

NORTHRIM BANCORP INC
Form 10-Q
August 10, 2015

UNITED STATES SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549
FORM 10-Q

(Mark One)

Quarterly report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the quarterly period ended June 30, 2015

Transition report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the transition period from _____ to _____

Commission File Number 000-33501

NORTHRIM BANCORP, INC.

(Exact name of registrant as specified in its charter)

Alaska

92-0175752

(State or other jurisdiction of incorporation or
organization)

(I.R.S. Employer Identification No.)

3111 C Street

Anchorage, Alaska 99503

(Address of principal executive offices) (Zip Code)

(907) 562-0062

(Registrant's telephone number, including area code)

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

Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes No

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

Large Accelerated Filer Accelerated Filer Non-accelerated Filer Smaller Reporting Company

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

Yes No

The number of shares of the issuer's Common Stock, par value \$1 per share, outstanding at August 10, 2015 was 6,854,413.

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PART I. FINANCIAL INFORMATION

These consolidated financial statements should be read in conjunction with the financial statements, accompanying notes and other relevant information included in Northrim BanCorp, Inc.'s Annual Report on Form 10-K for the year ended December 31, 2014.

ITEM 1. FINANCIAL STATEMENTS

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CONSOLIDATED FINANCIAL STATEMENTS

NORTHRIM BANCORP, INC.

Consolidated Balance Sheets

(Unaudited)

(In Thousands, Except Share Data)	June 30, 2015	December 31, 2014
ASSETS		
Cash and due from banks	\$44,017	\$36,036
Interest bearing deposits in other banks	60,054	36,020
Investment securities available for sale	225,868	281,730
Investment securities held to maturity	2,197	2,201
Total portfolio investments	228,065	283,931
Investment in Federal Home Loan Bank stock	1,817	3,404
Loans held for sale	73,593	43,866
Loans	974,849	924,504
Allowance for loan losses	(17,418)	(16,723)
Net loans	957,431	907,781
Purchased receivables, net	14,048	15,254
Accrued interest receivable	3,399	3,373
Other real estate owned, net	2,807	4,607
Premises and equipment, net	37,942	35,643
Goodwill	22,334	22,334
Other intangible assets, net	1,555	1,701
Other assets	53,269	55,399
Total assets	\$1,500,331	\$1,449,349
LIABILITIES		
Deposits:		
Demand	\$455,358	\$403,523
Interest-bearing demand	173,952	185,114
Savings	129,938	122,588
Alaska CDs	97,592	99,736
Money market	232,877	226,574
Certificates of deposit less than \$100,000	57,390	58,249
Certificates of deposit greater than \$100,000	91,610	83,963
Total deposits	1,238,717	1,179,747
Securities sold under repurchase agreements	17,895	19,843
Borrowings	22,309	26,304
Junior subordinated debentures	18,558	18,558
Other liabilities	31,770	40,456
Total liabilities	1,329,249	1,284,908
SHAREHOLDERS' EQUITY		
Preferred stock, \$1 par value, 2,500,000 shares authorized, none issued or outstanding	—	—
Common stock, \$1 par value, 10,000,000 shares authorized, 6,854,413 and 6,854,189 shares issued and outstanding at June 30, 2015 and December 31, 2014, respectively	6,854	6,854
Additional paid-in capital	61,965	61,729

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Retained earnings	101,343	95,493
Accumulated other comprehensive income	643	247
Total Northrim BanCorp shareholders' equity	170,805	164,323
Noncontrolling interest	277	118
Total shareholders' equity	171,082	164,441
Total liabilities and shareholders' equity	\$1,500,331	\$1,449,349
See notes to consolidated financial statements		

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NORTHRIM BANCORP, INC.
Consolidated Statements of Income
(Unaudited)

(In Thousands, Except Per Share Data)	Three Months Ended		Six Months Ended	
	June 30, 2015	2014	June 30, 2015	2014
Interest Income				
Interest and fees on loans	\$14,135	\$13,082	\$27,602	\$23,953
Interest on investment securities available for sale	759	750	1,644	1,480
Interest on investment securities held to maturity	25	22	48	45
Interest on deposits in other banks	24	41	35	90
Total Interest Income	14,943	13,895	29,329	25,568
Interest Expense				
Interest expense on deposits, borrowings and junior subordinated debentures	748	484	1,502	924
Net Interest Income	14,195	13,411	27,827	24,644
Provision for loan losses	376	(1,136)	702	(1,136)
Net Interest Income After Provision for Loan Losses	13,819	14,547	27,125	25,780
Other Operating Income				
Mortgage banking income	7,839	—	15,122	—
Employee benefit plan income	931	878	1,708	1,754
Electronic banking income	700	604	1,322	1,104
Service charges on deposit accounts	568	607	1,058	1,083
Purchased receivable income	562	484	1,151	965
Gain on sale of securities, net	16	349	130	446
Equity in earnings from RML	—	355	—	224
Other income	947	829	1,607	1,264
Total Other Operating Income	11,563	4,106	22,098	6,840
Other Operating Expense				
Salaries and other personnel expense	11,125	6,839	21,675	12,759
Occupancy expense	1,594	1,112	3,198	1,989
Professional and outside services	791	219	1,542	624
Marketing expense	642	394	1,259	1,008
Change in fair value, RML earn-out liability	587	—	2,089	—
Equipment expense	428	359	862	657
Insurance expense	345	284	669	469
Software expense	337	354	649	614
Internet banking expense	227	213	447	413
Intangible asset amortization expense	72	81	145	133
Merger and acquisition expense	—	312	—	705
Reserve for (recovery from) purchased receivables	(18)	243	(72)	206
OREO (income) expense, net rental income and gains on sale	(121)	(9)	176	(247)
Other operating expense	1,744	1,219	3,575	2,258
Total Other Operating Expense	17,753	11,620	36,214	21,588
Income Before Provision for Income Taxes	7,629	7,033	13,009	11,032
Provision for income taxes	2,686	2,569	4,433	3,866
Net Income	4,943	4,464	8,576	7,166
Less: Net income attributable to the noncontrolling interest	162	95	234	139
Net Income Attributable to Northrim BanCorp, Inc.	\$4,781	\$4,369	\$8,342	\$7,027

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Earnings Per Share, Basic	\$0.70	\$0.64	\$1.22	\$1.05
Earnings Per Share, Diluted	\$0.69	\$0.63	\$1.20	\$1.04
Weighted Average Shares Outstanding, Basic	6,854,338	6,829,897	6,854,264	6,683,897
Weighted Average Shares Outstanding, Diluted	6,941,671	6,919,568	6,938,879	6,774,434

See notes to consolidated financial statements

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NORTHRIM BANCORP, INC.
 Consolidated Statements of Comprehensive Income
 (Unaudited)
 2010

(In Thousands)	Three Months Ended June 30,		Six Months Ended June 30,	
	2015	2014	2015	2014
Net income	\$4,943	\$4,464	\$8,576	\$7,166
Other comprehensive income (loss), net of tax:				
Securities available for sale:				
Unrealized gains (losses) arising during the period	(\$152	) \$612	\$736	\$707
Reclassification of net gains included in net income (net tax expense of \$7 and \$143 for the second quarter of 2015 and 2014, respectively and \$53 and \$183 for the first six months of 2015 and 2014, respectively)	(9	)(206	)(77	)(263
Income tax expense related to unrealized gains	58	(221	)(263	)(260
Other comprehensive income (loss)	(103	)185	396	184
Comprehensive income	4,840	4,649	8,972	7,350
Less: comprehensive income attributable to the noncontrolling interest	162	95	234	139
Comprehensive income attributable to Northrim BanCorp, Inc.	\$4,678	\$4,554	\$8,738	\$7,211

See notes to consolidated financial statements

NORTHRIM BANCORP, INC.

Consolidated Statements of Changes in Shareholders' Equity
(Unaudited)

(In Thousands)	Common Stock Number of Shares	Par Value	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income	Non-controlling Interest	Total
Balance as of January 1, 2014	6,538	\$6,538	\$54,089	\$82,855	\$669	\$167	\$144,318
Purchase of Alaska Pacific	290	290	7,156	—	—	—	7,446
Cash dividend declared	—	—	—	(4,770)	—	—	(4,770)
Stock-based compensation expense	—	—	360	—	—	—	360
Exercise of stock options	26	26	28	—	—	—	54
Excess tax benefits from stock based payment arrangements	—	—	96	—	—	—	96
Distributions to noncontrolling interest	—	—	—	—	—	(508)	(508)
Other comprehensive loss, net of tax	—	—	—	—	(422)	—	(422)
Net income attributable to the noncontrolling interest	—	—	—	—	—	459	459
Net income attributable to Northrim BanCorp, Inc.	—	—	—	17,408	—	—	17,408
Twelve Months Ended December 31, 2014	6,854	\$6,854	\$61,729	\$95,493	\$247	\$118	\$164,441
Cash dividend declared	—	—	—	(2,492)	—	—	(2,492)
Stock-based compensation expense	—	—	237	—	—	—	237
Excess tax benefits from share-based payment arrangements	—	—	(1)	—	—	—	(1)
Distributions to noncontrolling interest	—	—	—	—	—	(75)	(75)
Other comprehensive income, net of tax	—	—	—	—	396	—	396
Net income attributable to the noncontrolling interest	—	—	—	—	—	234	234
Net income attributable to Northrim BanCorp, Inc.	—	—	—	8,342	—	—	8,342
Six Months Ended June 30, 2015	6,854	\$6,854	\$61,965	\$101,343	\$643	\$277	\$171,082

See notes to consolidated financial statements

NORTHRIM BANCORP, INC.
Consolidated Statements of Cash Flows
(Unaudited)

(In Thousands)	Six Months Ended June 30,	
	2015	2014
Operating Activities:		
Net income	\$8,576	\$7,166
Adjustments to Reconcile Net Income to Net Cash Provided by Operating Activities:		
Gain on sale of securities, net	(130	) (446
Depreciation and amortization of premises and equipment	1,122	900
Amortization of software	90	90
Intangible asset amortization	145	133
Amortization of investment security premium, net of discount accretion	(119	) (85
Deferred tax liability	(685	) (859
Stock-based compensation	237	189
Excess tax benefits from share-based payment arrangements	1	—
Deferral of loan fees and costs, net	(92	) 419
Provision (benefit) for loan losses	702	(1,136
Reserve for (recovery from) purchased receivables	(72	) 206
Purchases of loans held for sale	—	(75,877
Proceeds from the sale of loans held for sale	363,096	72,989
Origination of loans held for sale	(392,823) —
Gain on sale of other real estate owned	(136	) (368
Impairment on other real estate owned	268	45
Equity in undistributed earnings from mortgage affiliate	—	145
Net changes in assets and liabilities:		
(Increase) in accrued interest receivable	(26	) (407
Decrease (increase) in other assets	2,352	(557
Decrease in other liabilities	(8,731	) (2,998
Net Cash (Used) by Operating Activities	(26,225	) (451
Investing Activities:		
Investment in securities:		
Purchases of investment securities available for sale	(59,196	) (92,934
Proceeds from sales/maturities of securities available for sale	115,917	140,085
Purchases of domestic certificates of deposit	—	(3,500
Proceeds from maturities of domestic certificates of deposit	3,500	3,500
Proceeds from redemption of FHLB stock	1,587	95
Alaska Pacific acquisition, net of cash received	—	6,367
(Increase) decrease in purchased receivables, net	1,278	(1,561
Increase in loans, net	(50,597	) (19,052
Proceeds from sale of other real estate owned	1,971	1,599
Elliott Cove divestiture, net of cash received	219	—
Decrease in loan to Elliott Cove, net	—	49
Purchases of premises and equipment	(3,421	) (2,414
Net Cash (Used) Provided by Investing Activities	11,258	32,234
Financing Activities:		
Increase (decrease) in deposits	58,970	(24,895
Decrease in securities sold under repurchase agreements	(1,948) (1,367
Decrease in borrowings	(3,995) (4,341

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Distributions to noncontrolling interest	(75) (179)
Proceeds from the issuance of common stock	—	64)
Cash dividends paid	(2,470) (2,273)
Net Cash Provided (Used) by Financing Activities	50,482	(32,991)

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Net Change in Cash and Cash Equivalents	35,515	(1,208)
Cash and Cash Equivalents at Beginning of Period	68,556	85,591
Cash and Cash Equivalents at End of Period	\$104,071	\$84,383
Supplemental Information:		
Income taxes paid	\$4,011	\$1,877
Interest paid	\$1,556	\$858
Noncash commitments to invest in Low Income Housing Tax Credit Partnerships	\$55	\$8,518
Transfer of loans to other real estate owned	\$337	\$1,158
Transfer of premises to other real estate owned	\$—	\$904
Cash dividends declared but not paid	\$22	\$17
Acquisitions:		
Assets acquired	\$—	\$167,199
Liabilities assumed	\$—	\$153,172

See notes to consolidated financial statements

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

1. Basis of Presentation

The accompanying unaudited consolidated financial statements and corresponding footnotes have been prepared by Northrim BanCorp, Inc. (the "Company") in accordance with accounting principles generally accepted in the United States of America ("GAAP") and with instructions to Form 10-Q under the Securities Exchange Act of 1934, as amended. The year-end Consolidated Balance Sheet data was derived from the Company's audited financial statements. Accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statements. The Company owns a 100% interest in Residential Mortgage Holding Company, LLC ("RML"), the parent company of Residential Mortgage, LLC ("Residential Mortgage") and a 50.1% interest in Northrim Benefits Group, LLC ("NBG") and consolidates their balance sheets and income statements into its financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. Certain immaterial reclassifications have been made to prior year amounts to maintain consistency with the current year with no impact on net income or total shareholders' equity. The Company determined that it operates in two primary operating segments: Community Banking and Home Mortgage Lending. Prior to December 2014, the Company operated in a single segment: Community Banking. The Company has evaluated events and transactions through August 10, 2015 for potential recognition or disclosure. Operating results for the interim period ended June 30, 2015, are not necessarily indicative of the results anticipated for the year ending December 31, 2015. These consolidated financial statements should be read in conjunction with the Company's Annual Report on Form 10-K for the year ended December 31, 2014.

2. Significant Accounting Policies and Recent Accounting Pronouncements

The Company's significant accounting policies are discussed in Note 1 to the audited consolidated financial statements included in the Company's Annual Report on Form 10-K for the year ended December 31, 2014.

In January 2014, the Financial Accounting Standards Board ("FASB") issued ASU No. 2014-01, Accounting for Investments in Qualified Affordable Housing Projects. ASU 2014-01 permits an entity to make an accounting policy election to account for their investments in qualified affordable housing projects using the proportional amortization method if certain conditions are met. Under the proportional amortization method, an entity amortizes the initial cost of the investment in proportion to the tax credits and other tax benefits received and recognizes the net investment performance in the income statement as a component of income tax expense (benefit). The amendments are effective for annual and interim reporting periods beginning on or after December 15, 2014 and should be applied prospectively. The Company adopted ASU 2014-01 in its consolidated financial statements as of January 1, 2015. As a result, amortization expense related to the Company's investments in low income housing tax credit partnerships has been included in the line item entitled "Provision for income taxes" in the Consolidated Statements of Income for all periods presented.

In February 2015, the Financial Accounting Standards Board ("FASB") issued ASU 2015-02, Amendments to the Consolidation Analysis ("ASU 2015-02"). The amendments to the Codification in ASU 2015-02 affect reporting entities that are required to evaluate whether they should consolidate certain legal entities. The amendments in this update affect the following areas: 1) the effect of related parties on the primary beneficiary determination, 2) evaluating fees paid to a decision maker or a service provider as a variable interest, 3) the effect of fee arrangements on the primary beneficiary determination, and 4) certain investment funds. This ASU is effective for the Company's financial statements for annual and interim periods beginning on or after December 15, 2015, and must be applied prospectively. The Company does not believe that the adoption of this standard will have a material impact on the Company's consolidated financial position or results of operations.

In April 2015, the Financial Accounting Standards Board ("FASB") issued ASU 2015-03, Simplifying the Presentation of Debt Issuance Costs ("ASU 2015-03"). The amendments to the Codification in ASU 2015-03 identify, evaluate, and improve areas of generally accepted accounting principles (GAAP) for which cost and complexity can be reduced

while maintaining or improving the usefulness of the information provided to users of financial statements. To simplify presentation of debt issuance costs, the amendments in this Update require that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability, consistent with debt discounts. The recognition and measurement guidance for debt issuance costs are not affected by the amendments in this Update. This ASU is effective for the Company's financial statements for annual and interim periods beginning on or after December 15, 2015, and must be applied prospectively. The Company does not believe that the adoption of this standard will have a material impact on the Company's consolidated financial position or results of operations.

In June 2015, the Financial Accounting Standards Board ("FASB") issued ASU 2015-10, Technical Corrections and Improvements ("ASU 2015-10"). The amendments to the Codification in ASU 2015-10 cover a wide range of topics in the

Codification. The amendments generally fall into one of the following types: amendments related to differences between original guidance and the codification, guidance clarification and reference corrections, simplification, and minor improvements. The amendments in this Update represent changes to clarify the Codification, correct unintended application of guidance, or make minor improvements to the Codification that are not expected to have a significant effect on current accounting practice or create a significant administrative cost to most entities. Additionally, some of the amendments will make the Codification easier to understand and easier to apply by eliminating inconsistencies, providing needed clarifications, and improving the presentation of guidance in the Codification. This ASU is effective for the Company's financial statements for annual and interim periods beginning on or after December 15, 2015, and must be applied prospectively. The Company does not believe that the adoption of this standard will have a material impact on the Company's consolidated financial position or results of operations.

3. Business Combinations

Alaska Pacific Bancshares, Inc.

