period		--%		5.38%		4.36%
Interest expense during the period	$	524	$	1,150	$	794

Junior Subordinated Debentures and Mandatorily Redeemable Trust Preferred Securities: At December 31, 2007, six wholly-owned subsidiary grantor trusts, Banner Capital Trust, II, III, IV, V, VI and VII (BCT, II, III, IV, V, VI and VII), established by the Company had issued $120 million of pooled trust preferred securities as well as $3.7 million of common capital securities which were issued to the Company. Trust preferred securities and common capital securities accrue and pay distributions periodically at specified annual rates as provided in the indentures. The trusts used the net proceeds from the offerings to purchase a like amount of junior subordinated debentures (the “Debentures”) of the Company. The Debentures are the sole assets of the trusts. The Company’s obligations under the debentures and related documents, taken together, constitute a full and unconditional guarantee by the Company of the obligations of the trusts. The trust preferred securities are mandatorily redeemable upon the maturity of the Debentures, or upon earlier redemption as provided in the indentures. The Company has the right to redeem the Debentures in whole on or after specific dates, at a redemption price specified in the indentures plus any accrued but unpaid interest to the redemption date.

BCT II, the second issue, for $15 million, has a current interest rate of 8.59%, which is reset quarterly to equal three-month LIBOR plus 3.35%. BCT III, the third issue, also for $15 million, has a current interest rate 8.14%, which is reset quarterly to equal three-month LIBOR plus 2.90%. BCT IV, the fourth issue, also for $15 million has a current interest rate of 8.09% which is reset quarterly to equal three-month LIBOR plus 2.85%.
BCT V, the fifth issue, for $25 million has a current interest rate of 6.59% which is reset quarterly to equal three-month LIBOR plus 1.57%.
BCT VI, the sixth issue, for $25 million has a current interest rate of 6.56% which is fixed until December 15, 2011, then is reset quarterly to equal three-month LIBOR plus 1.62%.

BCT VII, the seventh issue, for $25 million has a current interest rate of 6.61% which is reset quarterly to equal three-month LIBOR plus 1.38%

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The following tables are a summary of trust preferred securities at December 31, 2007 and 2006 (dollars in thousands):

December 31, 2007							
Name of Trust	Aggregate Liquidation Amount of Trust Preferred Securities	Aggregate Liquidation Amount of Common Capital Securities	Aggregate Principal Amount of Junior Subordinated Debentures	Stated Maturity	Per Annum Interest Rate	Interest Deferral Period	Redemption Option
Banner Capital Trust II	$ 15,000	$ 464	$ 15,464	2033	8.59%	20 Consecutive Quarters	On or after April 7, 2008
Banner Capital Trust III	15,000	465	15,465	2033	8.14	20 Consecutive Quarters	On or after October 8, 2008
Banner Capital Trust IV	15,000	465	15,465	2034	8.09	20 Consecutive Quarters	On or after April 7, 2009
Banner Capital Trust V	25,000	774	25,774	2035	6.59	20 Consecutive Quarters	On or after November 23, 2010
Banner Capital Trust VI	25,000	774	25,774	2037	6.56	20 Consecutive Quarters	On or after March 1, 2012
Banner Capital Trust VII	25,000	774	25,774	2037	6.61	20 Consecutive Quarters	On or after July 31, 2012
Total TPS liability at par	$ 120,000	$ 3,716	$ 123,716		7.22 %		
Fair value adjustment			(10,446)				
Total TPS liability at fair value			$ 113,270				

December 31, 2006							
Name of Trust	Aggregate Liquidation Amount of Trust Preferred Securities	Aggregate Liquidation Amount of Common Capital Securities	Aggregate Principal Amount of Junior Subordinated Debentures	Stated Maturity	Per Annum Interest Rate	Interest Deferral Period	Redemption Option
Banner Capital Trust I	$ 25,000	$ 774	$ 25,774	2032	9.09%	Ten Consecutive Annual	On or after April 22, 2007

						Periods	
Banner Capital Trust II	15,000	464	15,464	2033	8.72	20 Consecutive Quarters	On or after January 7, 2008
Banner Capital Trust III	15,000	465	15,465	2033	8.27	20 Consecutive Quarters	On or after October 8, 2008
Banner Capital Trust IV	15,000	465	15,465	2034	8.22	20 Consecutive Quarters	On or after April 7, 2009
Banner Capital Trust V	25,000	774	25,774	2035	6.94	20 Consecutive Quarters	On or after November 23, 2010
Banner Capital Trust VI	25,000	774	25,774	2037	6.56	20 Consecutive Quarters	On or after March 1, 2012
Total TPS liability	$ 120,000	$ 3,716	$ 123,716		7.86%		

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Note 17: INCOME TAXES

Effective January 1, 2007, the Company adopted Financial Accounting Standards Board (FASB) Interpretation No. 48, Accounting for Uncertainties in Income Taxes, an Interpretation of FASB Statement No. 109 (FIN 48). Adoption of this standard did not have a significant impact on the Company's financial position or results of operations. FIN 48 prescribes a recognition threshold and measurement process for financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return, and also provides guidance on the derecognition of previously recorded benefits and their classification, as well as the proper recording of interest and penalties, accounting in interim periods, disclosures and transition. As of the January 1, 2007 date of adoption of FIN 48 and as of December 31, 2007, the Company had an insignificant amount of unrecognized tax benefits or uncertain positions, none of which would affect the effective tax rate if recognized. The Company does not anticipate that the amount of unrecognized tax benefits will significantly increase or decrease in the next twelve months. The Company's policy is to recognize interest and penalties on unrecognized tax benefits in the "Provision for Income Taxes" in the Consolidated Statements of Income. The amount of interest and penalties accrued for the year ended December 31, 2007 was immaterial. The Company and its wholly-owned subsidiaries file consolidated U.S. federal and state (Idaho and Oregon) income tax returns. The tax years which remain subject to examination by the taxing authorities are the years ending December 31, 2004, 2005 and 2006.

Provisions of the Small Business Job Protection Act of 1996 (the Job Protection Act) significantly altered the Company's tax bad debt deduction method and the circumstances that would require a tax bad debt reserve recapture. Prior to enactment of the Job Protection Act, savings institutions were permitted to compute their tax bad debt deduction through use of either the reserve method or the percentage of taxable income method. Banner Bank was a savings institution until October 30, 2000. The Job Protection Act repealed both of these methods for large savings institutions and allows bad debt deductions based only on actual current losses. While repealing the reserve method for computing tax bad debt deductions, the Job Protection Act allows savings institutions to retain their existing base year bad debt reserves but requires that reserves in excess of the balance at December 31, 1987, be recaptured into taxable income over six years. The reserve in excess of the base year (December 31, 1987) had been fully recaptured into taxable income as of December 31, 2003.

The base year reserve is recaptured into taxable income only in limited situations, such as in the event of certain excess distributions, complete liquidation or disqualification as a bank. None of the limited circumstances requiring recapture are contemplated by the Company. The amount of the Company's tax bad debt reserves subject to recapture in these circumstances approximates $5,318,000 at December 31, 2007. Due to the remote nature of events that may trigger the recapture provisions, no tax liability has been established in the accompanying Consolidated Financial Statements.

In addition, as a result of certain acquisitions, the Company is required to recapture certain tax bad debt reserves of the acquired institution. The Company has elected to recapture these reserves into income over a four-year period using the deferral method. The recapture does not result in a charge to earnings as the Company provided for this liability on the acquisition date.

