

STERLING FINANCIAL CORP /WA/

Form S-1/A

November 03, 2010

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As filed with the Securities and Exchange Commission on November 3, 2010

Registration No. 333-169579

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

**Pre-Effective Amendment No. 1**

**to**

**Form S-1**

**REGISTRATION STATEMENT**

*UNDER*

*THE SECURITIES ACT OF 1933*

**STERLING FINANCIAL CORPORATION**

(Exact name of registrant as specified in its charter)

<b>WASHINGTON</b> (State or other jurisdiction of incorporation or organization)	<b>6719</b> (Primary Standard Industrial Classification Code Number) <b>111 North Wall Street</b> <b>Spokane, Washington 99201</b>  <b>(509) 227-5389</b>	<b>91-1572822</b> (I.R.S. Employer Identification No.)
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(Address, including zip code, and telephone number, including area code, of registrant's principal executive offices)

**Andrew J. Schultheis, Secretary**  
**Sterling Financial Corporation**  
**111 North Wall Street**  
**Spokane, Washington 99201**  
**(509) 227-5389**

(Name, address, including zip code, and telephone number, including area code, of agent for service)

*Copies of communications to:*

<b>Andrew J. Schultheis, Esq.</b>  <b>Richard A. Repp, Esq.</b>  <b>Witherspoon, Kelley, Davenport &amp; Toole, P.S.</b>  <b>422 West Riverside Avenue, Suite 1100</b>  <b>Spokane, Washington 99201</b>  <b>(509) 624-5265</b>	<b>John L. Douglas, Esq.</b>  <b>Sarah K. Solum, Esq.</b>  <b>Davis Polk &amp; Wardwell LLP</b>  <b>1600 El Camino Real</b>  <b>Menlo Park, CA 94025</b>  <b>(650) 752-2011</b>
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**Approximate Date of Commencement of Proposed Sale to the Public:** As soon as practicable after the effective date of this Registration Statement, subject to market conditions and other factors.

If any of the securities being registered on this Form are to be offered on a delayed or continuous basis pursuant to Rule 415 under the Securities Act of 1933, check the following box.

If this Form is filed to register additional securities for an offering pursuant to Rule 462(b) under the Securities Act, please check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering.

If this Form is a post-effective amendment filed pursuant to Rule 462(c) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering:

If this Form is a post-effective amendment filed pursuant to Rule 462(d) under the Securities Act, check the following box and list the Securities Act registration number of the earlier effective registration statement for the same offering.

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 <input type="checkbox"/>	Accelerated filer <input checked="" type="checkbox"/>
Non-accelerated filer <input type="checkbox"/> (Do not check if a smaller reporting company)	Smaller reporting company <input type="checkbox"/>

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Title of each class of securities to be registered	Amount to be registered	Proposed maximum offering price per unit	Proposed maximum aggregate offering price	Amount of registration fee <sup>(1)</sup>
<b>Common Stock, having no par value<sup>(2)</sup></b>	4,028,750,000	\$0.62	\$2,497,825,000.00	\$178,094.92
<b>Common Stock, having no par value, issuable upon exercise of the Treasury Warrant<sup>(2)</sup></b>	6,437,677	\$0.20	\$1,287,535.40	\$91.80
<b>Common Stock, having no par value, issuable upon exercise of the Anchor Warrants<sup>(2)</sup></b>	173,250,000	\$0.22	\$38,115,000.00	\$2,717.60
<b>Total Common Stock</b>	4,208,437,677			
<b>Warrants</b>	179,687,677	\$0.62	\$111,406,359.70	\$7,943.27
<b>Total</b>			<b>\$2,648,633,895.10</b>	<b>\$188,847.59<sup>(3)</sup></b>

- (1) Estimated in accordance with Rule 457(c) under the Securities Act of 1933, as amended, solely for the purpose of calculating the registration fee, based on the average of the high and low prices of shares of Sterling Financial Corporation Common Stock reported on the NASDAQ Capital Market on September 20, 2010 with the exception of shares issuable upon exercise of warrants, which are based on the exercise price of the relevant warrant in accordance with Rule 457(i).
- (2) The common stock being registered hereby includes associated rights to acquire Series E Participating Cumulative Preferred Stock of Sterling Financial Corporation pursuant to the Rights Agreement described in the Prospectus contained in this registration statement.
- (3) Previously Paid.

The Registrant hereby amends this Registration Statement on such date or dates as may be necessary to delay its effective date until the Registrant shall file a further amendment which specifically states that this Registration Statement shall thereafter become effective in accordance with Section 8(a) of the Securities Act of 1933 or until the Registration Statement shall become effective on such date as the Commission acting pursuant to said Section 8(a), may determine.

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**The information in this Prospectus is not complete and may be changed. These securities may not be sold until the Registration Statement filed with the Securities and Exchange Commission is effective. This Prospectus is not an offer to sell these securities and neither we nor the selling shareholders are soliciting an offer to buy these securities in any state where the offer or sale is not permitted.**

**Subject to completion, dated November 3, 2010**

Prospectus

# STERLING FINANCIAL CORPORATION

*4,208,437,677 Shares of Common Stock*

*Warrants to Purchase 179,687,677 Shares of Common Stock*

This Prospectus relates to the offer and sale of up to 4,208,437,677 shares of our Common Stock, having no par value per share (the Common Stock), and two series of warrants to purchase a total of 179,687,677 shares of our Common Stock (the Warrants and together with the Common Stock, the Securities), by certain selling shareholders. We issued and sold the Securities as part of the Recapitalization Transactions (as defined below in Recapitalization Transactions). We are registering the resale of the Securities pursuant to agreements we entered into with the Selling Shareholders.

The Selling Shareholders may sell all or a portion of the Securities from time to time, in amounts, at prices and on terms determined at the time of offering. The Securities may be sold by any means described in the section of this Prospectus entitled Plan of Distribution beginning on page 62.

We will not receive any proceeds from the sale of the Securities by the Selling Shareholders. We will, however, receive cash proceeds equal to the total exercise price of any Warrants that are exercised for cash but will receive no cash if and to the extent that Warrants are exercised pursuant to the net, or cashless, exercise feature of the Warrants.

Our Common Stock is listed on the NASDAQ Capital Market under the symbol STSA. On November 1, 2010, the closing price of our Common Stock on the NASDAQ Capital Market was \$0.52 per share. The Warrants are not listed on the NASDAQ Stock Market (NASDAQ) or any other stock exchange.

The shares of Common Stock and Warrants offered pursuant to this Prospectus are subject to transfer restrictions related to the preservation of certain going-forward tax benefits and other restrictions, subject to certain exceptions. These restrictions will prevent you from acquiring, directly or indirectly, beneficial ownership of 4.95 percent or more of the Common Stock or certain other of our securities, subject to a number of exceptions. Beneficial ownership will be determined pursuant to the tax law and generally may include synthetic or derivative exposure to our securities or certain interests in investment vehicles or other entities that themselves beneficially own our securities. In the event that you own or acquire more than 4.95 percent of our shares, these restrictions will prevent you from disposing of our shares unless certain conditions apply. Furthermore, you will be restricted in your ability to transfer shares to another investor if that transfer would result in such investor owning in excess of 4.95 percent of our outstanding shares. In addition, investors not resident in Korea will be restricted in their ability to sell Securities to Korean residents, and Korean residents will be restricted in their ability to sell Securities to any Korean investor other than a professional investor, as defined under Korean law, subject to certain exceptions for open market transactions effected through the New York Stock Exchange or NASDAQ. See Transfer Restrictions and Rights Plan below.

**Investing in our Securities involves a high degree of risk. You should carefully read this Prospectus, our periodic reports and other information we have filed with the Securities and Exchange Commission (the SEC), and the information under the heading Risk Factors beginning on page 13 of this Prospectus, before buying any Securities.**

**Neither the SEC nor any state securities commission has approved or disapproved of the Securities or passed upon the adequacy or accuracy of this Prospectus. Any representation to the contrary is a criminal offense.**

**The Securities are not savings accounts, deposits or other obligations of any bank and are not insured or guaranteed by the Federal Deposit Insurance Corporation (the FDIC ), the Deposit Insurance Fund or any other governmental agency or instrumentality.**

The date of this Prospectus is [ ], 2010.

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### **ABOUT THIS PROSPECTUS**

We have not authorized anyone to provide any information or to make any representations other than those contained or incorporated by reference in this Prospectus or in any free writing prospectuses we have prepared. We take no responsibility for, and can provide no assurance as to the reliability of, any other information that others may give you. This Prospectus is an offer to sell only the securities offered hereby, but only under circumstances and in jurisdictions where it is lawful to do so. The information contained in this Prospectus is current only as of its date.

Neither we, nor any of our officers, directors, agents or representatives, make any representation to you about the legality of an investment in our Securities. You should not interpret the contents of this Prospectus to be legal, business, investment or tax advice. You should consult with your own advisors for that type of advice and consult with them about the legal, tax, business, financial and other issues that you consider before investing in our Securities.

This Prospectus does not offer to sell, or ask for offers to buy, any Securities in any state or jurisdiction where it would not be lawful or where the person making the offer is not qualified to do so.

Certificates evidencing the Common Stock will contain a legend referencing the Transfer Restrictions (as defined on pages 7-8). Any resale of the Common Stock must be made in accordance with these restrictions.

It is important for you to read and consider all of the information contained in this Prospectus in making your investment decision. You also should read and consider the information in the documents to which we have referred you in the sections entitled "Where You Can Find More Information" and "Incorporation of Certain Information by Reference."

References to Sterling, the Company, we, our, or us in this Prospectus refer to Sterling Financial Corporation, a Washington corporation, and consolidated subsidiaries on a combined basis, unless otherwise specified or the context otherwise requires. References to Sterling Savings Bank refer to our subsidiary Sterling Savings Bank, a Washington state-chartered commercial bank. References to our subsidiary bank or our banking subsidiary refer to Sterling Savings Bank.

### **WHERE YOU CAN FIND MORE INFORMATION**

We file annual, quarterly and current reports, proxy statements and other information with the SEC. Our SEC filings are available to the public at the SEC's website at [www.sec.gov](http://www.sec.gov). You may also read and copy any document we file with the SEC at its public reference facilities at 100 F Street, N.E., Washington, D.C. 20549. You can also obtain copies of the documents at prescribed rates by writing to the Public Reference Section of the SEC at 100 F Street, N.E., Washington, D.C. 20549. Please call the SEC at 1-800-SEC-0330 for further information on the operation of the public reference facilities.

We incorporate by reference into this Prospectus information we have filed with the SEC, which means that we are disclosing important information to you by referring you to documents incorporated by reference. The information incorporated by reference is an important part of this Prospectus. Some information contained in this Prospectus updates the information incorporated by reference.

### **INCORPORATION OF CERTAIN INFORMATION BY REFERENCE**

The SEC allows us to incorporate by reference into this Prospectus information in other documents we file with the SEC, which means that we can disclose important information to you by referring you to those documents. Information incorporated by reference is considered to be part of this Prospectus.

Other than any portions of any such documents that are not deemed filed under the Securities Exchange Act of 1934, as amended (the Exchange Act), in accordance with the Exchange Act and applicable SEC rules, we incorporate by reference the documents listed below, as amended:

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our Annual Report on Form 10-K, as amended, for the year ended December 31, 2009 (the 2009 Form 10-K );

our Amendment No. 1 on Form 10-K/A to the 2009 Form 10-K;

our Quarterly Reports on Form 10-Q for the quarter ended March 31, 2010 (the First Quarter Form 10-Q ) and the quarter ended June 30, 2010 (the Second Quarter Form 10-Q );

our Current Reports on Form 8-K filed on March 23 and 31, 2010; April 14, 15 and 27, 2010; May 3, 6, 17, 24, 26 and 27, 2010; June 8 and 9, 2010; August 13, 20, 26 and 30, 2010; September 23 and 28, 2010; and October 15 and 25, 2010

our Registration Statement on Form 8-A filed on April 15, 2010;

our Definitive Proxy Statement in connection with our special meeting of shareholders, filed on September 22, 2010 and

our Preliminary Proxy Statement in connection with our annual meeting of shareholders, filed on October 22, 2010.

You may request a copy of these filings, other than an exhibit to a filing unless that exhibit is specifically incorporated by reference into that filing, at no cost, by writing to or calling us at the following address:

Investor Relations

Sterling Financial Corporation

111 North Wall Street

Spokane, Washington 99201

(509) 227-5388 or (800) 336-6610 Ext. 1363

We maintain a website at [www.sterlingfinancialcorporation-spokane.com](http://www.sterlingfinancialcorporation-spokane.com) where the incorporated documents listed above can be accessed. Neither our website nor the information on our website is included or incorporated in, or is a part of, this Prospectus.

**CAUTIONARY NOTE REGARDING FORWARD-LOOKING STATEMENTS**

From time to time, Sterling and its senior managers have made and will make forward-looking statements that are not historical facts and that are intended to be covered by the safe harbor for forward-looking statements provided by the Private Securities Litigation Reform Act of 1995. These forward-looking statements may include, but are not limited to, statements about Sterling's plans, objectives, expectations and intentions and other statements contained in this Prospectus that are not historical facts and pertain to Sterling's future operating results. When used in this Registration Statement, the words expects, anticipates, intends, plans, believes, seeks, estimates and similar expressions are generally used to identify forward-looking statements. We make forward-looking statements regarding our ability to satisfy our undertakings to our state and federal regulators, our strategy of acquiring other banks in FDIC-assisted transactions and our ability to become qualified to bid in such transactions, our ability to obtain shareholder approval of certain proposed amendments to our Restated Articles of Incorporation in connection with our recapitalization efforts, our ability to strengthen asset quality oversight and resolution, our ability to emphasize growth in commercial business and consumer lending while reducing our exposure to construction and commercial real estate loans, our ability to expand and diversify our fee income, our ability to originate lower-cost core deposits with relationship banking initiatives, our ability to improve operating efficiency through improved expense management, projected sources of funds, use of proceeds, availability of acquisition and growth opportunities, our ability to repay government funds, payment of dividends, adequacy of our allowance for loan and lease losses and provision for loan and lease

losses, our real estate portfolio and subsequent charge-offs. Such statements may be contained in this Prospectus and in the documents that are incorporated by reference herein. Such statements may also be made by Sterling and its senior managers in oral or written presentations to investors or others.

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Actual results may differ materially from the results discussed in these forward-looking statements because such statements are inherently subject to significant assumptions, risks and uncertainties, many of which are difficult to predict and are generally beyond Sterling's control. These include but are not limited to:

our ability to maintain adequate liquidity and capital;

our ability to attract and retain deposits and loans;

demand for financial services in our market areas;

competitive market pricing factors;

further deterioration in economic conditions that could result in increased loan and lease losses;

risks associated with concentrations in real estate-related loans;

market interest rate volatility;

stability of funding sources and continued availability of borrowings;

changes in legal or regulatory requirements or the results of regulatory examinations that could restrict growth;

our ability to comply with the requirements of current and future regulatory orders issued to us and/or our banking subsidiary;

our ability to recruit and retain key management and staff;

risks associated with mergers and acquisitions and integration activities;

our ability to preserve our going-forward tax benefits, including net operating loss carry-forwards and certain built-in losses;

declines in our market value;

our ability to incur debt on reasonable terms;

regulatory limits on our subsidiary bank's ability to pay dividends to us;

effectiveness of legislative and regulatory reform of the financial sector; and

the impact of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act"), other regulatory reform, including but not limited to government-sponsored enterprise reform, and any related rules and regulations on Sterling's business operations and competitiveness, including the impact of executive compensation restrictions, which may affect Sterling's ability to retain and recruit executives in competition with other firms who do not operate under those restrictions.

Other factors that could cause actual conditions, events or results to differ significantly from those described in the forward-looking statements may be found under the headings "Risk Factors" below. Unless legally required, Sterling disclaims any obligation to update any forward-looking statements. You should consider any forward-looking statements in light of this explanation, and we caution you about relying on forward-looking statements.

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### PROSPECTUS SUMMARY

*This summary highlights certain information appearing elsewhere or incorporated by reference in this Prospectus. It does not contain all of the information that is important to you. For a more complete understanding of this offering, you should carefully read the entire Prospectus, the Registration Statement of which this is a part, and the information incorporated by reference in this Prospectus, including the financial statements.*

#### **Our Company**

##### **Business**

Sterling is a bank holding company, organized under the laws of Washington State in 1992. The principal operating subsidiary of Sterling is Sterling Savings Bank. Sterling Savings Bank, headquartered in Spokane, Washington, commenced operations in 1983 as a Washington state-chartered federally insured stock savings and loan association, and in 2005 converted to a commercial bank. Sterling Savings Bank offers commercial banking products and services, mortgage lending, construction financing and investment products to individuals, small businesses, commercial organizations and corporations.

Sterling is one of the largest commercial banks headquartered in the Pacific Northwest. Sterling's strategy centers on a community banking focus that brings the full product suite of a large regional institution to customers with the personalized service of a local community bank. Sterling believes that its dedication to personalized service and relationship banking has enabled it to attract both retail deposits and lending relationships in the western United States. Sterling originates loans and attracts FDIC insured and uninsured deposits from the general public throughout its five state footprint through its subsidiary bank, Sterling Savings Bank, and through its commercial real estate division INTERVEST-Mortgage Investment Company. Sterling also markets fixed income and equity products, mutual funds, fixed and variable annuities and other financial products through wealth management representatives located throughout Sterling's financial service center network.

At June 30, 2010, Sterling had total assets of \$9.74 billion, total liabilities of \$9.54 billion, including deposits of \$7.24 billion and total shareholders' equity of \$193.1 million, and operated 178 deposit-taking branches throughout the Western region of the United States, including the states of Washington, Oregon, Idaho, Montana and California. Our principal offices are located at 111 North Wall Street, Spokane, Washington 99201, and our telephone number at that location is (509) 227-5388 or (800) 336-6610 Ext. 1363.

##### **Strategy**

As a result of the recapitalization described below, Sterling and Sterling Savings Bank's capital levels as of September 30, 2010 were above those currently required to be deemed well-capitalized, and Sterling continues to pursue the following strategies:

*Strengthening Asset Quality Oversight and Resolution.* To address the deteriorating economic environment in early 2008, Sterling established a credit administration group to focus specifically on the identification and resolution of construction and commercial real estate-related assets that are currently or expected to become problem assets. This group operates independently from a parallel credit administration team dedicated to monitoring the performing loans in Sterling's loan portfolio. This separation of duties has allowed Sterling to continue its strategic goal of achieving targeted levels of loan portfolio diversification while addressing issues related to problem assets. In addition, the creation of a sales team to proactively handle the sale of other real estate owned has facilitated efficient asset resolution, which, in turn, has reduced the negative impact of carrying nonperforming assets on Sterling's balance sheet.

*Emphasizing Growth in Commercial Business and Consumer Lending While Reducing Exposure to Construction and Commercial Real Estate Loans.* Sterling continues to optimize its balance sheet mix to achieve increased risk adjusted returns by rebalancing loan-portfolio concentrations, aligning loan





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pricing with credit risk and improving the overall mix of earning assets. From December 31, 2008 to June 30, 2010, Sterling reduced its portfolio of construction loans by \$1.58 billion, or 62 percent.

*Originating Lower-Cost Core Deposits with Relationship Banking Initiatives.* Sterling has implemented a number of relationship-focused deposit initiatives over the last two years, resulting in growth of core deposits, including non-interest bearing checking accounts. The change in deposit mix has contributed to Sterling's cost of funds decreasing from 2.31 percent as of June 30, 2009 to 1.71 percent as of June 30, 2010. Our deposit-related fee income may increase to the extent there is an increase in transaction deposit account activity. In addition, the growth in our core deposits has begun to reduce our need for wholesale borrowings as a funding source.

*Expanding and Diversifying Our Fee Income.* Sterling continues to explore opportunities to grow fee income through existing products and services as well as new sources, including deposit fees, transaction fees and fees from mortgage banking. These activities focus on relationship banking and our Hometown Helpful value proposition. We are committed to providing our customers with knowledgeable bankers delivering valuable products and services at a fair price and in a convenient and accessible fashion. Income from mortgage banking operations grew by \$19.6 million, or 71.1 percent, during the year ended 2009, compared with the same period in 2008, and decreased by \$4.1 million, or 15.1 percent, during the six months ended June 30, 2010, compared with the six months ended June 30, 2009.

*Improving Operating Efficiency Through Improved Expense Management.* In an effort to improve operating efficiency, Sterling has implemented expense savings initiatives. Earlier this year, Sterling Savings Bank revised its branch staffing model and eliminated redundant positions. Through these and other efforts, Sterling Savings Bank reduced its full-time equivalent branch and administrative staffing by approximately 6.5 percent since the beginning of 2009 through June 30, 2010.

*Growth Through Opportunistic Acquisitions.* Multiple banks in Sterling's core and secondary markets in the Pacific Northwest region have been identified as potential troubled banks and Sterling believes other banks are considering potential strategic transactions in light of their performance in this latest business cycle. Post-recapitalization, Sterling's strategy is to position itself to serve as a consolidator and take advantage of opportunities to bid on both FDIC assisted and non-assisted transactions. However, in order to be qualified to bid on FDIC-assisted transactions, Sterling must, among other things, work with its regulators to satisfy the regulatory concerns that are embodied in agreements and undertakings with its state and federal regulators. Please refer to "Recapitalization Transactions Background" below. Although there can be no assurances that this strategic goal will be achieved in a short time frame or even at all, the amount of capital raised in the recapitalization transactions described below, the restructuring of our Board of Directors and the recent management changes are all designed to increase the possibility that Sterling will be in a position to pursue opportunistic expansion through acquisition. See "Risk Factors" We cannot determine whether or when certain agreements entered into with our regulators will be lifted and "Risk Factors" Our strategy of pursuing FDIC-assisted acquisition opportunities may not be successful.

The FDIC has adopted a Final Statement of Policy on Qualifications for Failed Bank Acquisitions (the "FDIC Policy Statement") that would, if applicable, impose heightened capital requirements on Sterling and substantial restrictions on certain investors were Sterling to acquire one or more failed banks. Moreover, as a result of recent changes to the FDIC Policy Statement, the FDIC has indicated that the Policy Statement will not apply to Sterling's Recapitalization (as defined below) or to the investors that participated in Sterling's Recapitalization because the capital raised in the Recapitalization was not contingent on the completion of failing bank acquisitions, *provided that* any future acquisition of one or more failed institutions by Sterling does not exceed, in combination, 100 percent of Sterling's total assets within an 18-month period following the Recapitalization. There can be no

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assurance that, if in a position to bid, Sterling will be successful in any such acquisition. Similarly, there can be no assurance that the FDIC will not change or modify the FDIC Policy Statement in the future. See **Risk Factors** The FDIC Policy Statement will limit our ability to acquire failed banks.

### **Recent Developments**

#### **Background**

As described in more detail below, Sterling recently completed several transactions as part of its recapitalization and recovery plan, which was initiated in response to a number of challenges in recent periods. These challenges resulted from current and prior period losses, driven by credit quality issues.

On October 9, 2009, Sterling Savings Bank consented to the issuance of a cease and desist order (the **SSB Consent Agreement**) with the FDIC and the Washington State Department of Financial Institutions (**WDFI**). Under the terms of the SSB Consent Agreement, Sterling Savings Bank agreed to, among other things, maintain a Tier 1 leverage ratio of not less than 10%. Pursuant to the SSB Consent Agreement, Sterling Savings Bank agreed to take certain actions, including: raising additional capital; reducing the number of nonperforming assets; reducing the number of commercial real estate and land development loans; restricting extensions of additional credit to borrowers with classified loans; implementing a liquidity and funds management policy that addresses liquidity needs and reduces reliance on non-core funding sources; restricting cash dividend payments; and complying with interest rate limitations on deposits. As discussed below in **Recent Developments Regulatory Agreements**, in September 2010, Sterling received notice that the SSB Consent Agreement had been terminated.