On April 1, 2014, the Company completed the acquisition of 100% of the outstanding shares of Alaska Pacific Bancshares, Inc. ("Alaska Pacific") for a total purchase price of \$13.9 million, which was comprised of the issuance of 290,212 shares of the Company's common stock (at a volume weighted average closing price of \$25.66 per share) and \$6.4 million in cash. The assets acquired and liabilities assumed have been accounted for under the acquisition method of accounting and were recorded at their estimated fair values as of the April 1, 2014 acquisition date. Estimated fair values recorded in the transaction were subject to change for up to one year after the closing date of the acquisition. The primary reason for the acquisition was to expand the Company's geographic footprint in Alaska.

The application of the acquisition method of accounting resulted in the recognition of a bargain purchase gain of \$170,000 and a core deposit intangible of \$623,000, or 0.5% of core deposits. The bargain purchase gain represents the excess of the estimated fair value of the net assets acquired in excess of the purchase price and is included in Other Income in the Consolidated Statements of Income in this Form 10-Q. This acquisition resulted in a bargain purchase gain primarily due to the inclusion of certain adjustments to the purchase price for potential risks identified by the Company during the due diligence and price negotiation stages of the acquisition that were concluded in October of 2013. The Company has concluded that the potential risks identified at that time do not represent a liability to the Company and, accordingly, they have not been allocated any value in the application of the acquisition method of accounting.

A summary of the net assets acquired and the estimated fair value adjustments of Alaska Pacific are presented below:

(In Thousands)	Alaska Pacific April 1, 2014	
Cost basis net assets	\$14,733	
Cash payment made	(6,423)
Common stock issued	(7,446)
Fair value adjustments:		
Net loans	(1,137)
Premises and equipment	547	
Other intangible assets	623	
Mortgage servicing rights	(119)
Deposits	(844)
Other	236	
Bargain purchase gain	\$170	

A summary of assets acquired and liabilities assumed at their estimated fair values are presented below:

(In Thousands)	Alaska Pacific April 1, 2014
Assets Acquired:	
Cash and equivalents	\$12,956
Investment securities	7,240
Loans	138,432
Premises and equipment	3,436
Other intangibles	623
Mortgage servicing rights	1,170
Other real estate owned	1,709
Other assets	1,645
Total assets acquired	\$167,211
Liabilities Assumed:	
Deposits	\$151,438
Other liabilities	1,734
Total liabilities assumed	\$153,172

Alaska Pacific purchased loans not subject to the requirements of FASB ASC 310-30 Loans and Debt Securities Acquired with Deteriorated Credit Quality ("ASC 310-30") are presented below at acquisition:

(In Thousands)	April 1, 2014
Contractually required principal payments	\$133,921
Purchase adjustment for credit, interest rate, and liquidity	612
Fair value of purchased non-credit impaired loans	\$134,533

Alaska Pacific purchased loans subject to the requirements of FASB ASC 310-30 Loans and Debt Securities Acquired with Deteriorated Credit Quality. The Company identified eighteen purchased credit impaired loans as of April 1, 2014. This group of loans consists primarily of commercial and commercial real estate loans, and unlike a pool of consumer mortgages, it is not practicable for the Company to analyze the accretable yield of these loans. As such, the Company has elected the cost recovery method of income recognition for these loans, and thus no accretable difference has been identified for these loans.

Purchased credit impaired loans at acquisition are presented below:

(In Thousands)	April 1, 2014
Contractually required principal payments	\$7,553
Nonaccretable difference	(3,654)
Fair value of purchased credit impaired loans	\$3,899

The acquisition of Alaska Pacific is not considered significant to the Company's financial statements. The operations of Alaska Pacific are included in our operating results from April 1, 2014, and the Company estimates that these operations added revenue of \$3.9 million, non-interest expense of \$2.7 million, and net income of \$1.2 million, before taxes, for the six months ended June 30, 2015. Alaska Pacific's results of operations prior to the acquisition are not included in our operating results. Additionally, merger-related costs of \$615,000 for the six months ended June 30, 2014 were incurred and expensed in connection with the acquisition of Alaska Pacific and recognized within the merger and acquisition expense on the Consolidated Statements of Income.

The following table presents unaudited pro forma results of operations for the six month period ended June 30, 2014 as if the acquisition of Alaska Pacific had occurred on January 1, 2014. The proforma results have been prepared for comparative purposes only and are not necessarily indicative of the results that would have been obtained had the acquisition actually occurred on January 1, 2014.

(In Thousands, except earnings per share data)	Six Months Ended June 30, 2014			Pro Forma Combined
	Company	Alaska Pacific ¹	Pro Forma Adjustments	
Net interest and other income	\$31,484	\$2,095	(\$10) ²	\$33,569
Net income attributable to Northrim BanCorp, Inc.	7,027	(1,282)	123 ³	5,868
Earnings Per Share, Basic	\$1.05			\$0.84
Earnings Per Share, Diluted	\$1.04			\$0.83
Weighted Average Shares Outstanding, Basic	6,683,897			6,974,109
Weighted Average Shares Outstanding, Diluted	6,774,434			7,064,646

¹ Alaska Pacific represents results from January 1 to March 31 for 2014.

² Amount of amortization/ accretion of the fair value adjustments on loans and certificates of deposit.

³ Amount of amortization/accretion of the fair value adjustments on loans and certificates of deposit, bargain purchase gain, amortization of core deposit intangible, and the change in the provision for income taxes.

Residential Mortgage Holding Company, LLC

On December 1, 2014, the Company completed the acquisition of 76.5% of the equity interest in RML, the parent company of Residential Mortgage, in a cash transaction valued at \$29.5 million, resulting in RML becoming an indirect wholly-owned subsidiary of the Company. The primary reason for the acquisition was to expand the Company's presence in the mortgage lending business in Alaska. The fair value of the Company's 23.5% equity interest in RML immediately prior to the acquisition was \$9.0 million. The Company recorded a \$3.0 million gain in the fourth quarter of 2014 as a result of remeasuring the Company's equity interest in RML immediately prior to the acquisition, which was included in the Company's Consolidated Statements of Income in the line item entitled "Gain on purchase of mortgage affiliate". The Company utilized a market value approach to value its equity interest in RML which included analysis of current trading values and historical acquisition multiples of comparable mortgage companies. The consideration transferred or transferable to the former owners of RML and the assets acquired and liabilities assumed have been accounted for under the acquisition method of accounting and were recorded at their estimated fair values as of the December 1, 2014 acquisition date. Estimated fair values recorded in the transaction are subject to change for up to one year after the closing date of the acquisition. The application of the acquisition method of accounting resulted in the recognition of goodwill in the amount of \$14.8 million and a trade name intangible of \$950,000. RML holds a 30% equity interest in Homestate Mortgage LLC.

The former owners of RML (the "sellers") will receive additional cash proceeds (the "earn-out" payments) based on the adjusted pretax earnings of RML for each of the twelve months periods ending November 30, 2015, 2016, 2017, 2018 and 2019. The Company recorded a \$7.3 million liability as of December 1, 2014 as part of its purchase accounting for future earn-out payments. Per the purchase agreement, the earn-out payments are calculated as follows:

First tier earn-out payment	Adjusted pretax earnings greater than \$1,000,000 and less than or equal to \$2,000,000	Payment will be calculated as product of amount of adjusted pretax earnings times 40%
Second tier earn-out payment	Adjusted pretax earnings greater than \$2,000,000 and less than or equal to \$3,000,000	The first tier earn-out payment, plus the product of amount of adjusted pretax earnings greater than \$2,000,000 and less than \$3,000,000 times 50%
Third tier earn-out payment	Adjusted pretax earnings greater than \$3,000,000 and less than or equal to \$4,000,000	The first tier plus the second tier earn-out payment, plus the product of amount of adjusted pretax earnings greater than \$3,000,000 and less than \$4,000,000 times 70%
Fourth tier earn- out payment	Adjusted pretax earnings greater than \$4,000,000 and less than or equal to \$6,000,000	The first, second and third tier earn-out payment, plus the product of amount of adjusted pretax earnings greater than \$4,000,000 and less than \$6,000,000 times 85%
Fifth tier earn-out payment	Adjusted pretax earnings greater than \$6,000,000	The first, second, third and fourth tier earn-out payment, plus the product of amount of adjusted pretax earnings greater than \$6,000,000 times 55%

The purchase agreement provides for these earn-out payments as a portion of the purchase price to be paid to the sellers in future periods, contingent on future events. Therefore the Company included an estimate of the acquisition-date fair value of the contingent consideration of \$7.3 million as part of the cost of the combination. The accounting treatment of the contingent consideration to be paid to those of the sellers who continue employment with the Company was evaluated to determine whether the amounts represent purchase consideration or a separate transaction, such as post-transaction employee compensation. Factors evaluated require significant judgment and include, among other factors; consideration of the terms of continuing employment, levels of post-transaction compensation, ownership interest of the sellers/employees, linkage of the contingent consideration to the transaction date combination valuation, and any other agreements or matters related to the transaction.

Based on an evaluation of the factors surrounding the transaction and the terms of the purchase agreement, the amount due under the earn-out provision was accounted for as acquisition consideration. The Company concluded that the contingent consideration to be paid to the sellers/employees was a significant component of the transaction date valuation of the acquired business. The calculation of the contingent payment was based upon factors established at the date of the transaction to be paid upon meeting the established earnings criteria of RML. The post transaction employment arrangements of the continuing employees are at market rates, and the formula for determining the contingent consideration is consistent with the business valuation methodologies, based upon a multiplier of earnings recognized from RML for five twelve month periods following the acquisition.

For the six month period ended June 30, 2015, the Company recorded an adjustment to increase the contingent liability by \$2.2 million. The increase in the contingent liability resulted from the excess of RML's pretax income from December 1, 2014 through the end of the second quarter of 2015 over and above estimates made at the close of the purchase of RML. The adjustment to the contingent liability for estimated future earn-out payments is recorded in the line item titled "Change in fair value, RML earn-out liability" in other operating expense on the Consolidated

Statements of Income. The total contingent liability as of June 30, 2015 is \$9.5 million.

A summary of the net assets acquired and the estimated fair value adjustments of RML are presented below:

(In Thousands)	RML December 1, 2014	
Cost basis net assets	\$11,915	
Cash payment made	(18,240)
Cash surrender value of life insurance paid	(3,896)
Liability for future earn out payments	(7,318)
Fair value adjustments:		
Loans	(360)
Trade name intangible	950	
Rate lock derivative asset	960	
Investment in Homestate Mortgage, LLC	1,490	
Other	(311)
Goodwill	(\$14,810)

A summary of assets acquired and liabilities assumed at their estimated fair values are presented below:

(In Thousands)	RML December 1, 2014
Assets Acquired:	
Cash and equivalents	\$10,828
Net loans	41,304
Premises and equipment	255
Trade name intangible	950
Rate lock derivative asset	960
Investment in Homestate Mortgage LLC	3,000
Other real estate owned	270
Other assets	10,291
Total assets acquired	\$67,858
Liabilities Assumed:	
Borrowings	\$37,541
Other liabilities	6,625
Total liabilities assumed	\$44,166

The acquisition of RML is not considered significant to the Company's financial statements under Regulation S-X; however, the Company has determined that the acquisition results in a new reporting segment, Home Mortgage Lending.

The operations of RML are included in our operating results from December 1, 2014, and added revenue of \$15.4 million, non-interest expense of \$10.9 million, and net income of \$4.6 million, before taxes, for the six month period ended June 30, 2015. RML's results of operations prior to the December 1, 2014 acquisition are included in our operating results under the equity method. Additionally, merger-related costs of \$90,000 for the six-month period ended June 30, 2014 were incurred and expensed in connection with the acquisition of RML and recognized within the merger and acquisition expense on the Consolidated Statements of Income.

The following table presents unaudited pro forma results of operations for the six month period ended June 30, 2014 as if the acquisition of RML had occurred on January 1, 2014. The proforma results have been prepared for comparative purposes only and are not necessarily indicative of the results that would have been obtained had the acquisition actually occurred on January 1, 2014.

(In Thousands, except earnings per share data)

	Six Months Ended June 30, 2014			
	Company	RML ¹	Pro Forma Adjustments	Pro Forma Combined
Net interest and other income	\$31,484	\$11,171	² (\$198)	³ \$42,457
Net income attributable to Northrim BanCorp, Inc.	7,027	1,760	2,857	⁴ 11,644
Earnings Per Share, Basic	\$1.05			\$1.74
Earnings Per Share, Diluted	\$1.04			\$1.72
Weighted Average Shares Outstanding, Basic	6,683,897			6,683,897
Weighted Average Shares Outstanding, Diluted	6,774,434			6,774,434

¹ RML represents results from January 1 to June 30.

² 2014 amount is comprised of net interest income of \$160,000 and \$11.0 million of other income.

³ Amount of accretion of the fair value adjustments on loans and income recognized under the equity method prior to the December 2014 acquisition.

⁴ Amount of accretion of the fair value adjustments on loans, income recognized under the equity method, gain on acquisition, earn out accretion, and the change in the provision for income taxes.

Prior to December 1, 2014, the Company accounted for RML under the equity method of accounting. As of December 1, 2014, the Company owns 100% interest in RML and consolidates RML's activity into the Company's Consolidated Financial Statements.

The following table presents unaudited combined pro forma results of operations for the six month period ended June 30, 2014 as if the acquisition of Alaska Pacific and RML had occurred on January 1, 2014. The proforma results have been prepared for comparative purposes only and are not necessarily indicative of the results that would have been obtained had the acquisitions actually occurred on January 1, 2014.

(In Thousands, except earnings per share data)

	Six Months Ended June 30, 2014				
	Company	Alaska Pacific ¹	RML ²	Pro Forma Adjustments	Pro Forma Combined
Net interest and other income	\$31,484	\$2,095	\$11,171	³ (\$218)	⁴ \$44,532
Net income attributable to Northrim BanCorp, Inc.	7,027	(1,282)	1,760	2,980	⁵ 10,485
Earnings Per Share, Basic	\$1.05				\$1.50
Earnings Per Share, Diluted	\$1.04				\$1.48
Weighted Average Shares Outstanding, Basic	6,683,897				6,974,109
Weighted Average Shares Outstanding, Diluted	6,774,434				7,064,646

¹ Alaska Pacific represents results from January 1 to March 31 for 2014.

² RML represents results from January 1 to June 30.

³ 2014 amount is comprised of net interest income of \$160,000 and \$11.0 million of other income.

⁴ Amount of amortization/ accretion of the fair value adjustments on loans and certificates of deposit for Alaska Pacific and amount of accretion of the fair value adjustments on loans and income recognized under the equity method prior to the December 2014 acquisition for RML.

⁵ Amount of amortization/accretion of the fair value adjustments on loans and certificates of deposit, bargain purchase gain, amortization of core deposit intangible, and the change in the provision for income taxes for Alaska Pacific and amount of accretion of the fair value adjustments on loans, income recognized under the equity method, gain on acquisition, earn out accretion, and the change in the provision for income taxes for RML.

4. Cash and Cash Equivalents

For purposes of reporting cash flows, cash and cash equivalents include cash on hand, amounts due from banks, interest-bearing deposits with other banks, banker's acceptances, commercial paper, securities purchased under agreement to resell, federal funds sold, and securities with maturities of less than 90 days at acquisition. As of June 30, 2015, the Company had no certificate of deposit in another bank with original maturity greater than 90 days. Cash and cash equivalent balances placed with the Federal Reserve of San Francisco is the only concentration representing more than 10% of the Company's equity.

5. Investment Securities

The carrying values and approximate fair values of investment securities at the periods indicated are presented below:

(In Thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
June 30, 2015				
Securities available for sale				
U.S. Treasury and government sponsored entities	\$172,748	\$549	\$52	\$173,245
Municipal securities	11,191	187	5	11,373
U.S. Agency mortgage-backed securities	924	3	1	926
Corporate bonds	38,971	326	—	39,297
Preferred stock	1,008	19	—	1,027
Total securities available for sale	\$224,842	\$1,084	\$58	\$225,868
Securities held to maturity				
Municipal securities	\$2,197	\$74	\$—	\$2,271
Total securities held to maturity	\$2,197	\$74	\$—	\$2,271
December 31, 2014				
Securities available for sale				
U.S. Treasury and government sponsored entities	\$226,624	\$105	\$539	\$226,190
Municipal securities	11,843	285	4	12,124
U.S. Agency mortgage-backed securities	1,024	6	1	1,029
Corporate bonds	38,820	415	—	39,235
Preferred stock	2,999	153	—	3,152
Total securities available for sale	\$281,310	\$964	\$544	\$281,730
Securities held to maturity				
Municipal securities	\$2,201	\$107	\$—	\$2,308
Total securities held to maturity	\$2,201	\$107	\$—	\$2,308

Gross unrealized losses on investment securities and the fair value of the related securities, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position, at June 30, 2015 and December 31, 2014 were as follows:

(In Thousands)	Less Than 12 Months		More Than 12 Months		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
June 30, 2015:						
Securities Available for Sale						
U.S. Treasury and government sponsored entities	\$56,109	\$52	\$—	\$—	\$56,109	\$52
Municipal Securities	3,142	4	81	1	3,223	5
Mortgage-backed Securities	325	1	—	—	325	1
Total	\$59,576	\$57	\$81	\$1	\$59,657	\$58
December 31, 2014:						
Securities Available for Sale						
U.S. Treasury and government sponsored entities	\$165,004	\$539	\$—	\$—	\$165,004	\$539
Municipal Securities	567	4	—	—	567	4
Mortgage-backed Securities	117	1	—	—	117	1
Total	\$165,688	\$544	\$—	\$—	\$165,688	\$544

There were twenty and twenty-nine available-for-sale securities with unrealized losses as of June 30, 2015 and December 31, 2014, respectively, that have been in a loss position for less than twelve months. There were two and no securities as of June 30, 2015 and December 31, 2014 that have been in an unrealized loss position for more than twelve months. The contractual terms of the investments in a loss position do not permit the issuer to settle the securities at a price less than the amortized cost of the investment. Because the Company does not intend to sell, nor is it required to sell these investments until a market price recovery or maturity, these investments are not considered other-than-temporarily impaired.