The provision for income taxes for the years ended December 31, 2007, 2006, and 2005 differs from that computed at the statutory corporate tax rate as follows (in thousands):

	Years Ended December 31		
	2007	2006	2005
		Restated	Restated

Taxes at statutory rate	$	19,185	$	16,660	$	5,907
Increase (decrease) in taxes:						
Tax-exempt interest		(751)		(647)		(667)
Investment in life insurance		(672)		(542)		(525)
ESOP market value adjustment		--		619		464
State income taxes net of federal tax benefit		740		587		98
Tax credits		(841)		(841)		(509)
Other		229		219		128
Provision for income taxes	$	17,890	$	16,055	$	4,896

The provision for income tax expense for the years ended December 31, 2007, 2006 and 2005 is composed of the following (in thousands):

				Years Ended December 31		
		2007		2006		2005
				Restated		Restated
Current	$	14,769	$	15,900	$	5,594
Deferred		3,121		155		(698)
	$	17,890	$	16,055	$	4,896

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Income taxes are provided for the temporary differences between the tax basis and financial statement carrying amounts of assets and liabilities. Components of the Company's net deferred tax assets (liabilities) at December 31, 2007 and 2006 consisted of the following (in thousands):

	December 31			
		2007		2006
Deferred tax assets:				
Loan loss reserves, book vs. tax	$	16,649	$	13,028
Deferred compensation		5,922		3,715
Book vs. tax amortization of intangibles		12		260
Book vs. tax amortization of loan and deposit acquisition premiums		367		115
Other		75		530
		23,025		17,648
Deferred tax liabilities:				
FHLB stock dividends		6,230		6,013
Depreciation		4,748		1,905
Deferred loan fees, servicing rights and loan origination costs		3,947		3,610
Book vs. tax amortization of intangibles		5,896		--
Book vs. tax accounting for investments and financial instruments accounted for under SFAS No. 159		4,799		--
		25,620		11,528
		(2,595)		6,120
Income tax benefit related to unrealized loss on securities available for sale		--		1,413
Deferred tax asset (liability), net	$	(2,595)	$	7,533

Management has evaluated the weight of available evidence and concluded that it is more likely than not that the Company will realize the deferred tax assets and no valuation is considered necessary.

Note 18: EMPLOYEE BENEFIT PLANS

Employee Retirement Plans—Substantially all of the Company's employees are eligible to participate in its 401(k)/Profit Sharing Plan, a defined contribution and profit sharing plan sponsored by the Company. Employees may elect to have a portion of their salary contributed to the plan in conformity with Section 401(k) of the Internal Revenue Code. At the discretion of the Company's Board of Directors, the Company may elect to make matching and/or profit sharing contributions for the employees' benefit. The Company's contributions under the plan charged to expense amounted to $1,864,000, $1,112,000 and $1,013,000 for the years ended December 31, 2007, 2006 and 2005, respectively.

Supplemental Retirement and Salary Continuation Plans—Through the Banks, the Company is obligated under various non-qualified deferred compensation plans to help supplement the retirement income of certain executives, including certain retired executives, selected by resolution of the Banks' Boards of Directors or in certain cases by the former directors of acquired banks. These plans are unfunded, include both defined benefit and defined contribution plans, and provide for payments after the executive's retirement. In the event of a participant employee's death prior to or during retirement, the Bank is obligated to pay to the designated beneficiary the benefits set forth under the plan. For

the years ended December 31, 2007, 2006, and 2005, expense recorded for supplemental retirement and salary continuation plan benefits totaled $868,000, $503,000 and $953,000, respectively. At December 31, 2007 and 2006, liabilities recorded for the various supplemental retirement and salary continuation plan benefits totaled $6,156,000 and $3,975,000, respectively, and are recorded in other liabilities.

Deferred Compensation Plans and Rabbi Trusts—The Company and the Banks also offer non-qualified deferred compensation plans to members of their Boards of Directors and certain employees. The plans permit each participant to defer a portion of director fees, non-qualified retirement contributions, salary or bonuses for future receipt. Compensation is charged to expense in the period earned. In connection with its acquisitions, the Company also assumed liability for certain deferred compensation plans for key employees, retired employees and directors.

In order to fund the plans' future obligations, the Company has purchased life insurance or other investments, including Banner Corporation common stock, which in certain instances are held in irrevocable trusts commonly referred to as "Rabbi Trusts." As the Company is the owner of the investments and the beneficiary of the insurance policies, and in order to reflect the Company's policy to pay benefits equal to the accumulations, the assets and liabilities are reflected in the Consolidated Statements of Financial Condition. Banner Corporation common stock held for such plans is reported as a contra-equity account and was recorded at an original cost of $7,847,000 at December 31, 2007 and $6,973,000 at December 31, 2006. At December 31, 2007 and 2006, liabilities recorded in connection with deferred compensation plan benefits totaled $13,087,000 ($7,847,000 in contra-equity) and $8,682,000 ($6,973,000 in contra-equity), respectively, and are recorded in other liabilities or equity as appropriate.

The Banks have purchased, or acquired through mergers, life insurance policies in connection with the implementation of certain executive supplemental retirement, salary continuation and deferred compensation retirement plans, as well as additional policies not related to any specific plan. These policies provide protection against the adverse financial effects that could result from the death of a key employee and provide tax-exempt income to offset expenses associated with the plans. It is the Banks' intent to hold these policies as a long-term investment. However, there will be an income tax impact if the Banks choose to surrender certain policies. Although the lives of individual current or former management-level employees are insured, the Banks are the owners and sole or partial beneficiaries. At December 31, 2007 and 2006, the cash surrender value of these policies was $51,483,000 and $38,527,000, respectively. The Banks are exposed to credit risk to the extent an insurance company is unable to fulfill its financial obligations under a policy. In order to mitigate this risk, the Banks use a variety of insurance companies and regularly monitor their financial condition.

Note 19: EMPLOYEE STOCK OWNERSHIP PLAN AND TRUST

The Company established for eligible employees an ESOP and related trust that became effective upon the former mutual holding company's conversion to a stock-based holding company. Eligible employees of the Bank as of January 1, 1995 and eligible employees of the Bank or Company employed after such date who have been credited with at least 1,000 hours during a twelve-month period are participants.

The ESOP borrowed $8,728,500 from the Company in order to purchase the common stock. The loan is repaid principally from the Company's contributions to the ESOP over a period not to exceed 25 years, and the collateral for the loan is the unreleased, restricted common stock purchased by the ESOP. Contributions to the ESOP are discretionary; however, the Company intends to make annual contributions to the ESOP in an aggregate amount at least equal to the principal and interest requirements of the debt. The interest rate for the loan is 8.75%. Shares are released to participants for allocation based on the cumulative debt service paid to the Company by the ESOP divided by cumulative debt service paid to date plus the scheduled debt service remaining. Dividends on allocated shares are distributed to the participants as additional earnings. Dividends on unallocated shares are used to reduce the Company's contribution to the ESOP.

Participants generally become 100% vested in their ESOP account after seven years of credited service or if their service was terminated due to death, early retirement, permanent disability or a change in control of the Company. Prior to the completion of one year of credited service, a participant who terminates employment for reasons other than death, retirement, disability or change in control of the Company will not receive any benefit. Forfeitures will be reallocated among remaining participating employees in the same proportion as contributions. Benefits are payable upon death, retirement, early retirement, disability or separation from service. The contributions to the ESOP are not fixed, so benefits payable under the ESOP cannot be estimated. ESOP compensation expense for the years ended December 31, 2007, 2006 and 2005 was $1,821,000, $2,235,000 and $2,245,000, respectively.

A summary of key transactions for the ESOP follows:

	Years Ended December 31		
	2007	2006	2005
ESOP contribution expense	$ 1,821,000	$ 2,235,000	$ 2,245,000
Total contribution to ESOP/Debt service	--	779,600	945,700
Interest portion of debt service	--	262,500	315,900
Dividends on unallocated ESOP shares used to reduce ESOP contribution	182,490	217,300	254,700

For the 2007 year the ESOP trustees have elected to use the 2007 contribution to purchase shares on the open market. As of December 31, 2007, the Company has 240,381 unearned, restricted shares remaining to be released to the ESOP. The fair value of unearned, restricted shares held by the ESOP trust was $6,906,146 at December 31, 2007. The ESOP held 654,559 allocated, earned shares at December 31, 2007.

Note 20: STOCK-BASED COMPENSATION PLANS AND STOCK OPTIONS

The Company operates the following stock-based compensation plans as approved by the shareholders: the 1996 Management Recognition and Development Plan (MRP), a restricted stock plan; and the 1996 Stock Option Plan, the 1998 Stock Option Plan and the 2001 Stock Option Plan (collectively, SOPs). In addition, during 2007 the Board of Directors approved the Banner Corporation Long-Term Incentive Plan.

MRP Stock Grants: Under the MRP, the Company was authorized to grant up to 528,075 shares of restricted stock to its directors, officers and employees. On July 26, 2006, this stock program expired with 522,660 shares having been granted and no additional shares eligible to be granted. Shares granted under the MRP vest ratably over a five-year period from the date of grant. The Consolidated Statements of Income for the years ended December 31, 2007, 2006 and 2005 reflect accruals of $159,000, $186,000 and $184,000, respectively, for these grant awards. The MRP stock grants' fair value equals their intrinsic value on the date of grant.