On December 24, 2009, Sterling entered into a written agreement (the **Reserve Bank Agreement**) with the Federal Reserve Bank of San Francisco (the **Reserve Bank**). The Reserve Bank Agreement is intended to enhance Sterling's ability to act as a source of strength to Sterling Savings Bank. Substantially all of the requirements of the Reserve Bank Agreement are similar to those that were imposed on Sterling Savings Bank by the FDIC and the WDFI pursuant to the SSB Consent Agreement, including restrictions on the payment of dividends and prohibitions on the purchase or redemption by Sterling of any shares of its stock.

In late 2009, Sterling failed to meet deadlines to raise additional capital and improve leverage ratios as required by the SSB Consent Agreement and the Reserve Bank Agreement. As a result of the uncertainty regarding Sterling's ability to comply with these agreements, Sterling's Independent Registered Public Accounting Firm added an explanatory paragraph in its audit opinion issued in connection with our December 31, 2009 consolidated financial statements, expressing substantial doubt regarding Sterling's ability to continue as a going concern.

During the fourth quarter of 2009, Sterling announced a management change that resulted in the appointment of a new President and Chief Executive Officer, a new Chief Operating Officer, as well as a new Chairman of the Board. The new management team developed several strategies to address the capital and liquidity needs of the organization, revamped Sterling's credit underwriting with a focus on consumer and commercial relationship banking and initiated recapitalization efforts designed to return Sterling to sound financial footing. As a result of the successful completion of the transactions described in **The Recapitalization** section below, Sterling and Sterling Savings Bank as of September 30, 2010 were capitalized in excess of levels currently required to be deemed well-capitalized, which is expected to help Sterling continue to pursue its goal of being the leading community bank in the West and position it to take advantage of potential growth opportunities in the regional banking market.

#### **The Recapitalization**

The recapitalization comprised three principal transactions (collectively, the **Recapitalization Transactions** or the **Recapitalization**):

an investment of approximately \$170.9 million by each of (a) Thomas H. Lee Equity Fund VI, L.P., Thomas H. Lee Parallel Fund VI, L.P., Thomas H. Lee Parallel (DT) Fund VI, L.P. and THL Sterling Equity Investors, L.P. (collectively, **THL** or an **Anchor Investor**) and (b) Warburg Pincus Private Equity X, L.P. ( **Warburg Pincus** or an **Anchor Investor**), pursuant to which each received 68,366,000 shares of Common Stock, 1,709,150 shares of Series B Convertible Participating Voting Preferred Stock (the **Series B Preferred Stock**) and a seven-year warrant to purchase 86,625,000 shares of Common Stock at an exercise price of \$0.22 per share (the **Anchor Investments**), effected pursuant to investment agreements between Sterling and each of the Anchor Investors (the **Anchor Investment Agreements**);



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the exchange of 303,000 shares of Fixed Rate Cumulative Perpetual Preferred Stock, Series A held by the U.S Department of the Treasury ( Treasury ) for 303,000 shares of Fixed Rate Cumulative Mandatorily Convertible Preferred Stock, Series C with a liquidation preference of \$303 million, conversion of such Series C preferred stock at a discounted exchange value of approximately \$75.8 million into 378,750,000 shares of Common Stock at a conversion price of \$0.20 per share, and amendment of the terms of the warrant held by Treasury (the Treasury Warrant ) to purchase 6,437,677 shares of Common Stock at an exercise price of \$7.06 per share to provide for an exercise price of \$0.20 per share for a ten-year term (the Treasury Exchange ), effected pursuant to an exchange agreement between Sterling and Treasury (the Exchange Agreement ); and

investments by accredited investors of approximately \$388.2 million in aggregate, pursuant to which such investors (the Private Placement Investors ) received in aggregate 155,268,000 shares of Common Stock and 3,881,700 shares of Series D Convertible Participating Voting Preferred Stock (the Series D Preferred Stock ) as part of a private placement (the Private Placement ), effected pursuant to subscription agreements between Sterling and each Private Placement Investor (the Subscription Agreements ).

Also in connection with the Recapitalization Transactions, new directors were appointed to our Board of Directors and certain directors retired. See The Recapitalization Governance below. For additional information regarding the Recapitalization Transactions, see The Recapitalization below.

**Special Meeting of Shareholders**

Pursuant to the terms of the Anchor Investment Agreements and the Subscription Agreements, Sterling agreed to call a special meeting of its shareholders (the Special Meeting ) and seek approval to (i) amend its Restated Articles of Incorporation to increase the number of authorized shares of its Common Stock from 750,000,000 to 10,000,000,000, in a manner sufficient to permit the full conversion of the Series B Preferred Stock and Series D Preferred Stock into, and exercise of the warrants issued to THL and Warburg Pincus for, shares of Common Stock and (ii) approve the conversion of the Series B Preferred Stock and the Series D Preferred Stock into, and the exercisability of the warrants issued to THL and Warburg Pincus for, shares of common stock.

On October 21, 2010, Sterling held the Special Meeting at which Sterling s shareholders approved each of the proposals detailed in Sterling s Definitive Proxy Statement on Schedule 14A, which was filed with the Securities and Exchange Commission on September 22, 2010. At the Special Meeting, shareholders approved: (1) the amendment of Sterling s Restated Articles of Incorporation to increase the authorized number of shares of common stock from 750,000,000 to 10,000,000,000; (2) the conversion of Sterling s outstanding Series B Convertible Participating Voting Preferred Stock and Series D Convertible Participating Voting Preferred Stock into, and exercisability of Sterling s outstanding warrants issued to THL and to Warburg Pincus for, shares of common stock; and (3) the amendment of Sterling s Restated Articles of Incorporation to effect a reverse stock split of Sterling s common stock at a ratio to be determined by Sterling s Board of Directors between one-for-50 and one-for-125 shares of common stock. Accordingly, each share of Series B Preferred Stock and Series D Preferred Stock was converted into 460 shares of Common Stock on October 22, 2010. Upon such conversion, all shares of Series B Preferred Stock and Series D Preferred Stock ceased to exist and resumed the status of authorized and unissued shares of Sterling s preferred stock. Additionally, the warrants held by THL and Warburg Pincus became exercisable for shares of Sterling Common Stock and are no longer exercisable for shares of Series B Preferred Stock.

**Regulatory Agreements**

On September 27, 2010, Sterling announced receipt of notice from its banking regulators that the SSB Consent Agreement put in place in October 2009 with Sterling Savings Bank had been terminated, reflecting a strengthened balance sheet and capital position. Although the SSB Consent Agreement is no

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longer applicable, Sterling Savings Bank will continue to be subject to enhanced supervisory scrutiny by the FDIC and WDFI under a memorandum of understanding (the SSB MOU ), pursuant to which Sterling Savings Bank must maintain Tier 1 capital in an amount that ensures that its leverage ratio is at least 8 percent. Sterling Savings Bank will also be required to meet certain asset quality targets, develop a written capital plan, develop a three-year strategic plan and comply with other requirements.

Under the terms of the Reserve Bank Agreement, Sterling is subject to restrictions on its ability to pay dividends and distributions, incur debt, purchase or redeem its stock and appoint new board members or senior executive officers. Under the Reserve Bank Agreement, Sterling is also required to act as a source of strength to Sterling Savings Bank and to report quarterly to the Reserve Bank on steps taken to improve its capital ratios and risk, liquidity and fund management and on other matters. See Risk Factors We cannot determine whether or when certain agreements entered into with our regulators will be lifted.

## **Results of Operations**

Sterling reported a net loss attributable to common shareholders during the nine months ended September 30, 2010 and 2009 of \$113.4 million and \$522.4 million, respectively, or \$0.81 and \$10.06 per common share, respectively. The 2010 results included a provision for credit losses of \$220.2 million, a one-time, non-cash increase to income available to common shareholders of \$84.3 million related to conversion of Treasury s preferred stock investment into common stock, and an increase in the allowance for deferred tax assets of \$76.0 million. The 2009 results included a provision for credit losses of \$341.1 million, a non-cash charge for goodwill of \$227.6 million and an allowance for deferred tax assets of \$143.0 million. Sterling s cumulative efforts to address credit quality have led to the lower provision for credit losses, and a decline in the balance of total classified assets.

Net interest income declined 23 percent and 18 percent over the respective three and nine months ended September 30, 2010 compared to the 2009 periods, reflecting the decline in average loan balances, the reversal of interest income on nonperforming loans, and the increase in cash and short term investments relative to loans. Loan originations during the three and nine months ended September 30, 2010 totaled \$810.5 million and \$2.03 billion, respectively, the majority of which were through the Home Loan Division for sale into the secondary market.

Sterling continued to deleverage its balance sheet throughout the nine months ended September 30, 2010, as reflected in assets with a 23 percent, or \$1.68 billion decline in loan balances, and in liabilities with a 71 percent, or \$762.5 million reduction of brokered deposits, 37 percent, or \$499.9 million decline in FHLB advances, and the 58 percent, or \$300.8 million decline in public transaction accounts. The concentration of construction loans declined, reflecting progress in credit risk management. Retail deposits increased as a percentage of total deposits reflecting improvement in the mix of the deposit base.

During the third quarter of 2010, Sterling Savings Bank returned to a well-capitalized status following the termination of the FDIC cease and desist order, with the termination of the order occurring subsequent to the receipt of aggregate proceeds of \$730.0 million from the Recapitalization. Driven by the inflow of funds from the Recapitalization Transactions, the investment securities portfolio grew by \$767.0 million during the third quarter. Key financial measures as of and for the periods ended September 30, 2010 include:

Tier 1 leverage ratio was 10.5% at September 30, 2010 compared with 2.0% at June 30, 2010.

Classified assets declined by \$315.0 million, or 19 percent from the beginning of the year.

Non-performing loans declined 10 percent to \$809.0 million, compared to \$895.9 million at December 31, 2009.

Construction loans were 12 percent of the loan portfolio as of September 30, 2010, as compared with 20 percent as of December 31, 2009.

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Retail deposits increased to 87 percent of total deposits from 76 percent of total deposits at the beginning of the year.

Deposit funding costs were 127 basis points during the third quarter of 2010, which was 70 basis points below the same period in 2009.

**Transfer Restrictions and Rights Plan**

We have generated considerable going-forward tax benefits, including net operating loss carry-forwards and certain built-in losses. Our ability to use these net operating loss carry-forwards and built-in losses to offset future taxable income will be limited if we experience an ownership change as defined in Section 382 of the Internal Revenue Code of 1986, as amended from time to time (the Code). See Risk Factors Our ability to use our deferred tax assets may be materially impaired below.

As further described in Transfer Restrictions and Rights Plan below, the Securities offered pursuant to this Prospectus, subject to certain exceptions, are subject to transfer restrictions as set forth in a proposed amendment to our Articles of Incorporation as though such proposed amendment were at all relevant times in effect. These transfer restrictions are designed to prevent (a) any person from acquiring ownership, for relevant tax purposes, of 5 percent or more of our shares and (b) the disposition of shares by any person that owns 5 percent or more of our shares, subject to certain exceptions. At our annual meeting, we intend to propose an amendment to our Articles of Incorporation that would impose these transfer restrictions on other holders of our Common Stock. For more information, see our preliminary proxy statement filed on October 22, 2010 in connection with the annual meeting on December 7, 2010.

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In addition, in order to reduce the likelihood that future transactions in our stock will result in an ownership change, we have adopted a shareholder rights plan (the "Rights Plan"). Subject to certain exceptions, the Rights Plan provides an economic disincentive for any one person or group to become a Threshold Holder (defined therein as, any one person or group owning, for relevant tax purposes, 5 percent or more of our shares) and for any existing Threshold Holder to acquire more than a specified amount of additional shares. As a result, the Rights Plan may adversely affect your ability to resell our Common Stock and negatively affect the trading price of our Common Stock.

Further, if you are an investor residing in a country other than the Republic of Korea, you may not sell, assign or transfer any shares of Common Stock to a Korean resident (as defined in the Foreign Exchange Transaction Law of Korea) on or prior to August 26, 2011. If you are an investor resident in the Republic of Korea, you may not sell, assign or transfer any shares of Common Stock to any Korean investor other than a professional investor (as defined in the Enforcement Decree of the Financial Investment Services and Capital Markets Act of Korea) on or prior to August 26, 2011. The restrictions in the prior sentences shall not apply to open market transactions effected through the New York Stock Exchange or NASDAQ.

The transfer restrictions set forth in the proposed amendment to our articles of incorporation and those related to Korea are referred to generally as the "Transfer Restrictions."

See "Transfer Restrictions and Rights Plan" below.

**Risk Factors**

An investment in our Common Stock involves certain risks. You should carefully consider the risks described under "Risk Factors" beginning on page 13 of this Prospectus, as well as other information included or incorporated by reference into this Prospectus, including our financial statements and the notes thereto, before making an investment decision.

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**The Offering**

<b>Issuer</b>	Sterling Financial Corporation
<b>Securities offered by us</b>	None.
<b>Securities offered by the selling shareholders</b>	4,208,437,677 shares of Common Stock, having no par value per share. Warrants to purchase 179,687,677 shares of Common Stock. <sup>(1)</sup>
<b>Common Stock outstanding after this offering</b>	shares of Common Stock. <sup>(2)</sup>
<b>Use of proceeds</b>	We will receive no proceeds from the shares of Common Stock sold by the Selling Shareholders. We may, however, receive cash proceeds equal to the total exercise price of any warrants that are exercised for cash, but will receive no cash if and to the extent that warrants are exercised pursuant to the net, or cashless, exercise feature of the warrants.
<b>NASDAQ symbol</b>	STSA
<b>Risk Factors</b>	For a discussion of risks associated with an investment in the Securities, see the section entitled Risk Factors.

- <sup>(1)</sup> Warrants are transferable in single share increments. The Warrants have been issued in two separate series. For more information, see the section entitled Description of the Warrants below.
- <sup>(2)</sup> The number of shares of Common Stock to be outstanding after this offering is based on shares outstanding as of , 2010 and assumes no exercise of warrants to purchase 179,687,677 shares of Common Stock or other outstanding securities that are convertible into or exercisable or exchangeable for Common Stock. As of , 2010, there were shares of Common Stock reserved for issuance under our stock option and stock incentive plans and agreements, of which options to purchase shares at an average price of \$ were outstanding.



**Table of Contents****SUMMARY CONSOLIDATED FINANCIAL DATA**

The following table sets forth summary consolidated financial data of Sterling. The financial data as of and for the six months ended June 30, 2010 and 2009 have been derived from our unaudited financial statements contained in our Quarterly Reports on Form 10-Q filed with the SEC. The financial data as of and for the years ended December 31, 2009, 2008, 2007, 2006 and 2005 have been derived from our audited financial statements contained in our Annual Reports on Form 10-K filed with the SEC. The summary condensed consolidated financial results are not indicative of our expected future operating results. The following summary historical financial information should be read together with Management's Discussion and Analysis of Financial Condition and Results of Operations and the historical financial statements and notes thereto incorporated by reference in this Prospectus.

	Six months ended June 30,		As of and for the years ended December 31,				
	2010	2009	2009	2008	2007	2006	2005
	(Dollars in thousands except per share data)						
<b>Income Statement</b>							
Interest income:							
Loans	\$ 190,861	\$ 250,871	\$ 479,436	\$ 599,192	\$ 679,991	\$ 458,558	\$ 296,306
MBS	38,442	57,458	108,513	102,863	79,266	88,398	88,682
Investments and cash equivalents	5,398	6,321	11,398	13,007	7,721	3,899	2,823
Total interest income	234,701	314,650	599,347	715,062	766,978	550,855	387,811
Interest expense:							
Deposits	52,514	92,922	169,261	234,337	277,614	185,273	91,990
Short-term borrowings	4,214	9,199	16,476	20,820	29,956	35,979	35,255
Long-term borrowings	29,988	36,562	69,633	100,353	104,048	65,691	44,031
Total interest expense	86,716	138,683	255,370	355,510	411,618	286,943	171,276
Net interest income	147,985	175,967	343,977	359,552	355,360	263,912	216,535
Provision for credit losses	(159,337)	(145,609)	(681,371)	(333,597)	(25,088)	(18,703)	(15,200)
Net interest income (loss) after provision for credit losses	(11,352)	30,358	(337,394)	25,955	330,272	245,209	201,335
Non-interest income:							
Fees and service charges	27,268	28,718	58,326	59,867	55,978	42,995	34,702
Mortgage banking operations	22,945	27,040	47,298	27,651	32,649	20,216	17,899
Loan servicing fees	738	555	2,378	431	1,442	1,812	434
BOLI	3,855	3,406	6,954	5,286	6,500	5,020	5,914
Gain (charge) related to early repayment of debt	0	0	0	0	(2,324)	(204)	645
Gains (losses) on sales of securities	17,260	11,557	13,467	409	5	0	(57)
Other non-interest expense	(5,541)	(2,958)	(4,609)	(1,749)	(844)	(675)	(445)
Total non-interest income	66,525	68,318	123,814	91,895	93,406	69,164	59,092
Non-interest expenses before impairment charge							
Goodwill impairment	0	0	227,558	223,765	0	0	0
Total non-interest expenses	193,292	185,137	597,532	529,282	285,465	206,197	169,804

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Income (loss) before income taxes	(138,119)	(86,461)	(811,112)	(411,432)	138,213	108,176	90,623
Income tax benefit (provision)	0	36,485	(26,982)	75,898	(44,924)	(34,230)	(29,404)
Net income (loss)	(138,119)	(49,976)	(838,094)	(335,534)	93,289	73,946	61,219
Preferred stock dividend	(8,881)	(8,694)	(17,369)	(1,208)	0	0	0
Net income (loss) applicable to common shareholders	\$ (147,000)	\$ (58,670)	\$ (855,463)	\$ (336,742)	\$ 93,289	\$ 73,946	\$ 61,219

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	As of and for the six months ended June 30,		As of and for the years ended December 31,				
	2010	2009	2009	2008	2007	2006	2005
(Dollars in thousands except per share data)							
<b>Selected Financial Data</b>							
Total Assets	\$ 9,737,781	\$ 12,399,775	\$ 10,877,423	\$ 12,790,716	\$ 12,149,775	\$ 9,834,492	\$ 7,562,377
Loans receivable, net	6,140,913	8,441,402	7,344,199	8,807,094	8,948,307	7,021,241	4,889,366
Mortgage-backed securities	1,741,395	2,433,075	1,944,989	2,420,012	1,785,031	1,687,672	1,960,582
Investments	214,495	283,146	232,982	395,108	201,033	134,077	91,331
Goodwill and other intangibles	19,378	251,834	21,827	254,283	484,763	275,814	130,332
Deposits	7,240,769	8,303,741	7,775,190	8,350,407	7,677,772	6,746,028	4,806,301
Borrowings	2,146,444	2,845,846	2,634,594	3,137,848	3,139,849	2,165,197	2,165,826
Shareholders' equity							
Preferred	295,203	293,084	294,136	291,964	0	0	0
Common	(102,084)	803,375	29,113	849,072	1,185,330	783,416	506,685
Total shareholders equity	193,119	1,096,459	323,249	1,141,036	1,185,330	783,416	506,685
Tangible common equity	(121,462)	551,541	7,286	594,789	700,567	507,602	376,353
Shareholders' equity to total assets	1.98%	8.84%	2.97%	8.92%	9.76%	7.97%	6.70%
Tangible common shareholders' equity to tangible assets	-1.25%	4.54%	0.07%	4.74%	6.01%	5.31%	5.07%
Allowance for loan losses	\$ 264,850	\$ 223,709	\$ 343,443	\$ 208,365	\$ 111,026	\$ 77,849	\$ 52,033
Net charge-offs to average net loans (annualized)	5.47%	3.26%	12.57%	7.80%	0.18%	0.06%	0.24%
Classified Assets	1,400,663	1,215,271	1,650,550	984,875	234,336	48,356	59,611
Classified Assets/total assets	14.38%	9.80%	15.17%	7.70%	1.93%	0.49%	0.79%
Loan loss allowance to total loans	4.13%	2.58%	4.47%	2.31%	1.23%	1.10%	1.05%
Loan loss allowance to nonperforming loans	30.0%	32.1%	38.3%	39.3%	89.4%	917.4%	531.9%
Loan loss allowance to nonperforming loans excluding nonaccrual loans carried at fair value	154.3%	87.0%	163.5%	88.1%	89.4%	917.4%	531.9%
Total nonperforming assets (NPA)	\$ 1,033,437	\$ 787,454	\$ 987,409	\$ 610,665	\$ 135,215	\$ 12,538	\$ 10,561
Specific reserve on nonperforming assets	(32,128)	(24,554)	(35,334)	(19,535)	(8,678)	(1,379)	(2,159)
Net nonperforming assets	\$ 1,001,309	\$ 762,900	\$ 952,075	\$ 591,130	\$ 126,537	\$ 11,159	\$ 8,402
NPA to total assets	10.61%	6.35%	9.08%	4.77%	1.11%	0.13%	0.14%
Loan delinquency ratio (60 days and over)	9.29%	6.45%	8.11%	4.86%	1.23%	0.10%	0.18%

**REGULATORY  
CAPITAL RATIOS:**Sterling Financial  
Corporation:

Tier 1 leverage (to average assets)	2.0%	8.7%	3.5%	9.2%	8.7%	8.7%	7.4%
Tier 1 (to risk-weighted assets)	3.0%	11.7%	4.9%	11.7%	10.1%	10.0%	9.5%
Total (to risk-weighted assets)	5.8%	13.0%	7.9%	13.0%	11.3%	11.1%	10.5%

**Per Share Data**

Earnings per common share basic	\$	(2.83)	\$	(1.13)	\$	(16.48)	\$	(6.51)	\$	1.87	\$	2.03	\$	1.77
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Earnings per common share diluted	\$	(2.83)	\$	(1.13)	\$	(16.48)	\$	(6.51)	\$	1.86	\$	2.01	\$	1.75
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Weighted average shares outstanding basic	51,994,737	51,909,350	51,922,275	51,721,671	49,786,349	36,423,095	34,633,952
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Weighted average shares outstanding diluted	51,994,737	51,909,350	51,922,275	51,721,671	50,217,515	36,841,866	35,035,029
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**Table of Contents****RATIO OF EARNINGS TO FIXED CHARGES AND PREFERRED DIVIDENDS**

The following table sets forth the consolidated ratio of earnings to combined fixed charges and preferred stock dividends:

	Six Months		Years Ended December 31,			
	Ended June 30, 2010	2009	2008	2007	2006	2005
(Dollars in thousands)						
<b>EXCLUDING INTEREST ON DEPOSITS:</b>						
Pre-tax income	\$ (138,119)	\$ (811,112)	\$ (411,432)	\$ 138,213	\$ 108,176	\$ 90,623
Preferred stock dividend	(8,881)	(17,369)	(1,208)	0	0	0
Pre-tax income available to common shareholders	(147,000)	(828,481)	(412,640)	138,213	108,176	90,623
Fixed charges	44,724	109,128	129,282	140,816	105,838	81,930
Earnings	\$ (102,276)	\$ (719,353)	\$ (283,358)	\$ 279,029	\$ 214,014	\$ 172,553
Interest expense-short term borrowings	\$ 4,214	\$ 16,476	\$ 20,820	\$ 29,956	\$ 35,979	\$ 35,255
Interest expense-long term borrowings	29,988	69,633	100,353	104,048	65,691	44,031
Preferred stock dividend	8,881	17,369	1,208	0	0	0
Portion of long-term leases representative of the interest factor**	1,641	5,650	6,901	6,812	4,168	2,644
Fixed charges	\$ 44,724	\$ 109,128	\$ 129,282	\$ 140,816	\$ 105,838	\$ 81,930
Earnings to fixed charges, excluding interest on deposits	*	*	*	1.98	2.02	2.11
<b>INCLUDING INTEREST ON DEPOSITS:</b>						
Pre-tax income	\$ (138,119)	\$ (811,112)	\$ (411,432)	\$ 138,213	\$ 108,176	\$ 90,623
Preferred stock dividend	(8,881)	(17,369)	(1,208)	0	0	0
Pre-tax income available to common shareholders	(147,000)	(828,481)	(412,640)	138,213	108,176	90,623
Fixed charges	97,238	278,389	363,619	418,430	291,111	173,920
Earnings	\$ (49,762)	\$ (550,092)	\$ (49,021)	\$ 556,643	\$ 399,287	\$ 264,543
Interest expense-short term borrowings	\$ 56,728	\$ 185,737	\$ 255,157	\$ 307,570	\$ 221,252	\$ 127,245
Interest expense-long term borrowings	29,988	69,633	100,353	104,048	65,691	44,031
Preferred stock dividend	8,881	17,369	1,208	0	0	0
Portion of long-term leases representative of the interest factor **	1,641	5,650	6,901	6,812	4,168	2,644
Fixed charges	\$ 97,238	\$ 278,389	\$ 363,619	\$ 418,430	\$ 291,111	\$ 173,920
Earnings to fixed charges, including interest on deposits	*	*	*	1.33	1.37	1.52

\*

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Earnings to fixed charges and preferred dividends were a deficiency of \$147.0 million for the six months ended June 30, 2010, and \$828.5 million and \$412.6 million for the years ended December 31, 2009 and 2008, respectively.