At June 30, 2015, \$57.5 million in securities, or 25%, of the investment portfolio was pledged for deposits and borrowings, as compared to \$54.1 million, or 19%, at December 31, 2014. We held no securities of any single issuer (other than government sponsored entities) that exceeded 10% of our shareholders' equity at June 30, 2015 and December 31, 2014.

The amortized cost and fair values of debt securities at June 30, 2015, are distributed by contractual maturity as shown below. Expected maturities may differ from contractual maturities because issuers may have the right to call or prepay obligations with or without call or prepayment penalties. Although preferred stock has no stated maturity, it is aggregated in the calculation of weighted average yields presented below in the category of investments that mature in ten years or more.

(In Thousands)	Amortized Cost	Fair Value	Weighted Average Yield	
US Treasury and government sponsored entities				
1-5 years	\$172,748	\$173,245	1.19	%
Total	\$172,748	\$173,245	1.19	%
U.S. Agency mortgage-backed securities				
1-5 years	\$44	\$44	2.19	%
5-10 years	271	271	3.14	%
Over 10 years	609	611	2.87	%
Total	\$924	\$926	2.91	%
Corporate bonds				
Within 1 year	\$10,623	\$10,733	1.92	%
1-5 years	28,348	28,564	1.24	%
Total	\$38,971	\$39,297	1.43	%
Preferred stock				
Over 10 years	\$1,008	\$1,027	4.15	%
Total	\$1,008	\$1,027	4.15	%
Municipal securities				
Within 1 year	\$661	\$671	2.63	%
1-5 years	7,817	7,951	2.45	%
5-10 years	4,910	5,022	4.54	%
Total	\$13,388	\$13,644	3.22	%

The proceeds and resulting gains and losses, computed using specific identification, from sales of investment securities for the six months ending June 30, 2015 and 2014, respectively, are as follows:

(In Thousands)	Proceeds	Gross Gains	Gross Losses
2015			
Available for sale securities	\$2,621	\$130	\$—
2014			
Available for sale securities	\$23,588	\$450	\$4

A summary of interest income for the six months ending June 30, 2015 and 2014 on available for sale investment securities is as follows:

(In Thousands)	2015	2014
US Treasury and government sponsored entities	\$1,120	\$775
U.S. Agency mortgage-backed securities	13	9
Other	344	488
Total taxable interest income	\$1,477	\$1,272
Municipal securities	\$167	\$208
Total tax-exempt interest income	\$167	\$208
Total	\$1,644	\$1,480

6. Loans Held for Sale

The Company acquired the remaining 76.5% of RML on December 1, 2014. RML originates 1-4 family residential mortgages and sells them to the secondary market. These loans are shown as loans held for sale on the Company's Consolidated Balance Sheet. RML originated \$392.8 million and sold \$363.1 million in loans during the six-month period ending June 30, 2015. Prior to December 1, 2014, the Company had a 23.5% ownership interest in RML and purchased residential loans from them. The Company then sold these loans in the secondary market. The Company purchased \$75.9 million and sold \$73.0 million in loans from RML during the six-month period ending June 30, 2014.

7. Loans

The following table presents total portfolio loans by portfolio segment and class of financing receivable, based on our asset quality rating ("AQR") criteria:

(In Thousands)	Commercial	Real estate construction one-to-four family	Real estate construction other	Real estate term owner occupied	Real estate term non-owner occupied	Real estate term other	Consumer secured by 1st deeds of trust	Consumer other	Total
June 30, 2015									
AQR Pass	\$318,663	\$38,233	\$101,683	\$105,213	\$291,900	\$38,139	\$28,658	\$30,397	\$952,886
AQR Special Mention	765	—	—	751	2,077	223	194	85	4,095
AQR Substandard	14,753	—	—	5,281	1,636	149	476	32	22,327
AQR Doubtful	—	—	—	—	—	—	—	—	—
AQR Loss	—	—	—	—	—	—	—	—	—
Subtotal	\$334,181	\$38,233	\$101,683	\$111,245	\$295,613	\$38,511	\$29,328	\$30,514	\$979,308
Less: Unearned origination fees, net of origination costs									(4,459)
Total									\$974,849
December 31, 2014									
AQR Pass	\$291,020	\$34,651	\$91,195	\$103,049	\$282,774	\$36,705	\$31,118	\$31,399	\$901,911
AQR Special Mention	11,618	—	—	5,817	2,095	39	396	47	20,012
AQR Substandard	3,905	191	—	606	1,747	150	486	47	7,132
AQR Doubtful	—	—	—	—	—	—	—	—	—
AQR Loss	—	—	—	—	—	—	—	—	—
Subtotal	\$306,543	\$34,842	\$91,195	\$109,472	\$286,616	\$36,894	\$32,000	\$31,493	\$929,055
Less: Unearned origination fees, net of origination costs									(4,551)
Total									\$924,504

Loans are carried at their principal amount outstanding, net of charge-offs, unamortized fees and direct loan origination costs. Loan balances are charged-off to the allowance for loan losses ("Allowance") when management believes that collection of principal is unlikely. Interest income on loans is accrued and recognized on the principal amount outstanding except for loans in a nonaccrual status. All classes of loans are placed on nonaccrual and considered impaired when management believes doubt exists as to the collectability of the interest or principal. Cash payments received on nonaccrual loans are directly applied to the principal balance. Generally, a loan may be

returned to accrual status when the delinquent principal and interest is brought current in accordance with the terms of the loan agreement. Additionally, certain ongoing performance criteria, which generally includes a performance period of six months, must be met in order for a loan to be returned to accrual status. Loans are reported as past due when installment payments, interest payments, or maturity payments are past due based on contractual terms.

Nonaccrual loans totaled \$5.0 million and \$4.7 million at June 30, 2015 and December 31, 2014, respectively.

Nonaccrual loans at the periods indicated, by segment, are presented below:

(In Thousands)	June 30, 2015	December 31, 2014
Commercial	\$3,049	\$2,031
Real estate construction one-to-four family	—	191
Real estate term owner occupied	43	135
Real estate term non-owner occupied	1,636	1,746
Real estate term other	—	39
Consumer secured by 1st deeds of trust	312	485
Consumer other	—	47
Total	\$5,040	\$4,674

Past due loans and nonaccrual loans at the periods indicated are presented below by AQR:

(In Thousands)	30-59 Days Past Due Still Accruing	60-89 Days Past Due Still Accruing	Greater Than 90 Days Still Accruing	Nonaccrual	Total Past Due	Current	Total
June 30, 2015							
AQR Pass	\$79	\$57	\$—	\$—	\$136	\$952,750	\$952,886
AQR Special Mention	189	—	—	—	189	3,906	4,095
AQR Substandard	—	4	—	5,040	5,044	17,283	22,327
AQR Doubtful	—	—	—	—	—	—	—
AQR Loss	—	—	—	—	—	—	—
Subtotal	\$268	\$61	\$—	\$5,040	\$5,369	\$973,939	\$979,308
Less: Unearned origination fees, net of origination costs							(4,459)
Total							\$974,849
December 31, 2014							
AQR Pass	\$696	\$545	\$—	\$—	\$1,241	\$900,670	\$901,911
AQR Special Mention	—	—	—	—	—	20,012	20,012
AQR Substandard	40	—	—	4,674	4,714	2,418	7,132
AQR Doubtful	—	—	—	—	—	—	—
AQR Loss	—	—	—	—	—	—	—
Subtotal	\$736	\$545	\$—	\$4,674	\$5,955	\$923,100	\$929,055
Less: Unearned origination fees, net of origination costs							(4,551)
Total							\$924,504

The Company considers a loan to be impaired when it is probable that it will be unable to collect all amounts due according to the contractual terms of the loan agreement. Once a loan is determined to be impaired, the impairment is measured based on the present value of the expected future cash flows discounted at the loan's effective interest rate, except that if the loan is collateral dependent, the impairment is measured by using the fair value of the loan's collateral. Nonperforming loans greater than \$50,000 are individually evaluated for impairment based upon the borrower's overall financial condition, resources, and payment record, and the prospects for support from any financially responsible guarantors.

At June 30, 2015 and December 31, 2014, the recorded investment in loans that are considered to be impaired was \$26.3 million and \$11.3 million, respectively. The following table presents information about impaired loans by class as of the periods indicated:

(In Thousands)	Recorded Investment	Unpaid Principal Balance	Related Allowance
June 30, 2015			
With no related allowance recorded			
Commercial - AQR special mention	\$163	\$163	\$—
Commercial - AQR substandard	11,992	12,137	—
Real estate construction other - AQR pass	731	731	—
Real estate term owner occupied- AQR pass	764	764	—
Real estate term owner occupied- AQR substandard	5,238	5,238	—
Real estate term non-owner occupied- AQR pass	540	540	—
Real estate term non-owner occupied- AQR special mention	2,070	2,070	—
Real estate term non-owner occupied- AQR substandard	1,636	1,636	—
Real estate term other - AQR substandard	149	149	—
Consumer secured by 1st deeds of trust - AQR pass	79	79	—
Consumer secured by 1st deeds of trust - AQR substandard	439	439	—
Subtotal	\$23,801	\$23,946	\$—
With an allowance recorded			
Commercial - AQR substandard	\$2,544	\$2,544	\$265
Subtotal	\$2,544	\$2,544	\$265
Total			
Commercial - AQR special mention	\$163	\$163	\$—
Commercial - AQR substandard	14,536	14,681	265
Real estate construction other - AQR pass	731	731	—
Real estate term owner-occupied - AQR pass	764	764	—
Real estate term owner-occupied - AQR substandard	5,238	5,238	—
Real estate term non-owner occupied - AQR pass	540	540	—
Real estate term non-owner occupied - AQR special mention	2,070	2,070	—
Real estate term non-owner occupied - AQR substandard	1,636	1,636	—
Real estate term other - AQR substandard	149	149	—
Consumer secured by 1st deeds of trust - AQR pass	79	79	—
Consumer secured by 1st deeds of trust - AQR substandard	439	439	—
Total	\$26,345	\$26,490	\$265

(In Thousands)	Recorded Investment	Unpaid Principal Balance	Related Allowance
December 31, 2014			
With no related allowance recorded			
Commercial - AQR special mention	\$170	\$170	\$—
Commercial - AQR substandard	3,000	3,045	—
Real estate construction one-to-four family - AQR special mention	191	191	—
Real estate construction other - AQR pass	772	772	—
Real estate term owner occupied - AQR pass	501	501	—
Real estate term owner occupied - AQR special mention	273	273	—
Real estate term owner occupied - AQR substandard	558	558	—
Real estate term non-owner occupied - AQR pass	549	549	—
Real estate term non-owner occupied - AQR special mention	2,088	2,088	—
Real estate term non-owner occupied - AQR substandard	1,709	1,709	—
Real estate term other - AQR substandard	150	150	—
Consumer secured by 1st deeds of trust - AQR pass	82	82	—
Consumer secured by 1st deeds of trust - AQR special mention	448	461	—
Subtotal	\$10,491	\$10,549	\$—
With an allowance recorded			
Commercial - AQR substandard	\$806	\$806	\$75
Subtotal	\$806	\$806	\$75
Total			
Commercial - AQR special mention	\$170	\$170	\$—
Commercial - AQR substandard	3,806	3,851	75
Real estate construction one-to-four family - AQR special mention	191	191	—
Real estate construction other - AQR pass	772	772	—
Real estate term owner occupied - AQR pass	501	501	—
Real estate term owner occupied - AQR special mention	273	273	—
Real estate term owner occupied - AQR substandard	558	558	—
Real estate term non-owner occupied - AQR pass	549	549	—
Real estate term non-owner occupied - AQR special mention	2,088	2,088	—
Real estate term non-owner occupied - AQR substandard	1,709	1,709	—
Real estate term other - AQR substandard	150	150	—
Consumer secured by 1st deeds of trust - AQR pass	82	82	—
Consumer secured by 1st deeds of trust - AQR special mention	448	461	—
Total	\$11,297	\$11,355	\$75

The unpaid principal balance included in the tables above represents the recorded investment at the dates indicated, plus amounts charged off for book purposes.

The following tables summarize our average recorded investment and interest income recognized on impaired loans for the three and six month periods ended June 30, 2015 and 2014, respectively:

Three Months Ended June 30, (In Thousands)	2015		2014	
	Average Recorded Investment	Interest Income Recognized	Average Recorded Investment	Interest Income Recognized
With no related allowance recorded				
Commercial - AQR pass	\$—	\$—	\$63	\$1
Commercial - AQR special mention	164	3	351	9
Commercial - AQR substandard	12,315	41	2,546	4
Real estate construction other - AQR pass	743	30	—	—
Real estate term owner occupied- AQR pass	766	17	508	15
Real estate term owner occupied- AQR special mention	—	—	363	4
Real estate term owner occupied- AQR substandard	5,269	19	1,414	14
Real estate term non-owner occupied- AQR pass	541	19	614	36
Real estate term non-owner occupied- AQR special mention	2,079	44	3,234	25
Real estate term non-owner occupied- AQR substandard	1,652	—	2,055	—
Real estate term other - AQR special mention	—	—	1,161	47
Real estate term other - AQR substandard	149	3	153	4
Consumer secured by 1st deeds of trust - AQR pass	80	1	85	—
Consumer secured by 1st deeds of trust - AQR substandard	444	4	379	—
Consumer other - AQR substandard	—	—	55	—
Subtotal	\$24,202	\$181	\$12,981	\$159
With an allowance recorded				
Commercial - AQR substandard	\$2,414	\$—	\$—	\$—
Consumer secured by 1st deeds of trust - AQR substandard	—	—	351	—
Subtotal	\$2,414	\$—	\$351	\$—
Total				
Commercial - AQR pass	\$—	\$—	\$63	\$1
Commercial - AQR special mention	\$164	\$3	\$351	\$9
Commercial - AQR substandard	14,729	41	2,546	4
Real estate construction other - AQR pass	743	30	—	—
Real estate term owner-occupied - AQR pass	766	17	508	15
Real estate term owner-occupied - AQR special mention	—	—	363	4
Real estate term owner-occupied - AQR substandard	5,269	19	1,414	14
Real estate term non-owner occupied - AQR pass	541	19	614	36
Real estate term non-owner occupied - AQR special mention	2,079	44	3,234	25
Real estate term non-owner occupied - AQR substandard	1,652	—	2,055	—
Real estate term other - AQR special mention	—	—	1,161	47
Real estate term other - AQR substandard	149	3	153	4
Consumer secured by 1st deeds of trust - AQR pass	80	1	85	—
Consumer secured by 1st deeds of trust - AQR substandard	444	4	730	—
Consumer other - AQR substandard	—	—	55	—
Total Impaired Loans	\$26,616	\$181	\$13,332	\$159

Six Months Ended June 30,	2015		2014	
(In Thousands)	Average Recorded Investment	Interest Income Recognized	Average Recorded Investment	Interest Income Recognized
With no related allowance recorded				
Commercial - AQR pass	\$—	\$—	\$32	\$1
Commercial - AQR special mention	166	7	242	10
Commercial - AQR substandard	7,703	70	1,476	8
Real estate construction one-to-four family - AQR special mention	—	—	176	6
Real estate construction other - AQR pass	753	59	—	—
Real estate construction other - AQR special mention	—	—	409	29
Real estate term owner occupied- AQR pass	634	28	509	27
Real estate term owner occupied- AQR special mention	135	5	322	9
Real estate term owner occupied- AQR substandard	2,967	28	1,143	27
Real estate term non-owner occupied- AQR pass	544	38	616	55
Real estate term non-owner occupied- AQR special mention	2,127	88	2,113	40
Real estate term non-owner occupied- AQR substandard	2,009	—	1,033	—
Real estate term other - AQR special mention	—	—	584	47
Real estate term other - AQR substandard	149	7	154	7
Consumer secured by 1st deeds of trust - AQR pass	81	2	86	2
Consumer secured by 1st deeds of trust - AQR substandard	560	4	190	—
Consumer other - AQR substandard	—	—	58	—
Subtotal	\$17,828	\$336	\$9,143	\$268
With an allowance recorded				
Commercial - AQR special mention	\$—	\$—	\$92	\$6
Commercial - AQR substandard	2,330	—	298	—
Real estate term other - AQR substandard	141	—	—	—
Consumer secured by 1st deeds of trust - AQR substandard	—	—	268	—
Subtotal	\$2,471	\$—	\$658	\$6

Total				
Commercial - AQR pass	\$—	\$—	\$32	\$1
Commercial - AQR special mention	\$166	\$7	\$334	\$16
Commercial - AQR substandard	10,033	70	1,774	8
Real estate construction one-to-four family - AQR special mention	—	—	176	6
Real estate construction other - AQR pass	753	59	—	—
Real estate construction other - AQR special mention	—	—	409	29
Real estate term owner-occupied - AQR pass	634	28	509	27
Real estate term owner-occupied - AQR special mention	135	5	322	9
Real estate term owner-occupied - AQR substandard	2,967	28	1,143	27
Real estate term non-owner occupied - AQR pass	544	38	616	55
Real estate term non-owner occupied - AQR special mention	2,127	88	2,113	40
Real estate term non-owner occupied - AQR substandard	2,009	—	1,033	—
Real estate term other - AQR special mention	—	—	584	47
Real estate term other - AQR substandard	290	7	154	7
Consumer secured by 1st deeds of trust - AQR pass	81	2	86	2
Consumer secured by 1st deeds of trust - AQR substandard	560	4	458	—
Consumer other - AQR substandard	—	—	58	—
Total Impaired Loans	\$20,299	\$336	\$9,801	\$274

As described in Note 3 above, the Company acquired 18 purchased credit impaired loans from Alaska Pacific on April 1, 2014 subject to the requirements of FASB ASC 310-30 Loans and Debt Securities Acquired with Deteriorated Credit Quality. This group of loans consists primarily of commercial and commercial real estate loans, and unlike a pool of consumer mortgages, it is not practicable for the Company to analyze the accretible yield of these loans. As such, the Company has elected the cost recovery method of income recognition for these loans, and thus no accretible difference has been identified for these loans. At the acquisition date, April 1, 2014, the fair value of this group of loans was \$3.9 million. The carrying value of these loans as of June 30, 2015 is \$2.6 million.