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A summary of the Company's unvested MRP shares activity during the years ended December 31, 2005, 2006 and 2007 follows:

	Shares		Weighted-Average Grant-Date Fair Value
Unvested at December 31, 2004	33,461	$	21.20
Granted	3,025		25.25
Vested	(8,406)		20.65
Forfeited	--		--
Unvested at December 31, 2005	28,080	$	21.80

	Shares		Weighted-Average Grant-Date Fair Value
Unvested at December 31, 2005	28,080	$	21.80
Granted	--		--
Vested	(8,720)		21.21
Forfeited	--		--
Unvested at December 31, 2006	19,360	$	22.07

	Shares		Weighted-Average Grant-Date Fair Value
Unvested at December 31, 2006	19,360	$	22.07
Granted	--		--
Vested	(8,620)		21.08
Forfeited	(700)		(24.92)
Unvested at December 31, 2007	10,040	$	22.73

Stock Options: Under the SOPs, we reserved 2,284,186 shares for issuance pursuant to the exercise of stock options to be granted to directors and employees. Authority to grant additional options under the 1996 Stock Option Plan terminated on July 26, 2006 with 6,613 stock options remaining ungranted at the time of termination. As of December 31, 2007, there were 4,047 options eligible for grants under the 1998 and 2001 plans. The exercise price of the stock options is set at 100% of the fair market value of the stock price on the date of grant. Such options have graded vesting of 20% per year from the date of grant and any unexercised incentive stock options will expire ten years after date of grant or 90 days after employment or service ends.

During the year ended December 31, 2007, the Company awarded 52,500 stock options. The Company did not grant any stock options during the year ended December 31, 2006. Also, there were no significant modifications made to any stock option grants during the period. The fair values of stock options granted are amortized as compensation expense on a straight-line basis over the vesting period of the grant.

Stock-based compensation costs related to the SOPs were $369,000 and $553,000 for the years ended December 31, 2007 and 2006, respectively. The SOPs' stock option grant compensation costs are generally based on the fair value calculated from the Black-Scholes option pricing on the date of the grant award. Assumptions used in the Black-Scholes model are an expected volatility based on the historical volatility at the date of the grant. The expected term is based on the remaining contractual life of the vesting period. The Company bases the estimate of risk-free interest rate on the U.S. Treasury Constant Maturities Indices in effect at the time of the grant. The dividend yield is

based on the current quarterly dividend in effect at the time of the grant.

	Years Ended December 31		
	2007	2006	2005
Annual dividend yield	2.46%	N/A	2.31 to 2.69%
Expected volatility	24.0 to 28.8%	N/A	29.2 to 31.2%
Risk free interest rate	4.64 to 4.82%	N/A	3.73 to 4.28%
Expected lives	5 to 9yrs	N/A	5 to 9yrs

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As part of the provisions of SFAS No 123(R), the Company is required to estimate potential forfeitures of stock grants and adjust compensation cost recorded accordingly. The estimate of forfeitures will be adjusted over the requisite service period to the extent that actual forfeitures differ, or are expected to differ, from such estimates. Changes in estimated forfeitures will be recognized through a cumulative catch-up adjustment in the period of change and will also impact the amount of stock compensation expense to be recognized in future periods.

A summary of the Company's SOPs' stock compensation activity for the years ended December 31, 2005, 2006 and 2007 follows (dollars in thousands, except shares and per share data):

	Shares		Weighted-Average Exercise Price	Weighted-Average Remaining Contractual Term, In Years		Aggregate Intrinsic Value
Outstanding at December 31, 2004	1,352,187	$	17.78			
Granted	30,150		26.37			
Exercised	(329,084)		13.48		$	5,108
Forfeited	(29,580)		18.84			
Outstanding at December 31, 2005	1,023,673	$	19.38	4.2	$	12,100
Outstanding at December 31, 2005	1,023,673	$	19.38			
Granted	--					
Exercised	(294,773)		15.15		$	6,345
Forfeited	(15,440)		23.97			
Outstanding at December 31, 2006	713,460	$	20.49	5.5	$	17,013
Outstanding at December 31, 2006	713,460	$	20.49			
Granted	52,500		30.88			
Exercised	(93,285)		18.39		$	1,741
Forfeited	(4,085)		26.96			
Outstanding at December 31, 2007	668,590	$	21.56	5.1	$	4,791
Vested at December 31, 2007 and expected to vest	662,885	$	21.52	5.1	$	4,779
Exercisable at December 31, 2007	505,650	$	19.74	4.3	$	4,545

The intrinsic value of stock options is calculated as the amount by which the market price of our common stock exceeds the exercise price of the option.

A summary of the Company's unvested stock option activity with respect to the years ended December 31, 2005, 2006 and 2007 follows:

	Shares		Weighted-Average Grant-Date Fair Value
Unvested at December 31, 2004	474,017		
Granted	30,150	$	7.65

Vested	(144,812)		
Forfeited	(18,700)		
Unvested at December 31, 2005	340,655		
Unvested at December 31, 2005	340,655	$	7.71
Granted	--		--
Vested	(118,095)		7.98
Forfeited	(10,750)		7.57
Unvested at December 31, 2006	211,810	$	7.57
Unvested at December 31, 2006	211,810	$	7.57
Granted	52,500		8.62
Vested	(98,270)		7.73
Forfeited	(3,100)		7.63
Unvested at December 31, 2007	162,940	$	7.81

The Company awarded 52,500 stock options during the year ended December 31, 2007.

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The Company had $313,000 of total unrecognized compensation costs related to stock options at December 31, 2007 that are expected to be recognized over a remaining period of 4.50 years.

During the year ended December 31, 2007, $1.7 million was received from the exercise of stock options. Cash was not used to settle any equity instruments previously granted. The Company issues shares from authorized but unissued shares upon the exercise of stock options. The Company does not currently expect to repurchase shares from any source to satisfy such obligations under the SOPs.

The following are the stock-based compensation costs recognized in the Company's condensed consolidated statements of income (in thousands):

	Years Ended December 31		
	2007	2006	2005
Salary and employee benefits	$ 528	$ 738	$ 184
Total decrease in income before provision for income taxes	528	738	184
Decrease in provision for income taxes	(111)	(107)	(66)
Decrease in net income	$ 417	$ 631	$ 118

Financial data pertaining to outstanding stock options granted or assumed as a result of certain acquisitions at December 31, 2007 were as follows:

Exercise Price	Weighted average exercise price of option shares granted	Number of option shares granted	Weighted average option shares vested and exercisable	Weighted average exercise price of option shares exercisable	Remaining contractual life
13.09 to 13.95	$ 13.39	86,046	86,046	$ 13.39	2.5 yrs
15.67 to 15.96	15.72	131,650	103,820	15.72	5.3 yrs
16.43 to 17.84	16.65	80,525	79,825	16.64	3.5 yrs
18.09 to 19.82	19.24	41,292	39,692	19.27	4.6 yrs
20.02 to 21.48	21.09	24,270	22,970	21.07	2.8 yrs
22.05 to 23.25	22.18	66,707	66,707	22.18	3.0 yrs
25.25 to 25.28	25.25	21,650	10,060	25.25	7.1 yrs
26.23 to 27.80	26.33	51,800	30,880	26.32	6.3 yrs
29.47	29.47	8,000	3,200	29.47	7.1 yrs
30.88 to 31.71	31.43	156,650	62,450	31.71	7.8 yrs
	$ 21.56	668,590	505,650	$ 19.74	

Banner Corporation Long-Term Incentive Plan: In June 2006, the Board of Directors adopted the Banner Corporation Long-Term Incentive Plan effective July 1, 2006. The Plan is an account-based type of benefit, the value of which is directly related to changes in the value of Company stock, dividends declared on the Company stock and changes in Banner Bank's average earnings rate and under SFAS 123(R) is considered a stock appreciation right ("SAR"). Each SAR entitles the holder to receive cash, upon vesting, equal to the excess of the fair market value of a share of the Company's common stock on the date of exercise over the fair market value of such share on the date granted plus the

dividends declared on the stock from the date of grant to the date of vesting. Vesting is upon the completion of 60 months of continuous service from the date of grant; provided, that at that time the SAR holder directly owns (other than through a qualified plan) Banner Corporation Stock equal in value to at least 50 percent of his or her base salary. The primary objective of the Plan is for executives who remain with the Company or the Bank for a sufficient period of time to share in the increases in the value of Company stock. Detailed information with respect to the plan was disclosed on a Form 8-K filed with SEC on July 19, 2006. SFAS 123(R) requires the Company to remeasure the fair value of SARs each reporting period until the award is settled. In addition, compensation expense must be recognized each reporting period for changes in fair value and vesting. The Company recognized compensation expense of $97,000 and $151,000, respectively, for the years ended December 31, 2007 and 2006 related to the increase in the fair value of SARs and additional vesting during the period.