\*\* The interest factor on long-term operating leases represented a reasonable approximation of the appropriate portion of operating lease expense considered to be representative of interest.

Ratios were derived from our annual reports on Form 10-K for the years ended December 31, 2009, 2008, 2007, 2006, and 2005, and our quarterly report on Form 10-Q for the six months ended June 30, 2010. The ratio of earnings to fixed charges and preferred stock dividends were computed by dividing earnings, as adjusted, by fixed charges and, where applicable, preferred dividends. For this purpose, earnings consist of income from continuing operations before taxes, fixed charges and preferred dividends. Fixed charges consist of interest expense on borrowings, including and excluding deposits, and imputed interest expense on operating leases. Prior to December 5, 2008, Sterling had no shares of preferred stock outstanding.

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**RISK FACTORS**

An investment in the Securities involves risks. Before making an investment, you should carefully consider the risks described below, as well as the other information included or incorporated by reference into this Prospectus. The risks described below are not the only ones facing our company. Additional risks not presently known to us or that we currently deem immaterial may also impair our business operations. Our business, financial condition, results of operations or prospects could be materially and adversely affected by any of these risks. The trading price of, and market for, the Securities could decline due to any of these risks, and you may lose all or part of your investment. This Prospectus, including the documents incorporated by reference herein, also contain forward-looking statements that involve risks and uncertainties. Our actual results could differ materially from those anticipated in these forward-looking statements as a result of certain factors, including the risks described below and in the documents incorporated by reference herein.

**If the proceeds from the Recapitalization are not sufficient to satisfy our capital and liquidity needs or to satisfy changing regulatory requirements, we may need even more capital and could be subject to further regulatory restrictions, either of which could significantly adversely affect us and the trading price of our stock.**

The proceeds from the Recapitalization have been raised to strengthen our common equity capital base. If the proceeds from the Recapitalization prove not to be sufficient, or if economic conditions continue to be difficult or worsen or fail to improve in a timely manner, or if our operations or financial condition deteriorates or fails to improve, particularly in the residential and commercial real estate markets where our business is located, we may need to raise significant additional capital. Factors affecting whether we would need to raise additional capital include, among others, changing requirements of regulators, additional provisions for loan losses and loan charge-offs and other risks discussed in this Risk Factors section. If we were to need to raise additional capital, we may not be able to do so in the amounts required and in a timely manner, or at all. Our ability to raise additional capital may be constrained by our need to preserve our deferred tax assets. For more information, see Our ability to use our deferred tax assets may be materially impaired below. In addition, any such additional capital raised may be significantly dilutive to our existing shareholders and may result in the issuance of securities that have rights, preferences and privileges that are senior to our Common Stock.

**We may issue securities that could dilute your ownership and may adversely affect the market price of our Common Stock and Warrants.**

We may decide to raise additional funds through public or private debt or equity financings for a number of reasons, including in response to regulatory or other requirements to meet our liquidity and capital needs as discussed above, to finance our operations and business strategy (including potential acquisitions) or for other reasons. If we raise funds by issuing equity securities or instruments that are convertible into equity securities, the percentage ownership of our existing shareholders will be reduced, the new equity securities may have rights, preferences and privileges superior to those of our Common Stock and additional issuances could be at a purchase price that is lower than the available market price for our Common Stock. The Anchor Investors and Private Placement Investors also have pre-emptive rights to maintain their ownership percentages in certain circumstances. In addition, there are anti-dilution adjustments in the Warrants that may protect the holders thereof against below-market issuances. There is no such protection available to holders of our Common Stock generally. To the extent that any new issuance of equity securities triggers these anti-dilution adjustments, your ownership could be further diluted. Except as described above, holders of our Common Stock have no pre-emptive rights that entitle them to purchase their pro rata share of any offering of shares of any class or series. The market price of our Common Stock or our Warrants could decline as a result of sales of a large number of shares of Common Stock, preferred stock or similar securities in the market as a result of future sales of Common Stock or the perception that such sales could occur. We may also issue equity securities as consideration for acquisitions we may make that could be dilutive to existing shareholders.

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### **We cannot determine whether or when certain agreements entered into with our regulators will be lifted.**

Following the September 17, 2010 termination of the SSB Consent Agreement, Sterling Savings Bank remains subject to enhanced supervisory scrutiny on an informal basis in the form of the SSB MOU. Though the SSB MOU's requirements are less strenuous than the SSB Consent Agreement's were, Sterling Savings Bank is required to maintain Tier 1 capital in an amount that ensures that the bank's leverage ratio is at least 8%. The SSB MOU also requires Sterling Savings Bank to meet certain asset quality targets, develop a written capital plan, develop a three-year strategic plan and accept other limitations.

Under the terms of the Reserve Bank Agreement, Sterling is subject to restrictions on its ability to pay dividends and distributions, incur debt, purchase or redeem its stock and appoint new board members or senior executive officers. Under the Reserve Bank Agreement, Sterling is also required to act as a source of strength to Sterling Savings Bank and to report quarterly to the Reserve Bank on steps taken to improve its capital ratios and risk, liquidity and fund management and on other matters.

We cannot determine whether or when the SSB MOU or the Reserve Bank Agreement will be lifted or terminated. Even if the Reserve Bank Agreement is lifted or terminated, we may remain subject to a memorandum of understanding or other undertaking with the Reserve Bank that restricts our activities and continues to impose higher capital ratios, as the SSB MOU does. The requirements and restrictions of the Reserve Bank Agreement are judicially enforceable, and Sterling Savings Bank is obligated to comply with the undertakings set forth in the SSB MOU. The failure to comply with the SSB MOU and the Reserve Bank Agreement may result in the issuance of a new cease and desist order or subject Sterling and Sterling Savings Bank to additional regulatory restrictions including: the imposition of civil monetary penalties; the issuance of directives to increase capital or enter into a strategic transaction, whether by merger or otherwise, with a third party; and other limitations or restrictions on our business or activities.

### **Our strategy of pursuing FDIC-assisted acquisition opportunities may not be successful.**

We anticipate that a part of our future business strategy will be to pursue the acquisition of failed banks that the FDIC plans to place in receivership. We are not currently qualified to bid on these transactions. Although we plan to be intensely focused on complying with and being released from the SSB MOU and the Reserve Bank Agreement and becoming qualified to bid on FDIC-assisted transactions, we may not be successful in the near term or at all. Prolonged or indefinite failure to achieve such qualification could cause us to miss the opportunity to bid on banks that we believe would be attractive acquisition candidates. Even if we become qualified to bid on these transactions, the FDIC may not place banks that meet our strategic objectives into receivership. Failed bank transactions are attractive opportunities in part because of loss sharing arrangements with the FDIC that limit the acquirer's downside risk on the purchased loan portfolio and, apart from the acquirer's assumption of deposit liabilities, the acquirer has significant discretion as to the non-deposit liabilities that it assumes. In addition, assets purchased from the FDIC are marked to their fair value and in many cases there is little or no addition to goodwill arising from an FDIC-assisted transaction. The bidding process for failing banks could become very competitive, and the FDIC does not provide information about bids until after the failing bank is closed. Sterling may not be able to match or beat the bids of other acquirers unless it bids aggressively by increasing the premium paid on assumed deposits, reducing the discount bid on assets purchased or taking other actions, any of which could make the acquisition less attractive.

### **The FDIC Policy Statement will limit our ability to acquire failed banks.**

As the agency responsible for resolving failed depository institutions, the FDIC has discretion to determine whether a party is qualified to bid on a failed institution. The FDIC Policy Statement imposes additional restrictions and requirements on certain private investors and institutions, to the extent that those investors or institutions seek to acquire a failed institution from the FDIC. These include, among others, a requirement that certain private



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investors in those institutions agree to a three-year transfer restriction on their shares. Since its initial adoption on August 26, 2009, the FDIC has issued several interpretations which have modified the Policy Statement and the FDIC may change it in the future. On April 23, 2010, the FDIC issued an interpretation that would permit a recapitalized institution (such as Sterling) to acquire failed banks without being subject to the FDIC Policy Statement, provided the assets of the failed banks acquired during the 18 months following Sterling's Recapitalization do not exceed 100 percent of the total assets of the recapitalized institution. It is not clear, based on the current FDIC Policy Statement, whether the total assets are measured by Sterling's assets at the holding company level or at the bank subsidiary level. In addition, it is not clear how the FDIC would calculate percentage of assets, and whether that percentage is based on assets at the time of the Recapitalization or whether the percentage is based on growth or contraction in an institution over time.

Sterling expects to bid on failed banks as a key component of its strategy, if and when it is permitted to do so by its regulators as described in the preceding risk factor. Sterling does not anticipate taking any action that would subject shareholders to the terms of the FDIC Policy Statement, which may limit Sterling's ability to pursue attractive acquisition opportunities and harm its competitive position.

It is possible that Sterling might wish to engage in an acquisition that could trigger applicability of the FDIC Policy Statement to it and to certain of its shareholders as a result of the size of a potential acquisition or possible changes to the FDIC Policy Statement. Were it to apply, Sterling would be required to maintain a ratio of Tier 1 common equity to total assets of at least 10% for a period of three years following a failed bank acquisition, and thereafter, so long as such shareholders continue to hold their investment in Sterling, to maintain a capital level sufficient to be well-capitalized under FDIC rules and regulations. Further, certain shareholders might be required to agree to hold their shares for three years, provide certain information to the FDIC and agree to certain other restrictions. Sterling does not intend to make any such acquisition absent the consent of those shareholders to whom the FDIC Policy Statement would apply, and it is possible that any such consent might not be obtained. If Sterling is able to obtain requisite shareholder consent to be bound by the Policy Statement and enters into such transactions, its operating flexibility could be harmed by having to comply with the other requirements set forth in the Policy Statement. On the other hand, if Sterling is not able to pursue transactions that it otherwise believes are attractive, its competitive position may be harmed.

### **Acquisitions present many risks, and we may not realize the financial and strategic goals that are contemplated at the time of any future acquisitions.**

Our strategy includes an intent to acquire other banks in FDIC-assisted transactions or otherwise. This strategy entails risk. Acquisitions and related transition and integration activities may disrupt our ongoing business and divert management's attention. In addition, an acquisition may not further our corporate strategy as we expected, we may pay more than the acquired banks or assets are ultimately worth or we may not integrate an acquired bank or assets as successfully as we expected, which could adversely affect our business, results of operations and financial condition. We may be adversely affected by liabilities or pre-existing contractual relationships that we assume and may also fail to anticipate or accurately estimate litigation or other exposure, unfavorable accounting consequences, increases in taxes due or a loss of anticipated tax benefits. Other potential adverse consequences include higher than anticipated costs associated with the acquired bank or assets or integration activities. The use of cash to pay for acquisitions may limit our use of cash for other potential activities, such as dividends. The use of equity securities to pay for acquisitions could significantly dilute existing shareholders. If we use debt to finance acquisitions, we may significantly increase our expenses, leverage and debt service requirements. The occurrence of any of these risks could have a material adverse effect on our business, results of operations, financial condition or cash flows, particularly in the case of a large acquisition or several concurrent acquisitions.

### **We could be materially and adversely affected if we or any of our officers or directors fail to comply with bank and other laws and regulations.**

As a bank holding company, we are subject to extensive regulation by U.S. federal and state regulatory agencies and face risks associated with investigations and proceedings by regulatory agencies, including those that we may believe to be immaterial. Like any corporation, we are also subject to risk arising from potential employee

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misconduct, including non-compliance with our policies. Any interventions by authorities may result in adverse judgments, settlements, fines, penalties, injunctions, suspension or expulsion of our officers or directors from the banking industry or other relief. In addition to the monetary consequences, these measures could, for example, impact our ability to engage in, or impose limitations on, certain of our businesses. The number of these investigations and proceedings, as well as the amount of penalties and fines sought, has increased substantially in recent years with regard to many firms in the industry. Significant regulatory action against us or our officers or directors could materially and adversely affect our business, financial condition or results of operations or cause us significant reputational harm, which could seriously harm our business.

### **Our Common Stock is equity and is subordinate to our existing and future indebtedness, and our Common Stock would be subordinate to any future preferred stock.**

Shares of our Common Stock are equity interests in us, do not constitute indebtedness, and, therefore, are not insured against loss by the FDIC, any other deposit insurance fund or by any other public or private entity. Shares of our Common Stock will rank junior to all of our indebtedness and to other non-equity claims against us and our assets available to satisfy claims against us, including in liquidation. Our Board of Directors is authorized to issue additional classes or series of preferred stock without any action on the part of the holders of our Common Stock, and the holders of our Common Stock do not have the right to prevent us from incurring indebtedness or other claims.

### **Holders of our Warrants will not be entitled to any rights with respect to our Common Stock, but will be subject to all changes made with respect to them.**

Holders of our Warrants will not be entitled to any rights with respect to our Common Stock (including, without limitation, voting rights and rights to receive any dividends or other distributions on our Common Stock) unless and until the holder elects to exercise its Warrants and receive Common Stock. Holders of the Warrants will be subject to all changes affecting our Common Stock. For example, if an amendment requiring shareholder approval is proposed to our certificate of incorporation or bylaws and the record date for determining the shareholders of record entitled to vote on the amendment occurs prior to a holder's exercise of its Warrants, such holder will not be entitled to vote on the amendment, although such holder will nevertheless be subject to any changes affecting our Common Stock.

### **Resales of our Common Stock may be impeded by the Transfer Restrictions.**

Subject to certain exceptions, the Securities offered pursuant to this Registration Statement are subject to transfer restrictions designed to prevent (a) any person from acquiring ownership, for relevant tax purposes, of 5 percent or more of our shares and (b) the disposition of shares by any person that owns 5 percent or more of our shares, subject to certain exceptions. These restrictions may adversely affect your ability to resell our Common Stock by rendering any transactions in violation of this prohibition void ab initio. In addition, we intend to propose, at our upcoming annual meeting, an amendment to our Articles of Incorporation that would impose these transfer restrictions on other holders of our Common Stock.

In addition, on April 14, 2010, we adopted a Shareholder Rights Plan, which is described in "Transfer Restrictions and Rights Plan" below as well as in our Form 8-K filed on April 15, 2010. The purpose of the Rights Plan is to minimize the likelihood of an ownership change, which is described below under "Our ability to use our deferred tax assets may be materially impaired," and thus to protect our ability to use our net operating loss carry-forward and certain built-in losses to offset future income. The Rights Plan provides an economic disincentive for any one person or group to become a Threshold Holder (as defined therein, generally an owner of 5 percent or more of our stock) and for any existing Threshold Holder to acquire more than a specified amount of additional shares, and so may adversely affect one's ability to resell our Common Stock and negatively affect the trading price of our Common Stock.

In addition, if you are an investor not in the Republic of Korea, you will not be permitted to sell or transfer your Securities to a Korean resident until August 26, 2011, and if you are an investor in the Republic of Korea, you will not be permitted to sell or transfer your Securities to another Korean resident other than a professional investor until August 26, 2011; provided that, in each case, such restrictions shall not apply to open market transactions effected through the New York Stock Exchange or NASDAQ. These restrictions may limit your ability to resell your Securities.

### **We are not currently able to pay dividends on our Common Stock.**

Under the terms of our junior subordinated notes and the trust documents relating to our trust preferred securities, we are allowed to defer payments of interest for up to 20 consecutive quarterly periods without default. During the deferral period, however, Sterling generally may not pay cash dividends on or repurchase Common Stock, until all accrued interest payments are paid and regularly scheduled interest payments are resumed. We are



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currently, and expect to continue to be, in deferral on the payment of interest relating to the trust preferred securities and will therefore be unable to pay cash dividends on Common Stock or preferred stock in the foreseeable future. Pursuant to the terms of the Treasury Exchange, subject to certain exceptions, we will be unable to pay cash dividends on Common Stock without the Treasury's consent until the earlier of December 5, 2011, or such time as the Treasury ceases to own any debt or equity securities acquired pursuant to the Exchange Agreement or the Treasury Warrant. In addition, under the SSB MOU and the Reserve Bank Agreement, Sterling is prohibited from paying dividends without the prior approval of the FDIC, WDFI and the Reserve Bank. See Dividend Policy below.

### **Sterling may suffer substantial losses due to its agreements to indemnify certain investors against a broad range of potential claims.**

In connection with Sterling's recapitalization efforts, Sterling has agreed to indemnify THL, Warburg Pincus, the Private Placement Investors and certain related parties for a broad range of claims, including any inaccuracies or breaches of Sterling's representations and warranties in the relevant Anchor Investment Agreements and Subscription Agreements and any losses arising out of or resulting from any legal, administrative or other proceedings arising out of the transactions contemplated by the relevant Anchor Investment Agreements and Subscription Agreements and the terms of the securities being offered. While these indemnities are capped at the aggregate purchase price of \$730 million, if all or some claims were successfully brought against Sterling, this could potentially result in significant losses for Sterling.

### **As a result of the Recapitalization Transactions, THL and Warburg Pincus are substantial holders of our Common Stock.**

Following the closing of the Recapitalization Transactions, THL and Warburg Pincus each became beneficial owners, as of November 1, 2010, of approximately 22.6 percent of our outstanding Common Stock, assuming full exercise of such Anchor Investor's warrant, and each has a representative on our Board of Directors. Accordingly, THL and Warburg Pincus will each have substantial influence over the election of directors to our board and over corporate policy, including decisions to enter into mergers or other extraordinary transactions. In addition, as part of the negotiations for the Anchor Investments, THL and Warburg Pincus requested, and our Board of Directors agreed to grant, pre-emptive rights to maintain THL's and Warburg Pincus's fully diluted percentage ownership of our Common Stock in the event of certain issuances of securities by us. In pursuing its economic interests, THL and Warburg Pincus may make decisions with respect to fundamental corporate transactions that may be different than the decisions of other shareholders.

### **Our stock price has been and may continue to be volatile, which could cause the value of investments in our Common Stock to decline.**

In recent periods, the trading price of our Common Stock has been and may continue to be highly volatile and subject to wide fluctuations in price. This volatility is in response to various factors, many of which are beyond our control, including:

actual or anticipated variations in quarterly operating results from historical results or estimates of results prepared by securities analysts;

announcements of new services or products by us or our competitors;

announcements by us of significant acquisitions, strategic partnerships, joint ventures or capital commitments;

conditions or trends in the financial industry;

additions or departures of key personnel;

general economic conditions and interest rates;

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the trading volume of our Common Stock;

instability in the United States and other financial markets and the ongoing and possible escalation of unrest in the Middle East, other armed hostilities or further acts or threats of terrorism in the United States or elsewhere;

sales of our Common Stock;

the potential impact of the secondary trading of our stock on foreign exchanges that are subject to less regulatory oversight than the NASDAQ Capital Market, without our permission, and the activity of the market makers of our stock on such exchanges, including the risk that such market makers may engage in naked short sales and/or other deceptive trading practices that may artificially depress or otherwise affect the price of our Common Stock on the NASDAQ Capital Market;

earnings estimates and recommendations of securities analysts;

the performance and stock price of other companies that investors and analysts deem comparable to us;

the soundness or predicted soundness of other financial institutions; and

the public perception of the banking industry and its safety and soundness.

In addition, the stock market in general, and the NASDAQ Capital Market and the market for commercial banks and other financial services companies in particular, has experienced significant price and volume fluctuations that sometimes have been unrelated or disproportionate to the operating performance of those companies. These broad market and industry factors may seriously harm the market price of our Common Stock, regardless of our operating performance. In the past, following periods of volatility in the market price of a company's securities, securities class action litigation has often been instituted. Sterling is currently engaged in securities class action litigation, ERISA class action litigation, and derivative class action litigation, and these actions or any other suit against us could result in substantial costs, potential liabilities and the diversion of management's attention and resources. As a result of these factors, among others, the value of your investment may decline, and you may be unable to sell your shares of our Common Stock at or above your purchase price.

**The trading volume of our Common Stock is lower than that of other financial services companies.**

Our Common Stock is listed on the NASDAQ Capital Market under the symbol STSA. The average daily trading volume for shares of our Common Stock is lower than larger financial institutions. During the 12 months ended October 31, 2010, the average daily trading volume for our Common Stock was 1,165,020 shares. As a result, sales of our Common Stock may place significant downward pressure on the market price of our Common Stock. Furthermore, it may be difficult for holders to resell their shares at prices they find attractive, or at all.

**No public market for our Warrants currently exists, and an active trading market may not develop or be sustained following this offering.**

Prior to this offering, there has been no public market for the Warrants. An active trading market may not develop following the closing of this offering or, if developed, may not be sustained. The lack of an active market may impair your ability to sell the Warrants at the time you wish to sell them or at a price that you consider reasonable. The lack of an active market may also reduce the fair market value of the Warrants. We are not currently able to comply with conditions required to list the Warrants on any securities exchange, and we may not be able to comply in the future. Failure to list the Warrants may further limit their trading market.

**Our ability to use our deferred tax assets may be materially impaired.**

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As of June 30, 2010, our net deferred tax asset was approximately \$325 million, which includes approximately \$222 million of federal and state net operating losses ( NOLs ). We currently have a valuation allowance of \$325 million against this deferred tax asset. Our ability to use our deferred tax assets to offset future taxable income will be limited if we experience an ownership change as defined in Section 382 of the Code. As a result of the Recapitalization Transactions we are now close to the ownership change threshold.

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In general, an ownership change will occur if there is a cumulative increase in our ownership by 5-percent shareholders (as defined in the Code) that exceeds 50 percentage points over a rolling three-year period. A corporation that experiences an ownership change will generally be subject to an annual limitation on the use of its pre-ownership change deferred tax assets equal to the equity value of the corporation immediately before the ownership change, multiplied by the long-term tax-exempt rate, which is currently 3.86 percent for ownership changes occurring in November 2010.

While we have taken measures to reduce the likelihood that future transactions in our stock will result in an ownership change, such an ownership change might occur in the future. More specifically, while the Rights Plan described below under Transfer Restrictions and Rights Plan provides an economic disincentive for any one person or group to become a Threshold Holder (as defined in the Rights Plan) and for any existing Threshold Holder to acquire more than a specified amount of additional shares, the Rights Plan might not deter a shareholder from increasing its ownership interests beyond the limits set by the Rights Plan. Such an increase could adversely affect our ownership change calculations.

In addition, while the Section 382 Transfer Restrictions and the Proposed Section 382 Articles Amendment, each described below under Transfer Restrictions and Rights Plan, are designed to prevent transactions that could lead to an ownership change, currently only certain of the Securities offered pursuant to this Prospectus are subject to the Section 382 Transfer Restrictions, our shareholders might not approve the Proposed Section 382 Articles Amendment, and these restrictions might not be sustained by a court or otherwise might not be entirely effective in preventing an ownership change.

Our calculations regarding our current cumulative change and the likelihood of a future ownership change are based on current law. Any change in applicable law may result in an ownership change.

### **We incurred significant losses over the last seven quarters and may continue do so in the future**

Cumulatively, from the fourth quarter of 2008 through the second quarter of 2010, we have incurred a net loss available to common shareholders of \$1.4 billion, or a loss of \$26.18 per common share, primarily due to a \$1.1 billion provision for credit losses, a \$451.3 million charge for goodwill impairment and the establishment of a \$325.0 million deferred tax asset valuation allowance. In light of the current economic environment, significant additional provisions for credit losses may be necessary to supplement the allowance for loan and lease losses in the future. As a result, we may incur significant credit costs throughout 2010, which would continue to have an adverse impact on our financial condition and results of operations and the value of our Securities. Additional credit losses or impairment charges could cause us to incur a net loss in the future and could adversely affect the price of, and market for, our Securities.

### **Our estimated allowance for losses in our loan portfolio may be inadequate, which would cause our results of operations and financial condition to be adversely affected.**

We maintain an allowance for credit losses, which is a reserve established through a provision for credit losses charged as an expense and represents management's best estimate of incurred losses within our existing portfolio of loans, which has been increasing in light of recent economic conditions. The level of the allowance reflects management's estimates based upon various assumptions and judgments as to specific credit risks, evaluation of industry concentrations, loan loss experience, current loan portfolio quality, present economic, political and regulatory conditions and unidentified losses inherent in the current loan portfolio. The determination of the appropriate level of the allowance for loan and lease losses inherently involves a high degree of subjectivity and requires management to make significant estimates and judgments regarding current credit risks and future trends, all of which may undergo material changes. If our estimates prove to be incorrect, our allowance for credit losses may not be sufficient to cover losses in our loan portfolio and our expense relating to the additional provision

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for credit losses could increase substantially. In addition, bank regulatory agencies periodically review the adequacy of our allowance for credit losses as part of their examination process, and may require an increase in the provision for possible credit losses or the recognition of further loan charge-offs. Any such increases in the allowance for credit losses may have a material adverse effect on our results of operations, financial condition and the value of our Securities.

### **We have received a notice of noncompliance from NASDAQ, and our Common Stock may be subject to delisting.**

On December 7, 2009, at which date our Common Stock was listed on the NASDAQ Global Select Market, we received a letter from NASDAQ notifying us that we no longer met NASDAQ's continued listing requirement under Listing Rule 5450(a)(1) (the Bid Price Rule) because the bid price for our Common Stock had closed below \$1.00 per share for 30 consecutive business days. On June 8, 2010, NASDAQ approved the transfer of the listing of our Common Stock to the NASDAQ Capital Market, thus providing us until December 6, 2010 to regain compliance with the Bid Price Rule. If compliance with the Bid Price Rule cannot be established prior to December 6, 2010, our Common Stock will be subject to delisting from the NASDAQ Capital Market. On October 21, 2010, our shareholders approved an amendment to our Restated Articles of Incorporation to effect a reverse stock split of our Common Stock at a ratio to be determined by Sterling's Board of Directors between one-for-50 and one-for-125 shares of Common Stock. We expect to effect the reverse stock split prior to the expiration of applicable grace periods under NASDAQ rules. However, we might not be successful at reestablishing or maintaining compliance with the Bid Price Rule prior to such expiration, and a delisting from NASDAQ would have a negative impact on the value and liquidity of our Common Stock and our ability to access the capital markets.

### **The effects of the current economic recession have been particularly severe in our primary market areas in the Pacific Northwest and Northern California.**

Substantially all of our loans are to businesses and individuals in Washington, Oregon, Idaho, Montana and California. The Pacific Northwest and Northern California have some of the nation's highest unemployment rates, and major employers in Washington, Oregon, Idaho and Northern California have implemented substantial employee layoffs or scaled back growth plans in recent periods. Severe declines in housing prices and property values have been particularly acute in our primary market areas. The State of California continues to face fiscal challenges, of which the long-term effects on California's economy cannot be predicted. A further deterioration in the economic conditions or a prolonged delay in economic recovery in our primary market areas could result in the following consequences, any of which could materially and adversely affect our business: collateral for loans made by us, especially real estate, may decline further in value, in turn reducing customers' borrowing power and further reducing the value of assets and collateral associated with our existing loans; loan delinquencies may increase; problem assets and foreclosures may increase; demand for our products and services may decrease; and access to low cost or noninterest bearing deposits may decrease.

### **A large percentage of our loan portfolio is secured by real estate. Continued deterioration in the real estate market or other segments of our loan portfolio would lead to additional losses, which could have a material adverse effect on our business, financial condition and results of operations.**

Approximately 87 percent of our loan portfolio was secured by real estate as of June 30, 2010. The secured loans include construction loans, which comprise 17 percent of our total real estate secured loans as of such date. As a result of increased levels of commercial and consumer delinquencies and declining real estate values, we have experienced increasing levels of net charge-offs and provisions for credit losses. Continued increases in commercial and consumer delinquency levels or continued declines in real estate market values would require increased net charge-offs and increases in the provision for loan and lease losses, which could have a material adverse effect on our business, financial condition and results of operations and prospects. Acts of nature, including earthquakes, floods and fires, which may cause uninsured damage and other loss of value to real estate that secures these loans, may also have a negative impact on our financial condition. In addition, we may face risks associated with our real estate lending under various federal, state and local environmental laws that impose certain requirements on the owner or operator of a property.



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### **We have a concentration in non-owner-occupied commercial real estate loans, which generally involve a higher degree of risk than residential mortgage loans.**

Sterling's Commercial Banking Group provides a full range of credit products to small and medium-sized businesses and to individuals, including lines of credit, receivable and inventory financing, equipment loans and owner occupied commercial real estate. At June 30, 2010, approximately 31 percent of our loan portfolio could be classified as commercial lending and approximately 24 percent of our real estate secured loans were secured by non-owner-occupied commercial real estate. Commercial loans generally involve a higher degree of credit risk than residential mortgage lending due, among other things, to the large amounts loaned to individual borrowers. In addition, unlike residential mortgage loans, commercial real estate loans generally depend on the cash flow from the property to service the debt. Cash flow may be significantly affected by general economic conditions. Losses incurred on loans to a small number of borrowers could have a material adverse impact on our income and financial condition. Also, many of our commercial real estate borrowers have more than one loan outstanding with us. Consequently, an adverse development with respect to one loan or one credit relationship can expose us to a significantly greater risk of loss compared to an adverse development with respect to a one- to four-family residential mortgage loan.

### **A rapid change in interest rates could make it difficult to maintain our current net interest income spread and could result in reduced earnings.**

Our earnings are largely derived from net interest income, which is interest income earned on loans and investments, less interest paid on deposits and other borrowings. Interest rates are highly sensitive to many factors that are beyond the control of our management, including general economic conditions and the policies of various governmental and regulatory authorities. As interest rates change, net interest income is affected. With fixed rate assets (such as fixed rate loans and most investment securities) and liabilities (such as certificates of deposit), the effect on net interest income depends on the cash flows associated with the maturity of the asset or liability. Asset/liability management policies may not be successfully implemented and from time to time our risk position is not balanced. An unanticipated rapid decrease or increase in interest rates could have an adverse effect on the spreads between the interest rates earned on assets and the rates of interest paid on liabilities, and therefore on the level of net interest income. For instance, any rapid increase in interest rates in the future could result in interest expense increasing faster than interest income because of fixed rate loans and longer-term investments. Further, substantially higher interest rates generally reduce loan demand and may result in slower loan growth than previously experienced. This could have an adverse negative effect on our earnings.

### **Our cost of funds may increase as a result of many factors, which may reduce our profitability.**

Our cost of funds may increase because of general economic conditions, unfavorable conditions in the capital markets, changes in interest rates, government intervention and support of competitors, government price controls and competitive pressures. We have traditionally obtained funds principally through deposits and, to a lesser extent, other borrowings, including repurchase agreements. As a general rule, deposits are a cheaper and more stable source of funds than borrowings. Checking and savings account balances and other forms of deposits can decrease when our deposit customers perceive alternative investments, such as the stock market or other non-depository investments, as providing superior expected returns, seek to spread their deposits over several banks to maximize FDIC insurance coverage or perceive weakness in our financial stability. Furthermore, technology and other changes have made it more convenient for bank customers to transfer funds into alternative investments, including products offered by other financial institutions or non-bank service providers. Additional increases in short-term interest rates could increase transfers of deposits to higher yielding deposits. Efforts and initiatives we undertake to retain and increase deposits, including deposit pricing, can increase our costs. When bank customers move money out of bank deposits in favor of alternative investments or into higher yielding deposits, or spread their accounts over several banks, we can lose a relatively inexpensive source of funds, thus increasing our funding costs. If, as a result of general economic conditions, market interest rates, competitive pressures or other factors, our level of deposits decreases relative to our overall banking activities, we may need to rely more heavily on borrowings and/or wholesale funding as a source of funds, and this may negatively impact our net interest margin and subject Sterling to additional liquidity and funding risks.

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### **We may have reduced access to wholesale funding sources.**

As a part of our liquidity management, we use a number of funding sources in addition to core deposit growth and repayments and maturities of loans and investments. Our financial flexibility will be severely constrained if we are unable to maintain our access to funding at acceptable interest rates. If we are required to rely more heavily on more expensive funding sources, our revenues may not increase proportionately to cover our costs, and our profitability would be adversely affected.

### **Our banking operations are subject to extensive governmental regulation, and further regulatory actions against us may impair our operations or restrict our growth.**

We and our subsidiaries are subject to extensive regulation under federal and state laws including those of the FDIC and the WDFI. These laws and regulations are primarily intended to protect customers, depositors and the Deposit Insurance Fund rather than shareholders. In addition, Sterling is subject to regulation and supervision by the Federal Reserve and the SEC and to the listing standards of the NASDAQ Capital Market. Our banking subsidiary is also subject to the supervision by and the regulations of the FDIC, and the state agencies for the states in which it conducts business. As a Washington state-chartered commercial bank, Sterling Savings Bank is primarily regulated by the WDFI.

Statutes and regulations affecting our business may be changed at any time, and the interpretation of these statutes and regulations by examining authorities may also change. Within the last several years, Congress and the President have passed and enacted significant changes to these statutes and regulations, including most recently, the Dodd-Frank Act signed into law on July 21, 2010. Such changes to the statutes and regulations or to their interpretation may adversely affect our business. In addition to governmental supervision and regulation, we are subject to changes in other federal and state laws, including changes in tax laws, which could materially affect the banking industry. The regulators may continue to limit our activities or growth and may impose monetary penalties, which could severely limit or end our operations. Banking laws and regulations change from time to time. Bank regulations can hinder our ability to compete with financial services companies that are not regulated in the same manner or are less regulated.

Bank regulatory authorities have the authority to bring enforcement actions against banks and bank holding companies for unsafe or unsound practices in the conduct of their businesses or for violations of any law, rule or regulation, any condition imposed in writing by the appropriate bank regulatory agency or any written agreement with the authority.

### **Recent changes have created regulatory uncertainty.**

Regulation of the financial services industry is undergoing major changes. The Dodd-Frank Act significantly revises and expands the rulemaking, supervisory and enforcement authority of federal bank regulators. Although the statute will have a greater impact on larger institutions than regional bank holding companies such as Sterling, many of its provisions will apply to us. Among other things, the Dodd-Frank Act:

is changing the capital requirements for bank holding companies and would require less favorable capital treatment for future issuances of trust preferred (although our existing trust preferred are grandfathered and therefore not subject to the new rules);

raises prudential standards by requiring, for instance, annual internal stress testing and establishment of independent risk committees for banks with \$10 billion or more in assets;

grants the FDIC back-up supervisory authority with respect to depository institution holding companies that engage in conduct that poses a foreseeable and material risk to the Deposit Insurance Fund, and heightens the Federal Reserve's authority to examine, prescribe regulations and take action with respect to all subsidiaries of a bank holding company;

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prohibits insured state-chartered banks from engaging in derivatives transactions unless the chartering state's lending limit laws take into consideration credit exposure to derivative transactions;

specifies that a bank holding company may acquire control of an out-of-state bank only if it is well-capitalized and well-managed, and does not allow interstate merger transactions unless the resulting bank would be well-capitalized and well-managed after the transaction;

changes how the FDIC calculates deposit insurance assessments and effectively requires increases in deposit insurance fees that will be borne primarily by institutions with assets of greater than \$10 billion;

subjects both large and small financial institutions to data and information gathering by a newly created Office of Financial Research;

requires retention of 5 percent of the credit risk in assets transferred, sold or conveyed through issuances of asset-backed securities, with the risk-retention obligation spread between securitizers and originators;

creates a new Consumer Bureau given rulemaking, examination and enforcement authority over consumer protection matters, imposes limits on debit card interchange fees that may be charged by card issuers with \$10 billion or more in assets and contains provisions on mortgage-related matters such as steering incentives, determinations as to a borrower's ability to repay and prepayment penalties; and

mandates and allows certain changes regarding corporate governance and executive compensation such as shareholder proxy access for publicly traded banks' director nominations, clawback of incentive-based compensation from executive officers and increased disclosure on compensation arrangements.

Some of these changes are effective immediately, though most will be phased in gradually. In addition, the statute in many instances calls for future rulemaking to implement its provisions, so the precise contours of the law and its effects on us cannot yet be fully understood. The provisions of the Dodd-Frank Act and the subsequent exercise by regulators of their revised and expanded powers thereunder could materially impact the profitability of our business, the value of assets we hold or the collateral available for our loans, require changes to business practices or force us to discontinue businesses and expose us to additional costs, taxes, liabilities, enforcement actions and reputational risk. Legislators and regulators are also considering a wide range of proposals beyond the Dodd-Frank Act that, if enacted, could result in major changes to the way banking operations are regulated.

**We may be subject to more stringent capital requirements.**

As discussed above, the Dodd-Frank Act would require the federal banking agencies to establish stricter risk-based capital requirements and leverage limits to apply to banks and bank holding companies. In addition, the Basel III standards recently announced by the Basel Committee on Banking Supervision (the Basel Committee), if adopted, could lead to significantly higher capital requirements, higher capital charges and more restrictive leverage and liquidity ratios. The standards would, among other things, impose more restrictive eligibility requirements for Tier 1 and Tier 2 capital; increase the minimum Tier 1 common equity ratio to 4.5 percent, net of regulatory deductions, and introduce a capital conservation buffer of an additional 2.5 percent of common equity to risk-weighted assets, raising the target minimum common equity ratio to 7 percent; increase the minimum Tier 1 capital ratio to 8.5 percent inclusive of the capital conservation buffer; increase the minimum total capital ratio to 10.5 percent inclusive of the capital buffer; and introduce a countercyclical capital buffer of up to 2.5 percent of common equity or other fully loss absorbing capital for periods of excess credit growth. Basel III also introduces a non-risk adjusted Tier 1 leverage ratio of 3 percent, based on a measure of total exposure rather than total assets, and new liquidity standards.



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The new Basel III capital standards will be phased in from January 1, 2013 until January 1, 2019, and it is not yet known how these standards will be implemented by U.S. regulators generally or how they will be applied to community banks of our size. Implementation of these standards, or any other new regulations, may adversely affect our ability to pay dividends, or require us to reduce business levels or raise capital, including in ways that may adversely affect our results of operations or financial condition.

**You may be subject to tax upon an adjustment to the number of shares of our Common Stock underlying the Warrants or the exercise price of the Warrants even though you do not receive a corresponding cash distribution.**

The number of shares of our Common Stock underlying the Warrants and the exercise price of the Warrants are subject to adjustment in certain circumstances. To the extent any such adjustment or failure to adjust results in an increase in your proportionate interest in our assets or our earnings and profits, you will be deemed to have received for U.S. federal income tax purposes a taxable dividend to the extent deemed paid out of our earnings and profits without the receipt of any cash. If you are a Non-U.S. Holder (as defined below), such deemed dividend generally will be subject to U.S. federal withholding tax (currently at a 30 percent rate, or such lower rate as may be specified by an applicable treaty), which may reduce the amount of shares of our Common Stock to be delivered upon exercise of Warrants. See Certain Material U.S. Federal Income and Estate Tax Considerations in this Prospectus.

**Difficult market conditions have adversely affected and may continue to have an adverse effect on our industry.**

The capital and credit markets have been experiencing difficulty for more than three years. Dramatic declines in the housing market over the past three years, with falling home prices and increasing foreclosures, unemployment and under-employment, have had a negative impact on the performance of mortgage loans and have resulted in significant write-downs of asset values by financial institutions, including government-sponsored entities as well as major commercial and investment banks. These write-downs have caused many financial institutions to seek additional capital, to merge with larger and stronger institutions and, in some cases, to fail. Reflecting concern about the stability of the financial markets generally and the strength of counterparties, many lenders and institutional investors have reduced or ceased providing funding to borrowers, including to other financial institutions. This market turmoil and tightening of credit have led to an increased level of commercial and consumer delinquencies, lack of consumer confidence, increased market volatility and widespread reduction of business activity generally. The resulting economic pressure on consumers and lack of confidence in the financial markets has adversely affected our business, financial condition and results of operations. We expect that the difficult conditions in the financial markets will improve only slowly in the near future. A worsening of these conditions would likely exacerbate the adverse effects of these difficult market conditions on us and others in the financial institutions industry. In particular, we may face the following risks in connection with these events:

While increased regulation and enforcement is now certain in the financial sector, with increased compliance costs, the scope of such regulation is uncertain, and that uncertainty affects our business opportunities and plans.

Our ability to assess the creditworthiness of our customers may be impaired if the models and approaches we use to select, manage, and underwrite our customers become less predictive of future behaviors.

The process we use to estimate losses inherent in our loan portfolio requires difficult, subjective and complex judgments, including forecasts of economic conditions and how these economic predictions might impair the ability of our borrowers to repay their loans, which may no longer be capable of accurate estimation and may, in turn, have a negative impact on the reliability of the process.

We will be required to pay significantly higher FDIC premiums because market developments have significantly depleted the insurance fund of the FDIC and reduced the ratio of reserves to insured deposits.

There may be additional downward pressure on our stock price.



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Our ability to engage in routine funding transactions could be adversely affected by the actions and commercial soundness of other financial institutions and government sponsored entities.

We may face increased competition due to intensified consolidation of the financial services industry. If a failure or slowing of the current modest recovery from recessionary conditions occurs, we may experience an adverse effect, which may be material, on our ability to access capital and on our business, financial condition and results of operations.

**We may realize losses on our investment securities in future periods if our management decides not to hold the investments to recovery, there is a change in management or the rating agencies assessment of credit risk on individual securities, or there is a change in regulatory or accounting requirements.**

As of June 30, 2010, we held a position in a security considered impaired because its fair value was less than its amortized cost basis. This security is a single-issuer trust preferred security with an amortized cost of \$24.8 million compared with a \$19.9 million market value. Although we have no intent to sell the security and it is not more likely than not that we will be required to sell the security before its anticipated recovery, certain events may occur where we would choose to or may be required to sell the security. If we choose to or are required to sell this investment before a recovery of the entire cost basis of the security, then we may recognize a loss on the security.

**As a bank holding company that conducts substantially all of our operations through our banking subsidiary, Sterling Savings Bank, our ability to pay dividends, repurchase our shares or to repay our indebtedness depends upon liquid assets held by the holding company and the results of operations of our subsidiary.**

Sterling is a separate and distinct legal entity from our subsidiaries, and we receive substantially all of our revenue from dividends paid from our banking subsidiary, Sterling Savings Bank. There are legal limitations on the extent to which our banking subsidiary may extend credit, pay dividends or otherwise supply funds to, or engage in transactions with, us. A prolonged inability to receive dividends from our banking subsidiary could adversely affect our business, financial condition, results of operations and prospects.

Our net income depends primarily upon Sterling Savings Bank's net interest income, which is the income that remains after deducting from total income generated by earning assets the expense attributable to the acquisition of the funds required to support earning assets (primarily interest paid on deposits). The amount of interest income is dependent on many factors including the volume of earning assets, the general level of interest rates, the dynamics of changes in interest rates and the levels of nonperforming loans. All of those factors affect our banking subsidiary's ability to pay dividends to the holding company.

Various statutory provisions restrict the amount of dividends Sterling Savings Bank can pay to us without regulatory approval. Sterling Savings Bank may not pay cash dividends if those payments could reduce the amount of their capital below that necessary to meet the adequately capitalized level in accordance with regulatory capital requirements. Sterling Savings Bank is also restricted from paying dividends to Sterling pursuant to the terms of the SSB MOU. It is also possible that, depending upon the financial condition of our banking subsidiary and other factors, regulatory authorities could assert that payment of dividends or other payments, including payments to us, is an unsafe or unsound practice. Under Washington banking law, our banking subsidiary may not pay a dividend greater than its retained earnings without WDFI approval.

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**Emergency measures designed to stabilize the U.S. financial markets are beginning to wind down.**

Since mid-2008, a host of government actions have been implemented in response to the financial crisis and the recession. Some of the programs are beginning to expire and the impact of the wind-down of these programs on the financial sector and on the nascent economic recovery is unknown. As government support schemes are cancelled, changed or withdrawn, there is a possibility that we, as well as other financial institutions, may have insufficient access to, or incur higher costs associated with, funding alternatives, which could have a material adverse effect on our business, financial condition, results of operations and prospects. In particular, although pursuant to the Dodd-Frank Act certain non-interest bearing transaction accounts will be fully guaranteed by the FDIC for an unlimited amount of coverage through the end of 2012, some accounts currently covered under the voluntary Transaction Account Guarantee ( TAG ) program, such as Negotiable Order of Withdrawal ( NOW ) checking accounts, will not benefit from this coverage extension that takes effect upon the TAG program's expiration on December 31, 2010. This change could adversely affect us, especially in light of the concerns about our financial viability. In addition, a stall in the economic recovery or continuation or worsening of current financial market conditions could exacerbate these effects.

**Because of our participation in the Troubled Asset Relief Program ( TARP ), we are subject to restrictions on compensation paid to our executives, which may make it difficult to attract and retain key members of management.**

Pursuant to the terms of the TARP Capital Purchase Program, we adopted certain standards for executive compensation and corporate governance for the period during which the Treasury owns any debt or equity securities acquired pursuant to the Exchange Agreement. These standards generally apply to our five most highly compensated senior executive officers, including our Chief Executive Officer and Chief Financial Officer, and certain of these restrictions also apply up to the next 20 most highly compensated senior executives. The standards include, among other things:

ensuring that incentive compensation for senior executives does not encourage unnecessary and excessive risks that threaten the value of the financial institution;

a required clawback of any bonus or incentive compensation paid to a senior executive officer or one of the next twenty most highly compensated employees based on statements of earnings, gains or other criteria that are later proven to be materially inaccurate;

a prohibition on making golden parachute payments to senior executive officers;

an agreement not to deduct for tax purposes annual compensation in excess of \$500,000 for each senior executive officer; and

limitations on bonuses and incentive compensation.

We depend on the services of existing management to carry out our business and investment strategies. In order for us to implement our strategy to emphasize relationship banking, we will need to continue to attract and retain additional management and other qualified staff. Competition for such personnel is significant in our geographic market areas. The loss of the services of any management personnel, or the inability to recruit and retain qualified personnel in the future, could have an adverse effect on our results of operations, financial condition and prospects. In particular, the change to the deductibility limit on executive compensation may increase the overall cost of our compensation programs in future periods and may make it more difficult to attract suitable candidates to serve as executive officers. Further, the possibility of lawsuits from former and current executives may increase because of our inability to fulfill certain compensation arrangements that are now restricted under TARP.

We are also obligated under the Exchange Agreement to take all necessary actions to comply with the executive compensation restrictions applicable to TARP recipients and to comply with any subsequent amendments to these restrictions for so long as we remain subject to such restrictions. For additional details about these restrictions and the Exchange Agreement provisions related thereto, see the description under Regulatory Matters Deposit Insurance and Assessments TARP Regulations below.





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### **The financial services industry is highly competitive.**

We face pricing competition for loans and deposits. We also face competition with respect to customer convenience, product lines, accessibility of service and service capabilities. Our most direct competition comes from other banks, brokerages, mortgage companies and savings institutions. We also face competition from credit unions, government-sponsored enterprises, mutual fund companies, insurance companies and other non-bank businesses. A number of these banks and other financial institutions are significantly larger than we are and have substantially greater access to capital and other resources, as well as larger lending limits and branch systems, and offer a wider array of banking services. Many of our non-bank competitors are not subject to the same extensive regulations that govern us. As a result, these non-bank competitors have advantages over us in providing certain services. This significant competition in attracting and retaining deposits and making loans as well as in providing other financial services throughout our market area may have an adverse impact on future earnings and growth.

### **The value of the securities in our investment securities portfolio may be negatively affected by continued disruptions in securities markets.**

The market for some of the investment securities held in our portfolio has become extremely volatile over the past two years. Volatile market conditions may detrimentally affect the value of these securities, such as through reduced valuations due to the perception of heightened credit and liquidity risks. Declines in market value associated with these disruptions may result in other-than-temporary or permanent impairments of these assets, which would lead to accounting charges that could have a material adverse effect on our net income and capital levels.

### **A substantial decline in the value of our Federal Home Loan Bank ( FHLB ) common stock may result in an other-than-temporary impairment charge.**

We own common stock of the FHLB in order to qualify for membership in the FHLB system, which enables us to borrow funds under the FHLB advance program. The carrying value of our FHLB common stock was approximately \$100.4 million as of June 30, 2010, the majority of which was with the FHLB of Seattle. The FHLB Seattle has experienced losses from credit-related charges associated with projected losses on their investments in private-label mortgage-backed securities, and is currently unable to repurchase or redeem capital stock or to pay dividends. Consequently, for this and other reasons, there is a risk that our investment in the common stock of the FHLB could be deemed other than temporarily impaired at some time in the future, which would adversely affect our earnings and the value of, or market for, our Securities.

### **Current and future increases in FDIC insurance premiums, including FDIC special assessments imposed on all FDIC-insured institutions, will decrease our earnings.**

In May 2009, the FDIC announced that it had voted to levy a special assessment on insured institutions in order to facilitate the rebuilding of the Deposit Insurance Fund. The assessment was equal to five basis points of Sterling's total assets minus Tier 1 capital as of June 30, 2009. This represented a charge of approximately \$5.6 million, which was included in noninterest expense during the second quarter of 2009.

The Dodd-Frank Act requires the FDIC to increase the Deposit Insurance Fund's reserves against future losses, which will necessitate increased assessments that are to be borne primarily by institutions with assets of greater than \$10 billion. The precise impact on us will not be clear until the proposal of implementing rules, which is not expected until 2011. Any future increases in assessments will decrease our earnings and could have a material adverse effect on the value of, or market for, our Securities.

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### **Our business is highly reliant on technology and our ability to manage the operational risks associated with technology.**

We depend on internal and outsourced technology to support all aspects of our business operations. Interruption or failure of these systems creates a risk of business loss such as civil fines or damage claims from privacy breaches and adverse customer experience. Risk management programs are expensive to maintain and will not protect Sterling from all risks associated with maintaining the security of customer information, proprietary data, external and internal intrusions, disaster recovery and failures in the controls used by vendors.

### **Changes in accounting standards may have a material impact on how we report our financial condition and results of operations.**

Our accounting policies and methods are fundamental to how we record and report our financial condition and results of operations. From time to time the Financial Accounting Standards Board changes the financial accounting and reporting standards that govern the preparation of our financial statements. These changes can be difficult to predict and can have a material impact on how we record and report our financial condition and results of operations. In some cases, we could be required to apply a new or revised standard retroactively, resulting in a restatement of prior period financial statements.

### **We may be required to repurchase mortgage loans in some circumstances, which could harm our liquidity, results of operations and financial condition.**

When we sell mortgage loans, whether as whole loans or pursuant to a securitization, we are required to make certain representations and warranties to the purchaser about the mortgage loans and the manner in which they were originated. Our whole loan sale agreements require us to repurchase or substitute mortgage loans in the event we breach any of these representations or warranties. In addition, we may be required to repurchase mortgage loans as a result of borrower fraud or in the event of early payment default of the borrower on a mortgage loan. Likewise, we are required to repurchase or substitute mortgage loans if we breach a representation or warranty in connection with our securitizations. The remedies available to us against the originating broker or correspondent may not be as broad as the remedies available to a purchaser of mortgage loans against us, and we face the further risk that the originating broker or correspondent may not have the financial capacity to perform remedies that otherwise may be available to us. Therefore, if a purchaser enforces its remedies against us, we may not be able to recover our losses from the originating broker or correspondent. If repurchase and indemnity demands increase, our liquidity, results of operations and financial condition will be adversely affected.

### **Our operations could be interrupted if our third-party service providers experience difficulty, terminate their services or fail to comply with banking regulations.**

We depend, and will continue to depend, to a significant extent, on a number of relationships with third-party service providers. Specifically, we receive core systems processing, essential web hosting and other Internet systems and deposit and other processing services from third-party service providers. If these third-party service providers experience difficulties or terminate their services, and we are unable to replace them with other service providers, our operations could be interrupted. If an interruption were to continue for a significant period of time, our business, financial condition and results of operations could be materially adversely affected.

### **Our internal control systems could fail to detect certain events.**

We are subject to certain operations risks, including but not limited to data processing system failures and errors and customer or employee fraud. We maintain a system of internal controls to mitigate against such occurrences and maintain insurance coverage for such risks, but should such an event occur that is not prevented or detected by our internal controls, uninsured or in excess of applicable insurance limits, it could have a significant adverse impact on our business, financial condition or results of operations.

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### **The network and computer systems on which we depend could fail or experience a security breach.**

Our computer systems could be vulnerable to unforeseen problems. Because we conduct part of our business over the Internet and outsource several critical functions to third parties, operations will depend on our ability, as well as the ability of third-party service providers, to protect computer systems and network infrastructure against damage from fire, power loss, telecommunications failure, physical break-ins or similar catastrophic events. Any damage or failure that causes interruptions in operations could have a material adverse effect on our business, financial condition and results of operations.

In addition, a significant barrier to online financial transactions is the secure transmission of confidential information over public networks. Our Internet banking system relies on encryption and authentication technology to provide the security and authentication necessary to effect secure transmission of confidential information. Advances in computer capabilities, new discoveries in the field of cryptography or other developments could result in a compromise or breach of the algorithms our third-party service providers use to protect customer transaction data. If any such compromise of security were to occur, it could have a material adverse effect on our business, financial condition and results of operations.

### **We could be held responsible for environmental liabilities of properties acquired through foreclosure.**

If we are forced to foreclose on a defaulted mortgage loan to recover our investment, we may be subject to environmental liabilities related to the underlying real property. Hazardous substances or wastes, contaminants, pollutants or sources thereof may be discovered on properties during our ownership or after a sale to a third party. The amount of environmental liability could exceed the value of real property. We may be fully liable for the entire cost of any removal and clean-up on an acquired property, the cost of removal and clean-up may exceed the value of the property, and we may be unable to recover costs from any third party. In addition, we may find it difficult or impossible to sell the property prior to or following any environmental remediation.

### **We are currently subject to certain pending shareholder litigation and may be subject to similar claims in the future.**

A securities class action lawsuit has been filed against Sterling and certain of our current and former officers alleging that the defendants violated sections 10(b) and 20(a) of the U.S. Exchange Act and SEC Rule 10b-5 by making false and misleading statements concerning our business and financial results. A shareholder derivative suit also has been filed against certain of our current and former officers and directors, and Sterling as a nominal defendant, alleging breaches of fiduciary duty, waste of corporate assets, and unjust enrichment. Class action lawsuits also have been filed against Sterling and certain of our current and former officers and directors alleging violations of the Employee Retirement Income Security Act of 1974, as amended ( ERISA ), by breaching their fiduciary duties to participants in the Sterling Savings Bank Employee Savings and Investment Plan and Trust. These lawsuits are all premised on similar allegations that: 1) the defendants failed to adequately disclose the extent of Sterling's delinquent commercial real estate, construction and land development loans, properly record losses for impaired loans, properly reserve for loan losses, and properly account for our goodwill and deferred tax assets, thereby causing Sterling's stock price to be artificially inflated during the purported class period; or 2) failed to prevent Sterling from issuing improper financial statements, maintain a sufficient allowance for loan and lease losses, and establish effective credit risk management and oversight mechanisms. It is possible that additional suits will be filed with respect to these same matters and also naming Sterling and/or our current and former officers and directors.

We cannot predict the outcome of any of these lawsuits. These lawsuits could divert the attention and resources of our management and cause Sterling to incur significant expenses for legal fees and costs, including those associated with Sterling's advancement of fees and costs on behalf of our current and former officers and directors. Since the legal responsibility and financial impact with respect to these lawsuits and claims, if any, cannot currently be ascertained, we have not established any reserves for any potential liability relating to the lawsuits. An unfavorable outcome in these lawsuits could result in the payment of substantial damages in connection with a settlement or judgment and have a material adverse effect on our business, financial condition, results of operations or cash flows.

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**REGULATORY MATTERS**

**Supervision, Regulation and Other Factors**

Like all bank holding companies, we are regulated extensively under federal and state law. In addition, our subsidiary bank and certain of our nonbank subsidiaries are subject to regulation under federal and state law. The following discussion sets forth some of the elements of the bank regulatory framework applicable to us and certain of our subsidiaries. The regulatory framework is intended primarily for the protection of depositors and the Deposit Insurance Fund and not for the protection of security holders and creditors. To the extent that the following information describes statutory and regulatory provisions, it is qualified in its entirety by reference to the particular statutory and regulatory provisions.

In the post-financial crisis era, regulation of the financial services industry is undergoing major changes. Among these changes is the Dodd-Frank Act, which significantly revises and expands the rulemaking, supervisory and enforcement authority of federal bank regulators. Some of these changes are effective immediately, though most will be phased in gradually. Because the Dodd-Frank Act in many instances calls for future rulemaking to implement its provisions, the precise contours of the law and its effects on us cannot yet be fully understood. Legislators and regulators are also considering a wide range of proposals beyond the Dodd-Frank Act that, if enacted, could result in major changes to the way banking operations are regulated. The provisions of the Dodd-Frank Act and the subsequent exercise by regulators of revised and expanded powers thereunder or otherwise could materially impact the profitability of our business. See Risk Factors Recent changes have created regulatory uncertainty.

**General**

As a bank holding company, Sterling is subject to regulation, examination and supervision by the Board of Governors of the Federal Reserve System (the Federal Reserve) under the Bank Holding Company Act of 1956, as amended (the BHCA), and by the WDFI. Our subsidiary Sterling Savings Bank is a Washington state-chartered commercial bank, and its deposits are insured by the FDIC. It is subject to regulation, examination and supervision by the FDIC and the WDFI. Numerous federal and state laws, as well as regulations promulgated by the Federal Reserve, the FDIC and state banking regulators, govern almost all aspects of the operation of our bank subsidiary, and Sterling's non-bank subsidiaries are also subject to regulation by applicable federal and state agencies for the states in which they conduct business.

**Bank Holding Company Regulation**

The BHCA limits a bank holding company's business to owning or controlling banks and engaging in other banking-related activities. Bank holding companies must obtain the Federal Reserve's approval before they: (1) acquire direct or indirect ownership or control of any voting shares of any bank that results in total ownership or control, directly or indirectly, of more than 5 percent of the voting shares of such bank; (2) merge or consolidate with another bank holding company; or (3) acquire substantially all of the assets of any additional banks. Subject to certain state laws, such as age and contingency restrictions, a bank holding company that is adequately capitalized and adequately managed may acquire the assets of both in-state banks and out-of-state banks. With certain exceptions, the BHCA prohibits bank holding companies from acquiring direct or indirect ownership or control of voting shares in any company that is not a bank or a bank holding company unless the Federal Reserve determines that the activities of such company are incidental or closely related to the business of banking. If a bank holding company is well-capitalized and meets certain criteria specified by the Federal Reserve, it may engage de novo in certain permissible non-banking activities without prior Federal Reserve approval.

A number of provisions of the Dodd-Frank Act, a few of which are described here, will affect the regulation and operations of bank holding companies. Pursuant to the statute, the FDIC is given back-up supervisory authority over bank holding companies engaging in conduct that poses a foreseeable and material risk to the Deposit Insurance Fund, and the Federal Reserve gains heightened authority to examine, prescribe regulations and take

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action with respect to all of a bank holding company's subsidiaries. A newly created agency, the Office of Financial Research, will have data collecting authority over all financial institutions for the purpose of studying threats to U.S. financial stability. Bank holding companies with \$10 billion or more in assets will also be required to conduct and publish the results of annual stress tests. See Risk Factors Recent changes have created regulatory uncertainty.

Holding companies of banks chartered under Washington law are subject to applicable provisions of Washington's banking laws and to the examination, supervision and enforcement powers of the WDFI. Among other powers, the WDFI has the authority to issue and enforce cease and desist orders on such holding companies and to bring actions to remove their directors, officers and employees.

## **Change in Control**

Subject to certain exceptions, the BHCA and the Change in Bank Control Act, together with regulations promulgated thereunder, require Federal Reserve approval prior to any person or company acquiring control of a bank or bank holding company. Control is conclusively presumed to exist if an individual or company acquires 25 percent or more of any class of voting securities. Control is rebuttably presumed to exist if a person acquires 10 percent or more, but less than 25 percent, of any class of an institution's voting securities and either that institution has registered securities under Section 12 of the Exchange Act or no other person owns a greater percentage of that class of voting securities immediately after the transaction. In certain cases, a company may also be presumed to have control under the Bank Holding Company Act if it acquires 5 percent or more of any class of voting securities.

On September 22, 2008, the Federal Reserve issued a policy statement on minority equity investments in banks and bank holding companies that permits investors without triggering the various regulatory requirements associated with control to (1) acquire up to 33 percent of the total equity of a target bank or bank holding company, subject to certain conditions including (but not limited to) the condition that the investing firm does not acquire 15 percent or more of any class of voting securities, and (2) designate at least one director.

Pursuant to the Dodd-Frank Act, a bank holding company may acquire control of an out-of-state bank only if the bank holding company is well-capitalized and well-managed, and interstate merger transactions are prohibited unless the resulting bank would be well-capitalized and well-managed following the transaction.

Washington state law requires that the WDFI be given at least thirty days notice of any proposed change of control of a Washington state-chartered bank. Washington law defines control of an entity to mean directly or indirectly, alone or in concert with others, to own, control or hold the power to vote 25 percent or more of the outstanding stock or voting power of the entity.

## **Capital Requirements**

We are required to comply with the capital adequacy standards established by the Federal Reserve, and our banking subsidiary must comply with similar capital adequacy standards established by the FDIC.

## **Capital Requirements**

Sterling and Sterling Savings Bank are each subject to requirements to maintain capital at or above certain levels. The Federal Reserve adopted guidelines pursuant to which it assesses the adequacy of capital in examining and supervising a bank holding company such as Sterling, and in analyzing applications to it under the Bank Holding Company Act. The FDIC has adopted similar guidelines to assess the adequacy of capital in state-chartered non-member banks such as Sterling Savings Bank. These guidelines include quantitative measures that assign risk weightings to assets and off-balance sheet items and that define and set minimum regulatory capital requirements. The definitions of capital and the tests for measuring the adequacy of capital required by the Federal Reserve for bank holding companies and by the FDIC for state-chartered non-member banks are similar, but not identical.

In general, all bank holding companies are required to maintain Tier 1 Capital of at least 4 percent of risk-weighted assets and off-balance sheet items, Total Capital (the sum of Tier 1 Capital and Tier 2 Capital) of at least 8 percent of risk-weighted assets and off-balance sheet items, and Tier 1 Capital of at least 3 percent of adjusted quarterly average assets.

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On September 12, 2010, the Basel Committee announced new capital standards commonly referred to as Basel III. The standards would, among other things, impose more restrictive eligibility requirements for Tier 1 and Tier 2 capital; increase the minimum Tier 1 common equity ratio to 4.5 percent, net of regulatory deductions, and introduce a capital conservation buffer of an additional 2.5 percent of common equity to risk-weighted assets, raising the target minimum common equity ratio to 7 percent; increase the minimum Tier 1 capital ratio to 8.5 percent inclusive of the capital conservation buffer; increase the minimum total capital ratio to 10.5 percent inclusive of the capital buffer; and introduce a countercyclical capital buffer of up to 2.5 percent of common equity or other fully loss absorbing capital for periods of excess credit growth. Basel III also introduces a non-risk adjusted Tier 1 leverage ratio of 3 percent, based on a measure of total exposure rather than total assets, and new liquidity standards. If adopted in the U.S., these standards could lead to significantly higher capital requirements, higher capital charges and more restrictive leverage and liquidity ratios. See Risk Factors We may be subject to more stringent capital requirements.

To be well-capitalized, a bank must generally maintain a Total Capital (the sum of Tier 1 Capital and Tier 2 Capital) ratio of 10 percent or greater, a Tier 1 Capital ratio of 6 percent or greater, and a leverage ratio of 5 percent or greater.

For the purposes of these tests, Tier 1 Capital generally consists of common equity, retained earnings and a limited amount of qualifying preferred stock, less goodwill and certain core deposit intangibles. Tier 2 Capital consists of non-qualifying preferred stock, certain types of debt and a limited amount of other items. The regulations require certain items, such as goodwill, to be deducted when calculating certain capital requirements.

In measuring the adequacy of capital, assets are generally weighted for risk at rates that range from zero percent to 100 percent. Certain assets, such as cash and U.S. government securities, have a zero percent risk weighting. Others, such as certain commercial and consumer loans, have a 100 percent risk weighting. Risk weightings are also assigned for off-balance sheet items such as loan commitments. The various items are multiplied by the appropriate risk-weighting to determine risk-adjusted assets for the capital calculations. For the leverage ratio mentioned above, assets are not risk-weighted.

If a depository institution fails to remain well-capitalized, it becomes subject to a variety of enforcement remedies that increase as the capital condition worsens. For instance, federal law generally prohibits a depository institution from making any capital distribution, including the payment of a dividend or paying any management fee to its holding company, if the depository institution would be undercapitalized as a result.

Undercapitalized depository institutions may not accept brokered deposits absent a waiver from the FDIC, are subject to growth limitations and are required to submit a capital restoration plan for approval, which must be guaranteed by the institution's holding company. Significantly undercapitalized depository institutions may be subject to a number of requirements and restrictions, including orders to sell sufficient voting stock to become adequately capitalized, requirements to reduce total assets, and cessation of receipt of deposits from correspondent banks.

Critically undercapitalized institutions are subject to the appointment of a receiver or conservator. See Prompt Corrective Action below.

As a result of the recently completed recapitalization described below, Sterling and Sterling Savings Bank's capital levels are now above those currently required to be deemed well-capitalized. As noted, capital requirements will likely be increasing gradually over the next several years as a result of the implementation of the Dodd-Frank Act and the U.S. federal banking regulators' implementation of the recently announced Basel III standards.

### **Commitments to Subsidiary Bank**

Under Federal Reserve policy, as well as pursuant to the Reserve Bank Agreement, we are expected to act as a source of financial strength to our subsidiary bank and to commit resources to support our subsidiary bank in circumstances when we might not do so absent such policy. The Dodd-Frank Act requires this Federal Reserve

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policy to be made law. Under the Bank Holding Company Act, the Federal Reserve may require a bank holding company to terminate any activity or relinquish control of a nonbank subsidiary, other than a nonbank subsidiary of a bank, upon the Federal Reserve's determination that such activity or control constitutes a serious risk to the financial soundness or stability of any depository institution subsidiary. Further, the Federal Reserve has discretion to require a bank holding company to divest itself of any bank or nonbank subsidiaries if the agency determines that any such divestiture may aid the depository institution's financial condition. In addition, any capital loans by us to our subsidiary bank would be subordinate in right of payment to depositors and to certain other indebtedness of such bank.

If we were to enter bankruptcy, any commitment by us to a federal bank regulatory agency to maintain the capital of our subsidiary bank would be assumed by the bankruptcy trustee and entitled to a priority of payment.

## **Prompt Corrective Action**

The Federal Deposit Insurance Corporation Improvement Act of 1991 ( FDICIA ) established a system of prompt corrective action to resolve the problems of undercapitalized insured depository institutions. Under this system, the federal banking regulators are required to rate insured depository institutions on the basis of five capital categories as described below. The federal banking regulators are also required to take mandatory supervisory actions and are authorized to take other discretionary actions with respect to insured depository institutions in the three undercapitalized categories, the severity of which will depend upon the capital category in which the insured depository institution is assigned. Generally, subject to a narrow exception, FDICIA requires the banking regulators to appoint a receiver or conservator for an insured depository institution that is critically undercapitalized. The federal banking agencies have specified by regulation the relevant capital level for each category. Under the regulations, all insured depository institutions are assigned to one of the following capital categories:

**Well-Capitalized** The insured depository institution exceeds the required minimum level for each relevant capital measure. A well-capitalized insured depository institution is one (1) having a total risk-based capital ratio of 10 percent or greater, (2) having a Tier 1 risk-based capital ratio of 6 percent or greater, (3) having a leverage capital ratio of 5 percent or greater, and (4) that is not subject to any order or written directive to meet and maintain a specific capital level for any capital measure.

**Adequately Capitalized** The insured depository institution meets the required minimum level for each relevant capital measure. An adequately capitalized insured depository institution is one (1) having a total risk-based capital ratio of 8 percent or greater, (2) having a Tier 1 risk-based capital ratio of 4 percent or greater, and (3) having a leverage capital ratio of 4 percent or greater or a leverage capital ratio of 3 percent or greater if the institution is rated composite 1 under the CAMELS (Capital, Assets, Management, Earnings, Liquidity and Sensitivity to market risk) rating system.

**Undercapitalized** The insured depository institution fails to meet the required minimum level for any relevant capital measure. An undercapitalized insured depository institution is one (1) having a total risk-based capital ratio of less than 8 percent, (2) having a Tier 1 risk-based capital ratio of less than 4 percent, or (3) a leverage capital ratio of less than 4 percent, or if the institution is rated a composite 1 under the CAMELS rating system, a leverage capital ratio of less than 3 percent.

**Significantly Undercapitalized** The insured depository institution is significantly below the required minimum level for any relevant capital measure. A significantly undercapitalized insured depository institution is one (1) having a total risk-based capital ratio of less than 6 percent, (2) a Tier 1 risk-based capital ratio of less than 3 percent, or (3) a leverage capital ratio of less than 3 percent.

**Critically Undercapitalized** The insured depository institution fails to meet a critical capital level set by the appropriate federal banking agency. A critically undercapitalized institution is one having a ratio of tangible equity to total assets that is equal to or less than 2 percent.



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The regulations permit the appropriate federal banking regulator to downgrade an institution to the next lower category if the regulator determines (1) after notice and opportunity for hearing or response, that the institution is in an unsafe or unsound condition or (2) that the institution has received and not corrected a less-than-satisfactory rating for any of the categories of asset quality, management, earnings or liquidity in its most recent examination. Supervisory actions by the appropriate federal banking regulator depend upon an institution's classification within the five categories.

FDICIA generally prohibits a depository institution from making any capital distribution, including payment of a dividend, or paying any management fee to its holding company if the depository institution would thereafter be undercapitalized. See Dividends. Undercapitalized depository institutions are subject to restrictions on borrowing from the Federal Reserve System. In addition, undercapitalized depository institutions are subject to growth limitations and are required to submit capital restoration plans. A depository institution's holding company must guarantee the capital plan, up to an amount equal to the lesser of 5 percent of the depository institution's assets at the time it becomes undercapitalized or the amount of the capital deficiency when the institution fails to comply with the plan. Federal banking agencies may not accept a capital plan without determining, among other things, that the plan is based on realistic assumptions and is likely to succeed in restoring the depository institution's capital. If a depository institution fails to submit an acceptable plan, it is treated as if it is significantly undercapitalized. Sterling and Sterling Savings Bank have until recently been undercapitalized. As a result of the recently completed recapitalization, their capital levels are now above those currently required to be deemed well-capitalized.

Significantly undercapitalized depository institutions may be subject to a number of requirements and restrictions, including orders to sell sufficient voting stock to become adequately capitalized, requirements to reduce total assets and cessation of receipt of deposits from correspondent banks. Critically undercapitalized depository institutions are subject to appointment of a receiver or conservator.

Washington state law gives the WDFI powers similar to those granted to the FDIC under the prompt corrective action provisions of FDICIA.

## **Dividends**

Sterling is a legal entity separate and distinct from its subsidiary bank and other subsidiaries. The principal source of funds for our payment of dividends on our common and preferred stock and principal and interest on our debt is dividends from our subsidiaries. Various federal and state statutory provisions and regulations limit the amount of dividends Sterling, Sterling Savings Bank and certain other subsidiaries may pay without regulatory approval.

Pursuant to the Reserve Bank Agreement, Sterling is prohibited from paying any dividends without the prior written approval of the Reserve Bank. Sterling is also prohibited from directly or indirectly taking dividends, or any other form of payment that would represent a reduction in capital from our banking subsidiary without the prior written approval of the Reserve Bank.

Under the Federal Reserve guidance reissued on February 24, 2009 the Federal Reserve may restrict our ability to pay dividends on any class of capital stock or any other Tier 1 capital instrument if we are not deemed to have a strong capital position. In addition, we may have to reduce or eliminate dividends if:

our net income available to shareholders for the past four quarters, net of dividends previously paid during that period, is not sufficient to fully fund the dividends;

our prospective rate of earnings retention is not consistent with the holding company's capital needs and overall current and prospective financial condition; or

we will not meet, or are in danger of not meeting, the minimum regulatory capital adequacy ratios.

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Federal bank regulatory agencies have the authority to prohibit Sterling Savings Bank from engaging in unsafe or unsound practices in conducting its business, and the payment of dividends, depending on the bank's financial condition, could be deemed an unsafe or unsound practice. Pursuant to the SSB MOU, Sterling Savings Bank is prohibited from paying dividends without the prior written consent of the FDIC and the WDFI. The ability of Sterling Savings Bank to pay dividends in the future will continue to be influenced by bank regulatory policies and capital guidelines.

FDICIA generally prohibits a depository institution from making any capital distribution, including payment of a dividend, or paying any management fee to its holding company if the institution would thereafter be undercapitalized. In addition, federal and state banking regulations applicable to us and our bank subsidiaries require minimum levels of capital that limit the amounts available for payment of dividends.

Pursuant to the terms of Sterling's participation in the Capital Purchase Program of the United States Department of the Treasury (the Treasury Department), Sterling is also prohibited from paying dividends on its common stock so long as Sterling's payments on its preferred stock remain deferred. Pursuant to the Exchange Agreement with Treasury, Sterling is further prohibited from increasing the dividends to be paid to shareholders above the \$0.10 per share quarterly dividend paid for the quarter ended September 30, 2008. This restriction on Sterling's ability to increase its dividends will continue until either Treasury ceases to own any debt or equity securities acquired pursuant to the Exchange Agreement or the Treasury Warrant or December 5, 2011, whichever is earliest.

For more information, see Dividend Policy.

### **Deposit Insurance and Assessments**

Deposits at our subsidiary bank are insured by the Deposit Insurance Fund (the DIF) as administered by the FDIC. The Dodd-Frank Act raised the standard maximum deposit insurance amount to \$250,000 per depositor, per insured depository institution for each account ownership category. The change makes permanent the temporary coverage limit increase from \$100,000 to \$250,000 that had been in effect since October 2008.

In November 2008, the FDIC expanded deposit insurance limits for qualifying transaction accounts under the Transaction Account Guarantee (TAG) program. The TAG program will continue until the end of 2010. Under it, noninterest-bearing transaction accounts and qualified NOW checking accounts at Sterling Savings Bank are fully guaranteed by the FDIC for an unlimited amount of coverage. Effective on December 31, 2010, and continuing through December 31, 2012, the Dodd-Frank Act provides unlimited FDIC insurance for noninterest-bearing transaction accounts in all banks. The new, two-year coverage picks up where the current TAG program leaves off, though some accounts currently covered under the TAG program, such as NOW checking accounts, will not benefit from the coverage extension.

The FDIC maintains the DIF by assessing each depository institution an insurance premium. The amount of the FDIC assessments paid by a DIF member institution is based on its relative risk of default as measured by the company's FDIC supervisory rating, and other various measures, such as the level of brokered deposits, unsecured debt and debt issuer ratings.

The DIF assessment base rate currently ranges from 12 to 45 basis points for institutions that do not trigger factors for brokered deposits and unsecured debt, and higher rates for those that do trigger those risk factors. On October 19, 2010, the FDIC announced plans to maintain assessment rates at their current levels and to update its loss and income projections at least semiannually, increasing or lowering assessment rates if required. An increase in the assessment rate could have a material adverse effect on Sterling's earnings, depending on the amount of the increase.

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The Dodd-Frank Act effects further changes to the law governing deposit insurance assessments. There is no longer an upper limit for the reserve ratio designated by the FDIC each year, and the maximum reserve ratio may not be less than 1.35% of insured deposits, or the comparable percentage of the assessment base. Under prior law the maximum reserve ratio was 1.15%. The Dodd-Frank Act permits the FDIC until September 30, 2020 to raise the reserve ratio, which is currently negative, to 1.35%. The FDIC is required to offset the effect of increased assessments necessitated by the Dodd-Frank Act on insured depository institutions with total consolidated assets of less than \$10 billion, but we cannot currently predict how this offset will affect us, and implementing rules are not expected until 2011. See Risk Factors Recent changes have created regulatory uncertainty and Risk Factors Current and future increases in FDIC insurance premiums, including FDIC special assessments imposed on all FDIC-insured institutions, will decrease our earnings. The Dodd-Frank Act also eliminates requirements under prior law that the FDIC pay dividends to member institutions if the reserve ratio exceeds certain thresholds, and the FDIC has proposed that in lieu of dividends, it will adopt lower rate schedules when the reserve ratio exceeds certain thresholds.

All FDIC-insured depository institutions must pay an annual assessment to provide funds for the payment of interest on bonds issued by the Financing Corporation, a federal corporation chartered under the authority of the Federal Housing Finance Board. The bonds, which are referred to as FICO bonds, were issued to capitalize the Federal Savings and Loan Insurance Corporation. FDIC-insured depository institutions paid between 1.02 cents to 1.14 cents per \$100 of DIF-assessable deposits in 2009. The FDIC established the FICO assessment rate effective for the first quarter of 2010 at approximately 1.06 cents and for the second, third and fourth quarters of 2010 at approximately 1.04 cents, annually per \$100 of assessable deposits.

### **Transactions with Affiliates and Insiders**

A variety of legal limitations restrict our subsidiary bank from lending or otherwise supplying funds or in some cases transacting business with us or our nonbank subsidiaries. Our subsidiary bank is subject to Sections 23A and 23B of the Federal Reserve Act and Federal Reserve Regulation W. Section 23A places limits on the amount of covered transactions which include loans or extensions of credit to, investments in or certain other transactions with, affiliates as well as the amount of advances to third parties collateralized by the securities or obligations of affiliates. The aggregate of all covered transactions is limited to 10 percent of the bank's capital and surplus for any one affiliate and 20 percent for all affiliates. Furthermore, within the foregoing limitations as to amount, each covered transaction must meet specified collateral requirements ranging from 100 to 130 percent. Also, banks are prohibited from purchasing low quality assets from an affiliate.

Section 23B, among other things, prohibits an institution from engaging in certain transactions with affiliates unless the transactions are on terms substantially the same, or at least as favorable to the bank, as those prevailing at the time for comparable transactions with nonaffiliated companies. Except for limitations on low quality asset purchases and transactions that are deemed to be unsafe or unsound, Regulation W generally excludes affiliated depository institutions from treatment as affiliates. Transactions between a bank and any of its subsidiaries that are engaged in certain financial activities may be subject to the affiliated transaction limits. The Federal Reserve also may designate bank subsidiaries as affiliates.

Banks are also subject to quantitative restrictions on extensions of credit to executive officers, directors, principal shareholders, and their related interests. In general, such extensions of credit (1) may not exceed certain dollar limitations, (2) must be made on substantially the same terms, including interest rates and collateral, as those prevailing at the time for comparable transactions with third parties and (3) must not involve more than the normal risk of repayment or present other unfavorable features. Certain extensions of credit also require the approval of a bank's Board of Directors.

The Dodd-Frank Act expands the 23A and 23B affiliate transaction rules. Among other things, upon the statutory changes' effective date, which will likely be mid- to late- 2012, the scope of the definition of covered transaction under 23A will expand, collateral requirements will increase and certain exemptions will be eliminated.

### **Standards for Safety and Soundness**

The Federal Deposit Insurance Act requires the federal bank regulatory agencies to prescribe, by regulation or guideline, operational and managerial standards for all insured depository institutions relating to: (1) internal controls; (2) information systems and audit systems; (3) loan documentation; (4) credit underwriting; (5) interest rate risk exposure; and (6) asset quality.

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The agencies also must prescribe standards for earnings, and stock valuation, as well as standards for compensation, fees and benefits. The federal banking agencies have adopted regulations and Interagency Guidelines Prescribing Standards for Safety and Soundness to implement these required standards. These guidelines set forth the safety and soundness standards used to identify and address problems at insured depository institutions before capital becomes impaired. Under the regulations, if a regulator determines that a bank fails to meet any standards prescribed by the guidelines, the regulator may require the bank to submit an acceptable plan to achieve compliance, consistent with deadlines for the submission and review of such safety and soundness compliance plans.

### **Regulatory Examination**

Federal and state banking agencies require us and our subsidiary banks to prepare annual reports on financial condition and to conduct an annual audit of financial affairs in compliance with minimum standards and procedures. Our banking subsidiary, and in some cases we and our nonbank affiliates, must undergo regular on-site examinations by the appropriate banking agency. A bank regulator conducting an examination has complete access to the books and records of the examined institution. The results of the examination are confidential. The cost of examinations may be assessed against the examined institution as the agency deems necessary or appropriate. The FDIC has developed a method for insured depository institutions to provide supplemental disclosure of the estimated fair market value of assets and liabilities, to the extent feasible and practicable, in any balance sheet, financial statement, report of condition or any other report.

### **State Law and Regulation**

Sterling Savings Bank as a Washington state-chartered institution, is subject to regulation by the WDFI, which conducts regular examinations to ensure that its operations and policies conform with applicable law and safe and sound banking practices. Among other things, state law regulates the amount of credit that can be extended to any one borrower and the amount of money that can be invested in various types of assets. Sterling Savings Bank generally cannot extend credit to any one borrower in an amount greater than 20 percent of Sterling Savings Bank's capital and surplus. State law also regulates the types of loans Sterling Savings Bank can make. With the WDFI's approval, Sterling Savings Bank can currently invest up to 10 percent of its total assets or 50 percent of its net worth (whichever is less) in other corporations, whether or not such corporations are engaged in activities related to Sterling Savings Bank's business, but such authority is subject to restrictions imposed by federal law. Sterling Savings Bank also operates depository branches within the states of Oregon, Idaho, California and Montana and therefore its operations in these states are subject to the supervision of the Oregon Department of Consumer and Business Services, the Idaho Department of Finance, the California Department of Financial Institutions and the Montana Department of Finance, as applicable. Sterling and its subsidiaries are also required to comply with applicable laws and regulations for activities in Alaska, Arizona, Colorado, Hawaii, Nevada, Texas and Utah.

### **Community Reinvestment Act**

The Community Reinvestment Act requires that the appropriate federal bank regulator evaluate the record of our banking subsidiary in meeting the credit needs of its local community, including low and moderate income neighborhoods. These evaluations are considered in evaluating mergers, acquisitions, and applications to open a branch or facility. Failure to adequately meet these criteria could result in additional requirements and limitations on the bank.

### **Consumer Protection Regulations**

Retail activities of banks are subject to a variety of statutes and regulations designed to protect consumers. The Dodd-Frank Act creates a Bureau of Consumer Financial Protection that, together with the statute's other enhancements to consumer protection laws such as limits on debit card interchange fees and provisions on mortgage-related matters, will likely increase the compliance costs of our consumer banking operations. Interest and

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other charges collected or contracted for by banks are subject to state usury laws and federal laws concerning interest rates. Loan operations are also subject to federal laws applicable to credit transactions, such as:

the federal Truth-In-Lending Act and Regulation Z issued by the Federal Reserve, governing disclosures of credit terms to consumer borrowers;

the Home Mortgage Disclosure Act and Regulation C issued by the Federal Reserve, requiring financial institutions to provide information to enable the public and public officials to determine whether a financial institution is fulfilling its obligation to help meet the housing needs of the community it serves;

the Equal Credit Opportunity Act and Regulation B issued by the Federal Reserve, prohibiting discrimination on the basis of race, creed or other prohibited factors in extending credit;

the Fair Credit Reporting Act and Regulation V issued by the Federal Reserve, governing the use and provision of information to consumer reporting agencies;

the Fair Debt Collection Act, governing the manner in which consumer debts may be collected by collection agencies; and

the guidance of the various federal agencies charged with the responsibility of implementing such federal laws.

Deposit operations also are subject to:

the Truth in Savings Act and Regulation DD issued by the Federal Reserve, which requires disclosure of deposit terms to consumers;

Regulation CC issued by the Federal Reserve, which relates to the availability of deposit funds to consumers;

the Right to Financial Privacy Act, which imposes a duty to maintain the confidentiality of consumer financial records and prescribes procedures for complying with administrative subpoenas of financial records; and

the Electronic Funds Transfer Act and Regulation E issued by the Federal Reserve, which governs automatic deposits to and withdrawals from deposit accounts and customers' rights and liabilities arising from the use of automated teller machines and other electronic banking services.

In addition, our subsidiary bank is also subject to certain state laws and regulations designed to protect consumers.

## **Commercial Real Estate Lending**

Lending operations that involve concentrations of commercial real estate loans are subject to enhanced scrutiny by federal banking regulators. The regulators have advised financial institutions of the risks posed by commercial real estate lending concentrations. Such loans generally include land development, construction loans and loans secured by multifamily property, and nonfarm, nonresidential real property where the primary source of repayment is derived from rental income associated with the property. The guidance prescribes the following guidelines for examiners to help identify institutions that are potentially exposed to concentration risk and may warrant greater supervisory scrutiny:

total reported loans for construction, land development and other land represent 100 percent or more of the institutions total capital,  
or

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total commercial real estate loans represent 300 percent or more of the institution's total capital, and the outstanding balance of the institution's commercial real estate loan portfolio has increased by 50 percent or more during the prior 36 months.

In October 2009, the federal banking agencies issued additional guidance on commercial real estate lending that emphasizes these considerations.

The Dodd-Frank Act contains provisions on credit risk retention that require federal banking regulators to adopt regulations mandating the retention of five percent of the credit risk of assets transferred, sold or conveyed through issuances of asset-backed securities. Implementing regulations will provide for the allocation of the risk retention obligation between securitizers and originators of loans, including residential and commercial mortgages.

### **Branching**

The Riegle-Neal Interstate Banking and Branching Efficiency Act of 1994 (the Interstate Act) permits nationwide interstate banking and branching under certain circumstances. This legislation generally authorizes interstate branching and relaxes federal law restrictions on interstate banking. Currently, bank holding companies may purchase banks in any state, and states may not prohibit these purchases. Additionally, banks are permitted to merge with banks in other states, as long as the home state of neither merging bank has opted out under the legislation. The Interstate Act requires regulators to consult with community organizations before permitting an interstate institution to close a branch in a low-income area.

Washington enacted opting in legislation in accordance with the Interstate Act, allowing banks to engage in interstate merger transactions, subject to certain aging requirements. Once an out-of-state bank has acquired a bank within the state, either through merger or acquisition of all or substantially all of the bank's assets, the out-of-state bank may open additional branches within the state. In addition, an out-of-state bank may establish a de novo branch in Washington or acquire a branch in Washington if the out-of-state bank's home state gives Washington banks substantially the same or more favorable rights to establish and maintain branches in that state.

### **Anti-Tying Restrictions**

In general, a bank may not extend credit, lease, sell property, or furnish any services or fix or vary the consideration for them on the condition that (1) the customer obtain or provide some additional credit, property, or services from or to the bank or bank holding company or their subsidiaries, or (2) the customer not obtain some other credit, property, or services from a competitor, except to the extent reasonable conditions are imposed to assure the soundness of the credit extended. A bank may, however, offer combined-balance products and may otherwise offer more favorable terms if a customer obtains two or more traditional bank products. Also, certain foreign transactions are exempt from the general rule.

### **Anti-Money Laundering**

Financial institutions must maintain anti-money laundering programs that include established internal policies, procedures, and controls; a designated compliance officer; an ongoing employee training program; and testing of the program by an independent audit function. We are prohibited from entering into specified financial transactions and account relationships and must meet enhanced standards for due diligence in dealings with foreign financial institutions and foreign customers. We also must take reasonable steps to conduct enhanced scrutiny of account relationships to guard against money laundering and to report any suspicious transactions. Recent laws provide law enforcement authorities with increased access to financial information maintained by banks. Anti-money laundering obligations have been substantially strengthened as a result of the Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act of 2001 (the USA Patriot Act), enacted in 2001 and renewed in 2006. Bank regulators routinely examine institutions for compliance with these obligations and are required to consider compliance in connection with the regulatory review of applications.

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The USA Patriot Act amended, in part, the Bank Secrecy Act and provides for the facilitation of information sharing among governmental entities and financial institutions for the purpose of combating terrorism and money laundering. The statute also creates enhanced information collection tools and enforcement mechanics for the U.S. government, including: (1) requiring standards for verifying customer identification at account opening; (2) promulgating rules to promote cooperation among financial institutions, regulators, and law enforcement entities in identifying parties that may be involved in terrorism or money laundering; (3) requiring reports by nonfinancial trades and businesses filed with the Treasury's Financial Crimes Enforcement Network for transactions exceeding \$10,000; and (4) mandating the filing of suspicious activities reports if a bank believes a customer may be violating U.S. laws and regulations. The statute also requires enhanced due diligence requirements for financial institutions that administer, maintain, or manage private bank accounts or correspondent accounts for non-U.S. persons.

The Federal Bureau of Investigation may send bank regulatory agencies lists of the names of persons suspected of involvement in terrorist activities. Our banks can be requested to search their records for any relationships or transactions with persons on those lists and may be required to report any identified relationships or transactions. Furthermore, the Office of Foreign Assets Control (OFAC) is responsible for helping to ensure that U.S. entities do not engage in transactions with certain prohibited parties, as defined by various Executive Orders and Acts of Congress. OFAC has sent, and will send, bank regulatory agencies lists of names of persons and organizations suspected of aiding, harboring or engaging in terrorist acts, known as Specially Designated Nationals and Blocked Persons. If we find a name on any transaction, account or wire transfer that is on an OFAC list, we must freeze such account, file a suspicious activity report and notify the appropriate authorities.

## **Privacy and Credit Reporting**

Financial institutions are required to disclose their policies for collecting and protecting confidential customer information. Customers generally may prevent financial institutions from sharing nonpublic personal financial information with nonaffiliated third parties, with some exceptions, such as the processing of transactions requested by the consumer. Financial institutions generally may not disclose certain consumer or account information to any nonaffiliated third party for use in telemarketing, direct mail marketing or other marketing. Federal and state banking agencies have prescribed standards for maintaining the security and confidentiality of consumer information, and we are subject to such standards, as well as certain federal and state laws or standards for notifying consumers in the event of a security breach.

Our banking subsidiary utilizes credit bureau data in underwriting activities. Use of such data is regulated under the Fair Credit Reporting Act and Regulation V on a uniform, nationwide basis, including credit reporting, prescreening, sharing of information between affiliates and the use of credit data. The Fair and Accurate Credit Transactions Act, which amended the Fair Credit Reporting Act, permits states to enact identity theft laws that are not inconsistent with the conduct required by the provisions of that Act.

## **Enforcement Powers**

Banks and their institution-affiliated parties, including management, employees, agents, independent contractors and consultants, such as attorneys and accountants and others who participate in the conduct of the institution's affairs, are subject to potential civil and criminal penalties for violations of law, regulations or written orders of a government agency. Violations can include failure to timely file required reports, filing false or misleading information or submitting inaccurate reports. Civil penalties may be as high as \$1,000,000 a day for such violations and criminal penalties for some financial institution crimes may include imprisonment for 20 years. Regulators have flexibility to commence enforcement actions against institutions and institution-affiliated parties, and the FDIC has the authority to terminate deposit insurance. When issued by a banking agency, cease-and-desist orders may, among other things, require affirmative action to correct any harm resulting from a violation or practice, including restitution, reimbursement, indemnifications or guarantees against loss. A financial institution may also be ordered to restrict its growth, dispose of certain assets, rescind agreements or contracts, or take other actions determined to be appropriate by the ordering agency. The federal banking agencies also may remove a director or officer from an insured depository institution (or bar them from the industry) if a violation is willful or reckless. The WDFI has similar enforcement powers.



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For information on the SSB MOU and the Reserve Bank Agreement applicable to Sterling, see Prospectus Summary Recapitalization Transactions Background.

### **Corporate Governance**

The Dodd-Frank Act contains a number of provisions that will require changes to financial institutions' corporate governance and executive compensation practices, including proxy access for publicly-traded banks' director nominations, clawback of incentive-based compensation from executive officers and increased disclosure on compensation arrangements. Publicly-traded bank holding companies with more than \$10 billion in assets will also be required to have risk committees with a number of independent directors to be determined by the Federal Reserve and that include at least one risk management expert with experience in risk management at large, complex companies.

### **Monetary Policy and Economic Controls**

The earnings of our bank subsidiaries, and therefore our earnings, are affected by the policies of regulatory authorities, including the monetary policy of the Federal Reserve. An important function of the Federal Reserve is to promote orderly economic growth by influencing interest rates and the supply of money and credit. Among the methods that have been used to achieve this objective are open market operations in U.S. government securities, changes in the discount rate for bank borrowings, expanded access to funds for nonbanks and changes in reserve requirements against bank deposits. These methods are used in varying combinations to influence overall growth and distribution of bank loans, investments and deposits, interest rates on loans and securities, and rates paid for deposits. In recent years, in response to the financial crisis, the Federal Reserve has created several innovative programs to stabilize certain financial institutions and to ensure the availability of credit. The effects of the various Federal Reserve policies on our future business and earnings cannot be predicted.

### **Depositor Preference Statute**

Federal law provides that deposits and certain claims for administrative expenses and employee compensation against an insured depository institution are afforded priority over other general unsecured claims against such institution, including federal funds and letters of credit, in the liquidation or other resolution of the institution by any receiver.

### **TARP Regulations**

Under the Emergency Economic Stabilization Act of 2008 ( EESA ), Congress has the ability to impose after-the-fact terms and conditions on participants in Treasury Department's Capital Purchase Program, a program created to deploy TARP funds. As a participant in the TARP Capital Purchase Program, we are subject to any such retroactive legislation. On February 10, 2009, the Treasury announced the Financial Stability Plan under the EESA, which is intended to further stabilize financial institutions and stimulate lending across a broad range of economic sectors. On February 18, 2009, President Obama signed the American Recovery and Reinvestment Act of 2009 ( ARRA ), a broad economic stimulus package that included additional restrictions on, and potential additional regulation of, financial institutions.

On June 10, 2009, under the authority granted to it under ARRA and EESA, the Treasury Department issued an interim final rule under Section 111 of EESA, as amended by ARRA, regarding compensation and corporate governance restrictions that would be imposed on TARP recipients, effective June 15, 2009. As a TARP recipient with currently outstanding TARP obligations, we are subject to the compensation and corporate governance restrictions and requirements set forth in the interim final rule, which, among other things: (1) prohibit us from paying or accruing bonuses, retention awards or incentive compensation, except for certain long-term stock awards, to our senior executives and next 20 most highly compensated employees; (2) prohibit us from making severance payments to any of our senior executive officers or next five most highly compensated employees; (3) require us to conduct semi-annual risk assessments to assure that our compensation arrangements do not encourage unnecessary and excessive risks or the manipulation of earnings to increase compensation; (4) require us to recoup or clawback any bonus, retention award or incentive compensation paid by us to a senior executive

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officer or any of our next 20 most highly compensated employees, if the payment was based on financial statements or other performance criteria that are later found to be materially inaccurate; (5) prohibit us from providing tax gross-ups to any of our senior executive officers or next 20 most highly compensated employees; (6) require us to provide enhanced disclosure of perquisites, and the use and role of compensation consultants; (7) required us to adopt a corporate policy on luxury and excessive expenditures; (8) require our chief executive officer and chief financial officer to provide period certifications about our compensation practices and compliance with the interim final rule; (9) require us to provide enhanced disclosure of the relationship between our compensation plans and the risk posed by those plans; and (10) require us to provide an annual non-binding shareholder vote, or say-on-pay proposal, to approve the compensation of our executives, consistent with regulations promulgated by the Securities and Exchange Commission ( SEC ). On January 12, 2010, the SEC adopted final regulations setting forth the parameters for such say-on pay proposals for public company TARP participants.

We are also obligated under the Exchange Agreement to take all necessary actions to comply with the executive compensation restrictions under EESA and any subsequent amendments thereto for so long as we remain subject to such restrictions. The Exchange Agreement further requires that we obtain a waiver with respect to the application of the executive compensation restrictions under EESA from each employee who is subject to the restrictions. The Exchange Agreement also reiterates the \$500,000 limitation on the deduction of compensation to our senior executive officers under EESA, ARRA and the regulations promulgated thereunder. Finally, if any payments are made that are in violation these Exchange Agreement provisions, such amounts must be subject to clawback and repayment to Sterling, and Sterling must provide notice to Treasury of any violation and clawback that occurs.

Additional regulations applicable to TARP recipients adopted as part of EESA, the Financial Stability Plan, ARRA or other legislation may subject us to additional regulatory requirements. The impact of these additional requirements may put us at competitive disadvantage in comparison to financial institutions that have either repaid all TARP funds or never accepted TARP funds and may materially adversely affect our business and results of operations.

### **THE RECAPITALIZATION**

On August 26, 2010, Sterling effected a recapitalization designed to return Sterling back to a sound capital footing. The transactions involved in the recapitalization are described in further detail in this section.

#### **Background to the Recapitalization**

The economic downturn in Sterling's market areas and resulting decline in real estate values had a direct and adverse effect on the financial condition and results of operations of Sterling and its wholly owned banking subsidiary, Sterling Savings Bank, including reductions in the capital levels of Sterling and Sterling Savings Bank as a result of elevated loan charge-offs and increases in the allowance for loan losses. Furthermore, Sterling and Sterling Savings Bank entered into agreements with the Reserve Bank and the FDIC, respectively, to take steps to further strengthen Sterling and Sterling Savings Bank, including increasing capital levels to return to well-capitalized status. As a result, Sterling initiated a recapitalization effort, which was effected on August 26, 2010. The amount of capital raised exceeds the amount required under Sterling and Sterling Savings Bank's agreements with their regulators and restored both Sterling and Sterling Savings Bank's regulatory ratios to levels that exceed well-capitalized thresholds under currently applicable guidelines.

The recapitalization comprised three transactions: (i) the Anchor Investments; (ii) the Treasury Exchange; and (iii) the Private Placement.

Sterling received aggregate gross proceeds from the recapitalization of \$730 million.

The recapitalization transactions are discussed in more detail below.

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**Anchor Investments**

**Overview**

On August 26, 2010, Sterling issued the following securities to each of (a) Thomas H. Lee Equity Fund IV, L.P., Thomas H. Lee Parallel Fund VI, L.P., Thomas H. Lee Parallel (DT) Fund VI, L.P. and THL Sterling Equity Investors, L.P. (collectively, THL or an Anchor Investor ) and (b) Warburg Pincus Private Equity X, L.P. ( Warburg Pincus or an Anchor Investor ), effected pursuant to investment agreements between Sterling and each of the Anchor Investors (the Anchor Investment Agreements ):

68,366,000 shares of Sterling's Common Stock at a price of \$0.20 per share;

1,709,150 shares of Sterling's Series B Preferred Stock at a price of \$92 per share and a liquidation preference of \$4.60 per share; and

a seven-year warrant to purchase 86,625,000 shares of Common Stock at an exercise price of \$0.22 per share, subject to adjustment (the Anchor Investor Warrants ).

Sterling received aggregate gross proceeds of approximately \$170.9 million from each of the Anchor Investors in connection with the Anchor Investors' acquisition of the above described securities (the Anchor Investments ).

Although the recapitalization would generally have required shareholder approval under the NASDAQ listing rules, Sterling sought and obtained approval from NASDAQ for an exception from these requirements under NASDAQ Listing Rule 5635(f) given that the delay in securing shareholder approval prior to effecting the recapitalization would have seriously jeopardized the financial viability of Sterling. NASDAQ also granted an exception to Sterling from the voting rights requirements of Listing Rule 5640 and IM-5640 with respect to the recapitalization transactions. Sterling's Audit Committee expressly approved reliance upon these exceptions. A copy of the letter that Sterling mailed to its shareholders in connection with these exceptions has previously been filed as Exhibit 99.1 to Sterling's Current Report on Form 8-K filed on August 13, 2010.

Pursuant to the terms of the Anchor Investment Agreements, following the closing of the Recapitalization Transactions, Sterling agreed to obtain the approval of its shareholders to, among other things, (i) amend its Restated Articles of Incorporation to increase the number of authorized shares of its Common Stock in a manner sufficient to permit the full conversion of the Series B Preferred Stock and Series D Preferred Stock into, and the exercise of the Anchor Investor Warrants for, shares of its Common Stock and (ii) approve the conversion of Series B Preferred Stock and the Series D Preferred Stock and the exercisability of the Anchor Investor Warrants. These items were approved at a special meeting of shareholders on October 21, 2010. As of \_\_\_\_\_, 2010, each Anchor Investor held 854,575,000 shares of Common Stock and a warrant to purchase 86,625,000 shares of Common Stock.

**Anchor Investor Warrants**

Each Anchor Investor was issued a warrant exercisable for a seven-year term to purchase 86,625,000 shares of Common Stock at an exercise price of \$0.22 per share. The resale of these warrants is covered by the Registration Statement of which this Prospectus forms a part. See Description of the Warrants Anchor Investor Warrants.

**Board Representation**

Under the terms of the Anchor Investment Agreements, each Anchor Investor is entitled to one seat on Sterling's Board of Directors (an Anchor Investor Board Representative ) and is also entitled to designate one person to attend meetings of the Board of Directors as a non-voting observer. This provision continues to apply for so long as such Anchor Investor owns 4.9 percent or more of the Common Stock, calculated in accordance with the terms of the Anchor Investment Agreement, on a fully exercised basis. Scott L. Jaeckel has been appointed to the board as THL's representative at the board, and David Coulter has been appointed as Warburg Pincus's



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representative on the board. In addition, Mr. Jaeckel has been appointed to Sterling's Governance and Nominating Committee and Mr. Coulter has been appointed to Sterling's Credit and Risk Committee and its Compensation Committee. If an Anchor Investor's share ownership drops below the threshold described above, such Anchor Investor will no longer be entitled to a board observer and, at the written request of the Board of Directors, an Anchor Investor is required to use its reasonable best efforts to cause its Anchor Investor Board Representative to resign.

### **Standstill**

Under the terms of the Anchor Investment Agreements, so long as an Anchor Investor owns at least 4.9 percent of our Common Stock, calculated in accordance with the terms of the Anchor Investment Agreement, on an as-converted and fully exercised basis, such Anchor Investor is not permitted, without prior approval of our Board of Directors, to directly or indirectly:

acquire, offer or propose to acquire or agree to acquire beneficial ownership of any voting securities if such acquisition would result in such Anchor Investor (i) being deemed to control Sterling within the meaning of the Bank Holding Company Act of 1956 and the Change in Bank Control Act of 1978, (ii) owning more than 33 percent of the total equity of Sterling, or (iii) having beneficial ownership of 25 percent or more of the outstanding shares of a class of voting securities or Common Stock;

make or in any way participate in any solicitation of proxies to vote, or seek to advise or influence any person or entity with respect to the voting of, any voting securities of Sterling or any subsidiary;

call or seek to call a meeting of the shareholders, form, join or in any way participate in a group with respect to any voting securities, or seek, propose or otherwise act alone or in concert with others, to influence or control the management, the Board of Directors or policies of Sterling;

enter into or agree, offer, propose or seek (whether publicly or otherwise) to enter into any acquisition transaction, merger or other business combination relating to all or part of Sterling or any of its subsidiaries or any acquisition transaction for all or part of the assets of Sterling or any subsidiary or any of their respective businesses; or

publicly disclose any intention, plan or arrangement inconsistent with any of the foregoing.

### **Registration Rights**

Under the terms of the Anchor Investment Agreements, each Anchor Investor received certain registration rights, subject to specified black-out rights during which time Sterling would not be required to effect a registration and dispositions of securities acquired in the Anchor Investments would be restricted. Sterling agreed to file a Registration Statement covering the Securities purchased by the Anchor Investors and to use its reasonable best efforts to cause the Registration Statement to be declared or become effective. In addition, each Anchor Investor received the right to demand that Sterling file a registration statement and facilitate an underwritten offering of the Anchor Investors' Securities. If an underwritten offering is requested in accordance with the agreements with the Anchor Investors, Sterling is obligated to participate in and facilitate such underwriting, including making management and executives of Sterling available for road shows, similar sales events and other marketing activities. This Prospectus forms a part of a Registration Statement that was filed for the purpose of fulfilling those requirements.

### **Pre-emptive Rights**

Under the terms of the Anchor Investment Agreements, so long as an Anchor Investor owns at least 4.9 percent of our Common Stock, calculated in accordance with the terms of the Anchor Investment Agreement, on an as-converted and fully exercised basis, such Anchor Investor will have pre-emptive rights to participate on a pro rata basis in any equity capital raises to maintain its ownership percentage, subject to certain exceptions. In addition, until the earlier of August 26, 2011 and the date on which the Anchor Investor owns less than 3 percent of our Common Stock, the Anchor Investor will be entitled to similar pre-emptive rights.



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### **Other**

Under the terms of the Anchor Investment Agreements, we have agreed to indemnify each Anchor Investor for losses resulting from (i) inaccuracies in our representations or warranties in its Anchor Investment Agreement (which will generally survive until November 26, 2011), (ii) breaches of our agreements or covenants in its Anchor Investment Agreement and (iii) subject to certain limited exceptions, any legal, administrative or other proceedings relating to or arising out of such Anchor Investments.

With respect to breaches of representation only under the terms of each Investment Agreement:

claims for individual losses of less than \$50,000 are disregarded;

no indemnity is made unless the aggregate amount of all losses (excluding those below \$50,000) exceeds \$1.5 million; and

the total indemnity is capped at each Anchor Investor's purchase price.

The indemnity is an Anchor Investor's exclusive post-closing remedy, except in respect of intentional and willful fraud, intentional and willful misrepresentation or intentional and willful misconduct. See "Risk Factors" Sterling may suffer substantial losses due to its agreements to indemnify certain investors against a broad range of potential claims.

Under the terms of the Anchor Investment Agreements, the Securities purchased by the Anchor Investors are subject to certain transfer restrictions. For additional information on the transfer restrictions applicable to the Securities offered pursuant to this Prospectus, see "Transfer Restrictions and Rights Plan."

### **Private Placements**

#### **Overview**

On August 26, 2010, Sterling issued, in the aggregate, to the Private Placement Investors, pursuant to the Subscription Agreements, the following securities:

155,268,000 shares of Common Stock at a price of \$0.20 per share; and

3,881,700 shares of Series D Preferred Stock at a price of \$92 per share.

Sterling received aggregate gross proceeds of approximately \$388.2 million from the Private Placement Investors collectively in connection with the Private Placement.

Pursuant to the terms of the Subscription Agreements, Sterling agreed to obtain the approval of its shareholders to, among other things, (i) amend its Restated Articles of Incorporation to increase the number of authorized shares of its Common Stock in a manner sufficient to permit the full conversion of the Series B Preferred Stock and Series D Preferred Stock into, and exercise of the Anchor Investor Warrants for, shares of its Common Stock and (ii) approve the conversion of the Series B Preferred Stock and the Series D Preferred Stock and the exercisability of the Anchor Investor Warrants. These items were approved at a special meeting of shareholders on October 21, 2010.

As of \_\_\_\_\_, 2010, the Private Placement Investors collectively held 1,940,850,000 shares of Common Stock.

#### **Registration Rights**

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Pursuant to the terms of the Subscription Agreements, each Private Placement Investor received certain registration rights, subject to specified black-out rights during which time Sterling would not be required to effect a registration and dispositions of securities acquired in



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the Private Placement Investments would be restricted. Sterling agreed to file a Registration Statement covering the Securities purchased by the Private Placement Investors and to use its reasonable best efforts to cause the Registration Statement to be declared or become effective within 60 days of this filing. This Prospectus forms a part of a Registration Statement that was filed for the purpose of fulfilling those requirements.

### **Pre-emptive Rights**

Pursuant to the terms of the Subscription Agreements, those Private Placement Investors who hold a minimum qualifying ownership interest of 3 percent of Sterling's Common Stock (the **Qualifying Ownership Percentage**) have a contractual right to participate on a pro rata basis in future equity raises, subject to certain exceptions, to maintain their ownership percentage for a period equal to the shorter of 12 months from the closing of the Recapitalization Transactions (August 26, 2011) or the date on which the Private Placement Investor no longer holds a **Qualifying Ownership percentage**.

### **Other**

We agreed to indemnify each Private Placement Investor for losses resulting from (i) inaccuracies in our representations or warranties in the Subscription Agreement (which will generally survive until November 26, 2011), and (ii) breaches of our agreements or covenants in the Subscription Agreement.

With respect to breaches of representation only under the terms of the Subscription Agreement:

claims for individual losses of less than \$50,000 are disregarded;

no indemnity is made unless the aggregate amount of all losses (excluding those below \$50,000) exceeds \$1.5 million; and

the total indemnity is capped at each Private Placement Investor's purchase price.

The indemnity is a Private Placement Investor's exclusive post-closing remedy, except in respect of intentional and willful fraud, intentional and willful misrepresentation or intentional and willful misconduct. See **Risk Factors** Sterling may suffer substantial losses due to its agreements to indemnify certain investors against a broad range of potential claims.

Under the terms of the Subscription Agreements, the Common Stock purchased by the Private Placement Investors is subject to certain transfer restrictions. For additional information on the transfer restrictions applicable to the Securities offered pursuant to this Prospectus, see **Transfer Restrictions and Rights Plan**.

## **Treasury Exchange**

### **Overview**

On August 26, 2010, pursuant to the Exchange Agreement, Sterling and Treasury effected the Treasury Exchange, comprising:

the exchange of 303,000 shares of Fixed Rate Cumulative Perpetual Preferred Stock, Series A (**TARP Preferred Stock**) held by Treasury for 303,000 shares of Fixed Rate Cumulative Mandatorily Convertible Preferred Stock, Series C (**New Treasury Preferred Stock**) with a liquidation preference of \$303 million;

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conversion of the New Treasury Preferred Stock at a discounted exchange value of approximately \$75.8 million into 378,750,000 shares of Common Stock at a conversion price of \$0.20 per share; and

amendment of the terms of the Treasury warrant to purchase 6,437,677 shares of Common Stock at an exercise price of \$7.06 per share, to provide for an exercise price of \$0.20 per share for a ten-year term following the closing of the recapitalization (such amended warrant, the Treasury Warrant ).

As of , 2010, Treasury held 378,750,000 of Sterling s outstanding Common Stock and a warrant exercisable for 6,437,677 shares of Common Stock.

Pursuant to the Exchange Agreement, Treasury has agreed to attend all meetings of Sterling s shareholders in person or by proxy for purposes of obtaining a quorum. Treasury has also agreed to vote, or cause to be voted, all common shares beneficially owned by it with respect to each matter on which holders of Common Stock are entitled to vote or consent in the same proportion (for, against or abstain) as all other shares of Sterling s Common Stock, other than those held by the Anchor Investors, are voted or consents are given with respect to the Proposed Section 382 Article Amendment and any other matter on which holders of Sterling s Common Stock are entitled to vote, other than (a) the election and removal of directors, (b) the approval of any business combination, (c) the approval of a sale of all or substantially all of the assets or property of Sterling, (d) the approval of a dissolution of Sterling, (e) the approval of any issuance of any securities of Sterling on which holders of Common Stock are entitled to vote, (f) the approval of any amendment to the Articles of Incorporation or Bylaws of Sterling on which holders of Common Stock are entitled to vote and (g) the approval of any other matters reasonably incidental to the foregoing, as determined by Treasury (the matters referred to in (a) through (g), the Designated Matters ). With respect to Designated Matters, Treasury has retained the right under the Exchange Agreement to vote its shares in its sole discretion.

**Other Matters**

The foregoing descriptions do not purport to be complete and each is qualified in its entirety by reference to the complete copy of the applicable agreements or securities. The Anchor Investment Agreements and amendments thereto, form of Subscription Agreement between Sterling and each of the Private Placement Investors, the Exchange Agreement and Warrants are filed as Exhibits to the Registration Statement of which this Prospectus forms a part and are incorporated by reference herein.

**Governance**

In connection with Sterling s Recapitalization, Sterling agreed to appoint a representative of THL and a representative of Warburg Pincus to Sterling s board. Sterling also decided, in an effort to improve its governance and bring additional banking expertise to the board, to appoint Leslie S. Biller to serve as a member and Chairman of the Board. These appointments became effective as of August 26, 2010. The board also decided that it was in Sterling s best interests that the board have a smaller number of members. Therefore, certain members of the board decided to retire from the board. The board now consists of Mr. Biller, Ellen R.M. Boyer, Robert C. Donegan, William L. Eisenhart, Robert H. Hartheimer, Michael F. Reuling, Sterling CEO J. Gregory Seibly, Warburg Pincus designee David A. Coulter and THL designee Scott L. Jaeckel. Biographical information for each Director is provided below:

**Leslie ( Les ) S. Biller**

Mr. Biller, 62, has served as a Director of Sterling and as Chairman of the Board of Directors since his appointment in August 2010 and currently serves as Chair of Sterling s Governance and Nominating Committee and as a member of Sterling s Compensation Committee and Credit and Risk Committee. Mr. Biller has more than 30 years of banking and investment experience. He began Greendale Capital, a private investment company, after retiring in 2002 as vice chairman and chief operating officer of Wells Fargo & Company. Prior to Wells Fargo, Mr. Biller was president and chief operating officer of Norwest Corporation. He has also served in executive leadership roles at Bank of America and at Citicorp. Mr. Biller earned his bachelor s degree in chemical engineering from City College of New York and a master s degree in business administration from Xavier University in Cincinnati, Ohio. He serves on the boards of Ecolab, Inc., Knowledge Schools, Inc., and Knowledge Universe Education LLP. He also serves as a director of the

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Autry National Center. The qualifications of Mr. Biller considered in his appointment as a Director of Sterling included his management experience; banking experience; national recognition and relationships within the banking industry; finance experience; and Master of Business Administration degree.

**Ellen R. M. Boyer**

Ms. Boyer, 50, has served as a Director of Sterling since her appointment in December 2007 and currently serves as the Chair of Sterling's Audit Committee and as a member of Sterling's Compensation Committee. She currently holds the position of Chief Operating Officer and Chief Financial Officer at Kibble & Prentice, where she has been employed since 2002. Kibble & Prentice is an insurance and financial services company that provides a single source for property casualty insurance, employee benefits, retirement plan services, executive benefits and business continuation services. Ms. Boyer previously served as the Chief Financial Officer for several technology companies in the Pacific Northwest. Ms. Boyer has been a Certified Public Accountant since 1984 and received her Bachelor's degrees from Oregon State University in 1982. The qualifications of Ms. Boyer considered in her appointment as a Director of Sterling included her financial management experience; accounting experience; insurance and financial services experience; business operations experience; and relationships with the Puget Sound business community. The board has determined that Ms. Boyer is an audit committee financial expert as defined by the SEC.

**David A. Coulter**

Mr. Coulter, 63, has served as a Director of Sterling since his appointment in August 2010 and currently serves as a member of Sterling's Compensation Committee and Credit and Risk Committee. Mr. Coulter is a Managing Director and Senior Advisor at Warburg Pincus, LLC. He was previously Vice Chairman of J.P. Morgan Chase & Co. from December 2000 to December 2005. Prior to joining J.P. Morgan Chase, Mr. Coulter led the West Coast operations of the Beacon Group, a private investment and strategic advisory firm, and prior to that, Mr. Coulter served as the Chairman and Chief Executive Officer of the BankAmerica Corporation, where he worked from 1976 to 1999. Mr. Coulter is a member of the Board of Directors of Strayer Education, Inc., Webster Bank, Aeolus Re, and MBIA, Inc. Mr. Coulter holds a bachelor's degree in mathematics and economics and a master's degree in industrial administration, both from Carnegie Mellon University. The qualifications of Mr. Coulter considered in his appointment as a Director of Sterling included his management experience; banking experience; investment banking experience; national recognition and relationships within the banking industry; finance experience; and Master of Industrial Administration degree.

**Robert C. Donegan**

Mr. Donegan, 56, has served as a Director of Sterling since his appointment in October 2010 and currently serves as a member of Sterling's Audit Committee and Compensation Committee. Prior to joining Sterling as a Director, Mr. Donegan served as a Director of Golf Savings Bank from 2006 until Golf Savings Bank was merged with and into Sterling Savings Bank. Mr. Donegan has been President of Ivar's, Inc., one of Seattle's oldest restaurant companies with more than 60 locations, since September of 2001. From 1997-2001, Mr. Donegan served as Chief Financial Officer of Ivar's, Inc. Prior to joining Ivar's, Inc. in 1997, Mr. Donegan was Executive Vice President and Chief Financial Officer of Peet's Coffee. Mr. Donegan received his Masters Degree in Public and Private Management from the Yale School of Management. The qualifications considered in Mr. Donegan's appointment as a director of Sterling included his management experience; banking experience; relationships with the Puget Sound business community and his management degree.

**William ( Ike ) L. Eisenhart**

Mr. Eisenhart, 58, has served as a Director of Sterling since his appointment in January 2004, as Chairman of the Board of Directors from October 2009 to August 2010 and currently serves as Chair of Sterling's Compensation Committee and as a member of Sterling's Credit and Risk Committee. He serves as an independent financial consultant to privately held and publicly traded companies on investment banking matters. Previously, Mr. Eisenhart was a Managing Director at Dain Bosworth, Inc., in Seattle, Washington, a Partner in Corporate Finance for Cable Howse & Ragen in Seattle, Washington, and Vice President of Corporate Finance at Goldman, Sachs & Co. in New York City. Currently, he serves as a member of the Finance Committee of the YMCA of Greater Seattle, and is Co-Chair of the Schools Committee of the Harvard Club of Seattle. Mr. Eisenhart received a Bachelor's degree from Harvard University and a Master of Business Administration degree from the University of Chicago. The qualifications of Mr. Eisenhart considered in his appointment as a Director of Sterling included his financial management experience; investment banking experience; financial services experience; relationships with the Puget Sound business community; and Master of Business Administration degree.

**Robert H. Hartheimer**

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Mr. Hartheimer, 53, has served as a Director of Sterling since his appointment in September 2010 and currently serves as the Chair of Sterling's Credit and Risk Committee and as a member of Sterling's Governance and Nominating Committee. Mr. Hartheimer is President of Hartheimer LLC, based in Washington, D.C., which provides senior-level counsel to banks, investment firms and financial services companies on financial, regulatory, strategic and governance matters.

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From 2002 to 2008 Mr. Hartheimer was a Managing Director at Promontory Financial Group, a preeminent regulatory consulting firm. In 1991, Mr. Hartheimer joined the FDIC, where he and a small team created the Division of Resolutions to sell failed banks. He went on to serve as director of this division. Both before and after the FDIC, Mr. Hartheimer was an investment banker working with banks and financial services companies including Merrill Lynch, Smith Barney, and Friedman, Billings Ramsey. Mr. Hartheimer received a Bachelor's degree from Hamilton College and a Master's of Business Administration from The Wharton School of the University of Pennsylvania. The qualifications of Mr. Hartheimer considered in his appointment as a director of Sterling included his financial management experience; investment banking experience; financial services experience; regulatory experience; relationships within the banking industry and regulatory community and Master of Business Administration degree.

### **Scott L. Jaeckel**

Mr. Jaeckel, 39, has served as a Director of Sterling since his appointment in August 2010 and currently serves as a member of Sterling's Governance and Nominating Committee. Mr. Jaeckel is a Managing Director at THL. Prior to joining THL, Mr. Jaeckel worked at Morgan Stanley & Co. Incorporated in the Corporate Finance Department. Mr. Jaeckel brings significant finance and managerial experience to the Board that he gained from his years at THL and Morgan Stanley. In addition, due to his service as a director at several public and private companies throughout the years, he is familiar with how various boards handle a wide range of corporate and business issues. Mr. Jaeckel is currently a Director of Ceridian Corporation, MoneyGram International, Inc. and Warner Music Group Corp. Mr. Jaeckel holds a B.B.A. with distinction in Economics and Mathematics from The University of Virginia and an M.B.A. from Harvard Business School. The qualifications of Mr. Jaeckel considered in his appointment as a Director of Sterling included his management experience; finance experience; investment banking experience; and relationships within the banking industry; and Master of Business Administration degree.

### **Michael F. Reuling**

Mr. Reuling, 64, has served as a Director of Sterling since his appointment in December 2006 and currently serves a member of Sterling's Audit Committee and Governance and Nominating Committee. He has been a self-employed real estate development consultant in Boise, Idaho since retiring as Vice Chairman of Albertson's, Inc., a national supermarket/superdrugstore company, where he held various positions for 28 years. Additionally, he has been a Senior Advisor to Clarion Consulting, a real estate consulting firm based in Irvine, California, since April of 2009. Mr. Reuling received a Bachelor's degree from Carleton College in Northfield, Minnesota in 1968 and a Juris Doctorate from the University of Michigan in Ann Arbor, Michigan in 1971. The qualifications of Mr. Reuling considered in his appointment as a Director of Sterling included his management experience; real estate industry experience; relationships with the real estate community; and relationships with the Boise business community.

### **J. Gregory Seibly**

Mr. Seibly, 47, has served as a Director and Chief Executive Officer of Sterling since his appointment became effective in November 2009. His appointments as President of Sterling and as Chief Executive Officer and a Director of Sterling Savings Bank became effective in December 2009. Mr. Seibly began serving as acting President and Chief Executive Officer of Sterling and Sterling Savings Bank, subject to regulatory approval, in October 2009 and previously served as President of Sterling Savings Bank beginning in January 2009. In 2007 Mr. Seibly joined Sterling as Executive Vice President and Chief Production Officer with more than 20 years of experience in the financial industry. Before joining Sterling, Mr. Seibly was the President of U.S. Bank - California. He has also held executive-level positions in commercial banking at Wells Fargo Bank and in healthcare finance at Bank of America. Mr. Seibly currently serves on the Executive Board of the Boy Scouts of America - Inland Northwest Council and the Board of the United Way of Greater Spokane. He received his Bachelor's degree in business administration and finance from Indiana University. The qualifications of Mr. Seibly considered in his appointment as a Director of Sterling included his management experience; banking experience; relationships within banking industry; finance experience; finance degree; business degree; and relationships with the Spokane business community.

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**Table of Contents****Executive Officers**

The current management team of Sterling consists of: J. Gregory Seibly, President and Chief Executive Officer of Sterling and Sterling Savings Bank; Ezra A. Eckhardt, Chief Operating Officer of Sterling and President and Chief Operating Officer of Sterling Savings Bank; Daniel G. Byrne, Chief Financial Officer of Sterling; Donn C. Costa, Executive Vice President, Home Loan Division of Sterling Savings Bank; and David S. DePillo, Chief Credit Officer of Sterling Savings Bank. The biographical information for each executive officer, other than for Mr. Seibly, which is provided above, is included below:

**Ezra A. Eckhardt**

Mr. Eckhardt, 40, serves as Chief Operating Officer of Sterling and as President and Chief Operating Officer of Sterling Savings Bank. Mr. Eckhardt previously served as acting Chief Operating Officer of Sterling and acting President of Sterling Savings Bank, until his appointments to Sterling and Sterling Savings Bank became effective in November and December 2009, respectively. He began serving as Executive Vice President and Chief Operating Officer of Sterling Savings Bank in January 2009. He previously served as Chief Administrative Officer of Sterling Savings Bank. He joined Sterling in August 2004. Mr. Eckhardt is an adjunct professor at the Gonzaga University Graduate School of Business, a member of the Greater Spokane Incorporated Higher Education Leadership Group and a member of the Board of Directors for the Spokane affiliate of Habitat for Humanity. He is a distinguished graduate of the U.S. Military Academy at West Point. Mr. Eckhardt also has earned a Masters of Business Administration from Gonzaga University and has advanced training in applied statistics from the Rochester Institute of Technology.

**Daniel G. Byrne**

Mr. Byrne, 56, serves as Executive Vice President-Finance, Chief Financial Officer and Assistant Secretary of Sterling and Assistant Secretary of Sterling Savings Bank. He has served in these capacities with Sterling and Sterling Savings Bank, since he joined Sterling in 1983. Mr. Byrne is also the Assistant Secretary and Treasurer of INTERVEST-Mortgage Investment Company. Before joining Sterling, Mr. Byrne was employed by the accounting firm of Coopers & Lybrand in Spokane, Washington. He is a past Lieutenant Governor of Kiwanis International. Mr. Byrne is a past member of the Board of Trustees of Gonzaga Preparatory School, including its Executive Committee and its Finance Committee. He is President of the Board of Directors of Spokane Community Mental Health and past Chairman of the Parish Council of St. Thomas More Church. He is also a board member and Audit Committee Chairman for Ambassadors Group, Inc., a publicly traded corporation. He serves as a member of the American Institute of Certified Public Accountants, the Washington Society of Certified Public Accountants, the Financial Managers Society and is a past member of the American Community Bankers Association's Accounting Committee. Mr. Byrne is a certified public accountant, and received a Bachelor's degree in Accounting from Gonzaga University.

**Donn C. Costa**

Mr. Costa, 49, serves as Executive Vice President, Home Loan Division, of Sterling Savings Bank. He joined Sterling in July 2006 and served as the Executive Vice President of Golf Savings Bank until the merger of Golf Savings Bank with and into Sterling Savings Bank in July of 2010. Mr. Costa was formerly President of Lynnwood Financial Corporation, the former parent company of Golf Savings Bank, until the merger of Lynnwood Financial Corporation with and into Sterling in 2006. Mr. Costa is currently on the Seattle Mortgage Bankers Association Board of Directors and the Board of the Washington Mortgage Lenders Association. He received a Bachelor's degree in Business Administration from Washington State University.

**David S. DePillo**

Mr. DePillo, 49, was appointed as Chief Credit Officer of Sterling Savings Bank effective October 2010. Mr. DePillo has more than 25 years of financial management, banking and investment experience. He most recently served as the Vice Chairman of the Board of Fremont General Corporation and of Fremont Investment & Loan, its wholly owned bank subsidiary and served as President of both companies from 2007 to 2009. From 1999 through 2006, he served as the Vice Chairman, President and Chief Operating Officer of Commercial Capital Bancorp Inc. (CCBI) and its subsidiary companies. Prior to CCBI, Mr. DePillo served as a first Vice President and Director of multifamily banking for Home Savings of America, and as the President and Chief Operating Officer for its real estate development subsidiaries and for H.F. Ahmanson & Co., its thrift holding company.



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**USE OF PROCEEDS**

We will receive no proceeds from shares of Common Stock sold by the Selling Shareholders.

A portion of the shares of Common Stock covered by this Prospectus are issuable upon exercise of warrants issued to the Selling Shareholders. The exercise price of the warrants held by the Anchor Investors issued is \$0.22 per share. The exercise price of the warrant held by Treasury is \$0.20 per share. Upon any exercise of the warrants for cash, the Selling Shareholders will pay us the exercise price. However, the warrants also may be exercised on a cashless basis. We will not receive any cash payment from the Selling Shareholders upon any exercise of the warrants on a cashless basis. To the extent we receive proceeds from the cash exercise of the warrants, we may use such proceeds for general corporate purposes or may contribute a portion of the proceeds to Sterling Savings Bank. General corporate purposes may include the pay down of liabilities and the funding of potential acquisitions, including potential acquisitions of banks in FDIC-assisted transactions.



**Table of Contents****SELLING SHAREHOLDERS**

The table below sets forth information concerning the resale of Securities by the Selling Shareholders. The Selling Shareholders acquired Securities pursuant to the Recapitalization Transactions. We will not receive any proceeds from the resale of Securities by the Selling Shareholders. Except as discussed in footnotes 49, 62 and 63 below, the Selling Shareholders have not held any position or office or had any other material relationship with us or any of our predecessors or affiliates within the past three years.

The following table is based on information provided to us by the Selling Shareholders on or about August 18, 2010 and as of such date. Because the Selling Shareholders may sell all, some or none of the Securities, no estimate can be given as to the amount of shares that will be held by the Selling Shareholders upon termination of this offering. For purposes of the table below, we have assumed that no Securities will be held by the Selling Shareholders at such time.

Name and Address of Beneficial Owner	Beneficial Ownership Prior to the Offering			Shares Being Offered	Beneficial Ownership After the Offering		
	Number of Shares Beneficially Owned <sup>(1)</sup>	Number of Warrants Beneficially Owned <sup>(1)</sup>	Percent <sup>(2)</sup>		Number of Warrants Being Offered	Number of Shares Beneficially Owned	Percent
<b>Selling Shareholders</b>							
American Funds Insurance Series Growth Fund <sup>(3)</sup> 333 South Hope Street, 55th Floor  Los Angeles, CA 90071	80,625,000		1.976	80,625,000	0		*
Anchorage Capital Master Offshore, Ltd. <sup>(4)</sup> c/o Anchorage Advisors  610 Broadway, 6th Floor  New York, NY 10012	150,000,000		3.676	150,000,000	0		*
Andrew K. Boszharist, Jr 660 Madison Avenue, Suite 1405  New York, NY 10065	375,000		*	375,000	0		*
Bay Pond Investors (Bermuda) L.P. <sup>(5)</sup> c/o Wellington Management Company, LLP  75 State Street  Boston, MA 02109	34,218,000		*	34,218,000	0		*
Bay Pond Partners, L.P. <sup>(6)</sup> c/o Wellington Management Company, LLP  75 State Street  Boston, MA 02109	69,945,500		1.714	69,945,500	0		*
Brandytrust Multi Strategy NGA LLC <sup>(7)</sup> c/o New Generation Advisors  49 Union Street	1,842,000		*	1,842,000	0		*

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Manchester, MA 01944					
CastleRock Fund II SPC Ltd. <sup>(8)</sup>	238,150	*	238,150	0	*
101 Park Avenue, 23rd Floor					
New York, NY 10178					
CastleRock Master Fund, Ltd. <sup>(9)</sup>	10,613,600	*	10,613,600	0	*
101 Park Avenue, 23rd Floor					
New York, NY 10178					
CastleRock Partners II, L.P. <sup>(10)</sup>	2,108,750	*	2,108,750	0	*
101 Park Avenue, 23rd Floor					
New York, NY 10178					
CastleRock Partners, L.P. <sup>(11)</sup>	28,320,700	*	28,320,700	0	*
101 Park Avenue, 23rd Floor					
New York, NY 10178					
Cheetah Investment Partnership L.P. <sup>(12)</sup>	890,000	*	890,000	0	*
Schneider Capital Management					
460 E. Swedesford Rd., Suite 2000					
Wayne, PA 19087					
Crescent 1, L.P. <sup>(13)</sup>	20,000,000	*	20,000,000	0	*
c/o Cyrus Capital Partners, L.P.					
399 Park Avenue, 39th Floor					
New York, NY 10022					
CRS Fund, Ltd. <sup>(14)</sup>	21,000,000	*	21,000,000	0	*
c/o Cyrus Capital Partners, L.P.					
399 Park Avenue, 39th Floor					
New York, NY 10022					

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Name and Address of Beneficial Owner	Beneficial Ownership Prior to the Offering			Shares Being Offered	Beneficial Ownership After the Offering		
	Number of Shares Beneficially Owned <sup>(1)</sup>	Number of Warrants Beneficially Owned <sup>(1)</sup>	Percent <sup>(2)</sup>		Warrants Being Offered	Number of Shares Owned	Number of Warrants Beneficially Owned
Cyrus Opportunities Master Fund II, Ltd. <sup>(15)</sup> c/o Cyrus Capital Partners, L.P.  399 Park Avenue, 39th Floor  New York, NY 10022	49,000,000		1.201	49,000,000	0		*
Cyrus Select Opportunities Master Fund, Ltd. <sup>(16)</sup> c/o Cyrus Capital Partners, L.P.  399 Park Avenue, 39th Floor  New York, NY 10022	10,000,000		*	10,000,000	0		*
Endurance Fund <sup>(17)</sup> 4749 Nicasio Valley Road  Nicasio, CA 94946	1,125,000		*	1,125,000	0		*
Far West Capital Partners LP <sup>(18)</sup> 4749 Nicasio Valley Road  Nicasio, CA 94946	18,450,000		*	18,450,000	0		*
GAM Equity Six, Inc. <sup>(19)</sup> c/o Luxor Capital Group LP  767 5th Avenue, 19th Floor  New York, NY 10153	13,599,500		*	13,599,500	0		*
Great Oaks Strategic Investment Partners, LP <sup>(20)</sup> 660 Madison Avenue, Suite 1405  New York, NY 10065	1,250,000		*	1,250,000	0		*
Harbor Capital Group Trust <sup>(21)</sup> Schneider Capital Management  460 E. Swedesford Rd.,  Suite 2000  Wayne, PA 19087	2,300,000		*	2,300,000	0		*
Heungkuk Global Alpha Private Securities Investment Trust 2 <sup>(22)</sup> 101-1, 1Ka, Euljiro, Chung-ku  Seoul, 100-719, Korea	3,663,000		*	3,663,000	0		*
	13,837,000		*	13,837,000	0		*

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Heungkuk Global Alpha Private Securities Investment Trust 3 <sup>(23)</sup> 101-1, 1Ka, Euljiro, Chung-ku  Seoul, 100-719, Korea					
Heungkuk Global Alpha Private Securities Investment Trust 4 <sup>(24)</sup> 101-1, 1Ka, Euljiro, Chung-ku  Seoul, 100-719, Korea					
	35,000,000	*	35,000,000	0	*
HFR HE Systematic Master Trust <sup>(25)</sup> c/o CastleRock Asset Management, Inc.  101 Park Avenue, 23rd Floor  New York, NY 10178					
	6,346,650	*	6,346,650	0	*
Institutional Benchmarks Series (Master Feeder) Limited <sup>(26)</sup> c/o CastleRock Asset Management, Inc.  101 Park Avenue, 23rd Floor  New York, NY 10178					
	1,372,150	*	1,372,150	0	*
Ithan Creek Master Investment Partnership (Cayman) II, L.P. <sup>(27)</sup> c/o Wellington Management Company, LLP  75 State Street  Boston, MA 02109					
	6,541,500	*	6,541,500	0	*
Ithan Creek Master Investors (Cayman) L.P. <sup>(28)</sup> c/o Wellington Management Company, LLP  75 State Street  Boston, MA 02109					
	62,900,500	1.541	62,900,500	0	*
Jae Yon Won 15th Floor, Narakium Bldg., 1-2 Jeo-dong 1-ga, Jung-gu  Seoul, Korea					
	175,000,000	4.288	175,000,000	0	*
J&D IB Co., Ltd <sup>(29)</sup> Donghoon Tower, 12th Floor, 702-19  Yeoksam-dong, Gangnam-Gu  Seoul, Korea					
	20,000,000	*	20,000,000	0	*
Luxor Capital Partners Offshore Master Fund, LP <sup>(30)</sup> c/o Luxor Capital Group LP  767 5th Avenue, 19th Floor  New York, NY 10153					
	73,710,000	1.806	73,710,000	0	*
Luxor Capital Partners, LP <sup>(31)</sup> c/o Luxor Capital Group LP  767 5th Avenue, 19th Floor					
	51,738,500	1.268	51,738,500	0	*

New York, NY 10153

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Name and Address of Beneficial Owner	Beneficial Ownership Prior to the Offering			Shares Being Offered	Beneficial Ownership After the Offering		
	Number of Shares Beneficially Owned <sup>(1)</sup>	Number of Warrants Beneficially Owned <sup>(1)</sup>	Percent <sup>(2)</sup>		Warrants Being Offered	Number of Shares Beneficially Owned	Number of Warrants Beneficially Owned
Luxor Wavefront, LP <sup>(32)</sup>	22,577,000		*	22,577,000	0		*
c/o Luxor Capital Group LP							
767 5th Avenue, 19th Floor							
New York, NY 10153							
Malta Hedge Fund II, L.P. <sup>(33)</sup>	40,000		*	40,000	0		*
780 Third Avenue, 5th Floor							
New York, NY 10017							
Malta Hedge Fund, L.P. <sup>(34)</sup>	8,000		*	8,000	0		*
780 Third Avenue, 5th Floor							
New York, NY 10017							
Malta MLC Offshore, Ltd. <sup>(35)</sup>	10,000		*	10,000	0		*
780 Third Avenue, 5th Floor							
New York, NY 10017							
Malta Offshore, Ltd. <sup>(36)</sup>	14,000		*	14,000	0		*
780 Third Avenue, 5th Floor							
New York, NY 10017							
Malta MLC Fund, LP <sup>(37)</sup>	28,000		*	28,000	0		*
780 Third Avenue, 5th Floor							
New York, NY 10017							
Marine Western South, L.L.C. <sup>(38)</sup>	137,375,000		3.366	137,375,000	0		*
National Corporate Research, Ltd.							
615 South DuPont Highway							
Dover, DE 19901							
Marine Western, L.L.C. <sup>(39)</sup>	58,875,000		1.443	58,875,000	0		*
National Corporate Research, Ltd.							
615 South DuPont Highway							

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Dover, DE 19901					
MD Sass Maximus Partners, L.P. <sup>(40)</sup>	20,000,000	*	20,000,000	0	*
1185 Avenue of the Americas,					
18th Floor					
New York, NY 10036					
Min Joo Lee	175,000,000	4.288	175,000,000	0	*
5F, Je-il Bldg., 168-26 Samseong-1 Dong, Gangnam-Gu					
Seoul, Korea					
MW Special Situations LP <sup>(41)</sup>	535,500	*	535,500	0	*
c/o New Generation Advisors					
49 Union Street					
Manchester, MA 01944					
New Generation Limited Partnership <sup>(42)</sup>	6,352,500	*	6,352,500	0	*
c/o New Generation Advisors					
49 Union Street					
Manchester, MA 01944					
New Generation Turnaround Fund (Bermuda) LP <sup>(43)</sup>	13,682,500	*	13,682,500	0	*
c/o New Generation Advisors					
49 Union Street					
Manchester, MA 01944					
NGA Ann Arbor Partners LP <sup>(44)</sup>	87,500	*	87,500	0	*
c/o New Generation Advisors					
49 Union Street					
Manchester, MA 01944					
Paul P. Tanico	1,000,000	*	1,000,000	0	*
101 Park Avenue, 23rd Floor					
New York, NY 10178					
Post Total Return Master Fund, L.P. <sup>(45)</sup>	50,000,000	1.225	50,000,000	0	*
c/o Beach Point Capital Management LLP					
1620 26th Street, Suite 6000N					
Santa Monica, CA 90404					
RBB/Schneider Small Cap Value Fund <sup>(46)</sup>	4,100,000				