Loans classified as troubled debt restructurings (“TDR”) totaled \$9.0 million and \$7.7 million at June 30, 2015 and December 31, 2014, respectively. A TDR is a loan to a borrower that is experiencing financial difficulty that has been modified from its original terms and conditions in such a way that the Company is granting the borrower a concession that it would not grant otherwise. The Company has granted a variety of concessions to borrowers in the form of loan modifications. The modifications granted can generally be described in the following categories:

Rate Modification: A modification in which the interest rate is changed.

Term Modification: A modification in which the maturity date, timing of payments, or frequency of payments is changed.

Payment Modification: A modification in which the dollar amount of the payment is changed, or in which a loan is converted to interest only payments for a period of time is included in this category.

Combination Modification: Any other type of modification, including the use of multiple categories above.

AQR pass graded loans included above in the impaired loan data are loans classified as TDRs. By definition, TDRs are considered impaired loans. All of the Company's TDRs are included in impaired loans.

The following table presents the breakout between newly restructured loans that occurred during the six months ended June 30, 2015 and restructured loans that occurred prior to 2015 that are still included in portfolio loans:

(In Thousands)	Accrual Status	Nonaccrual Status	Total Modifications
New Troubled Debt Restructurings			
Commercial - AQR substandard	\$202	\$1,240	\$1,442
Subtotal	\$202	\$1,240	\$1,442
Existing Troubled Debt Restructurings	\$5,534	\$1,979	\$7,513
Total	\$5,736	\$3,219	\$8,955

The following table presents newly restructured loans that occurred during the six months ended June 30, 2015, by concession (terms modified):

(In Thousands)	Number of Contracts	June 30, 2015				Combination Modification	Total Modifications
		Rate Modification	Term Modification	Payment Modification			
Pre-Modification Outstanding Recorded Investment:							
Commercial - AQR substandard	3	\$—	\$—	\$—	\$1,035	\$1,035	
Total	3	\$—	\$—	\$—	\$1,035	\$1,035	
Post-Modification Outstanding Recorded Investment:							
Commercial - AQR substandard	3	\$—	\$—	\$—	\$1,442	\$1,442	
Total	3	\$—	\$—	\$—	\$1,442	\$1,442	

The Company had no commitments to extend additional credit to borrowers whose terms have been modified in TDRs. There were no charge offs in the six months ended June 30, 2015 on loans that were later classified as TDRs. All TDRs are also classified as impaired loans and are included in the loans individually evaluated for impairment in the calculation of the Allowance. There were two TDRs with a total recorded investment of \$1.4 million and a specific impairment amount totaling \$111,000 at June 30, 2015 and no TDRs with specific impairment at December 31, 2014, respectively.

The loans in the following table are past due, and they are nonaccrual loans. The following table presents TDRs that occurred during the last twelve months that subsequently defaulted, for the periods ending June 30, 2015 and 2014, respectively:

(In Thousands)	Number of Contracts	June 30, 2015 Recorded Investment	Number of Contracts	June 30, 2014 Recorded Investment
Troubled Debt Restructurings that Subsequently Defaulted:				
Real estate construction one-to-four family - AQR special mention	—	\$—	1	\$353
Total	—	\$—	1	\$353

The Company had no TDRs that subsequently defaulted within the first twelve months of restructure, during the periods ending June 30, 2015 and December 31, 2014.

8. Allowance for Loan Losses

The following tables detail activity in the Allowance for the periods indicated:

Three Months Ended June 30,	Commercial	Real estate construction one-to-four family	Real estate construction other	Real estate term owner occupied	Real estate term non-owner occupied	Real estate term other	Consumer secured by 1st deed of trust	Consumer other	Unallocated	Total
2015										
Balance, beginning of period	\$6,091	\$757	\$1,663	\$1,570	\$4,794	\$756	\$274	\$402	\$640	\$16,947
Charge-Offs	—	—	—	—	—	—	—	—	—	—
Recoveries	91	—	—	—	—	—	—	4	—	95
Provision (benefit)	(495)	(68)	200	(100)	94	(85)	(9)	9	830	376
Balance, end of period	\$5,687	\$689	\$1,863	\$1,470	\$4,888	\$671	\$265	\$415	\$1,470	\$17,418
Balance, end of period:										
Individually evaluated for impairment	\$265	\$—	\$—	\$—	\$—	\$—	\$—	\$—	\$—	\$265
Balance, end of period:										
Collectively evaluated for impairment	\$5,422	\$689	\$1,863	\$1,470	\$4,888	\$671	\$265	\$415	\$1,470	\$17,153
2014										
Balance, beginning of period	\$5,657	\$513	\$623	\$1,407	\$4,293	\$655	\$313	\$384	\$2,187	\$16,032
Charge-Offs	—	—	—	—	—	—	(39)	(24)	—	(63)
Recoveries	576	613	—	—	—	—	—	10	—	1,199
Provision (benefit)	(1,099)	(556)	207	(23)	(169)	(13)	(2)	—	519	(1,136)
Balance, end of period	\$5,134	\$570	\$830	\$1,384	\$4,124	\$642	\$272	\$370	\$2,706	\$16,032
Balance, end of period:										
Individually evaluated for impairment	\$—	\$—	\$—	\$—	\$—	\$—	\$14	\$—	\$—	\$14
Balance, end of period:										
Collectively evaluated for impairment	\$5,134	\$570	\$830	\$1,384	\$4,124	\$642	\$258	\$370	\$2,706	\$16,018

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Six Months Ended June 30,	Commercial	Real estate construction one-to-four family	Real estate construction other	Real estate term owner occupied	Real estate term non-owner occupied	Real estate term other	Consumer secured by 1st deed of trust	Consumer other	Unallocated	Total
2015										
Balance, beginning of period	\$5,643	\$644	\$1,653	\$1,580	\$4,704	\$656	\$285	\$410	\$1,148	\$16,723
Charge-Offs	(107)	—	—	—	—	(81)	—	—	—	(188)
Recoveries	158	—	—	—	—	17	—	6	—	181
Provision (benefit)	(7)	45	210	(110)	184	79	(20)	(1)	322	702
Balance, end of period	\$5,687	\$689	\$1,863	\$1,470	\$4,888	\$671	\$265	\$415	\$1,470	\$17,418
Balance, end of period:										
Individually evaluated for impairment	\$265	\$—	\$—	\$—	\$—	\$—	\$—	\$—	\$—	\$265
Balance, end of period:										
Collectively evaluated for impairment	\$5,422	\$689	\$1,863	\$1,470	\$4,888	\$671	\$265	\$415	\$1,470	\$17,153
2014										
Balance, beginning of period	\$5,779	\$557	\$539	\$1,583	\$4,297	\$537	\$322	\$390	\$2,278	\$16,282
Charge-Offs	(320)	—	—	—	—	—	(39)	(33)	—	(392)
Recoveries	630	625	—	—	—	—	—	23	—	1,278
Provision (benefit)	(955)	(612)	291	(199)	(173)	105	(11)	(10)	428	(1,136)
Balance, end of period	\$5,134	\$570	\$830	\$1,384	\$4,124	\$642	\$272	\$370	\$2,706	\$16,032
Balance, end of period:										
Individually evaluated for impairment	\$—	\$—	\$—	\$—	\$—	\$—	\$14	\$—	\$—	\$14
Balance, end of period:										
Collectively evaluated for impairment	\$5,134	\$570	\$830	\$1,384	\$4,124	\$642	\$258	\$370	\$2,706	\$16,018

The following is a detail of the recorded investment in the loan portfolio, segregated by amounts evaluated individually or collectively in the Allowance at the periods indicated:

(In Thousands)	Commercial	Real estate construction one-to-four family	Real estate construction other	Real estate term owner occupied	Real estate term non-owner occupied	Real estate term other	Consumer secured by 1st deed of trust	Consumer other	Total
June 30, 2015									
Balance, end of period	\$334,181	\$38,233	\$101,683	\$111,245	\$295,613	\$38,511	\$29,328	\$30,514	\$979,308
Balance, end of period:									
Individually evaluated									
for impairment	\$14,699	\$—	\$731	\$6,002	\$4,246	\$149	\$518	\$—	\$26,345
Balance, end of period:									
Collectively evaluated									
for impairment	\$319,482	\$38,233	\$100,952	\$105,243	\$291,367	\$38,362	\$28,810	\$30,514	\$952,963
December 31, 2014									
Balance, end of period	\$306,543	\$34,842	\$91,195	\$109,472	\$286,616	\$36,894	\$32,000	\$31,493	\$929,055
Balance, end of period:									
Individually evaluated									
for impairment	\$3,976	\$191	\$772	\$1,332	\$4,346	\$150	\$530	\$—	\$11,297
Balance, end of period:									
Collectively evaluated									
for impairment	\$302,567	\$34,651	\$90,423	\$108,140	\$282,270	\$36,744	\$31,470	\$31,493	\$917,758

The following represents the balance of the Allowance for the periods indicated segregated by segment and class:

(In Thousands)	Total	Commercial	Real estate construction 1-4 family	Real estate construction other	Real estate term owner occupied	Real estate term non-owner occupied	Real estate term other	Consumer secured by 1st deeds of trust	Consumer other	Unallocated
June 30, 2015										
Individually evaluated for impairment										
AQR Substandard	\$265	\$265	\$—	\$—	\$—	\$—	\$—	\$—	\$—	\$—
Collectively evaluated for impairment:										
AQR Pass	15,602	5,385	689	1,863	1,444	4,888	667	262	404	—
	60	25	—	—	26	—	4	3	2	—

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AQR Special Mention											
AQR Substandard	21	12	—	—	—	—	—	—	9	—	
Unallocated	1,470	—	—	—	—	—	—	—	—	1,470	
	\$17,418	\$5,687	\$689	\$1,863	\$1,470	\$4,888	\$671	\$265	\$415	\$1,470	
December 31, 2014											
Individually evaluated for impairment:											
AQR Substandard	\$75	\$75	\$—	\$—	\$—	\$—	\$—	\$—	\$—	\$—	
Collectively evaluated for impairment:											
AQR Pass	14,643	4,938	644	1,653	1,382	4,703	651	278	394	—	
AQR Special Mention	832	621	—	—	198	—	5	7	1	—	
AQR Substandard	25	9	—	—	—	1	—	—	15	—	
Unallocated	1,148	—	—	—	—	—	—	—	—	1,148	
	\$16,723	\$5,643	\$644	\$1,653	\$1,580	\$4,704	\$656	\$285	\$410	\$1,148	

9. Purchased Receivables

Purchased receivables are carried at their principal amount outstanding, net of a reserve for anticipated losses that have not yet been identified, and have a maturity of less than one year. Purchased receivable balances are charged against this reserve when management believes that collection of principal is unlikely. Management evaluates the adequacy of the reserve for purchased receivable losses based on historical loss experience by class of receivable and its assessment of current economic conditions. As of June 30, 2015, the Company has one class of purchased receivables. There were no purchased receivables past due at June 30, 2015 or December 31, 2014, respectively, and there were no restructured purchased receivables at June 30, 2015 or December 31, 2014.

Income on purchased receivables is accrued and recognized on the principal amount outstanding using an effective interest method except when management believes doubt exists as to the collectability of the income or principal. As of June 30, 2015, the Company is accruing income on all purchased receivable balances outstanding.

The following table summarizes the components of net purchased receivables for the periods indicated:

(In Thousands)	June 30, 2015	December 31, 2014
Purchased receivables	\$14,295	\$15,543
Reserve for purchased receivable losses	(247)	(289)
Total	\$14,048	\$15,254

The following table sets forth information regarding changes in the purchased receivable reserve for the three and six month periods ending June 30, 2015 and 2014, respectively:

(In Thousands)	Three Months Ended June 30,		Six Months Ended June 30,	
	2015	2014	2015	2014
Balance at beginning of period	\$265	\$236	\$289	\$273
Charge-offs	—	(239)	—	(239)
Recoveries	—	3	30	3
Charge-offs net of recoveries	—	(236)	30	(236)
Reserve for (recovery from) purchased receivables	(18)	243	(72)	206
Balance at end of period	\$247	\$243	\$247	\$243

The Company did not record any charge-offs in the first six months of 2015. The Company recorded one partial charge-off for \$214,000 and one full charge-off for \$25,000 in the first six months of 2014.

10. Goodwill and Intangible Assets

The Company acquired Alaska Pacific on April 1, 2014. The Company did not record goodwill related to the acquisition of Alaska Pacific. The Company recorded a core deposit intangible of \$623,000 related to deposits acquired from Alaska Pacific that will be amortized over its estimated useful life of ten years using an accelerated method. See Note 3 above for further discussion of this transaction.

The Company acquired the remaining 76.5% of RML on December 1, 2014. The Company recorded \$14.8 million of goodwill and \$950,000 of trade name intangible as part of the acquisition of RML. These assets have indefinite useful lives and are not amortized. See Note 3 above for further discussion of this transaction.

The Company performs goodwill impairment testing annually in accordance with the policy described in Note 1 of the Company's Annual Report on Form 10-K for the year ended December 31, 2014. There was no indication of impairment as of June 30, 2015. The Company continues to monitor the Company's goodwill for potential impairment on an ongoing basis. No assurance can be given that there will not be an impairment charge to earnings during 2015 for goodwill impairment, if, for example, our stock price declines and trades at a significant discount to its book value, although there are many qualitative and quantitative factors that we analyze in determining the impairment of goodwill.

11. Deposit Activities

Total deposits at June 30, 2015 and December 31, 2014 were \$1.2 billion and \$1.2 billion, respectively. The only deposit category with stated maturity dates is certificates of deposit. At June 30, 2015, the Company had \$149.0 million in certificates of deposit as compared to certificates of deposit of \$142.2 million at December 31, 2014. At June 30, 2015, \$76.2 million, or 51%, of the Company's certificates of deposits are scheduled to mature over the next 12 months as compared to \$81.9 million, or 58%, of total certificates of deposit at December 31, 2014.

12. Derivatives

The Company enters into commercial loan interest rate swap agreements in order to provide commercial loan customers the ability to convert from variable to fixed interest rates. Under these agreements, the Company enters into a variable-rate loan agreement with a customer in addition to a swap agreement that effectively converts the customer's variable rate loan into a fixed rate. The Company then simultaneously enters into a corresponding swap agreement with a third party financial institution ("counterparty") in order to offset its exposure on the fixed component of the customer's interest rate swap. The Company has an agreement with its counterparty that contains a provision that provides that if the Company fails to maintain its status as a well-capitalized institution, then the counterparty could terminate the derivative positions and the Company would be required to settle its obligations under the agreement. This agreement also requires that the Company and the counterparty collateralize any fair value shortfalls that exceed \$250,000 with eligible collateral, which includes cash and securities backed with the full faith and credit of the federal government. Similarly, the Company could be required to settle its obligations under the agreement if specific regulatory events occur, such as if the Company were issued a prompt corrective action directive or a cease and desist order, or if certain regulatory ratios fall below specified levels. The Company pledged \$262,000 and zero in available for sale securities to collateralize fair value shortfalls on interest rate swap agreements as of June 30, 2015 and December 31, 2014, respectively.

The interest rate swap agreements with our customers and the counterparty are not designated as hedging instruments under the Derivatives and Hedging topic of the FASB ASC 815, rather they are accounted for as free standing derivatives with changes in fair value reported in income. The Company had interest rate swaps with an aggregate notional amount of \$22.5 million and \$23.6 million at June 30, 2015 and December 31, 2014, respectively. At June 30, 2015, the notional amount of interest rate swaps is made up of two swaps totaling \$11.2 million, a variable to fixed rate swap to a commercial loan customer and two swaps totaling \$11.2 million fixed to variable rate swap with a counterparty. Changes in fair value from these four interest rate swaps offset each other in the second quarter of 2015. The Company did not recognize any fee income related to interest rate swaps in the three month and six month periods ending June 30, 2015 or 2014, respectively. Interest rate swap income is recorded in other income on the Consolidated Statements of Income.

The Company also uses derivatives to hedge the risk of changes in the fair values of interest rate lock commitments. None of the Company's derivatives are designated as hedging instruments. Rather, they are accounted for as free-standing derivatives, or economic hedges, with changes in the fair value of the derivatives reported in income. The Company primarily utilizes forward interest rate contracts in its derivative risk management strategy.

RML enters into commitments to originate residential mortgage loans, and it enters into forward delivery contracts to sell mortgage-backed securities to broker/dealers at specific prices and dates in order to hedge the interest rate risk in its residential mortgage loan commitments. Market risk with respect to commitments to originate loans arises from changes in the value of contractual positions due to changes in interest rates. RML had commitments to originate mortgage loans held for sale totaling \$87.5 million and \$39.6 million at June 30, 2015 and December 31, 2014, respectively. Changes in the value of RML's interest rate derivatives are recorded in the mortgage banking income on the Consolidated Statements of Income.

The following table presents the fair value of derivatives not designated as hedging instruments at June 30, 2015 and December 31, 2014:

(In Thousands)	Asset Derivatives		
	Balance Sheet Location	June 30, 2015 Fair Value	December 31, 2014 Fair Value
Interest rate contracts	Other assets	\$86	\$78
Interest rate lock commitments	Other assets	1,487	841
Total		\$1,573	\$919
(In Thousands)	Liability Derivatives		
	Balance Sheet Location	June 30, 2015 Fair Value	December 31, 2014 Fair Value
Interest rate contracts	Other liabilities	\$125	\$158

The following table presents the gains of derivatives not designated as hedging instruments for the six month period ending June 30, 2015:

(In Thousands)	Income Statement Location	June 30, 2015
Interest rate contracts	Mortgage banking income	\$508

13. Stock Incentive Plan

The Company adopted the 2014 Stock Option Plan ("2014 Plan") following shareholder approval of the 2014 Plan at the 2014 Annual Meeting. Subsequent to the adoption of the 2014 Plan, no additional grants may be issued under the prior plans. The 2014 Plan provides for grants of up to 350,000 shares of common stock.