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Note 21: REGULATORY CAPITAL REQUIREMENTS

The Company is a bank holding company registered with the Federal Reserve. Bank holding companies are subject to capital adequacy requirements of the Federal Reserve under the Bank Holding Company Act of 1956, as amended (BHCA), and the regulations of the Federal Reserve. Banner Bank is a state-chartered federally insured institution subject to the capital requirements established by the FDIC.

The capital adequacy requirements are quantitative measures established by regulation that require the Company and the Banks to maintain minimum amounts and ratios of capital. The Federal Reserve requires the Company to maintain capital adequacy that generally parallels the FDIC requirements. The FDIC requires the Bank to maintain minimum ratios of total capital and Tier 1 capital to risk-weighted assets as well as Tier 1 leverage capital to average assets.

The Federal Deposit Insurance Corporation Improvement Act of 1991 (FDICIA) created a statutory framework that increased the importance of meeting applicable capital requirements. For the Banks, FDICIA established five capital categories: well-capitalized, adequately capitalized, undercapitalized, significantly undercapitalized and critically undercapitalized. An institution's category depends upon where its capital levels are in relation to relevant capital measures, which include a risk-based capital measure, a leverage ratio capital measure, and certain other factors. The federal banking agencies (including the FDIC) have adopted regulations that implement this statutory framework. Under these regulations, an institution is treated as well-capitalized if its ratio of total capital to risk-weighted assets is 10.00% or more, its ratio of core capital to risk-weighted assets is 6.00% or more, its ratio of core capital to adjusted total assets is 5.00% or more and it is not subject to any federal supervisory order or directive to meet a specific capital level. In order to be adequately capitalized, an institution must have a total risk-based capital ratio of not less than 8.00%, a Tier 1 risk-based capital ratio of not less than 4.00%, and leverage ratio of not less than 4.00%. Any institution which is neither well-capitalized nor adequately capitalized will be considered undercapitalized.

Undercapitalized institutions are subject to certain prompt corrective action requirements, regulatory controls and restrictions which become more extensive as an institution becomes more severely undercapitalized. Failure by the Banks to comply with applicable capital requirements would, if unremedied, result in restrictions on its activities and lead to enforcement actions against it by the FDIC, including, but not limited to, the issuance of a capital directive to ensure the maintenance of required capital levels. FDICIA requires the federal banking regulators to take prompt corrective action with respect to depository institutions that do not meet minimum capital requirements. Additionally, FDIC approval of any regulatory application filed for its review may be dependent on compliance with capital requirements.

FDIC regulations recognize two types or tiers of capital: core (Tier 1) capital and supplementary (Tier 2) capital. Tier 1 capital generally includes common stockholders' equity and noncumulative perpetual preferred stock, less most intangible assets. Tier 2 capital, which is limited to 100% of Tier 1 capital, includes such items as qualifying general loan loss reserves, cumulative perpetual preferred stock, mandatory convertible debt, term subordinated debt and limited life preferred stock; however, the amount of term subordinated debt and intermediate term preferred stock (original maturity of at least five years but less than 20 years) that may in included in Tier 2 capital is limited to 50% of Tier 1 capital.

The FDIC currently measures an institution's capital using a leverage limit together with certain risk-based ratios. The FDIC's minimum leverage capital requirement specifies a minimum ratio of Tier 1 capital to average total assets. Most banks are required to maintain a minimum leverage ratio of at least 4% to 5% of total assets. The FDIC retains the right to require a particular institution to maintain a higher capital level based on an institution's particular risk profile.

FDIC regulations also establish a measure of capital adequacy based on ratios of qualifying capital to risk-weighted assets. Assets are placed in one of four categories and given a percentage weight—0%, 20%, 50% or 100%—based on the relative risk of the category. In addition, certain off-balance-sheet items are converted to balance-sheet credit equivalent amounts, and each amount is then assigned to one of the four categories. Under the guidelines, the ratio of total capital (Tier 1 capital plus Tier 2 capital) to risk-weighted assets must be at least 8%, and the ratio of Tier 1 capital to risk-weighted assets must be at least 4%. In evaluating the adequacy of a bank's capital, the FDIC may also consider other factors that may affect the bank's financial condition. Such factors may include interest rate risk exposure, liquidity, funding and market risks, the quality and level of earnings, concentration of credit risk, risks arising from nontraditional activities, loan and investment quality, the effectiveness of loan and investment policies, and management's ability to monitor and control financial operating risks.

FDIC capital requirements are designated as the minimum acceptable standards for banks whose overall financial condition is fundamentally sound, which are well-managed and have no material or significant financial weaknesses. The FDIC capital regulations state that, where the FDIC determines that the financial history or condition, including off-balance-sheet risk, managerial resources and/or the future earnings prospects of a bank are not adequate and/or a bank has a significant volume of assets classified substandard, doubtful or loss or otherwise criticized, the FDIC may determine that the minimum adequate amount of capital for the bank is greater than the minimum standards established in the regulation.

The Company may not declare or pay cash dividends on, or repurchase, any of its shares of common stock if the effect thereof would cause equity to be reduced below applicable regulatory capital maintenance requirements or if such declaration and payment would otherwise violate regulatory requirements.

The following table shows the regulatory capital ratios of the Company and the Banks and the minimum regulatory requirements:

	Actual		Minimum for capital adequacy purposes		Minimum to be categorized as "well-capitalized" under prompt corrective action provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
(dollars in thousands)						
December 31, 2007:						
The Company—consolidated						
Total capital to risk-weighted assets	$ 471,864	11.72	$ 332,219	8.00	N/A	N/A
Tier 1 capital to risk-weighted assets	426,037	10.58	161,109	4.00	N/A	N/A
Tier 1 leverage capital to average assets	426,037	10.04	169,701	4.00	N/A	N/A
Banner Bank						
Total capital to risk-weighted assets	406,775	10.44	313,397	8.00	$ 389,633	10.00
Tier 1 capital to risk-weighted assets	362,298	9.30	155,856	4.00	235,788	6.00
Tier 1 leverage capital to average assets	362,298	8.87	163,369	4.00	204,212	5.00
Islanders Bank						
Total capital to risk-weighted assets	17,889	13.59	10,528	8.00	13,160	10.00
Tier 1 capital to risk-weighted assets	16,540	12.57	5,264	4.00	7,896	6.00
Tier 1 leverage capital to average assets	16,540	11.01	6,008	4.00	7,510	5.00
December 31, 2006:						
The Company—consolidated						
Total capital to risk-weighted assets	$ 372,790	11.80%	$ 252,644	8.00%	N/A	N/A
Tier 1 capital to risk-weighted assets	300,884	9.53	126,322	4.00	N/A	N/A
Tier 1 leverage capital to average assets	300,884	8.76	137,444	4.00	N/A	N/A

Banner Bank							
Total capital to risk-weighted assets	338,211	10.73	252,087	8.00	$	315,108	10.00%
Tier 1 capital to risk-weighted assets	301,945	9.58	126,043	4.00		189,065	6.00
Tier 1 leverage capital to average assets	301,945	8.80	137,198	4.00		171,498	5.00

Company management believes that under the current regulations as of December 31, 2007, the Company and the Banks individually met all capital adequacy requirements to which they were subject. Further, there have been no conditions or events since that date that have materially adversely changed the Tier 1 or Tier 2 capital of the Company or the Banks. However, events beyond the control of the Banks, such as weak or depressed economic conditions in areas where the Banks have most of their loans, could adversely affect future earnings and, consequently, the ability of the Banks to meet their respective capital requirements.

Note 22: CONTINGENCIES

In the normal course of business, the Company and/or its subsidiaries have various legal proceedings and other contingent matters outstanding. These proceedings and the associated legal claims are often contested and the outcome of individual matters is not always predictable. These claims and counter-claims typically arise during the course of collection efforts on problem loans or with respect to action to enforce liens on properties in which the Banks hold a security interest. Based upon the information known to management at this time, the Company and the Banks are not a party to any legal proceedings that management believes would have a material adverse effect on the results of operations or consolidated financial position at December 31, 2007.

In connection with certain asset sales, the Banks typically make representations and warranties about the underlying assets conforming to specified guidelines. If the underlying assets do not conform to the specifications, the Bank may have an obligation to repurchase the assets or indemnify the purchaser against any loss. The Banks believe that the potential for loss under these arrangements is remote. Accordingly, the fair value of such obligations is not material.

Note 23: INTEREST RATE RISK

The financial condition and operation of the Company are influenced significantly by general economic conditions, including the absolute level of interest rates as well as changes in interest rates and the slope of the yield curve. The Company's profitability is dependent to a large extent on its net interest income, which is the difference between the interest received from its interest-earning assets and the interest expense incurred on its interest-bearing liabilities.

The activities of the Company, like all financial institutions, inherently involve the assumption of interest rate risk. Interest rate risk is the risk that changes in market interest rates will have an adverse effect on the institution's earnings and underlying economic value. Interest rate risk is determined by the maturity and repricing characteristics of an institution's assets, liabilities and off-balance-sheet contracts. Interest rate risk is measured by the variability of financial performance and economic value resulting from changes in interest rates. Interest rate risk is the primary market risk impacting the Company's financial performance.

The greatest source of interest rate risk to the Company results from the mismatch of maturities or repricing intervals for rate-sensitive assets, liabilities and off-balance-sheet contracts. Additional interest rate risk results from mismatched repricing indices and formulae (basis risk and yield curve risk), product caps and floors, and early repayment or withdrawal provisions (option risk), which may be contractual or market driven, that are generally more favorable to customers than to the Company.

The Company's primary monitoring tool for assessing interest rate risk is "asset/liability simulation modeling," which is designed to capture the dynamics of balance sheet, interest rate and spread movements, and to quantify variations in net interest income and net market value resulting from those movements under different rate environments. Another monitoring tool used by the Company to assess interest rate risk is "gap analysis." The matching of repricing characteristics of assets and liabilities may be analyzed by examining the extent to which such assets and liabilities are "interest sensitive" and by monitoring the Company's interest sensitivity "gap." Management is aware of the sources of interest rate risk and in its opinion actively monitors and manages it to the extent possible, and considers that the Company's current level of interest rate risk is reasonable.

Note 24: GOODWILL AND INTANGIBLES

The Company accounts for intangible assets in accordance with SFAS No. 142, Goodwill and Other Intangible Assets. Goodwill is no longer amortized but is reviewed annually for impairment. Other intangible assets are amortized over their useful lives. The following table provides the gross carrying value and accumulated amortization for intangible assets as of December 31, 2007 and 2006 (in thousands):

Goodwill and intangibles consisted of the following (in thousands):

	December 31			
		2007		2006
Costs in excess of net assets acquired (goodwill) net of accumulated amortization of $12,594,000	$	121,108	$	36,229
Refundable membership(s)		--		39
Core deposit intangible, net of accumulated amortization of $2.6 million and $714,000, respectively		16,529		--
Internet domain name, net of accumulated amortization of $8,000 and $6,000, respectively		17		19
	$	137,654	$	36,287

Intangible Assets: The gross carrying amount and accumulated amortization of the Company's intangible assets other than goodwill is as follows (in thousands):

	December 31, 2007					
		Gross Carrying Amount		Accumulated Amortization		Net Carrying Amount
Core Deposit Intangible (CDI)	$	19,124	$	(2,595)	$	16,529
Mortgage Servicing Rights (MSR)*		3,854		(1,047)		2,807
Internet Domain Name		25		(8)		17
	$	23,003	$	(3,650)	$	19,353

	December 31, 2006					
		Gross Carrying Amount		Accumulated Amortization		Net Carrying Amount
Core Deposit Intangible (CDI)	$	714	$	(714)	$	--
Mortgage Servicing Rights (MSR)*		3,513		(829)		2,684
Refundable membership(s)		39		--		39
Internet Domain Name		25		(6)		19
	$	4,291	$	(1,549)	$	2,742

*Amortization of mortgage servicing rights is recorded as a reduction of loan servicing income. Mortgage servicing rights are recorded on an individual basis with the gross carrying amount and accumulated amortization fully written off if the loan repays in full.

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Amortization expense for the years ended December 31, 2007, 2006 and 2005 includes $1,881,000, $31,000 and $87,000, respectively, of expense related to the CDI amortization and $758,000, $518,000 and $507,000, respectively, of expense related to the MSR amortization. MSRs capitalized/recognized for the years ended December 31, 2007, 2006 and 2005 were $781,000, $1,643,000 and $502,000, respectively.

Estimated amortization expense in future years with respect to existing intangibles (in thousands):

Year Ended	CDI	MSR	Internet Domain Name	TOTAL
December 31, 2008	$ 2,828	$ 553	$ 2	$ 3,383
December 31, 2009	2,644	460	2	3,106
December 31, 2010	2,459	383	2	2,844
December 31, 2011	2,276	318	2	2,596
December 31, 2012	2,092	264	2	2,358
Thereafter	4,230	829	7	14,287
Net Carrying Amount	$ 16,529	$ 2,807	$ 17	$ 19,353

Note 25: FAIR VALUE OF FINANCIAL INSTRUMENTS

The following disclosure of the estimated fair value of financial instruments is made in accordance with the requirements of SFAS No. 107, Disclosures About Fair Value of Financial Instruments. The estimated fair value amounts have been determined by the Company using available market information and appropriate valuation methodologies. However, considerable judgment is necessary to interpret market data in the development of the estimates of fair value. Accordingly, the estimates presented herein are not necessarily indicative of the amounts the Company could realize in a current market exchange. The use of different market assumptions and/or estimation methodologies may have a material effect on the estimated fair value amounts. The estimated fair value of financial instruments is as follows (in thousands):

	Years Ended December 31			
	2007		2006	
	Carrying value	Estimated fair value	Carrying value	Estimated fair value
Assets:				
Cash and due from banks	$ 98,430	$ 98,430	$ 73,385	$ 73,385
Securities at fair value	202,863	202,863	--	--
Securities available for sale	--	--	226,153	226,153
Securities held to maturity	53,516	54,721	47,872	49,008
Loans receivable held for sale	4,596	4,680	5,080	5,136
Loans receivable	3,759,194	3,773,061	2,925,375	2,915,784
FHLB stock	37,371	37,371	35,844	35,844
Mortgage servicing rights	2,807	3,182	2,684	2,937
Liabilities:				
Demand, NOW and money market accounts	1,163,290	1,091,176	873,161	818,022
Regular savings	609,073	597,800	364,957	352,953

Certificates of deposit	1,848,230	1,864,191	1,556,474	1,554,839
FHLB advances	--	--	177,430	176,825
FHLB advances at fair value	167,045	167,045	--	--
Junior subordinated debentures	--	--	123,716	125,118
Junior subordinated debentures at fair value	113,270	113,270	--	--
Other borrowings	91,724	91,586	103,184	103,098
Off-balance-sheet financial instruments:				
Commitments to originate loans	(8)	(8)	(35)	(35)
Commitments to sell loans	8	8	35	35
Commitments to purchase securities	--	--	--	--
Interest rate swaps	1,214	1,214	--	--

Fair value estimates, methods and assumptions are set forth below for the Company’s financial and off-balance-sheet instruments:

Cash and due from banks: The carrying amount of these items is a reasonable estimate of their fair value.

Securities: The estimated fair values of investment securities and mortgaged-backed securities at fair value, available for sale and held to maturity are priced using matrix pricing based on the securities’ relationship to other benchmark quoted prices.

Loans Receivable: Fair values are estimated first by stratifying the portfolios of loans with similar financial characteristics. Loans are segregated by type such as multifamily real estate, residential mortgage, nonresidential mortgage, commercial/agricultural, consumer and other. Each loan category is further segmented into fixed- and adjustable-rate interest terms and by performing and non-performing categories. For performing loans held in portfolio, the fair value is based on discounted cash flows using as a discount rate the current rate offered on similar products.

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The fair value of performing residential mortgages held for sale is estimated based upon secondary market sources by type of loan and terms such as fixed or variable interest rates.