Stock Options: Under the 2014 Plan and previous plans, certain key employees have been granted the option to purchase set amounts of common stock at the market price on the day the option was granted. Optionees, at their own discretion, may cover the cost of exercise through the exchange at the then fair value of already owned shares of the Company's stock. Options are granted for a 10-year period and vest on a pro-rata basis over the initial three years from grant.

The Company measures the fair value of each stock option at the date of grant using the Black-Scholes option pricing model. For the quarters ended June 30, 2015 and 2014, the Company recognized \$22,000 and \$16,000, respectively, in stock option compensation expense as a component of salaries and other personnel expense. For the six months ended June 30, 2015 and 2014, the Company recognized \$44,000 and \$32,000, respectively, in stock option compensation expense as a component of salaries and other personnel expense.

The Company issued 224 shares from the exercise of stock options in the three and six months ended June 30, 2015, respectively. Proceeds from the exercise of stock options in the three and six months ended June 30, 2015 were \$49,000, respectively. The Company withheld \$49,000 to pay for stock option exercises or income taxes that resulted from the exercise of stock options in the three and six months ended June 30, 2015, respectively.

Proceeds from the exercise of stock options in the three and six months ended June 30, 2014 were \$64,000, respectively. The Company withheld no funds to pay for stock option exercises or income taxes that resulted from the exercise of stock options in the three and six months ended June 30, 2014, respectively.

There were no stock options granted in the second quarter of 2015.

Restricted Stock Units: The Company grants restricted stock units to certain key employees periodically. Recipients of restricted stock units do not pay any cash consideration to the Company for the shares and receive all dividends with respect to

such shares when the shares vest. Restricted stock units cliff vest at the end of a three-year time period. For the three months ended June 30, 2015 and 2014, the Company recognized \$97,000 and \$66,000, respectively, in restricted stock unit compensation expense as a component of salaries and other personnel expense. For the six months ended June 30, 2015 and 2014, the Company recognized \$193,000 and \$157,000, respectively, in restricted stock unit compensation expense as a component of salaries and other personnel expense.

There were no restricted stock units granted in the second quarter of 2015.

14. Fair Value of Assets and Liabilities

The Company groups its assets and liabilities measured at fair value in three levels, based on the markets in which the assets and liabilities are traded and the reliability of the assumptions used to determine fair value. These levels are:

Level 1: Valuation is based upon quoted prices for identical instruments traded in active exchange markets, such as the New York Stock Exchange. Valuations are obtained from readily available pricing sources for market transactions involving identical assets or liabilities.

- Level 2: Valuation is based upon quoted market prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-based valuation techniques for which all significant assumptions are observable in the market.

- Level 3: Valuation is generated from model-based techniques that use significant assumptions not observable in the market. These unobservable assumptions reflect the Company's estimation of assumptions that market participants would use in pricing the asset or liability. Valuation techniques include use of option pricing models, discounted cash flow models and similar techniques.

The following methods and assumptions were used to estimate fair value disclosures. All financial instruments are held for other than trading purposes.

Cash and cash equivalents: Due to the short term nature of these instruments, the carrying amounts reported in the balance sheet represent their fair values.

Investment securities: Fair values for investment securities are based on quoted market prices, where available. If quoted market prices are not available, fair values are based on quoted market prices of comparable instruments. Investments in Federal Home Loan Bank stock are recorded at cost, which also represents fair value.

Loans held for sale: Due to the short term nature of these instruments, the carrying amounts reported in the balance sheet approximate their fair values.

Loans: Fair values were generally determined by discounting both principal and interest cash flows on pools of loans expected to be collected using a discount rate for similar instruments with adjustments that the Company believes a market participant would consider in determining fair value. The Company estimates the cash flows expected to be collected using internal credit risk, interest rate and prepayment risk models that incorporate the Corporation's best estimate of current key assumptions, such as default rates, loss severity and prepayment speeds for the life of the loan. The carrying value of loans is presented net of the Allowance (see Note 8). Impaired loans are carried at fair value. Specific valuation allowances are included in the Allowance.

Purchased receivables: Fair values for purchased receivables are based on their carrying amounts due to their short duration and repricing frequency. Generally, purchased receivables have a duration of less than one year.

Mortgage servicing rights: MSR are measured at fair value on a recurring basis. These assets are classified as Level 3. In order to determine the fair value of MSRs, the present value of net expected future cash flows is estimated.

Assumptions used include market discount rates, anticipated prepayment speeds, escrow calculations, delinquency rates, and ancillary fee income net of servicing costs. The model assumptions are also compared to publicly filed information from several large MSR holders, as available.

Accrued interest receivable: Due to the short term nature of these instruments, the carrying amounts reported in the balance sheet represent their fair values.

Deposits: The fair value for deposits with stated maturities was determined by discounting contractual cash flows using current market rates for instruments with similar maturities. For deposits with no stated maturities, the carrying value was considered to

approximate fair value and does not take into account the significant value of the cost advantage and stability of the Company's long-term relationships with depositors.

Accrued interest payable: Due to the short term nature of these instruments, the carrying amounts reported in the balance sheet represent their fair values.

Securities sold under repurchase agreements: Fair values for securities sold under repurchase agreements are based on their carrying amounts due to their short duration and repricing frequency.

Borrowings: Due to the short term nature of these instruments, the carrying amount of short-term borrowings reported in the balance sheet approximate the fair value. Fair values for long-term borrowings are estimated using a discounted cash flow calculation that applies currently offered interest rates to a schedule of aggregate expected monthly payments.

Contingent liability, earn-out payments related to acquisition of RML: The contingent liability for estimated earn-out payments included as a portion of the purchase price for RML is recorded in the balance sheet at its estimated fair value, and fair value adjustments to the liability are reported in other operating expense. The fair value for this contingent liability is estimated based on management's assessment of expected pre-tax income at RML over the remaining earn out period. These cash flows are discounted to present value using the appropriate FHLB borrowing rate. Inputs to this assessment include the general economic conditions in our markets that impact mortgage loan originations, current and anticipated trends in local market demand for mortgage, including interest rates, and RML's estimated market share.

Junior subordinated debentures: Fair value adjustments for junior subordinated debentures are based on discounted cash flows to maturity using current interest rates for similar financial instruments. Management utilized a market approach to determine the appropriate discount rate for junior subordinated debentures.

Derivative instruments: The fair value of the interest rate lock commitments are estimated using quoted or published market prices for similar instruments, adjusted for factors such as pull-through rate assumptions based on historical information, where appropriate. The pull-through rate assumptions are considered Level 3 valuation inputs and are significant to the interest rate lock commitment valuation; as such, the interest rate lock commitment derivatives are classified as Level 3. Interest rate contracts are valued in a model, which uses as its basis a discounted cash flow technique incorporating credit valuation adjustments to reflect nonperformance risk in the measurement of fair value. Although the Bank has determined that the majority of inputs used to value its interest rate derivatives fall within Level 2 of the fair value hierarchy, the credit valuation adjustments associated with its derivatives utilize Level 3 inputs, such as estimates of current credit spreads to evaluate the likelihood of default by itself and its counterparties. However, as of June 30, 2015, the Bank has assessed the significance of the impact of these adjustments on the overall valuation of its interest rate positions and has determined that they are not significant to the overall valuation of its interest rate derivatives. As a result, the Bank has classified its interest rate derivative valuations in Level 2 of the fair value hierarchy.

Assets subject to nonrecurring adjustment to fair value: The Company is also required to measure certain assets such as equity method investments, goodwill, intangible assets, impaired loans, and other real estate owned ("OREO") at fair value on a nonrecurring basis in accordance with GAAP. Any nonrecurring adjustments to fair value usually result from the write down of individual assets.

The Company uses either in-house evaluations or external appraisals to estimate the fair value of OREO and impaired loans as of each reporting date. In-house appraisals are considered Level 3 inputs and external appraisals are considered Level 2 inputs. The Company's determination of which method to use is based upon several factors. The Company takes into account compliance with legal and regulatory guidelines, the amount of the loan, the size of the assets, the location and type of property to be valued and how critical the timing of completion of the analysis is to the assessment of value. Those factors are balanced with the level of internal expertise, internal experience and market information available, versus external expertise available such as qualified appraisers, brokers, auctioneers and equipment specialists.

The Company uses external sources to estimate fair value for projects that are not fully constructed as of the date of valuation. These projects are generally valued as if complete, with an appropriate allowance for cost of completion, including contingencies developed from external sources such as vendors, engineers and contractors. The Company

believes that recording other real estate owned that is not fully constructed based on as if complete values is more appropriate than recording other real estate owned that is not fully constructed using as is values. We concluded that as-is-complete values are appropriate for these types of projects based on the accounting guidance for capitalization of project costs and subsequent measurement of the value of real estate. GAAP specifically states that estimates and cost allocations must be reviewed at the end of each reporting period and reallocated based on revised estimates. The Company adjusts the carrying value of other real estate owned in accordance

with this guidance for increases in estimated cost to complete that exceed the fair value of the real estate at the end of each reporting period.

Commitments to extend credit and standby letters of credit: The fair value of commitments is estimated using the fees currently charged to enter into similar agreements, taking into account the remaining terms of the agreements and the present creditworthiness of the counterparties. For fixed-rate loan commitments, fair value also considers the difference between current levels of interest rates and the committed rates. The fair value of letters of credit is based on fees currently charged for similar agreements or on the estimated cost to terminate them or otherwise settle the obligation with the counterparties at the reporting date.

Limitations: Fair value estimates are made at a specific point in time, based on relevant market information and information about the financial instrument. These estimates do not reflect any premium or discount that could result from offering for sale at one time the Company's entire holdings of a particular financial instrument. Because no market exists for a significant portion of the Company's financial instruments, fair value estimates are based on judgments regarding future expected loss experience, current economic conditions, risk characteristics of various financial instruments, and other factors. These estimates are subjective in nature and involve uncertainties and matters of significant judgment and therefore cannot be determined with precision. Changes in assumptions could significantly affect the estimates.

Estimated fair values as of the periods indicated are as follows:

(In Thousands)	June 30, 2015		December 31, 2014	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Financial assets:				
Level 1 inputs:				
Cash, due from banks and deposits in other banks	\$104,071	\$104,071	\$72,056	\$72,056
Investment securities	29,214	29,214	45,570	45,570
Level 2 inputs:				
Investment securities	198,851	198,925	238,361	238,468
Investment in Federal Home Loan Bank stock	1,817	1,817	3,404	3,404
Accrued interest receivable	3,399	3,399	3,373	3,373
Interest rate contracts	86	86	78	78
Level 3 inputs:				
Loans and loans held for sale, net	1,031,024	1,031,375	951,647	957,643
Purchased receivables, net	14,048	14,048	15,254	15,254
Interest rate lock commitments	1,487	1,487	841	841
Mortgage servicing rights	942	942	1,010	1,010
Financial liabilities:				
Level 2 inputs:				
Deposits	\$1,238,717	\$1,238,771	\$1,179,747	\$1,180,136
Securities sold under repurchase agreements	17,895	17,895	19,843	19,843
Borrowings	22,309	22,306	26,304	26,485
Accrued interest payable	53	53	18	18
Interest rate contracts	125	125	158	158
Level 3 inputs:				
RML earn-out liability	9,459	9,459	7,324	7,324
Junior subordinated debentures	18,558	16,657	18,558	17,239
Unrecognized financial instruments:				
Commitments to extend credit ⁽¹⁾	\$235,388	\$2,354	\$219,349	\$2,193
Standby letters of credit ⁽¹⁾	6,070	61	6,004	60

⁽¹⁾ Carrying amounts reflect the notional amount of credit exposure under these financial instruments.

The following table sets forth the balances as of the periods indicated of assets measured at fair value on a recurring basis:

(In Thousands)	Total	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
June 30, 2015				
Assets:				
Available for sale securities				
U.S. Treasury and government sponsored entities	\$173,245	\$15,150	\$158,095	\$—
Municipal securities	11,373	—	11,373	—
U.S. Agency mortgage-backed securities	926	—	926	—
Corporate bonds	39,297	13,037	26,260	—
Preferred stock	1,027	1,027	—	—
Total available for sale securities	\$225,868	\$29,214	\$196,654	\$—
Interest rate contracts	\$86	\$—	\$86	\$—
Interest rate lock commitments	1,487	—	—	1,487
Mortgage servicing rights	942	—	—	942
Total other assets	\$2,515	\$—	\$86	\$2,429
Liabilities:				
Interest rate contracts	\$125	\$—	\$125	\$—
December 31, 2014				
Assets:				
Available for sale securities				
U.S. Treasury and government sponsored entities	\$226,190	\$15,545	\$210,645	\$—
Municipal securities	12,124	—	12,124	—
U.S. Agency mortgage-backed securities	1,029	—	1,029	—
Corporate bonds	39,235	26,873	12,362	—
Preferred stock	3,152	3,152	—	—
Total available for sale securities	\$281,730	\$45,570	\$236,160	\$—
Interest rate contracts	\$78	\$—	\$78	\$—
Interest rate lock commitments	841	—	—	841
Mortgage servicing rights	1,010	—	—	1,010
Total other assets	\$1,929	\$—	\$78	\$1,851
Liabilities:				
Interest rate contracts	\$158	\$—	\$158	\$—

As of and for the six months ending June 30, 2015 and 2014, no impairment or valuation adjustment was recognized for assets recognized at fair value on a nonrecurring basis, except for certain assets as shown in the following table. For loans measured for impairment, the Company classifies fair value measurements using observable inputs, such as external appraisals, as Level 2 valuations in the fair value hierarchy, and unobservable inputs, such as in-house evaluations, as Level 3 valuations in the fair value hierarchy.

(In Thousands)	Total	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total (gains) losses
June 30, 2015					
Loans measured for impairment	\$2,544	\$—	\$318	\$2,226	\$190
Other real estate owned	649	—	—	649	268
Total	\$3,193	\$—	\$318	\$2,875	\$458
June 30, 2014					
Loans measured for impairment	\$349	\$—	\$—	\$349	\$2
Other real estate owned	227	—	—	227	45
Total	\$576	\$—	\$—	\$576	\$47

Assets and Liabilities Measured at Fair Value Using Significant Unobservable Inputs (Level 3)

The following table provides a description of the valuation technique, unobservable input, and qualitative information about the unobservable inputs for the Company's assets and liabilities classified as Level 3 and measured at fair value on a nonrecurring basis at June 30, 2015:

Financial Instrument	Valuation Technique	Unobservable Input	Weighted Average Rate Range
Loans measured for impairment	In-house valuation of real estate; discounted cash flow	Discount rate	25% - 100%
		Cash flows	NA ⁽¹⁾
Other real estate owned	Fair value of collateral	Estimated selling and holding costs	7% - 25%
Interest rate lock commitment	External pricing model	Pull through rate	92.8 %
Mortgage servicing rights	Discounted cash flow	Constant prepayment rate	9.95% - 25.77%
		Discount rate	9.25% - 10%
RML earn-out liability	Discounted cash flow	Financial projections of mortgage operations	0.47% - 1.99%

⁽¹⁾ Fair value of impaired collateral dependent loans was calculated using contractual cash flows for specific impaired loan.

15. Segment Information

The Company operates two primary segments: Community Banking and Home Mortgage Lending. The Community Banking segment's principal business focus is the offering of loan and deposit products to business and consumer customers in its primary market areas. As of June 30, 2015, the Community Banking segment operated 14 branches throughout Alaska. The Home Mortgage Lending segment's principal business focus is the origination and sale of mortgage loans for 1-4 family residential properties.

Prior to December 1, 2014, Home Mortgage Lending income was limited to equity in earnings from RML.

Summarized financial information for the Company's reportable segments and the reconciliation to the consolidated financial results is shown in the following tables:

(In Thousands)	Three Months Ended June 30, 2015		
	Community Banking	Home Mortgage Lending	Consolidated
Interest income	\$14,354	\$589	\$14,943
Interest expense	370	378	748
Net interest income	13,984	211	14,195
Provision (benefit) for loan losses	376	—	376
Other operating income	3,724	7,839	11,563
Other operating expense	12,017	5,736	17,753
Income before provision for income taxes	5,315	2,314	7,629
Provision for income taxes	1,730	956	2,686
Net income	3,585	1,358	4,943
Less: net income attributable to the noncontrolling interest	162	—	162
Net income attributable to Northrim BanCorp, Inc.	\$3,423	\$1,358	\$4,781

(In Thousands)	Six Months Ended June 30, 2015		
	Community Banking	Home Mortgage Lending	Consolidated
Interest income	\$28,344	\$985	\$29,329
Interest expense	844	658	1,502
Net interest income	27,500	327	27,827
Provision (benefit) for loan losses	702	—	702
Other operating income	6,976	15,122	22,098
Other operating expense	25,341	10,873	36,214
Income before provision for income taxes	8,433	4,576	13,009
Provision for income taxes	2,543	1,890	4,433
Net income	5,890	2,686	8,576
Less: net income attributable to the noncontrolling interest	234	—	234
Net income attributable to Northrim BanCorp, Inc.	\$5,656	\$2,686	\$8,342

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(In Thousands)	Three Months Ended June 30, 2014		Consolidated
	Community Banking	Home Mortgage Lending	
Interest income	\$13,895	\$—	\$13,895
Interest expense	484	—	484
Net interest income	13,411	—	13,411
Provision (benefit) for loan losses	(1,136	) —	(1,136
Other operating income (loss)	3,751	355	4,106
Other operating expense	11,620	—	11,620
Income before provision for income taxes	6,678	355	7,033
Provision for income taxes	2,423	146	2,569
Net income (loss)	4,255	209	4,464
Less: net income attributable to the noncontrolling interest	95	—	95
Net income (loss) attributable to Northrim BanCorp, Inc.	\$4,160	\$209	\$4,369

(In Thousands)	Six Months Ended June 30, 2014		Consolidated
	Community Banking	Home Mortgage Lending	
Interest income	\$25,568	\$—	\$25,568
Interest expense	924	—	924
Net interest income	24,644	—	24,644
Provision (benefit) for loan losses	(1,136	) —	(1,136
Other operating income (loss)	6,616	224	6,840
Other operating expense	21,588	—	21,588
Income before provision for income taxes	10,808	224	11,032
Provision for income taxes	3,774	92	3,866
Net income (loss)	7,034	132	7,166
Less: net income attributable to the noncontrolling interest	139	—	139
Net income (loss) attributable to Northrim BanCorp, Inc.	\$6,895	\$132	\$7,027

June 30, 2015			
(In Thousands)	Community Banking	Home Mortgage Lending	Consolidated
Total assets	\$1,411,506	\$88,825	\$1,500,331
Loans held for sale	\$—	\$73,593	\$73,593
Borrowings	\$2,142	\$20,167	\$22,309

December 31, 2014

(In Thousands)	Community Banking	Home Mortgage Lending	Consolidated
Total assets	\$1,391,862	\$57,487	\$1,449,349
Loans held for sale	\$—	\$43,866	\$43,866
Borrowings	\$2,164	\$24,140	\$26,304

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

This discussion should be read in conjunction with the unaudited consolidated financial statements of Northrim BanCorp, Inc. (the "Company") and the notes thereto presented elsewhere in this report and with the Company's Annual Report on Form 10-K for the year ended December 31, 2014.

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

Note Regarding Forward Looking-Statements

This quarterly report on Form 10-Q includes "forward-looking statements," as that term is defined for purposes of Section 21D of the Securities Exchange Act of 1934, as amended, which are not historical facts. These forward-looking statements describe management's expectations about future events and developments such as future operating results, growth in loans and deposits, continued success of the Company's style of banking, and the strength of the local economy. All statements other than statements of historical fact, including statements regarding industry prospects and future results of operations or financial position, made in this report are forward-looking. We use words such as "anticipate," "believe," "expect," "intend" and similar expressions in part to help identify forward-looking statements. Forward-looking statements reflect management's current plans and expectations and are inherently uncertain. Our actual results may differ significantly from management's expectations, and those variations may be both material and adverse. Forward-looking statements are subject to various risks and uncertainties that may cause our actual results to differ materially and adversely from our expectations as indicated in the forward-looking statements. These risks and uncertainties include: the general condition of, and changes in, the Alaska economy; factors that impact our net interest margin; our ability to maintain asset quality and expand our market share or net interest margin; financial benefits from the acquisition of Residential Mortgage Holding Company, LLC might not be realized within the expected timeframes and costs or difficulties relating to integration matters might be greater than expected; and our ability to execute our business plan. Further, actual results may be affected by competition on price and other factors with other financial institutions; customer acceptance of new products and services; the regulatory environment in which we operate; and general trends in the local, regional and national banking industry and economy. Many of these risks, as well as other risks that may have a material adverse impact on our operations and business, are identified in Part II. Item 1A Risk Factors of this report and Item 1A in the Company's Annual Report on form 10-K for the year ended December 31, 2014, as well as in our other filings with the Securities and Exchange Commission. However, you should be aware that these factors are not an exhaustive list, and you should not assume these are the only factors that may cause our actual results to differ from our expectations. In addition, you should note that we do not intend to update any of the forward-looking statements or the uncertainties that may adversely impact those statements, other than as required by law.

Critical Accounting Policies

The preparation of the consolidated financial statements requires us to make a number of estimates and assumptions that affect the reported amounts and disclosures in the consolidated financial statements. On an ongoing basis, we evaluate our estimates and assumptions based upon historical experience and various other factors and circumstances. We believe that our estimates and assumptions are reasonable; however, actual results may differ significantly from these estimates and assumptions which could have a material impact on the carrying value of assets and liabilities at the balance sheet dates and on our results of operations for the reporting periods.

The accounting policies that involve significant estimates and assumptions by management, which have a material impact on the carrying value of certain assets and liabilities, are considered critical accounting policies. The Company's critical accounting policies include those that address the accounting for the allowance for loan losses ("Allowance"), valuation of goodwill and other intangible assets, and the valuation of other real estate owned. These critical accounting policies are further described in Item 7,

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Management's Discussion and Analysis, and in Note 1, Summary of Significant Accounting Policies, of the Notes to Consolidated Financial Statements in the Company's Form 10-K for the year ended December 31, 2014. Management has applied its critical accounting policies and estimation methods consistently in all periods presented in these consolidated financial statements.

Update on Economic Conditions

The Company believes that the Alaskan state economy continues to demonstrate stability despite declines in global energy prices. Although revenues tied to the state's energy industry are a significant contributor to the state government's budget, the Alaska state government has significant resources, both in its reserve funds and the Alaska Permanent Fund, which the Company believes will help finance expected state government funding gaps for the next couple of years. North Slope investment and operating activity is at record levels despite low oil prices, which the Company believes reflect the long-term nature of these conventional oil projects. Overall North Slope capital investments are estimated at \$4.45 billion this year and are expected to increase to \$4.88 billion in 2016, according to figures given by companies to the Alaska State Department of Revenue. The projected years are based in state fiscal years, with the current fiscal year 2015 starting last July 1 and fiscal year 2016 beginning this July 1. By comparison, the industry spent \$3.73 billion for capital projects in 2014, the fiscal year ending last June 30.

Highlights and Summary of Performance - Second Quarter of 2015

Year over year loan growth of 5% and deposit growth of 10%, increased net interest income, and continued solid credit quality contributed to increases in net income in the three and six month periods ending June 30, 2015 as compared to the same periods in 2014. The integration of the assets and operations acquired by the Company in connection with the acquisitions of Alaska Pacific Bancshares, Inc. ("Alaska Pacific") and Residential Mortgage Holding Company, LLC ("RML"), that were completed in 2014 also contributed to these increases. Additionally, management determined that as a result of the acquisition of RML, the Company now operates two business segments: Community Banking and Home Mortgage Lending, with RML's operations falling under the Home Mortgage Lending segment. See Note 15 of the Notes to Consolidated Financial Statements included in Item 1 of this report for further discussion on our business segments and results of operations for each such business segment. Year-to-date profits increased 19% to \$8.3 million, or \$1.20 per diluted share at June 30, 2015, from \$7.0 million, or \$1.04 per diluted share at June 30, 2014.

Total revenues, which include net interest income plus other operating income, were \$25.8 million in the second quarter of 2015, a 47% increase from total revenues of \$17.5 million in the second quarter a year ago.

Net interest income increased 6% to \$14.2 million in the second quarter of 2015, compared to \$13.4 million in the quarter ended June 30, 2014.

Return on average assets was 1.33% and return on average equity was 11.46% at June 30, 2015, as compared to 1.30% and 11.21% at June 30, 2014, respectively.

Average portfolio loans increased 5% to \$967.0 million for the second quarter of 2015 as compared to \$924.9 million for the second quarter of 2014, reflecting organic loan growth.

Net interest margin improved to 4.44% in the second quarter of 2015 as compared to 4.43% in the second quarter of 2014 and 4.41% in the first six months of 2015 as compared to 4.36% for the first six months of 2014, mainly reflecting the increased yield on earning assets and a stable cost of funds.

Northrim paid a quarterly cash dividend of \$0.18 per share in June of 2015, compared to the \$0.17 per share dividend paid in June 2014. The dividend provides a yield of approximately 2.8% at current market share prices.

Tangible book value¹ was \$21.47 per share at June 30, 2015 as compared to \$20.48 per share at December 31, 2014.

Tangible book value is a non-GAAP ratio that represents total shareholders' equity less goodwill and intangible assets divided by the number of shares outstanding. Although we believe this non-GAAP financial measure is frequently used by stakeholders in the evaluation of companies in the banking industry, there are limitations, it is not required to be uniformly applied, and it is not audited. The most comparable GAAP measure of book value per share consists of total shareholders' equity divided by the number of shares outstanding, which was \$24.96 at June 30, 2015, compared to \$23.99 at December 31, 2014.

The Company remains well-capitalized with Tier 1 Capital to Risk Adjusted Assets at June 30, 2015, of 12.67%, compared to 13.06% at December 31, 2014. The decrease in Tier 1 Capital to Risk Adjusted Assets at June 30, 2015

is a result of the new BASEL III requirements.

Tangible common equity to tangible assets² was 9.97% at June 30, 2015, compared to 9.85% December 31, 2014. Tangible common equity to tangible assets is a non-GAAP ratio that represents total equity less goodwill and intangible assets divided by total assets less goodwill and intangible assets. Although we believe this non-GAAP financial measure is frequently used by stakeholders in the evaluation of companies in the banking industry, there are limitations, it is not required to be uniformly applied, and it is not audited.

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The most comparable GAAP measure of equity to assets consists of total equity divided by total assets. Total equity to total assets was 11.40% at June 30, 2015 as compared to 11.35% at December 31, 2014.

¹ Tangible book value is a non-GAAP measure defined as shareholders' equity, less intangible assets, divided by shares outstanding. The reconciliation of tangible book value per share to book value per share is shown in the table below:

(In thousands, except per share data)	June 30, 2015	December 31, 2014
Total shareholders' equity	\$171,082	\$164,441
Divided by common shares outstanding	6,854,413	6,854,189
Book value per share	\$24.96	\$23.99

(In thousands, except per share data)	June 30, 2015	December 31, 2014
Total shareholders' equity	\$171,082	\$164,441
Less: goodwill and intangible assets, net	23,889	24,035
	\$147,193	\$140,406
Divided by common shares outstanding	6,854,413	6,854,189
Tangible book value per share	\$21.47	\$20.48

² Tangible common equity to tangible assets is a non-GAAP ratio that represents total equity less goodwill and intangible assets divided by total assets less goodwill and intangible assets. This ratio has received more attention over the past several years from stock analysts and regulators. The most comparable GAAP measure of common equity to assets is calculated by dividing total equity by total assets. The reconciliation of total shareholders' equity to tangible common shareholders' equity (non-GAAP) and total assets to tangible assets is shown in the table below:

(In Thousands)	June 30, 2015	December 31, 2014	
Total shareholders' equity	\$171,082	\$164,441	
Less: goodwill and other intangible assets, net	23,889	24,035	
Tangible common shareholders' equity	\$147,193	\$140,406	
Total assets	\$1,500,331	\$1,449,349	
Less: goodwill and other intangible assets, net	23,889	24,035	
Tangible assets	\$1,476,442	\$1,425,314	
Tangible common equity ratio	9.97	% 9.85	%

The Company reported net income and diluted earnings per share of \$4.8 million and \$0.69, respectively, for the second quarter of 2015 compared to net income and diluted earnings per share of \$4.4 million and \$0.63, respectively, for the second quarter of 2014. The Company reported net income and diluted earnings per share of \$8.3 million and \$1.20, respectively, year to date as of June 30, 2015 compared to net income and diluted earnings per share of \$7.0 million and \$1.04, respectively, for the same period in 2014. The increase in net income for both of these periods in 2015 as compared to the same periods of 2014 was primarily the result of mortgage banking income recognized from RML's home mortgage lending operations combined with increased interest and fees on loans. The increase in interest and fees on loans in both the three and six month periods ending June 30, 2015 is the result of organic loan growth, and the acquisition of Alaska Pacific on April 1, 2014 also contributed to this increase for the six month period ending June 30, 2015 as compared to the same period in 2014. These increases were partially offset by increased operating expenses primarily resulting from the acquisitions of RML and Alaska Pacific as well as expense recorded in connection with the change in fair value of our earn-out liability associated with the acquisition of RML. Additionally, the increases in other operating income and net interest income for these periods in 2015 as compared to the same periods in 2014 were partially offset by a loan loss provision of \$702,000 recorded for the first six months of 2015 compared to a \$1.1 million benefit for loan losses recorded in the same period of 2014 due to net recoveries in 2014 that led to a negative loan loss provision.

The Company's total assets were \$1.5 billion and \$1.4 billion at June 30, 2015 and December 31, 2014, respectively. Increases in loans and loans held for sale were partially offset by decreases in investment securities available for sale. Net loans increased to \$957.4 million at June 30, 2015 as compared to \$907.8 million at December 31, 2014 due to increases in commercial, commercial real estate, and construction loans in the first six months of 2015.

Credit Quality

Nonperforming assets: Nonperforming assets at June 30, 2015 decreased \$1.5 million, or 16% to \$7.8 million as compared to \$9.3 million at December 31, 2014. Nonaccrual loans increased \$366,000 to \$5.0 million and total other real estate owned ("OREO") decreased \$1.8 million to \$2.8 million at June 30, 2015 as compared to \$4.7 million and \$4.6 million at December 31, 2014, respectively. Nonperforming purchased receivables were zero at June 30, 2015 and December 31, 2014, respectively. Government guarantees included in nonperforming assets totaled \$1.6 million at June 30, 2015 as compared to \$2.1 million at December 31, 2014. These represent the portion of nonperforming assets that are guaranteed by governmental agencies including the Small Business Administration, the United States Department of Agriculture, the Bureau of Indian Affairs, and the Alaska Industrial Development and Export Authority.

The following table summarizes OREO activity for the three and six month periods ending June 30, 2015 and 2014:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2015	2014	2015	2014
	(In Thousands)			
Balance, beginning of the period	\$4,209	\$3,443	\$4,607	\$2,402
Transfers from loans	156	21	337	1,158
Transfers from premises and equipment	—	—	—	904
Acquired from Alaska Pacific	—	1,709	—	1,709
Proceeds from the sale of other real estate owned	(1,660)	(305)	(1,971)	(1,599)
Gain on sale of other real estate owned, net	136	74	136	368
Deferred gain on sale of other real estate owned	(34)	—	(34)	—
Impairment on other real estate owned	—	(45)	(268)	(45)
Balance at end of period	\$2,807	\$4,897	\$2,807	\$4,897

Potential problem loans: Potential problem loans are loans which are currently performing that have developed negative indications that the borrower may not be able to comply with present payment terms and which may later be included in nonaccrual, past due, or impaired loans. At June 30, 2015, management had identified potential problem loans of \$16.6 million as compared to potential problem loans of \$18.0 million at December 31, 2014.

Troubled debt restructurings ("TDRs"): TDRs are those loans for which concessions, including the reduction of interest rates below a rate otherwise available to that borrower, have been granted due to the borrower's weakened financial condition. Interest on TDRs will be accrued at the restructured rates when it is anticipated that no loss of original principal will occur, and the interest can be collected, which is generally after a period of six months. The Company had \$5.7 million in loans classified as TDRs that were performing and \$3.2 million in TDRs included in nonaccrual loans at June 30, 2015 for a total of approximately \$9.0 million. At December 31, 2014 there were \$5.4 million in loans classified as TDRs that were performing and \$2.3 million in TDRs included in nonaccrual loans for a total of \$7.7 million. See Note 6 of the Notes to Consolidated Financial Statements included in Item 1 of this report for further discussion of TDRs.

RESULTS OF OPERATIONS

Income Statement

Net Income

Net income attributable to the Company for the second quarter of 2015 increased \$412,000, or 9%, to \$4.8 million as compared to \$4.4 million for the same period in 2014. Net income attributable to the Company for the six months ended June 30, 2015 increased \$1.3 million, or 19%, to \$8.3 million as compared to the same period in 2014. The increases in net income for the three and six month periods ending June 30, 2015 as compared to the same periods in 2014 was primarily due to the acquisition of the remaining 76.5% of RML in the fourth quarter of 2014, the acquisition of Alaska Pacific in the second quarter of 2014, as well as organic loan growth.

Net Interest Income / Net Interest Margin

Net interest income for the second quarter of 2015 increased \$784,000, or 6%, to \$14.2 million as compared to \$13.4 million for the second quarter in 2014. Net interest income increased \$3.2 million, or 13%, to \$27.8 million in the first six months of 2015 as compared to \$24.6 million for the same period in 2014. The Company's tax-equivalent net interest margin, calculated as net interest income as a percentage of average interest-earning assets on a tax equivalent basis increased by 1 and 5 basis points to 4.44% and 4.41% for the three and six month periods ending June 30, 2015, respectively, as compared to the same periods in 2014. Tax equivalent net interest margin is a non-GAAP measure subject to limitations. Although we believe this non-GAAP financial measure is frequently used by stakeholders in the evaluation of companies in the banking industry, it is not required to be uniformly applied and it is not audited. For the reconciliation to the most comparable GAAP measure of net interest margin see "Components of Net Interest Margin" beginning on page 46 of this report. The increase in net interest income in the second quarter of 2015 as compared to the second quarter of 2014 is primarily the result of increased average loan balances, partially offset by increases in both volume and cost for interest-bearing liabilities. The increase in both net interest income and the tax-equivalent net interest margin in the six month period ended June 30, 2015 as compared to 2014 is primarily the result of increased average loan balances, partially offset by decreased yield on loans and increases in both volume and cost for interest-bearing liabilities.

Average loans, the largest category of interest-earning assets, increased by \$42.1 million, or 5% to \$967.0 million in the three-month period ending June 30, 2015, and increased \$108.6 million, or 13% to \$956.6 million in the six-month period ending June 30, 2015, as compared to the same periods in 2014, respectively. Total interest income from loans increased \$607,000 for the second quarter of 2015 and increased \$2.8 million in the six-month period ending June 30, 2015 as compared to the same period in 2014, respectively, mainly due to increased average balances. Average loan balances increased in the three month period ended June 30, 2015 compared to the same period in 2015 primarily as a result of loan growth from the Company's legacy operations (excluding the impact of loans acquired in connection with the transaction with Alaska Pacific), which increased for both the three and six month periods ending June 30, 2015, as compared to the same periods a year ago. Additionally, the acquisition of Alaska Pacific contributed to the increase in average loan balances in the six month period ending June 30, 2015 as compared to 2014.

Average loans held for sale increased by \$55.2 million, or 510% to \$66.1 million in the three-month period ending June 30, 2015, and increased \$46.1 million, or 528% to \$54.8 million in the six-month period ending June 30, 2015, as compared to the same periods in 2014, respectively. Total interest income from loans held for sale increased \$446,000 for the second quarter of 2015 and increased \$806,000 in the six-month period ending June 30, 2015 as compared to the same period in 2014, respectively, as a result of the increase in average balances. Average balances and net interest income for loans held for sale increased in both the second quarter and first half of 2015 primarily as a result of loans acquired by the Company in connection with the Company's acquisition of the remaining 76.5% of RML on December 1, 2014 and loans generated by RML subsequent to the acquisition.

Average investments decreased by \$22.8 million, or 8% to \$268.7 million in the three-month period ending June 30, 2015, and decreased \$19.5 million, or 7% to \$277.0 million in the six-month period ending June 30, 2015, as compared to the same periods in 2014. The decrease in average investments for the three and six-month periods ending June 30, 2015 as compared to the same periods in 2014 is mainly a result of proceeds from called and matured investments being used to fund our growth in loans.

Average interest-bearing liabilities increased \$48.0 million, or 6%, to \$839.6 million during the second quarter of 2015 and increased \$101.9 million, or 14%, to \$836.9 million in the six-month period ending June 30, 2015, as compared to \$791.6 million and \$735.0 million, for the same periods in 2014, respectively. These increases were primarily the result of increased borrowings resulting from a warehouse line of credit acquired as a result of our acquisition of RML. Additionally, certificates of deposits increased in both periods compared to 2014 mainly as a result of a campaign the Company ran in the fourth quarter of 2014. Average interest-bearing liabilities increased in the six months ended June 30, 2015 as compared to 2014 mostly due to the deposit balances acquired in connection with the acquisition of Alaska Pacific. The average cost of interest-bearing liabilities increased \$264,000 and \$578,000, or 55% and 63%, for the three and six-month periods ending June 30, 2015, respectively, as compared to the same periods in 2014, due to increases in both average balances and interest rates for both deposits and

borrowings. Interest rates on deposits increased due to a change in the mix of the Company's deposits. Average certificates of deposits accounted for 12% and 10% for the second quarters of 2015 and 2014, respectively, and 12% and 9% of total average deposits year-to-date at June 30, 2015 and 2014, respectively. Additionally, interest rates on short term borrowings increased mainly due to the Company's use of some higher cost short term funding lines used to fund mortgage originations.

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Components of Net Interest Margin

The following table compares average balances and rates as well as net tax equivalent margins on earning assets for the three-month periods ended June 30, 2015 and 2014:

(Dollars in Thousands)

	Three Months Ended June 30,				Interest income/ expense				Average Yields/Costs Tax Equivalent ³		
	Average Balances		Change		Change		Change		Change		
	2015	2014	\$	%	2015	2014	\$	%	2015	2014	%
Loans ^{1,2}	\$966,952	\$924,881	\$42,071	5 %	\$13,548	\$12,941	\$607	5 %	5.67 %	5.65 %	0.02 %
Loans held for sale	66,074	10,827	55,247	510 %	587	141	446	316 %	3.56 %	4.03 %	(0.47) %
Short-term investments	39,229	48,466	(9,237)	(19) %	24	41	(17)	(41) %	0.25 %	0.33 %	(0.08) %
Long-term investments	229,485	243,096	(13,611)	(6) %	784	772	12	2 %	1.50 %	1.39 %	0.11 %
Total investments	268,714	291,562	(22,848)	(8) %	808	813	(5)	(1) %	1.32 %	1.22 %	0.10 %
Interest-earning assets	1,301,740	1,227,270	74,470	6 %	14,943	13,895	1,048	8 %	4.67 %	4.58 %	0.09 %
Nonearning assets	143,404	116,450	26,954	23 %							
Total	\$1,445,144	\$1,343,720	\$101,424	8 %							
Interest-bearing deposits	\$784,972	\$748,537	\$36,435	5 %	\$493	\$348	\$145	42 %	0.25 %	0.19 %	0.06 %
Borrowings	54,644	43,063	11,581	27 %	255	136	119	88 %	1.85 %	1.23 %	0.62 %
Total interest-bearing liabilities	839,616	791,600	48,016	6 %	748	484	264	55 %	0.36 %	0.24 %	0.12 %
Demand deposits and other noninterest-bearing liabilities	438,230	395,841	42,389	11 %							
Equity	167,298	156,279	11,019	7 %							
Total	\$1,445,144	\$1,343,720	\$101,424	8 %							
Net interest income					\$14,195	\$13,411	\$784	6 %			
Net tax equivalent margin on interest earning assets ³									4.44 %	4.43 %	0.01 %

¹Interest income includes loan fees. Loan fees recognized during the period and included in the yield calculation totaled \$934,000 and \$717,000 in the second quarter of 2015 and 2014, respectively.

²Nonaccrual loans are included with a zero effective yield. Average nonaccrual loans included in the computation of the average loans were \$4.9 million and \$3.8 million in the second quarter of 2015 and 2014 respectively.

³Tax-equivalent net interest margin is a non-GAAP performance measurement in which interest income on non-taxable investments and loans is presented on a tax-equivalent basis using a combined federal and state statutory rate of 41.11% in both 2015 and 2014. Although we believe this non-GAAP financial measure is frequently used by stakeholders in the evaluation of companies in the banking industry, there are limitations, it is not required to be uniformly applied, and it is not audited. The most comparable GAAP measure, net interest margin, was 4.37% and 4.38%, respectively, for the second quarter of 2015 and 2014.

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The following table is a reconciliation of tax-equivalent net interest margin to net interest margin for the periods indicated:

(In Thousands)	Three Months Ended June 30,		
	2015	2014	
Net interest income	\$14,195	\$13,411	
Divided by average interest-bearing assets	1,301,740	1,227,270	
Net interest margin	4.37	%4.38	%
(In Thousands)	2015	2014	
Net interest income	\$14,195	\$13,411	
Plus: reduction in tax expense related to tax-exempt interest income	199	129	
	\$14,394	\$13,540	
Divided by average interest-bearing assets	1,301,740	1,227,270	
Tax-equivalent net interest margin	4.44	%4.43	%

The following table compares average balances and rates as well as net tax equivalent margins on earning assets for the six-month periods ended June 30, 2015 and 2014:

(Dollars in Thousands)	Six Months Ended June 30,												
	Average Balances		Change		Interest income/ expense				Average Yields/Costs Tax Equivalent ³				
	2015	2014	\$	%	2015	2014	\$	%	2015	2014	Change	%	
Loans ^{1,2}	\$956,571	\$848,007	\$108,564	13	%	\$26,620	\$23,777	\$2,843	12	%	5.65	%5.68	%(0.03)
Loans held for sale	54,780	8,727	46,053	528	%	982	176	806	458	%	3.62	%4.07	%(0.45)
Short-term investments	26,972	53,275	(26,303)	(49)	%	35	90	(55)	(61)	%	0.26	%0.34	%(0.08)
Long-term investments	250,000	243,200	6,800	3	%	1,692	1,525	167	11	%	1.49	%1.39	%0.10
Total investments	276,972	296,475	(19,503)	(7)	%	1,727	1,615	112	7	%	1.38	%1.21	%0.17
Interest-earning assets	1,288,323	1,153,209	135,114	12	%	29,329	25,568	3,761	15	%	4.65	%4.52	%0.13
Nonearning assets	148,888	109,046	39,842	37	%								
Total	\$1,437,211	\$1,262,255	\$174,956	14	%								
Interest-bearing deposits	\$780,099	\$692,212	\$87,887	13	%	\$970	\$634	\$336	53	%	0.25	%0.18	%0.07
Borrowings	56,801	42,752	14,049	33	%	532	290	242	83	%	1.84	%1.34	%0.50
Total interest-bearing liabilities	836,900	734,964	101,936	14	%	1,502	924	578	63	%	0.36	%0.25	%0.11
Demand deposits and other noninterest-bearing liabilities	433,198	376,051	57,147	15	%								
Equity	167,113	151,240	15,873	10	%								
Total	\$1,437,211	\$1,262,255	\$174,956	14	%								
Net interest income						\$27,827	\$24,644	\$3,183	13	%			

Net tax equivalent margin on interest earning assets³

4.41 % 4.36 % 0.05 %

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¹Interest income includes loan fees. Loan fees recognized during the period and included in the yield calculation totaled \$1.8 million and \$1.4 million in the first six months of 2015 and 2014, respectively.

²Nonaccrual loans are included with a zero effective yield. Average nonaccrual loans included in the computation of the average loans were \$4.8 million and \$2.9 million in the first six months of 2015 and 2014 respectively.

³Tax-equivalent net interest margin is a non-GAAP performance measurement in which interest income on non-taxable investments and loans is presented on a tax-equivalent basis using a combined federal and state statutory rate of 41.11% in both 2015 and 2014. Although we believe this non-GAAP financial measure is frequently used by stakeholders in the evaluation of companies in the banking industry, there are limitations, it is not required to be uniformly applied, and it is not audited. The most comparable GAAP measure, net interest margin, was 4.36% and 4.31%, respectively, for the first six months of 2015 and 2014.

The following table is a reconciliation of tax-equivalent net interest margin to net interest margin for the periods indicated:

(In Thousands)	Six Months Ended June 30,		
	2015	2014	
Net interest income	\$27,827	\$24,644	
Divided by average interest-bearing assets	1,288,323	1,153,209	
Net interest margin	4.36	% 4.31	%
(In Thousands)	2015	2014	
Net interest income	\$27,827	\$24,644	
Plus: reduction in tax expense related to tax-exempt interest income	351	280	
	\$28,178	\$24,924	
Divided by average interest-bearing assets	1,288,323	1,153,209	
Tax-equivalent net interest margin	4.41	% 4.36	%

The following tables set forth the changes in consolidated net interest income attributable to changes in volume and to changes in interest rates for the three and six-month periods ending June 30, 2015 and 2014. Changes attributable to the combined effect of volume and interest rate have been allocated proportionately to the changes due to volume and the changes due to interest rates:

(In Thousands)	Three Months Ended June 30, 2015 vs. 2014		
	Increase (decrease) due to		
	Volume	Rate	Total
Interest Income:			
Loans	\$651	(\$44)	) \$607
Loans held for sale	457	(11)	) 446
Short-term investments	(7)	) (10)	) (17)
Long-term investments	(28)	) 40	12
Total interest income	\$1,073	(\$25)	) \$1,048
Interest Expense:			
Interest-bearing deposits	\$19	\$126	\$145
Borrowings	41	78	119
Total interest expense	\$60	\$204	\$264

(In Thousands)	Six Months Ended June 30, 2015 vs. 2014		
	Increase (decrease) due to		
	Volume	Rate	Total
Interest Income:			
Loans	\$3,044	(\$201	) \$2,843
Loans held for sale	822	(16	) 806
Short-term investments	(41	)(14	)(55
Long-term investments	47	120	167
Total interest income	\$3,872	(\$111	) \$3,761
Interest Expense:			
Interest-bearing deposits	\$79	\$257	\$336
Borrowings	105	137	242
Total interest expense	\$184	\$394	\$578

Provision for Loan Losses

We recorded a provision for loan losses of \$376,000 and a benefit for the provision for loan losses of \$1.1 million for the second quarters of 2015 and 2014, respectively. We recorded a provision for loan losses of \$702,000 and a benefit for the provision of loan losses of \$1.1 million for the six month periods ending June 30, 2015 and 2014, respectively. The increase in the provision for loan losses in both periods of 2015 as compared to 2014 is primarily the result of an increase in portfolio loans and net recoveries in 2014 that led to a loan loss benefit. See "Analysis of the Allowance for Loan Losses" under the "Financial Condition-Balance Sheet Overview" and Note 8 of the Notes to Consolidated Financial Statements included in Part I of this report for more information on changes in the Company's Allowance.

Other Operating Income

Other operating income for the three-month period ending June 30, 2015, increased \$7.5 million, or 182%, to \$11.6 million as compared to the same period in 2014. This increase is primarily the result of \$7.8 million in mortgage banking income earned in the second quarter of 2015. The Company acquired the remaining 76.5% of RML on December 1, 2014 making RML a wholly-owned, consolidated subsidiary of the Company. RML's results of operations prior to the December 1, 2014 acquisition were included in our operating results under the equity method. Additionally, other income increased \$118,000 in the second quarter of 2015 compared to the same period in 2014 primarily due to \$179,000 in gains on loans acquired in connection with the acquisition of Alaska Pacific in 2014 at a discount to par values that were paid off in the second quarter of 2015. These increases were partially offset by a decrease of \$333,000 in gains on the sale of securities.

Other operating income for the six-month period ending June 30, 2015, increased \$15.3 million, or 223%, to \$22.1 million as compared to the same period in 2014. This increase is primarily the result of \$15.1 million in mortgage banking income earned in the first six months of 2015 as a result of the acquisition noted above. Additionally, other income increased \$343,000 the first half of 2015 compared to the same period of 2014 primarily due to \$226,000 in gains recognized on the disposition of loans acquired in connection with the acquisition of Alaska Pacific in 2014 at a discount, as well as an increase in rental income of \$174,000 due to new tenants occupying space in the Company's main office building beginning August 1, 2014. These increases were partially offset by a decrease of \$316,000 in gains on the sale of securities.

Other Operating Expense

Other operating expense for the second quarter of 2015 increased \$6.1 million, or 53%, to \$17.8 million as compared to the same period in 2014, mainly reflecting a \$4.3 million increase in salaries and other personnel expense and an expense of \$587,000 incurred in the second quarter of 2015 related to the earn out liability attributable to the RML acquisition. The increase in salaries and other personnel expense was primarily due to an increase in average full time equivalent employees from 312 at June 30, 2014 to 428 at June 30, 2015, primarily due to the acquisition of RML. Additionally, professional and outside services expense, occupancy expense, and marketing expense increased \$572,000, \$482,000 and \$248,000, respectively, in the second quarter of 2015 as compared to the second quarter of 2014. Professional and outside services expense increased mainly due to integration issues related to the acquisition of RML and development of a new loan servicing program. Occupancy expense increased primarily due to the acquisition of RML, and marketing expense increased due to the opening of a new branch location in Anchorage and sales campaigns launched in the second quarter of 2015.

Other operating expense for the six-month period ending June 30, 2015 increased \$14.6 million, or 68%, to \$36.2 million as compared to the same period in 2014, primarily due to an \$8.9 million increase in salaries and other personnel expense primarily due to the acquisitions of RML and Alaska Pacific, and an expense of \$2.1 million related to the earn out liability attributable to the RML acquisition. The following are other changes in other operating expense: an increase of \$1.2 million in occupancy expense, an increase of \$918,000 in professional and other outside services, and an increase in marketing expense of \$251,000. These expenses increased primarily due to the same factors discussed above for the second quarter. Additionally, equipment expense and insurance expense also increased by \$205,000 and \$200,000, respectively, due to the acquisitions of Alaska Pacific and RML. OREO expense net of rental income and gains on sale increased by \$423,000 in the first half of 2015 compared to the same period of 2014 primarily as a result of an increase in impairment on OREO properties. These increases were partially offset by a decrease of \$705,000 in merger and acquisition expense, which mostly resulted from costs incurred in connection with the acquisitions of Alaska Pacific and RML in 2014 and a \$278,000 decrease in the reserve for purchased receivables.

Income Taxes

The provision for income taxes for the three and six-month periods ending June 30, 2015 increased \$117,000 and \$567,000, or 5% and 15%, respectively, as compared to the same period in 2014 primarily due to increases in pre-tax net income. The effective tax rate for the six-month periods ending June 30, 2015 and 2014 was 34% and 35%, respectively.

FINANCIAL CONDITION

Balance Sheet Overview

Investment Securities

Investment securities at June 30, 2015 decreased \$55.9 million, or 20%, to \$228.1 million from \$283.9 million at December 31, 2014. This decrease was primarily due to sales, maturities, and security calls of available for sale securities, which were only partially offset by purchases. The Company used proceeds from the net decrease in investment securities to fund loan growth in the first six months of 2015.

Loans and Lending Activities

Our loan products include short and medium-term commercial loans, commercial credit lines, construction and real estate loans, and consumer loans. From our inception, we have emphasized commercial, land development and home construction, and commercial real estate lending. This type of lending has provided us with market opportunities and higher net interest margins than other types of lending. However, it also involves greater risks, including greater exposure to changes in local economic conditions, than certain other types of lending.

Portfolio loans increased by \$50.3 million, or 5%, to \$974.8 million at June 30, 2015 from \$924.5 million at December 31, 2014, primarily the result of organic growth in commercial, commercial real estate and real estate construction loans.

The following table details loan balances by loan type as of the dates indicated:

(In Thousands)	June 30, 2015		December 31, 2014		
	Dollar Amount	Percent of Total	Dollar Amount	Percent of Total	
Commercial	\$334,181	34.3	% \$306,543	33.2	%
Real estate construction one-to-four family	38,233	3.9	% 34,842	3.8	%
Real estate construction other	101,683	10.4	% 91,195	9.9	%
Real estate term owner occupied	111,245	11.4	% 109,472	11.8	%
Real estate term non-owner occupied	295,613	30.3	% 286,616	31.0	%
Real estate term other	38,511	4.0	% 36,894	4.0	%
Consumer secured by 1st deeds of trust	29,328	3.0	% 32,000	3.5	%
Consumer other	30,514	3.1	% 31,493	3.4	%
Subtotal	\$979,308		\$929,055		
Less: Unearned origination fee, net of origination costs	(4,459)	)(0.4	)% (4,551	)(0.6)%
Total loans	\$974,849		\$924,504		

Analysis of Allowance for Loan Losses

The Company maintains an Allowance to reflect losses inherent in the loan portfolio. The Allowance is increased by provisions for loan losses and loan recoveries and decreased by loan charge-offs. The size of the Allowance is determined through quarterly assessments of probable estimated losses in the loan portfolio.

Our methodology for making such assessments and determining the adequacy of the Allowance includes the following key elements:

A specific allocation for impaired loans. Management determines the fair value of the majority of these loans based on the underlying collateral values. This analysis is based upon a specific analysis for each impaired loan, including external appraisals on loans secured by real property, management's assessment of the current market, recent payment history, and an evaluation of other sources of repayment. In-house evaluations of fair value are used in the impairment analysis in some situations. Inputs to the in-house evaluation process include information about sales of comparable properties in the appropriate markets and changes in tax assessed values. The Company obtains appraisals on real and personal property that secure its loans during the loan origination process in accordance with regulatory guidance and its loan policy. The Company obtains updated appraisals on loans secured by real or personal property based upon its assessment of changes in the current market or particular projects or properties, information from other current appraisals, and other sources of information. Appraisals may be adjusted downward by the Company based on its evaluation of the facts and circumstances on a case by case basis. External appraisals may be discounted when management believes that the absorption period used in the appraisal is unrealistic, when expected liquidation costs exceed those included in the appraisal, or when management's evaluation of deteriorating market conditions warrants an adjustment. Additionally, the Company may also adjust appraisals in the above circumstances between appraisal dates. The Company uses the information provided in these updated appraisals along with its evaluation of all other information available on a particular property as it assesses the collateral coverage on its performing and nonperforming loans and the impact that may have on the adequacy of its Allowance. The specific allowance for impaired loans, as well as the overall Allowance, may increase based on the Company's assessment of updated appraisals. When the Company determines that a loss has occurred on an impaired loan, a charge-off equal to the difference between carrying value and fair value is recorded. If a specific allowance is deemed necessary for a loan, and then that loan is partially charged off, the loan remains classified as a nonperforming loan after the charge-off is recognized. Loans measured for impairment based on collateral value and all other loans measured for impairment are accounted for in the same way. As of June 30, 2015 and December 31, 2014, 4% and 6% of nonperforming loans, which totaled \$5.0 million and \$4.7 million, respectively, had partially charged-off balances.

A general allocation. The Company has identified segments and classes of loans not considered impaired for purposes of establishing the general allocation allowance. The Company determined the disaggregation of the loan portfolio into segments and classes based on its assessment of how different pools of loans with like characteristics in the portfolio behave over time. This determination is based on historical experience and management's assessment of how current facts and circumstances are expected to affect the loan portfolio.

The Company has the following loan segments: commercial, real estate construction one-to-four family, real estate construction other, real estate term owner occupied, real estate term non-owner occupied, real estate term other, consumer secured by 1st deeds of trust, and other consumer loans. The Company has five loan classes: pass, special mention, substandard, doubtful, and loss.

After the portfolio has been disaggregated into segments and classes, the Company calculates a general reserve for each segment and class based on the average year loss history for each segment and class using a five year look-back period.

After the Company calculates a general allocation using its loss history, the general reserve is then adjusted for qualitative factors by segment and class. Qualitative factors are based on management's assessment of current trends that may cause losses inherent in the current loan portfolio to differ significantly from historical losses. Some factors that management considers in determining the qualitative adjustment to the general reserve include loan quality trends in our own portfolio, national and local economic trends, business conditions, underwriting policies and standards, trends in local real estate markets, effects of various political activities, peer group data, and internal factors such as underwriting policies and expertise of the Company's employees.

An unallocated reserve. The unallocated portion of the Allowance provides for other credit losses inherent in the Company's loan portfolio that may not have been contemplated in the specific and general components of the Allowance, and it acknowledges the inherent imprecision of all loss prediction models. The unallocated component is reviewed periodically based on trends in credit losses and overall economic conditions.

At June 30, 2015, the unallocated portion of the Allowance as a percentage of the total Allowance was 8%. The unallocated portion of the Allowance as a percentage of the total Allowance was 7% at December 31, 2014.

Further discussion of the enhancement to the Company's Allowance methodology can be found in Item 7 in the Company's Annual Report on Form 10-K for the year ended December 31, 2014.

Allowance related to acquired loans: In accordance with generally accepted accounting principles, loans acquired in connection with the acquisition of Alaska Pacific on April 1, 2014 were recorded at their fair value at the acquisition date. Credit discounts were included in the determination of fair value; therefore, an allowance for loan losses was not recorded at the acquisition date. Purchased credit impaired loans were evaluated on a loan by loan basis and the valuation allowance for these loans was netted against the carrying value. Deterioration in credit quality of the acquired loans subsequent to acquisition date results in the establishments of an allowance. There was no allowance related to acquired loans at June 30, 2015.

The following table sets forth information regarding changes in the Allowance for the periods indicated:

(In Thousands)	Three Months Ended June 30,		Six Months Ended June 30,		
	2015	2014	2015	2014	
Balance at beginning of period	\$16,947	\$16,032	\$16,723	\$16,282	
Charge-offs:					
Commercial	—	—	107	320	
Real estate term other	—	—	81	—	
Consumer secured by 1st deeds of trust	—	39	—	39	
Consumer other	—	24	—	33	
Total charge-offs	—	63	188	392	
Recoveries:					
Commercial	91	576	158	630	
Real estate construction one-to-four family	—	613	—	625	
Real estate term other	—	—	17	—	
Consumer other	4	10	6	23	
Total recoveries	95	1,199	181	1,278	
Net, charge-offs (recoveries)	(95) (1,136) 7	(886)
Provision for loan losses	376	(1,136) 702	(1,136)
Balance at end of period	\$17,418	\$16,032	\$17,418	\$16,032	

While management believes that it uses the best information available to determine the Allowance, unforeseen market conditions and other events could result in adjustment to the Allowance, and net income could be significantly affected if circumstances differed substantially from the assumptions used in making the final determination of the Allowance. Moreover, bank regulators frequently monitor banks' loan loss allowances, and if regulators were to determine that the Company's Allowance is inadequate, they may require the Company to increase the Allowance, which may adversely impact the Company's net income and financial condition.

Deposits

Deposits are the Company's primary source of funds. Total deposits increased \$59.0 million or 5% with a balance of \$1.2 billion at June 30, 2015 and December 31, 2014, respectively. The following table summarizes the Company's composition of deposits as of the periods indicated:

(In thousands)	June 30, 2015		December 31, 2014		
	Balance	% of total	Balance	% of total	
Demand deposits	\$455,358	37	% \$403,523	35	%
Interest-bearing demand	173,952	14	% 185,114	15	%
Savings deposits	129,938	10	% 122,588	10	%
Alaska CDs	97,592	8	% 99,736	8	%
Money market deposits	232,877	19	% 226,574	20	%
Time deposits	149,000	12	% 142,212	12	%
Total deposits	\$1,238,717		\$1,179,747		

The Company's mix of deposits continues to contribute to a low cost of funds with balances in transaction accounts representing 88% of total deposits at both June 30, 2015 and December 31, 2014. There were no depositors with deposits representing 10% or more of total deposits at June 30, 2015 or December 31, 2014.

Borrowings

The Company has a maximum line of credit with the Federal Home Loan Bank of Des Moines, or "FHLB" approximating 35% of eligible assets. FHLB advances are subject to collateral criteria that require the Company to pledge assets under a blanket pledge arrangement as collateral for its borrowings from the FHLB. Based on assets currently pledged and advances currently outstanding at June 30, 2015, the Company's available borrowing line from the FHLB, was \$194.0 million, representing approximately 13% of the Company's assets. The Company has an outstanding FHLB advance of \$2.1 million and \$2.2 million as of June 30, 2015 and December 31, 2014, respectively, that was originated in the first quarter of 2013. FHLB advances are dependent on the availability of acceptable collateral such as marketable securities or real estate loans, although all FHLB advances are secured by a blanket pledge of the Company's assets. The \$2.2 million FHLB advance that the Company drew in the first quarter of 2013 was to match fund a \$2.2 million loan to one borrower for the construction of a low income housing project that qualified for a long term fixed interest rate of 3.12%. This FHLB borrowing originally had an eighteen year term with a 30 year amortization period, which mirrors the term of the construction loan made to the borrower. The maturity date of this borrowing is March 21, 2031.

The Company, through RML, had borrowings of \$20.2 million and \$24.1 million at June 30, 2015 and December 31, 2014, respectively. This borrowing is a line of credit used by RML to fund mortgage originations that matures on August 12, 2015.

At June 30, 2015 and December 31, 2014, the Company had no short-term (original maturity of one year or less) borrowings that exceeded 30% of shareholders' equity.

Liquidity and Capital Resources

The Company manages its liquidity through its Asset and Liability Committee. In addition to the \$104.1 million of cash and due from banks and interest bearing deposits in other banks and \$168.3 million in unpledged available for sale securities held at June 30, 2015, the Company had additional funding sources which include fed fund borrowing lines and advances available at the FHLB of Des Moines and the Federal Reserve Bank of approximately \$291.2 million as of June 30, 2015.

At June 30, 2015, \$57.5 million in securities, or 25%, of the investment portfolio was pledged, as compared to \$54.1 million, or 19%, at December 31, 2014. As shown in the Consolidated Statements of Cash Flows included in Part I - Item 1 "Financial Statements" of this report, net cash used by operating activities was \$26.2 million for the first six months of 2015 primarily due to net originations of loans held for sale and a decrease in other liabilities. Net cash provided by investing activities was \$11.3 million for the same period, primarily due proceeds from sales and maturities of securities available for sale. These proceeds were partially offset by loan fundings and purchases of investment securities available for sale. Net cash provided by financing activities was \$50.5 million, primarily due to an increase in deposits.

The Company issued 224 shares of its common stock in the first six months of 2015 and did not repurchase any shares of its common stock under the Company's publicly announced repurchase program. At June 30, 2015, the Company had 6,854,413 shares of its common stock outstanding.

Capital Requirements and Ratios

The Company and its wholly-owned subsidiary, Northrim Bank (the "Bank"), are subject to various regulatory capital requirements administered by the federal banking agencies. Failure to meet minimum regulatory capital requirements can result in certain mandatory, and possibly additional discretionary, actions by regulators that, if undertaken, could have a direct material adverse effect on the Company's financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Company and the Bank must meet specific capital guidelines that involve quantitative measures of assets, liabilities, and certain off-balance sheet items as calculated under regulatory accounting practices. The capital amounts and classifications are also subject to qualitative judgments by regulators about the components of regulatory capital, risk weightings, and other factors. The regulatory agencies may establish higher minimum requirements if, for example, a bank or bank holding company has previously received special attention or has a high susceptibility to interest rate risk.

Effective January 1, 2015, both the Company and the Bank were required to meet more stringent minimum capital requirements standards, commonly referred to as "Basel III". As such, the ratios presented as of June 30, 2015 are calculated under the new regulations of Basel III. The ratios presented as of December 31, 2014 are calculated under the prior regulations of Basel II.

The requirements address both risk-based capital and leverage capital. At June 30, 2015, all capital ratios of the Company and the Bank exceeded the ratios required for a "well-capitalized" institution under regulatory guidelines. The following table sets forth the actual capital ratios for the Company and the Bank as calculated under regulatory guidelines, compared to the regulatory minimum capital ratios and the regulatory minimum capital ratios needed to be eligible to qualify as a "well-capitalized" institution as of June 30, 2015.

	Adequately-Capitalized	Well-Capitalized	Northrim BanCorp, Inc.	Northrim Bank
June 30, 2015				
Common equity tier 1 capital	4.50%	6.50%	11.27%	11.63%
Tier 1 risk-based capital	6.00%	8.00%	12.67%	11.65%
Total risk-based capital	8.00%	10.00%	13.92%	12.90%
Leverage ratio	4.00%	5.00%	10.25%	10.57%
December 31, 2014				
Tier 1 risk-based capital	4.00%	6.00%	13.06%	12.05%
Total risk-based capital	8.00%	10.00%	14.31%	13.30%
Leverage ratio	4.00%	5.00%	11.21%	10.35%

The regulatory capital ratios for the Company exceed those for the Bank in certain categories primarily because the \$18.6 million junior subordinated debenture offerings that the Company completed in the third quarter of 2003 and the fourth quarter of 2005 are included in the Company's capital for regulatory purposes although such securities are accounted for as a long-term debt in its financial statements. The junior subordinated debentures are not accounted for

on the Bank's financial statements nor are they included in its capital. As a result, the Company has \$18.6 million more in regulatory capital than the Bank.

Off-Balance Sheet Items

The Company is a party to financial instruments with off-balance sheet risk. Among the off-balance sheet items entered into in the ordinary course of business are commitments to extend credit and the issuance of letters of credit. These instruments involve, to varying degrees, elements of credit and interest rate risk in excess of the amounts recognized on the balance sheet. Certain commitments are collateralized. As of June 30, 2015 and December 31, 2014, the Company's commitments to extend credit and to provide letters of credit which are not reflected on its balance sheet amounted to \$241.5 million and \$219.3 million, respectively. Since many of the commitments are expected to expire without being drawn upon, these total commitment amounts do not necessarily represent future cash requirements. The Company has established reserves of \$120,000 and \$112,000 at June 30, 2015 and December 31, 2014, respectively, for losses related to these commitments that are recorded in other liabilities on the consolidated balance sheet.

Capital Expenditures and Commitments

At June 30, 2015 the Company has capital commitments of \$1.3 million related to the construction of new branch locations and \$1.8 million related to planned improvements to the Company's corporate office building. The Company expects these capital expenditures to be incurred in the third and fourth quarters of 2015.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Our assessment of market risk as of June 30, 2015 indicates that there are no material changes in the quantitative and qualitative disclosures from those in our Annual Report on Form 10-K for the year ended December 31, 2014.

ITEM 4. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

As of the end of the period covered by this report, we evaluated the effectiveness of our disclosure controls and procedures (as defined in Rule 13a-15(e) or Rule 15d-15(e) under the Securities Exchange Act of 1934). Our principal executive and financial officers supervised and participated in this evaluation. Based on this evaluation, our principal executive and financial officers each concluded that as of June 30, 2015, the disclosure controls and procedures are effective in timely alerting them to material information required to be included in the periodic reports to the Securities and Exchange Commission. The design of any system of controls is based in part upon various assumptions about the likelihood of future events, and there can be no assurance that any of our plans, products, services or procedures will succeed in achieving their intended goals under future conditions.

Changes in Internal Control over Disclosure and Reporting

There was no change in our internal control over financial reporting (as defined in Rule 13a-15(f) and 15-d-15(f) of the Securities Exchange Act of 1934) that occurred during the quarterly period ended June 30, 2015 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

PART II - OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

During the normal course of its business, the Company is a party to various debtor-creditor legal actions, disputes, claims, and litigation related to the conduct of its banking business. These include cases filed as a plaintiff in collection and foreclosure cases, and the enforcement of creditors' rights in bankruptcy proceedings. Management does not expect that the resolution of these matters will have a material effect on the Company's business, financial position, results of operations, or cash flows.

ITEM 1A. RISK FACTORS

For information regarding risk factors, please refer to Item 1A in the Company's Annual Report on Form 10-K for the year ended December 31, 2014. These risk factors have not materially changed as of June 30, 2015.

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

(a)-(b) Not applicable

(c) There were no stock repurchases by the Company during the six months ending June 30, 2015.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

ITEM 4. MINE SAFETY DISCLOSURES

Not applicable.

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ITEM 5. OTHER INFORMATION

(a) Not applicable

(b) There have been no material changes to the procedures by which shareholders may nominate directors to the Company's board of directors.

ITEM 6. EXHIBITS

31.1	Certification of Chief Executive Officer required by Rule 13a-14(a) or Rule 15d-14(a)
31.2	Certification of Chief Financial Officer required by Rule 13a-14(a) or Rule 15d-14(a)
32.1	Certification of Chief Executive Officer required by Rule 13a-14(b) or Rule 15d-14(b) and Section 906 of the Sarbanes-Oxley Act of 2002, 18 U.S.C. Section 1350
32.2	Certification of Chief Financial Officer required by Rule 13a-14(b) or Rule 15d-14(b) and Section 906 of the Sarbanes-Oxley Act of 2002, 18 U.S.C. Section 1350
101.INS	XBRL Instance Document
101.SCH	XBRL Schema Document
101.CAL	XBRL Calculation Linkbase Document
101.LAB	XBRL Labels Linkbase Document
101.PRE	XBRL Presentation Linkbase Document
101.DEF	XBRL Definition Linkbase Document

Notes to Exhibits List:

Attached as Exhibit 101 to this report are the following formatted in XBRL (Extensible Business Reporting Language): (i) Consolidated Balance Sheet, (ii) Consolidated Statements of Income, (iii) Consolidated Statements of Comprehensive Income and Changes in Shareholders' Equity, (iv) Consolidated Statements of Cash Flows, and (v) Notes to the Consolidated Financial Statements. In accordance with Rule 406T of Regulation S-T, the XBRL related information in Exhibit 101 to this Quarterly Report on Form 10-Q shall not be deemed to be "filed" for purposes of Section 18 of the Exchange Act, or otherwise subject to the liability of that section, and shall not be part of any registration statement or other document filed under the Securities Act or the Exchange Act, except as shall be expressly set forth by specific reference in such filing.

SIGNATURES

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

NORTHRIM BANCORP, INC.

August 10, 2015

By /s/ Joseph M. Beedle
Joseph M. Beedle
President and Chief Executive Officer
(Principal Executive Officer)

August 10, 2015

By /s/ Latosha M. Frye
Latosha M. Frye
Executive Vice President, Chief Financial Officer
(Principal Financial and Accounting Officer)