Fair value for significant non-performing loans is based on recent appraisals or estimated cash flows discounted using rates commensurate with risk associated with the estimated cash flows. Assumptions regarding credit risk, cash flows and discount rates are judgmentally determined using available market information and specific borrower information.

FHLB Stock: The fair value is based upon the redemption value of the stock which equates to its carrying value.

Mortgage Servicing Rights: Fair values are estimated based on current pricing for sales of servicing for new loans adjusted up or down based on the serviced loan's interest rate vs. current loan sales of servicing.

Deposit Liabilities: The fair value of deposits with no stated maturity, such as savings, checking and NOW accounts, is estimated by applying decay rate assumptions to segregated portfolios a similar deposit types to generate cash flows with are then discounted using short-term market interest rates. The market value of certificates of deposit is based upon the discounted value of contractual cash flows. The discount rate is determined using the rates currently offered on comparable instruments.

FHLB Advances and Other Borrowings: Advances from FHLB are priced using discounted cash flows to the date of maturity based on the FHLB of Seattle's current rate sheet for member bank advances on the date of valuation.

Junior Subordinated Debentures: Fair values are estimated using discounted cash flows to maturity or the next available redemption date as appropriate on the date of valuation based on recent issuances or quotes from brokers for comparable bank holding companies.

Commitments: Commitments to sell loans with notional balances of $20,645,000 and $22,292,000 at December 31, 2007 and 2006, respectively, have a carrying value of $8,000 and $35,000, representing the fair value of such commitments. Interest rate lock commitments to originate loans held for sale with notional balances of $20,645,000 and $22,292,000 at December 31, 2007 and 2006, respectively, have a carrying value of ($8,000) and ($35,000). Other commitments to fund loans totaled $1,113,883,000 and $1,050,691,000 at December 31, 2007 and 2006, respectively, and have a carrying value of $0 at both dates, representing the cost of such commitments. There are no commitments to purchase securities at December 31, 2007 or 2006. There were no commitments to sell securities at December 31, 2007 or 2006.

Interest Rate Swaps: Interest rate swaps with notional balances of $20,438,000 and $0 at December 31, 2007 and 2006, respectively, have a carrying value of $1,214,000 and $0, respectively. The fair value of the derivative instrument is estimated using quoted or published market prices for similar instruments.

Limitations: The fair value estimates presented herein are based on pertinent information available to management as of December 31, 2007. Although management is not aware of any factors that would significantly affect the estimated fair value amounts, such amounts have not been comprehensively revalued for purposes of these financial statements since that date and, therefore, current estimates of fair value may differ significantly from the amounts presented herein.

Fair value estimates are based on existing on- and off-balance-sheet financial instruments without attempting to estimate the value of anticipated future business. The fair value has not been estimated for assets and liabilities that are not considered financial instruments. Significant assets and liabilities that are not financial instruments include the deferred tax assets/liabilities; land, buildings and equipment; costs in excess of net assets acquired; and real estate held

for sale.

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Note 26: BANNER CORPORATION
(PARENT COMPANY ONLY)

Summary financial information is as follows (in thousands):

Statements of Financial Condition
December 31, 2007 and 2006

	December 31	
	2007	2006
ASSETS		Restated
Cash	$ 35,329	$ 29,137
Investment in trust equities	3,716	3,716
Investment in subsidiaries	512,673	334,853
Deferred tax asset	1,247	597
Other assets	6,376	10,142
	$ 559,341	$ 378,445
LIABILITIES AND STOCKHOLDERS' EQUITY		
Liabilities	$ 8,225	$ 4,122
Junior subordinated debentures	--	123,716
Junior subordinated debentures at fair value	113,270	--
Stockholders' equity	437,846	250,607
	$ 559,341	$ 378,445

Statements of Income
For the years ended December 31, 2007, 2006 and 2005

		Years Ended December 31	
	2007	2006	2005
INTEREST INCOME:		Restated	Restated
Certificates, time deposits and dividends	$ 1,135	$ 728	$ 525
OTHER INCOME (EXPENSE):			
Dividend income from subsidiaries	17,686	18,778	10,667
Equity in undistributed income of subsidiaries	18,662	18,525	5,576
Other Income	30	268	187
Net change in valuation of financial instruments carried at fair value	11,038	--	--
Interest on other borrowings	(8,887)	(8,029)	(5,453)
Other expense	(2,239)	(2,013)	(1,886)
	37,425	28,257	9,616
BENEFIT FROM INCOME TAXES	(502)	(3,287)	(2,364)
NET INCOME	$ 36,923	$ 31,544	$ 11,980

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Explanation of Responses:

Statements of Cash Flows
For the years ended December 31, 2007, 2006 and 2005

	Years Ended December 31		
	2007	2006	2005
OPERATING ACTIVITIES:		Restated	Restated
Net income	$ 36,923	$ 31,544	$ 11,980
Adjustments to reconcile net income to net cash provided by operating activities:			
Equity in undistributed earnings of subsidiaries	(18,662)	(18,525)	(5,576)
Amortization	57	171	141
(Increase) decrease in deferred taxes	99	(160)	(62)
Tax benefits realized from equity-based compensation	(58)	(1,882)	(860)
Net change in valuation of financial instruments carried at fair value	(11,078)	--	--
(Increase) decrease in other assets	2,386	(3,682)	3,883
Increase (decrease) in other liabilities	3,333	880	668
Net cash provided (used) by operating activities	13,000	8,346	10,174
INVESTING ACTIVITIES:			
Funds transferred to deferred compensation trust	(209)	(174)	(166)
Payments received on loan to ESOP for release of shares	--	2,301	2,116
Additional funds invested in subsidiaries	(33,118)	(30,000)	(17,000)
Net cash provided (used) by investing activities	(33,327)	(27,873)	(15,050)
FINANCING ACTIVITIES:			
Proceeds from issuance of junior subordinated debentures	25,774	25,774	25,774
Investment in trust securities related to junior subordinated debentures	(774)	(774)	(774)
Repayment of trust securities related to junior subordinated debentures	(25,000)	--	--
Issuance of stock	37,460	122	--
Net proceeds from exercise of stock options	1,715	2,019	1,341
Repurchases of stock	(2,116)	--	--
Tax benefits realized from equity-based compensation	58	1,882	860
Cash dividends paid	(10,598)	(8,551)	(7,846)
Net cash provided (used) by financing activities	26,518	20,472	19,355
NET INCREASE (DECREASE) IN CASH	6,192	945	14,479
CASH, BEGINNING OF PERIOD	29,137	28,192	13,713
CASH, END OF PERIOD	$ 35,329	$ 29,137	$ 28,192

	Years Ended December 31		
	2007	2006	2005
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:			
Interest paid	$ 8,269	$ 7,650	$ 4,886
Taxes paid	21,643	10,142	9,356
Non-cash transactions:			
Net change in accrued dividends payable	924	188	142
Net change in unrealized gain (loss) in deferred compensation trust and related liability, including subsidiaries	713	479	473

Stock-based consideration issued for acquisitions	125,019	--	--
Adoption of SFAS Nos. 157 and 159:			
Securities available for sale transferred to fair value, held by subsidiary	226,153	--	--
FHLB advances adjustment to fair value, held by subsidiary	678	--	--
Junior subordinated debentures including unamortized origination costs adjustment to fair value	2,079	--	--
Deferred tax asset related to fair value adjustments	504	--	--

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Note 27: STOCK REPURCHASE

The Company has periodically engaged in stock repurchase activity. During the years ended December 31, 2007 and 2006, the Company repurchased 69,467 and 65,642 shares of its stock at average prices of $30.46 and $37.28 per share, respectively. In the current year, the Company purchased 57,800 shares of stock on the open market and also repurchased 11,667 shares in connection with the exercise of stock options or the forfeiture of stock grants. In 2006, all repurchases occurred in connection with the exercise of stock options. On July 26, 2007, the Company's Board of Directors authorized the repurchase of up to 750,000 shares of the Company's outstanding common stock over the ensuing twelve months.

Note 28: CALCULATION OF WEIGHTED AVERAGE SHARES OUTSTANDING USED TO CALCULATE EARNINGS PER SHARE (in thousands)

	Years Ended December 31		
	2007	2006	2005
Basic weighted average shares outstanding	14,581	11,906	11,558
Plus unvested MRP and stock option incremental shares considered outstanding for diluted EPS calculations	257	333	386
Diluted weighted average shares outstanding	14,838	12,239	11,944

Note 29: SELECTED QUARTERLY FINANCIAL DATA (UNAUDITED)

Results of operations on a quarterly basis were as follows (in thousands except for per share data):

	Year Ended December 31, 2007			
	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
Interest income	$ 65,446	$ 74,411	$ 79,210	$ 76,242
Interest expense	33,269	36,301	38,540	37,580
Net interest income before provision for loan losses	32,177	38,110	40,670	38,662
Provision for loan losses	1,000	1,400	1,500	2,000
Net interest income	31,177	36,710	39,170	36,662
Other operating income	6,334	4,986	10,534	16,729
Other operating expenses	26,071	31,299	34,846	35,273
Income before provision for income taxes	11,440	10,397	14,858	18,118
Provision for income taxes	3,627	3,286	4,871	6,106
Net income	$ 7,813	7,111	9,987	12,012
Basic earnings per share	$ 0.63	$ 0.49	$ 0.64	$ 0.75

Diluted earnings per share	$	0.62	$	0.48	$	0.64	$	0.74
Cumulative dividends declared	$	0.19	$	0.19	$	0.19	$	0.20

	Year Ended December 31, 2006 (Restated)							
		First Quarter		Second Quarter		Third Quarter		Fourth Quarter
Interest income	$	52,987	$	58,933	$	64,900	$	66,199
Interest expense		23,083		27,708		32,239		33,084
Net interest income before provision from loan losses		29,904		31,225		32,661		33,115
Provision for loan losses		1,200		2,300		1,000		1,000
Net interest income		28,704		28,925		31,661		32,115
Other operating income (loss)		4,502		5,000		5,436		5,637
Other operating expenses		23,198		20,011		25,336		25,836
Income before provision for income taxes		10,008		13,914		11,761		11,916
Provision (benefit) for income taxes		3,374		4,710		3,907		4,064
Net income (loss)	$	6,634	$	9,204	$	7,854	$	7,852
Basic earnings (loss) per share	$	0.56	$	0.77	$	0.66	$	0.65
Diluted earnings (loss) per share	$	0.55	$	0.75	$	0.64	$	0.64
Cumulative dividends declared	$	0.18	$	0.18	$	0.18	$	0.19

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Note 29: SELECTED QUARTERLY FINANCIAL DATA (UNAUDITED) (continued)

	Year Ended December 31, 2005 (Restated)			
	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
Interest income	$ 42,659	$ 46,371	$ 49,966	$ 51,164
Interest expense	17,430	19,658	21,883	22,406
Net interest income before provision for loan losses	25,229	26,713	28,083	28,758
Provision for loan losses	1,203	1,300	1,300	1,100
Net interest income	24,026	25,413	26,763	27,658
Other operating income	3,997	4,625	4,981	(3,059)
Other operating expenses	21,303	22,800	23,561	29,884
Income before provision for income taxes	6,720	7,238	8,203	(5,285)
Provision for income taxes	2,129	2,338	2,653	(2,224)
Net income	$ 4,591	$ 4,900	$ 5,550	$ (3,061)
Basic earnings per share	$ 0.40	$ 0.42	$ 0.48	$ (0.26)
Diluted earnings per share	$ 0.39	$ 0.41	$ 0.46	$ (0.25)
Cumulative dividends declared	$ 0.17	$ 0.17	$ 0.17	$ 0.18

Note 30: BUSINESS SEGMENTS

The Company is managed by legal entity and not by lines of business. Each of the Banks is a community oriented commercial bank chartered in the State of Washington. The Banks' primary business is that of a traditional banking institution, gathering deposits and originating loans for portfolio in its respective primary market areas. The Banks offer a wide variety of deposit products to its consumer and commercial customers. Lending activities include the origination of real estate, commercial/agriculture business and consumer loans. Banner Bank is also an active participant in the secondary market, originating residential loans for sale on both a servicing released and servicing retained basis. In addition to interest income on loans and investment securities, the Banks receive other income from deposit service charges, loan servicing fees and from the sale of loans and investments. The performance of the Banks is reviewed by the Company's executive management and Board of Directors on a monthly basis. All of the executive officers of the Company are members of Banner Bank's management team.

Generally accepted accounting principles establish standards to report information about operating segments in annual financial statements and require reporting of selected information about operating segments in interim reports to stockholders. The Company has determined that its current business and operations consist of a single business segment.

Note 31: FINANCIAL INSTRUMENTS WITH OFF-BALANCE-SHEET RISK

The Banks have financial instruments with off-balance-sheet risk in the normal course of business to meet the financing needs of their customers. These financial instruments include commitments to extend credit and standby letters of credit. Those instruments involve, to varying degrees, elements of credit and interest rate risk in excess of

the amount recognized in the Consolidated Statements of Financial Condition.

The Banks' exposure to credit loss in the event of nonperformance by the other party to the financial instrument from commitments to extend credit and standby letters of credit is represented by the contractual notional amount of those instruments. The Banks use the same credit policies in making commitments and conditional obligations as for on-balance sheet instruments. As of December 31, 2007, outstanding commitments for which no liability has been recorded consist of the following:

		Contract or Notional Amount (in thousands)
Financial instruments whose contract amounts represent credit risk:		
Commitments to extend credit		
Real estate secured for commercial, construction or land development	$	398,019
Revolving open-end lines secured by 1-4 family residential properties		90,822
Credit card lines		47,510
Other, primarily business and agricultural loans		561,270
Real estate secured by one- to four-family residential properties		20,645
Standby letters of credit and financial guarantees		16,212
Total	$	1,134,478
Commitments to sell loans secured by one- to four-family residential properties	$	20,645

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Commitments to extend credit are agreements to lend to a customer, as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Many of the commitments may expire without being drawn upon, therefore the total commitment amounts do not necessarily represent future cash requirements. Each customer's creditworthiness is evaluated on a case-by-case basis. The amount of collateral obtained, if deemed necessary upon extension of credit, is based on management's credit evaluation of the customer. Collateral held varies, but may include accounts receivable, inventory, property, plant and equipment, and income producing commercial properties.

Standby letters of credit are conditional commitments issued to guarantee a customer's performance or payment to a third party. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to customers.

Interest rates on residential one- to four-family mortgage loan applications are typically rate locked (committed) to customers during the application stage for periods ranging from 15 to 45 days, the most typical period being 30 days. Typically, pricing for the sale of these loans is locked with various qualified investors under a best-efforts delivery program at or near the time the interest rate is locked with the customer. The Banks make every effort to deliver these loans before their rate locks expire. This arrangement generally requires the Banks to deliver the loans prior to the expiration of the rate lock. Delays in funding the loans can require a lock extension. The cost of a lock extension at times is borne by the customer and at times by the Banks. These lock extension costs paid by the Banks are not expected to have a material impact to operations. This activity is managed daily. Changes in the value of rate lock commitments are recorded as assets and liabilities as explained in the Note 1: "Derivative Instruments."

NOTE 32: INTEREST RATE SWAPS

The Company has stand-alone derivative instruments in the form of interest rate swap agreements, which derive their value from underlying interest rates (see Note 1). These transactions involve both credit and market risk. The notional amount is the amount on which calculations, payments, and the value of the derivative are based. The notional amount does not represent direct credit exposure. Direct credit exposure is limited to the net difference between the calculated amount to be received and paid. This difference represents the fair value of the derivative instrument.

The Company is exposed to credit-related losses in the event of nonperformance by the counterparty to these agreements. Credit risk of the financial contract is controlled through the credit approval, limits, and monitoring procedures and we do not expect the counterparty to fail its obligations.

Information pertaining to outstanding interest rate swaps at December 31, 2007 and 2006 follows (dollars in thousands):

	December 31			
		2007		2006
Notional amount	$	20,438	$	N/A
Weighted average pay rate		5.54%		
Weighted average receive rate		5.13%		
Weighted average maturity in years		8.5		
Unrealized gain (loss) relating to interest rate swaps	$	1,214		

The net changes in fair value of the derivatives are recorded in loans and other liabilities.

All of the Company’s interest rate swap agreements are with the Pacific Coast Bankers Bank (PCBB) as the counterparty. The Company has swapped fixed-rate cash flows that it receives from its customers for variable-rate cash flows that it receives from PCBB.

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BANNER CORPORATION

Exhibit | Index of Exhibits

3{a} Articles of Incorporation of Registrant [incorporated by reference to Exhibit B to the Proxy Statement for the Annual Meeting of Stockholders dated June 10, 1998].

3{b} Bylaws of Registrant [incorporated by reference to Exhibit 3.2 filed with the Current Report on Form 8-K dated July 24, 1998 (File No. 0-26584)].

10{a} Employment Agreement with Gary L. Sirmon, dated as of January 1, 2004 [incorporated by reference to exhibits filed with the Annual Report on Form 10-K for the year ended December 31, 2003 (File No. 0-26584)].

10{b} Executive Salary Continuation Agreement with Gary L. Sirmon [incorporated by reference to exhibits filed with the Annual Report on Form 10-K for the year ended March 31, 1996 (File No. 0-26584)].

10{c} Employment Agreement with Michael K. Larsen [incorporated by reference to exhibits filed with the Annual Report on Form 10-K for the year ended March 31, 1996 (File No. 0-26584)].

10{d} Executive Salary Continuation Agreement with Michael K. Larsen [incorporated by reference to exhibits filed with the Annual Report on Form 10-K for the year ended March 31, 1996 (File No. 0-26584)].

10{e} 1996 Stock Option Plan [incorporated by reference to Exhibit 99.1 to the Registration Statement on Form S-8 dated August 26, 1996 (File No. 333-10819)].

10{f} 1996 Management Recognition and Development Plan [incorporated by reference to Exhibit 99.2 to the Registration Statement on Form S-8 dated August 26, 1996 (File No. 333-10819)].

10{g} Consultant Agreement with Jesse G. Foster, dated as of December 19, 2003. [incorporated by reference to exhibits filed with the Annual Report on Form 10-K for the year ended December 31, 2003 (File No. 0-23584)].

10{h} Supplemental Retirement Plan as Amended with Jesse G. Foster [incorporated by reference to exhibits filed with the Annual Report on Form 10-K for the year ended March 31, 1997 (File No. 0-26584)].

10{i} Towne Bank of Woodinville 1992 Stock Option Plan [incorporated by reference to exhibits filed with the Registration Statement on Form S-8 dated April 2, 1998 (File No. 333-49193)].

10{j} Whatcom State Bank 1991 Stock Option Plan [incorporated by reference to exhibits filed with the Registration Statement on Form S-8 dated February 2, 1999 (File No. 333-71625)].

10{k} Employment Agreement with Lloyd W. Baker [incorporated by reference to exhibits filed with the Annual Report on Form 10-K for the year ended December 31, 2001 (File No. 0-26584)].

10{l} Employment Agreement with D. Michael Jones [incorporated by reference to exhibits filed with the Annual Report on Form 10-K for the year ended December 31, 2001 (File No. 0-26584)].

10{m}

Supplemental Executive Retirement Program Agreement with D. Michael Jones [incorporated by reference to exhibits filed with the Annual Report on Form 10-K for the year ended December 31, 2003 (File No. 0-26584)].

10{n} Form of Supplemental Executive Retirement Program Agreement with Gary Sirmon, Michael K. Larsen, Lloyd W. Baker and Cynthia D. Purcell [incorporated by reference to exhibits filed with the Annual Report on Form 10-K for the year ended December 31, 2001 (File No. 0-26584)].

10{o} 1998 Stock Option Plan [incorporated by reference to exhibits filed with the Registration Statement on Form S-8 dated February 2, 1999 (File No. 333-71625)].

10{p} 2001 Stock Option Plan [incorporated by reference to Exhibit 99.1 to the Registration Statement on Form S-8 dated August 8, 2001 (File No. 333-67168)].

10{q} Form of Employment Contract entered into with Cynthia D. Purcell, Richard B. Barton, Paul E. Folz, John R. Neill and Douglas M. Bennett [incorporated by reference to exhibits filed with the Annual Report on Form 10-K for the year ended December 31, 2003 (File No. 0-26584)].

10{r} 2004 Executive Officer and Director Stock Account Deferred Compensation Plan [incorporated by reference to exhibits filed with the Annual Report on Form 10-K for the year ended December 31, 2005 (File No. 0-26584)].

10{s} 2004 Executive Officer and Director Investment Account Deferred Compensation Plan [incorporated by reference to exhibits filed with the Annual Report on Form 10-K for the year ended December 31, 2005 (File No. 0-26584)].

10{t} Long-Term Incentive Plan. [Incorporated by reference to the exhibits filed with the Form 8-K on June 19, 2006]

14 Code of Ethics [incorporated by reference to exhibits filed with the Annual Report on Form 10-K for the year ended December 31, 2004 (File No. 0-26584)].

21 Subsidiaries of the Registrant.

23.1 Consent of Registered Independent Public Accounting Firm -- Moss Adams LLP.

31.1 Certification of Chief Executive Officer pursuant to the Securities Exchange Act Rules 13a-14(a) and 15d-14(a) as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

31.2 Certification of Chief Financial Officer pursuant to the Securities Exchange Act Rules 13a-14(a) and 15d-14(a) as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

32 Certificate of Chief Executive Officer and Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

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EXHIBIT 21

SUBSIDIARIES OF THE REGISTRANT

Parent		
Banner Corporation		
Subsidiaries	Percentage of Ownership	Jurisdiction of State of Incorporation
Banner Bank (1)	100%	Washington
Islanders Bank (1)	100%	Washington
Community Financial Corporation (2)	100%	Oregon
Northwest Financial Corporation (2)	100%	Washington

(1) Wholly owned by Banner Corporation
(2) Wholly owned by Banner Bank

EXHIBIT 23.1

CONSENT OF REGISTERED INDEPENDENT PUBLIC ACCOUNTING FIRM

We consent to the incorporation by reference in Registration Statement Nos. 333-10819, 333-49193, 333-71625, and 333-67168 of Banner Corporation and subsidiaries on Form S-8 and Registration Statement Nos. 333-139520, 333-138162 on Form S-3 of our report dated March 14, 2008, with respect to the consolidated statements of financial condition of Banner Corporation and subsidiaries as of December 31, 2007 and 2006, and the related consolidated statements of income, comprehensive income, changes in stockholders' equity, and cash flows for each of the years in the three-year period ended December 31, 2007 and the effectiveness of internal control over financial reporting as of December 31, 2007, which report appears in the December 31, 2007, annual report on Form 10-K of Banner Corporation.

/s/ Moss Adams LLP
Spokane, Washington
March 14, 2008

EXHIBIT 31.1

CERTIFICATION OF CHIEF EXECUTIVE OFFICER OF BANNER CORPORATION
PURSUANT TO RULES 13a-14(a) AND 15d-14(a) UNDER THE SECURITIES ACT OF 1934

I, D. Michael Jones, certify that:

1. I have reviewed this Annual Report on Form 10-K of Banner Corporation;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f) for the registrant and have:

    a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

    b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

    c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

    d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent functions):

a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

March 14, 2008

/s/D. Michael Jones
D. Michael Jones
Chief Executive Officer

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EXHIBIT 31.2

CERTIFICATION OF CHIEF FINANCIAL OFFICER OF BANNER CORPORATION
PURSUANT TO RULES 13a-14(a) AND 15d -14(a) UNDER THE SECURITIES ACT OF 1934

I, Lloyd W. Baker, certify that:

1. I have reviewed this Annual Report on Form 10-K of Banner Corporation;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f) for the registrant and have:

   a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

   c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5.

The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent functions):

a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

March 14, 2008

/s/Lloyd W. Baker
Lloyd W. Baker
Chief Financial Officer

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EXHIBIT 32

CERTIFICATION OF CHIEF EXECUTIVE OFFICER AND CHIEF FINANCIAL OFFICER
OF BANNER CORPORATION
PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

The undersigned hereby certifies in his capacity as an officer of Banner Corporation pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 and in connection with this Annual Report on Form 10-K, that:

- the report fully complies with the requirements of Sections 13(a) and 15(d) of the Securities Exchange Act of 1934, as amended, and

- the information contained in the report fairly presents, in all material respects, the Company’s financial condition and results of operations as of the dates and for the periods presented in the financial statements included in such report.

March 14, 2008

/s/D. Michael Jones
D. Michael Jones
Chief Executive Officer

March 14, 2008

/s/Lloyd W. Baker
Lloyd W. Baker
Chief Financial Officer

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Explanation of Responses: