Section 1: 10-K (10-K)

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

FORM 10-K

(Mark One)

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

For the fiscal year ended December 31, 2017

OR

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

Commission File Number 001-37875

FB FINANCIAL CORPORATION
(Exact name of Registrant as specified in its Charter)

Tennessee	**62-1216058**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
211 Commerce Street, Suite 300 Nashville, Tennessee 37201	**37201**
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number, including area code: (615) 564-1212

Securities registered pursuant to Section 12(b) of the Act: Common Stock, Par Value $1.00 Per Share; Common stock traded on the New York Stock Exchange

Securities registered pursuant to Section 12(g) of the Act: **None**

Indicate by check mark if the Registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. YES ☐ NO ☒

Indicate by check mark if the Registrant is not required to file reports pursuant to Section 13 or 15(d) of the Act. YES ☐ NO ☒

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

Indicate by check mark whether the Registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the Registrant was required to submit and post such files). YES ☒ NO ☐

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

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

Large accelerated filer	☐	Accelerated filer	☒
Non-accelerated filer	☐ (Do not check if a small reporting company)	Small reporting company	☐
Emerging growth company	☒		

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. ☒

Indicate by check mark whether the Registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). YES ☐ NO ☒

As of June 30, 2017, the last business day of the Registrant's most recently completed second fiscal quarter, the aggregate market value of the Registrant's common stock held by non-affiliates of the registrant was $417.6 million, based on the closing sales price of $36.19 per share as reported on the New York Stock Exchange.

The number of shares of Registrant's Common Stock outstanding as of March 12, 2018 was 30,650,758.

Portions of the Registrant's Definitive Proxy Statement relating to the Annual Meeting of Shareholders, scheduled to be held on May 17, 2018, are incorporated by reference into Part III of this Report.

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In this Annual Report on Form 10-K (this "Annual Report"), references to "we," "our," "us," "FB Financial" or "the Company" refer to FB Financial Corporation, a Tennessee corporation, and our wholly-owned banking subsidiary, FirstBank, a Tennessee state chartered bank, unless otherwise indicated or the context otherwise requires. References to "Bank" or "FirstBank" refer to FirstBank, our wholly-owned banking subsidiary.

Cautionary note regarding forward-looking statements

Certain statements contained in this Annual Report are forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended (the "Securities Act"), and Section 21E of the Securities Exchange Act of 1934, as amended (the "Exchange Act"). These forward-looking statements include, without limitation, statements relating to our business, cash flows, condition (financial or otherwise), credit quality, financial performance, liquidity, long-term performance goals, prospects, results of operations, strategic initiatives and the timing, benefits, costs and synergies of future acquisition, disposition and other growth opportunities. These statements, which are based on certain assumptions and estimates and describe our future plans, results, strategies and expectations, can generally be identified by the use of the words and phrases "may," "will," "should," "could," "would," "goal," "plan," "potential," "estimate," "project," "believe," "intend," "anticipate," "expect," "target," "aim," "predict," "continue," "seek," "projection" and other variations of such words and phrases and similar expressions.

These forward-looking statements are not historical facts, and are based upon current expectations, estimates and projections about our industry, management's beliefs and certain assumptions made by management, many of which, by their nature, are inherently uncertain and beyond our control. The inclusion of these forward-looking statements should not be regarded as a representation by us or any other person that such expectations, estimates and projections will be achieved. Accordingly, we caution you that any such forward-looking statements are not guarantees of future performance and are subject to risks, assumptions and uncertainties that are difficult to predict and that are beyond our control. Although we believe that the expectations reflected in these forward-looking statements are reasonable as of the date of this Annual Report, actual results may prove to be materially different from the results expressed or implied by the forward-looking statements. There are or will be important factors that could cause our actual results to differ materially from those indicated in these forward-looking statements, including, but not limited to, the following:

- business and economic conditions nationally, regionally and in our target markets, particularly in Tennessee and the geographic areas in which we operate;
- the concentration of our loan portfolio in real estate loans and changes in the prices, values and sales volumes of commercial and residential real estate;
- the concentration of our business within our geographic areas of operation in Tennessee and neighboring markets;
- credit and lending risks associated with our commercial real estate, commercial and industrial, and construction portfolios;
- increased competition in the banking and mortgage banking industry, nationally, regionally and locally;
- our ability to execute our business strategy to achieve profitable growth;
- the dependence of our operating model on our ability to attract and retain experienced and talented bankers in each of our markets;
- risks that our cost of funding could increase, in the event we are unable to continue to attract stable, low-cost deposits and reduce our cost of deposits;
- our ability to increase our operating efficiency;
- failure to keep pace with technological change or difficulties when implementing new technologies;
- risks related to the recent conversion of our core operating platform;
- risks related to our acquisition, disposition, growth and other strategic opportunities and initiatives;
- negative impact on our mortgage banking services, including declines in our mortgage originations or profitability due to rising interest rates and increased competition and regulation, the Bank's or third party's failure to satisfy mortgage servicing obligations, and the possibility of the Bank being required to repurchase mortgage loans or indemnify buyers;
- our ability to attract and maintain business banking relationships with well-qualified businesses, real estate developers and investors with proven track records in our market areas;
- our ability to attract sufficient loans that meet prudent credit standards, including in our commercial and industrial and owner-occupied commercial real estate loan categories;
- failure to maintain adequate liquidity and regulatory capital and comply with evolving federal and state banking regulations;

- inability of our risk management framework to effectively mitigate credit risk, interest rate risk, liquidity risk, price risk, compliance risk, operational risk, strategic risk and reputational risk;
- failure to develop new, and grow our existing, streams of noninterest income;
- our ability to oversee the performance of third party service providers that provide material services to our business;
- our ability to maintain expenses in line with our current projections;
- our dependence on our management team and our ability to motivate and retain our management team;
- risks related to any future acquisitions, including failure to realize anticipated benefits from future acquisitions;
- inability to find acquisition candidates that will be accretive to our financial condition and results of operations;
- system failures, data security breaches (including as a result of cyber-attacks), or failures to prevent breaches of our network security;
- data processing system failures and errors;
- fraudulent and negligent acts by individuals and entities that are beyond our control;
- fluctuations in our market value and its impact in the securities held in our securities portfolio;
- the adequacy of our reserves (including allowance for loan losses) and the appropriateness of our methodology for calculating such reserves;
- the makeup of our asset mix and investments;
- our focus on small and mid-sized businesses;
- an inability to raise necessary capital to fund our growth strategy or operations, or to meet increased minimum regulatory capital levels;
- the sufficiency of our capital, including sources of such capital and the extent to which capital may be used or required;
- interest rate shifts and its impact on our financial condition and results of operation;
- the expenses that we will incur to operate as a public company and our inexperience complying with the requirements of being a public company;
- the institution and outcome of litigation and other legal proceeding against us or to which we become subject;
- changes in accounting standards;
- the impact of recent and future legislative and regulatory changes, including, without limitation, the Tax Cuts and Jobs Act of 2017;
- governmental monetary and fiscal policies;
- changes in the scope and cost of Federal Deposit Insurance Corporation, or FDIC, insurance and other coverage; and
- future equity issuances under our 2016 Incentive Plan and our Employee Stock Purchase Plan and future sales of our common stock by us, our controlling shareholder or our executive officers or directors.

The foregoing factors should not be construed as exhaustive and should be read in conjunction with the sections entitled “Risk factors” and “Management’s discussion and analysis of financial condition and results of operations” included in this Annual Report. If one or more events related to these or other risks or uncertainties materialize, or if our underlying assumptions prove to be incorrect, actual results may differ materially from our forward-looking statements. Accordingly, you should not place undue reliance on any such forward-looking statements. Any forward-looking statement speaks only as of the date of this Annual Report, and we do not undertake any obligation to publicly update or review any forward-looking statement, whether as a result of new information, future developments or otherwise, except as required by law. New risks and uncertainties may emerge from time to time, and it is not possible for us to predict their occurrence or how they will affect us.

PART I

ITEM - 1. Business

Overview

FB Financial Corporation is a bank holding company, headquartered in Nashville, Tennessee. Our wholly-owned bank subsidiary, FirstBank, is the third largest Tennessee-headquartered bank, based on total assets. FirstBank provides a comprehensive suite of commercial and consumer banking services to clients in select markets primarily in Tennessee, North Alabama and North Georgia. Our footprint includes 56 full-service bank branches and 9 other banking locations serving the metropolitan markets of Nashville, Chattanooga, Knoxville, Memphis, Jackson and Huntsville (AL) in addition to 12 community markets. FirstBank also provides mortgage banking services utilizing its bank branch network and mortgage banking offices strategically located throughout the southeastern United States in addition to its national internet delivery channel. As of December 31, 2017, we had total assets of $4.73 billion, loans held for investment of $3.17 billion, total deposits of $3.66 billion, and total shareholders' equity of $596.7 million.

Throughout our history, we have steadfastly maintained a community banking approach of personalized relationship-based service. As we have grown, maintaining this relationship-based approach utilizing local, talented and experienced bankers in each market has been an integral component of our success. Our bankers utilize their local knowledge and relationships to deliver timely solutions to our clients. We empower these bankers by giving them local decision making authority supplemented by appropriate risk oversight. In our experience, business owners and operators prefer to deal with decision makers, and our banking model is built to place the decision maker as close to the client as possible. We have designed our operations, technology, and centralized risk oversight processes to specifically support our operating model. We deploy this operating model universally in each of our markets, regardless of size. We believe we have a competitive advantage in our markets versus both smaller community banks and larger regional and national banks. Our robust offering of products, services and capabilities differentiate us from community banks and our significant local market knowledge, client service level and the speed with which we are able to make decisions and deliver our services to customers differentiate us from larger regional and national banks.

We seek to leverage our operating model by focusing on profitable growth opportunities across our footprint, focused primarily on both high-growth metropolitan markets and stable and growing community markets. As a result, we are able to strategically deploy our capital across our markets to take advantage of those opportunities that we believe provide the greatest certainty of profitable growth and the highest returns.

Our operating model is executed by a talented management team lead by our Chief Executive Officer, Christopher T. Holmes. Mr. Holmes, a 26-year banking veteran originally from Lexington, Tennessee, joined the Bank in 2010 as Chief Banking Officer and was elected Chief Executive Officer in 2013. Mr. Holmes has an extensive background in both metropolitan and community banking gained from his time at community banks and larger public financial institutions. Mr. Holmes has assembled a highly effective management team, blending members that have a long history with FirstBank and members that have significant banking experience at other in-market banks.

Our history

Originally chartered in 1906, we are one of the longest continually operating banks in Tennessee. While our deep community roots go back over 100 years, our growth trajectory changed in 1984 when Tennessee businessman James W. Ayers, our Executive Chairman and controlling shareholder, acquired Farmers State Bank with an associate. In 1988, we purchased the assets of First National Bank of Lexington, Tennessee and changed our name to FirstBank, forming the foundation of our current franchise. In 1990, Mr. Ayers became our sole shareholder and remained our sole shareholder until our initial public offering in September 2016. Under Mr. Ayers' ownership, we grew from a community bank with only $14 million in assets in 1984 to the third largest bank headquartered in Tennessee, based on total assets.

From 1984 to 2001, we operated as a community bank growing organically and through small acquisitions in community markets in West Tennessee. In 2001, our strategy evolved from serving purely community markets to include a modest presence in metropolitan markets, expanding our reach and enhancing our growth. We entered Nashville and Memphis in 2001 by opening a branch in each of those markets. In 2004 and 2008, we opened our first branches in Knoxville and Chattanooga, respectively. Although we experienced some growth in each metropolitan market, it did not become a major strategic focus until we implemented our current metropolitan growth strategy in the Nashville metropolitan statistical area ("MSA") in 2012. Additionally, we expanded into the Huntsville, Alabama MSA in 2014 by opening a branch in Huntsville and loan production office in Florence, Alabama. The successful implementation of this strategy has resulted in 155% deposit growth in the Nashville MSA from June 30, 2012 to June 30, 2017, making it our largest market with 29% of our loans held for investment and 23% of our total deposits, as of December 31, 2017. As a result of this evolution and recent acquisitions discussed above, we now operate a balanced business model that serves a diverse customer base in both metropolitan and community markets.

Recent acquisitions

On September 18, 2015, we completed the acquisition of Northwest Georgia Bank ("NWGB"), a 110-year old institution with six branches, serving clients in the Chattanooga MSA. We acquired net assets with a fair value of $272 million which included a bargain purchase gain of $2.8 million, loans with a fair value of $79 million and deposits with a fair value of $246 million. This acquisition accelerated our already planned expansion in Chattanooga by significantly augmenting our client base, increasing our brand awareness and providing us with the scale to attract leading bankers to further enhance our market penetration and profitable growth.

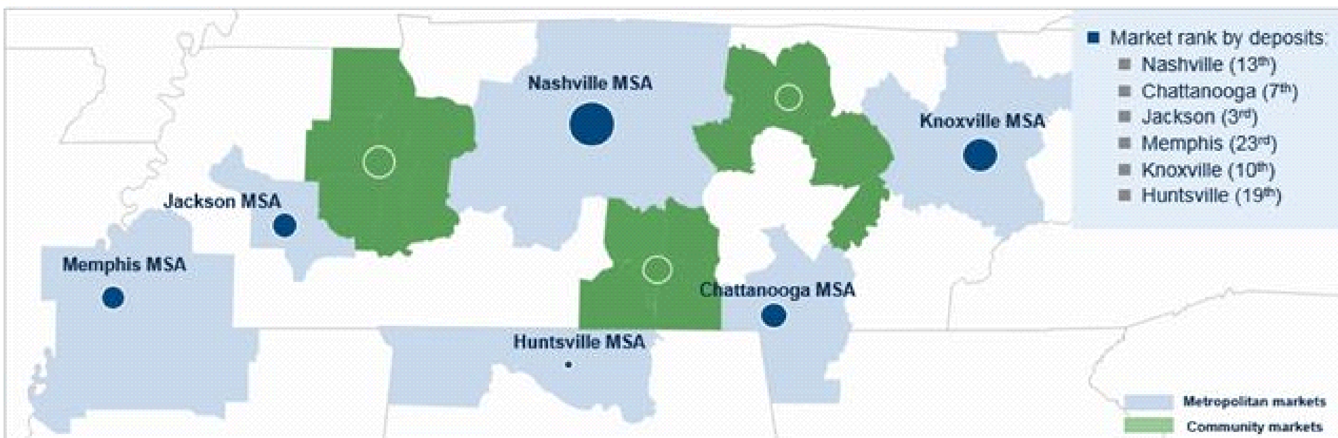
On July 31, 2017, the Bank completed its merger with Clayton Bank and Trust ("CBT") and American City Bank ("ACB" and together with CBT, the "Clayton Banks"), pursuant to the Stock Purchase Agreement with Clayton HC, Inc., a Tennessee corporation ("Seller"), and James L. Clayton, the majority shareholder of Seller, dated February 8, 2017, as amended on May 26, 2017, with a purchase price of approximately $236.5 million. The Company issued 1,521,200 shares of common stock and paid cash of $184.2 million to purchase all of the outstanding shares of the Clayton Banks. At closing, the Clayton Banks merged with and into FirstBank, with FirstBank continuing as the surviving banking entity. As of July 31, 2017, the estimated fair value of loans acquired and deposits assumed as a result of the merger was $1,059.7 million and $979.5 million, respectively.

See Note 2, "Mergers and acquisitions" in the Notes to the consolidated financial statements for additional details regarding these transactions.

Our markets

Our market footprint is the southeastern United States, centered around Tennessee, and includes portions of North Alabama and North Georgia.

Our current footprint[1]



Top metropolitan markets

Market	Market Rank	Branches (#)	Deposits ($mm)	Deposit market share	Percent of total deposits
Nashville	13	14	1,085	1.9%	28.5%
Knoxville	10	5	414	2.5%	10.9%
Jackson	3	7	343	15.4%	9.0%
Chattanooga	7	6	336	3.5%	8.8%
Memphis	23	4	220	0.7%	5.8%
Huntsville	19	1	44	0.6%	1.2%

Top community markets[1]

Market	Market Rank	Branches (#)	Deposits ($mm)	Deposit market share	Percent of total deposits
Lexington	1	6	329	58.3%	8.7%
Tullahoma	1	3	183	17.8%	4.8%
Huntingdon	2	5	122	23.5%	3.2%
Paris	3	2	102	17.5%	2.7%
Camden	2	2	100	22.8%	2.6%
Smithville	3	1	96	24.3%	2.5%

Note: Financial data as of December 31, 2017. Market data as of June 30, 2017. Size of bubble represents size of company deposits in a given market
Source: Company data and S&P Global Market Intelligence; Branch numbers adjusted for branch closures since June 30, 2017; [1] Statistics based on county data.

Our core client profile across our footprint includes small businesses, corporate clients, commercial real estate owners and consumers. We target business clients with substantial operating history that have annual revenues of up to $250 million. Our typical business client would keep business deposit accounts with us, and we would look to provide banking services to the owners and employees of the business as well. We also have an active consumer lending business that includes deposit products, mortgages, home equity lines and small consumer finance loans. We continuously strive to build deeper relationships by actively cross-selling incremental products to meet the banking needs of our clients.

The following tables show our deposit market share ranking among all banks and community banks (which we define as banks with less than $25 billion in assets) in Tennessee as of June 30, 2017 (the most recent date where such information is publicly available). Of the 10 largest banks in the state based on total deposits, 6 are national or regional banks, which we believe provides us with significant opportunities to gain market share from these banks.

Top 10 Banks in Tennessee:

Rank	Company name	Headquarters	Branches (#)	Total deposits ($bn)	Deposit market share (%)
1	First Horizon National Corp. (TN)	Memphis, TN	199	22.9	15.5
2	Regions Financial Corp. (AL)	Birmingham, AL	221	18.7	12.6
3	SunTrust Banks Inc. (GA)	Atlanta, GA	122	13.7	9.3
4	Bank of America Corp. (NC)	Charlotte, NC	58	11.5	7.8
5	Pinnacle Financial Partners (TN)	Nashville, TN	47	9.7	6.6
6	**FB Financial Corp (TN)**	**Nashville, TN**	**56**	**3.6**	**2.4**
7	U.S. Bancorp (MN)	Minneapolis, MN	103	3.2	2.2
8	Franklin Financial Network, Inc. (TN)	Franklin, TN	14	2.9	2.0
9	BB&T Corp. (NC)	Winston-Salem, NC	46	2.7	1.8
10	Wilson Bank Holding Co. (TN)	Lebanon, TN	27	2.0	1.4

Top 10 banks under $25bn assets in Tennessee:

Rank	Company name	Headquarters	Branches (#)	Total deposits ($bn)	Deposit market share (%)
1	Pinnacle Financial Partners (TN)	Nashville, TN	47	9.7	6.6
2	**FB Financial Corp (TN)**	**Nashville, TN**	**56**	**3.6**	**2.4**
3	Franklin Financial Network, Inc. (TN)	Franklin, TN	14	2.9	2.0
4	Wilson Bank Holding Co. (TN)	Lebanon, TN	27	2.0	1.4
5	Simmons First National Corp. (AR)	Pine Bluff, AR	45	2.0	1.4
6	Home Federal Bank of Tennessee (TN)	Knoxville, TN	23	1.7	1.2
7	Renasant Corp. (MS)	Tupelo, MS	19	1.5	1.0
8	First Citizens Bancshares Inc. (TN)	Dyersburg, TN	24	1.3	0.9
9	Reliant Bancorp, Inc. (TN)	Brentwood, TN	15	1.3	0.9
10	BancorpSouth, Inc. (MS)	Tupelo, MS	27	1.3	0.9

Source: SNL Financial and Company reports as of June 30, 2017; total assets as of December 31, 2017, adjusted for acquisitions as of March 7, 2018.

Our six metropolitan markets.

We currently operate in the six metropolitan markets listed below.

Nashville is the largest MSA in Tennessee, our largest market and one of the fastest growing cities in the U.S. Nashville has experienced 14.7% population growth from 2010 to 2018, and its population is expected to grow by an additional 6.9% by 2023 according to S&P Global Market Intelligence.

Memphis is the 2nd largest MSA in Tennessee. It has a diversified business base and the busiest cargo airport in North America. Memphis is headquarters to three Fortune 500 companies, AutoZone, International Paper and FedEx, which together employs over 30,000 people in Memphis.

Knoxville is the 3rd largest MSA in Tennessee. It is home to the University of Tennessee system's flagship campus, and employs over 30,000 healthcare professionals. Our recent acquisition of the Clayton Banks has helped strengthen our presence in the attractive Knoxville MSA.

Chattanooga is the 4th largest MSA in Tennessee. It has a diverse economy with over 20,000 businesses that employ over 260,000 people and generate an estimated $45 billion in annual sales. Chattanooga has experienced population growth of 5.5% between 2010 and 2018 and is expected to experience 4% population growth by 2023 according to S&P Global Market Intelligence.

Jackson is the 6th largest MSA in Tennessee and is the 2nd largest city in West Tennessee following Memphis. Jackson has developed into a leading industrial and distribution center in the state of Tennessee, with particular strength in manufacturing.

Huntsville is the 2nd largest MSA in Alabama and has one of the strongest technology and engineering economies in the nation, with the highest concentration of engineers in the nation and the 6th largest county by military spending in the country.

Our community markets.

We are a leading bank in many of the Tennessee community markets that we serve. These community markets continue to offer us opportunities to profitably grow our market share. The table below shows our presence, as of June 30, 2017, in the six community markets where we have the largest amount of deposits. In total, we have over $1.2 billion in deposits in our community markets.

Top FirstBank community markets

Market	FB market rank	FB branches (#)	FB deposits ($mm)	FB deposit market share	Percent of total FB deposits
Lexington	1	6	329	58.3%	8.7%
Tullahoma	1	3	183	17.8%	4.8%
Huntingdon	2	5	122	23.5%	3.2%
Paris	3	2	102	17.5%	2.7%
Camden	2	2	100	22.8%	2.6%
Smithville	3	1	96	24.3%	2.5%

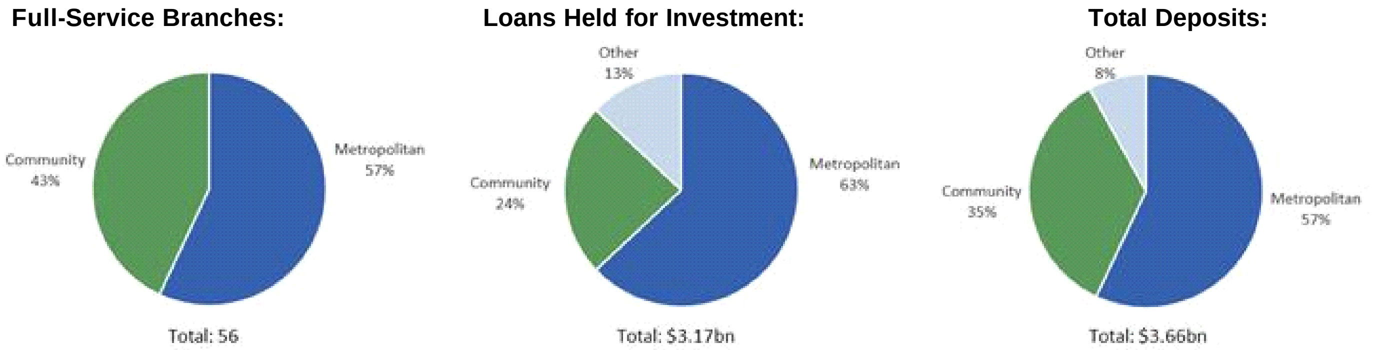
Note: Market data sourced from S&P Global Market Intelligence as of June 30, 2017. Statistics based on county data.

Market characteristics and mix.

Metropolitan markets. Our metropolitan markets are characterized by attractive demographics and strong economies and offer substantial opportunity for future growth. We compete in these markets with national and regional banks that currently have the largest market share positions and with community banks primarily focused only on a particular geographic area or business niche. We believe we are well positioned to grow our market penetration among our target clients of small to medium sized businesses and the consumer base working and living in these metropolitan markets. In our experience, such clients demand the product sophistication of a larger bank, but prefer the customer service, relationship focus and local connectivity of a community bank. We believe that our size, product suite and operating model offer us a competitive advantage in these markets versus our smaller competitors, many of which are focused only on specific counties or industries. Our operating model driven by local talent with strong community ties and local authority serves as a key competitive advantage over our larger competitors. We believe that, as a result, we are well positioned to leverage our existing franchise to expand our market share in our metropolitan markets.

Community markets. Our community markets tend to be more stable throughout various economic cycles, with primarily retail and small business customer opportunities and more limited competition. We believe this leads to an attractive profitability profile and smaller ticket, more granular loan and deposit portfolios. Our community markets are standalone markets and not suburbs of larger markets. We primarily compete in these markets with community banks that have less than $1 billion in total assets. Our strategy is to compete against these smaller community banks by providing a broader and more sophisticated set of products and capabilities while still maintaining our local service model. We believe these markets are being deemphasized by national and regional banks which provides us with opportunities to hire talented bankers in these communities and gain market share in these community markets.

Market mix. The charts below show our branch, loan and deposit mix between our metropolitan and community markets as of December 31, 2017.



Our competitive strengths

We believe the following strengths provide us with competitive advantages over other banks in our markets and provide us with the necessary foundation to successfully execute our growth strategies.

Depth and experience of senior management team. We have a deep and experienced senior management team led by our chief executive officer, Christopher Holmes, and chief financial officer, James Gordon. The team, as evidenced by the leaders of our Banking and Mortgage Segments, combines long histories at FirstBank with significant market and industry knowledge gained from employment with other successful banks.

In addition to our senior management team, our market leaders have an average tenure of more than 11 years with us. We believe that we also have depth in our overall management in lending, credit administration, finance, operations and information technology.

Strong growth coupled with profitability. We have delivered attractive growth and returns since the implementation of our strategic plan designed to leverage our competitive advantages in both metropolitan and community markets in 2012. Our execution of the plan has delivered strong growth, primarily from our Nashville metropolitan strategy and mortgage expansion, coupled with positive returns from our legacy community markets.

Ability to recruit and retain talented people. The success of our operating model, which depends on local knowledge and decision making, is directly related to our ability to attract and retain talented bankers in each of our markets. We strive to attract and retain these bankers by fostering an entrepreneurial environment, empowering them with local authority and providing them with sufficient infrastructure and resources to support their growth while also providing management with appropriate oversight. We believe that our family culture built around respect, teamwork and empowerment makes us attractive for talented bankers and associates across our geographic footprint. We pride ourselves on being a great place to work, which is evidenced by our recognition as a Top Workplace for 2017 by The Tennessean, Nashville's principal newspaper. In the Nashville market alone, we have added 22 new bankers since 2012, including the current President of our Middle and East Tennessee region, Allen Oakley, a 35-year banking veteran.

Scalable, decentralized operating model. We operate each of our markets as individual markets, with an experienced market leader in charge of each market. Each of our market leaders and bankers is empowered to make local decisions up to specified limits approved by the Bank's board of directors and our senior management team based on experience and track record. We believe that the delivery by our bankers of in-market client decisions, coupled with strong, centralized risk and credit support, allows us to best serve our clients. This operating model has been proven successful in our existing markets, and we believe it is highly replicable and scalable. We have a robust infrastructure bolstered by our conversion to a new core processing system in the second quarter of 2016 that can support our model as we grow in existing and new markets either organically or through opportunistic acquisitions.

Disciplined and deliberate risk management. Risk management is a cornerstone of our culture and is emphasized throughout every area of the organization. Our decentralized operating model is balanced by individual lending authorities based on demonstrated experience and expertise. Larger credit decisions involve credit officers and/or senior management. We have invested in technology to monitor compliance of credits with our policies. We strive for a balanced loan portfolio taking into consideration borrower and industry concentrations. Our risk management strategy also includes rigorous systems and processes to monitor liquidity, interest rate, operations and compliance risk.

Proven acquirer. We have a strong record of adding value through acquisitions and have completed nine bank and three mortgage related acquisitions under our current ownership. Our key operational associates have integration experience with FirstBank and other institutions. We are a disciplined acquirer focused on opportunities that meet our internal return targets, maintain or enhance our earnings per share and add to our strong core deposit franchise. Our long-term personal relationships with many of the bank owners and CEOs in our markets lead to a natural dialogue when they choose to explore a sale of their company. Additionally, we believe that our size and ability to operate effectively in both community and metropolitan markets make us an attractive option to smaller banks seeking an acquirer.

Our business strategy

Our overall business strategy is comprised of the following core strategies.

Enhance market penetration in metropolitan markets. In recent years, we have successfully grown our franchise in the Nashville MSA by executing our metropolitan growth strategy. The strategy is centered on the following: recruiting the best bankers and empowering them with local authority; developing branch density; building brand awareness and growing our business and consumer banking presence; and expanding our product offering and capabilities. These strategies coupled with our personalized, relationship-based client service have contributed significantly to our success. Additionally, we believe that our scale, resources and sophisticated range of products provides us with a competitive advantage over the smaller community banks in the Nashville MSA and our other MSAs. As a result of these competitive advantages and growth strategies, the Nashville MSA has become our largest market. With approximately a 1.9% market share, based on deposits as of June 30, 2017, we are still in the early stage of executing our Nashville growth strategy and intend to continue to efficiently increase our market penetration.

Based on market and competitive similarities, we believe our growth strategies are transferable to our other metropolitan markets. We implemented these strategies with an initial focus on the Chattanooga MSA. Our acquisition of Northwest Georgia Bank has accelerated our growth and profitability in Chattanooga and, our acquisition of the Clayton Banks has begun to show the same results on a larger scale in the Knoxville MSA.

Pursue opportunistic acquisitions. While most of our growth has been organic, we have completed nine acquisitions under our current ownership, including our recent acquisition of the Clayton Banks. We pursue acquisition opportunities that meet our internal return targets, maintain or enhance our earnings per share, enhance market penetration, and possess strong core deposits. We believe that numerous small to mid-sized banks or branch networks will be available for acquisition in metropolitan and community markets throughout Tennessee as well as in attractive contiguous markets in the coming years due to industry trends, such as scale and operational challenges, regulatory pressure, management succession issues and shareholder liquidity needs. In Tennessee alone, there are approximately 130 banks with total assets of less than $1 billion, and in the contiguous states of Alabama, Georgia, North Carolina, South Carolina and Virginia, there are over 500 banks under $1 billion in assets. We believe that we are positioned as a natural consolidator because of our financial strength, reputation and operating model.

Improve efficiency by leveraging technology and consolidating operations. We have invested significantly in our bankers, infrastructure and technology in recent years, including our conversion to a new core processing system in the second quarter of 2016, which we believe has created a scalable platform that will support future growth across all of our markets. Our bankers and branches, especially in the Nashville MSA, continue to scale in size, and we believe there is capacity to grow our business without adding significantly to our branch network. We plan to continue to invest, as needed, in our technology and business infrastructure to support our future growth and increase operating efficiencies. We intend to leverage these investments to consolidate and centralize our operations and support functions while protecting our decentralized client service model.

Seize opportunities to expand noninterest income. While our primary focus is on capturing opportunities in our core banking business, we have successfully seized opportunities to grow our noninterest income by providing our people with the flexibility to take advantage of market opportunities. As part of our strategic focus to grow our noninterest income, we have significantly expanded our mortgage business by hiring experienced loan officers, implementing our Consumer Direct internet delivery channel in 2014 along with expanding our third party origination business via our correspondent channel in 2016. This has allowed us to continue offering our mortgage clients the personalized attention that is the cornerstone of our Bank. We have also successfully expanded our fee-based businesses to include more robust treasury management, trust and investment services. We intend to continue emphasizing these business lines, which we believe will serve as strong customer acquisition channels and provide us with a range of cross-selling opportunities, while making our business stronger and more profitable.

Products and Services

We operate our business in two business segments: Banking and Mortgage. See Note 21, “Segment Reporting,” in the notes to our consolidated financial statements for a description of these business segments.

Banking services

While we operate through two segments, Banking and Mortgage, Banking has been, and is, the cornerstone of our operations and underlying philosophy since our beginnings in 1906. As the third largest Tennessee headquartered bank, we are dedicated to serving the banking needs of businesses, professionals and individuals in our metropolitan and community markets through our community banking approach of personalized, relationship-based service. We strive to become trusted advisers to our clients and achieve long-term relationships. We deliver a wide range of banking products and services tailored to meet the needs of our clients across our footprint.

Lending activities

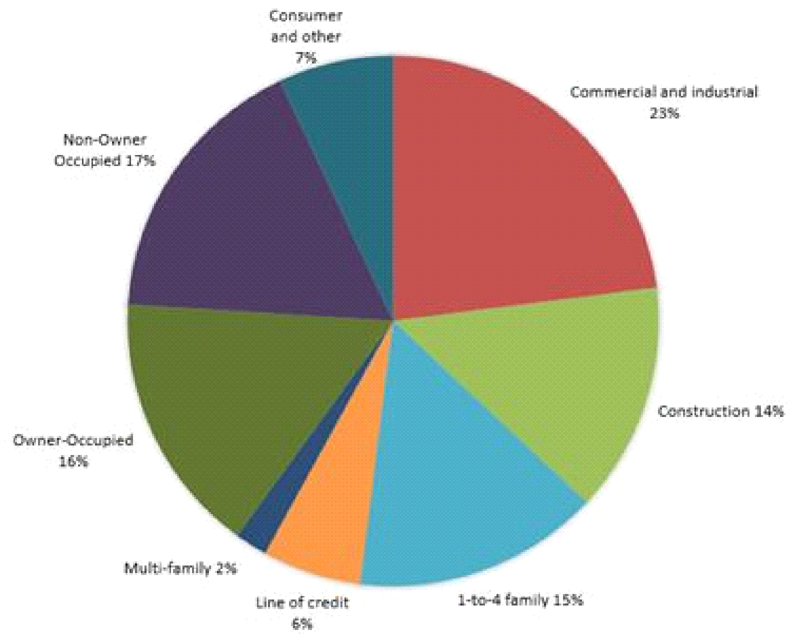
Through the Bank, we offer a broad range of lending products to our targeted clients, which includes businesses with up to $250 million in annual revenues, business owners, real estate investors and consumers. Our commercial lending products include working capital lines of credit, equipment loans, owner-occupied and non-owner-occupied real estate construction loans, “mini-perm” real estate term loans, and cash flow loans to a diversified mix of clients, including small and medium sized businesses. Our consumer lending products include first and second residential mortgage loans, home equity lines of credit and consumer installment loans to purchase cars, boats and other recreational vehicles. At December 31, 2017, we had loans held for investment of $3.17 billion. Throughout the following discussion of our banking services, we present our loan information as loans excluding loans held for sale.

Lending strategy

Our strategy is to grow our loan portfolio by originating commercial and consumer loans that produce revenues consistent with our financial objectives. Through our operating model and strategies, we seek to be the leading provider of lending products and services in our market areas to our clients. We market our lending products and services to our clients through our personalized service. As a general practice, we originate substantially all of our loans, but we occasionally participate in syndications, limiting participations to loans originated by lead banks with which we have a close relationship and which share our credit philosophies.

We also actively pursue and maintain a balanced loan portfolio by type, size and location. Our loans are generally secured and supported by personal guarantees.

Loan portfolio mix as of December 31, 2017



Commercial and industrial loans. Our commercial and industrial loans are typically made to small- and medium-sized manufacturing, wholesale, retail and service businesses for working capital and operational needs and business expansions, including the purchase of capital equipment. Commercial and industrial loans generally include lines of credit and loans with maturities of five years or less. Because we are a community bank with long standing ties to the businesses and professionals operating in our market areas, we are able to tailor our commercial and industrial loan programs to meet the needs of our clients. We target high-quality businesses in our markets with a proven track record and up to $250 million in annual revenues. As of December 31, 2017, we had outstanding commercial and industrial loans, of $715.1 million, or 23% of our loan portfolio. Growing our commercial and industrial loan portfolio is an important area of emphasis for us, and we intend to continue to grow this portfolio.

Commercial and industrial loans are generally made with operating cash flows as the primary source of repayment, but may also include collateralization by inventory, accounts receivable, equipment and personal guarantees. As a result, the repayment risk is subject to the ongoing business operations of the borrower. Any interruption or discontinuance of operating cash flows from the business, which may be influenced by events not under the control of the borrower such as economic events and changes in governmental regulations, could materially affect the ability of the borrower to repay the loan. Further, commercial and industrial loans may be secured by the collateral described above, which if the business is unsuccessful, typically have values insufficient to satisfy the loan without a loss.

Commercial real estate loans. Our commercial real estate loans consist of both owner-occupied and non-owner occupied commercial real estate loans. The total amount of commercial real estate loans outstanding as of December 31, 2017 was $1,047.5 million, or 33% of our loan portfolio. The real estate securing our existing commercial real estate loans includes a wide variety of property types, such as offices, warehouses, production facilities, health care facilities, hotels, mixed-use residential/commercial, retail centers, restaurants, churches, assisted living facilities and agricultural based facilities. As of December 31, 2017, $495.9 million of our commercial real estate loan portfolio, or 16% of our loan portfolio, was owner-occupied commercial real estate loans, and $551.6 million of our commercial real estate loan portfolio, or 17% of our loan portfolio, was non-owner occupied commercial real estate loans. We are primarily focused on growing the owner-occupied portion of our commercial real estate loan portfolio.

With respect to our owner-occupied commercial real estate loans, we target local companies with a proven operating history that tend to be business-operators and professionals within our markets. Owner-occupied real estate loans are typically repaid through the ongoing business operations of the borrower, and hence are dependent on the success of the underlying business for repayment and are more exposed to general economic conditions.

With respect to our non-owner occupied commercial real estate loans, we target experienced, local real estate developers and investors with whom our bankers have long-standing relationships. Our non-owner occupied commercial real estate loans also tend to involve retail, hotel, office, warehouse, industrial, healthcare, assisted living and mix-used properties. Non-owner occupied real estate loans are typically repaid with the funds received from the sale of the completed property or rental proceeds from such property, and are therefore more sensitive to adverse conditions in the real estate market, which can also be affected by general economic conditions.

Commercial real estate loans are often larger and involve greater risks than other types of lending. Adverse developments affecting commercial real estate values in our market areas could increase the credit risk associated with these loans, impair the value of property pledged as collateral for these loans, and affect our ability to sell the collateral upon foreclosure without a loss. Furthermore, adverse developments affecting the business operations of the borrowers of our owner-occupied commercial real estate loans could significantly increase the credit risk associated with these loans. Due to the larger average size of commercial real estate loans, we face the risk that losses incurred on a small number of commercial real estate loans could have a material adverse impact on our financial condition and results of operations.

Residential real estate loans. Our residential real estate loans consist of 1-4 family loans, home equity loans and multi-family loans. The residential real estate loans described below exclude mortgage loans that are held for sale. As of December 31, 2017, the total amount of residential real estate loans outstanding was $738.3 million, or 23% of our loan portfolio.

Our 1-4 family mortgage loans are primarily made with respect to and secured by single family homes, which are both owner-occupied and investor owned. We seek to make our 1-4 family mortgage loans to well-qualified homeowners and investors with a proven track record that satisfy our credit and underwriting standards. As of December 31, 2017, our 1-4 family mortgage loans comprised $481.0 million, or 15%, of loans.

Our home equity loans are primarily revolving, open-end lines of credit secured by 1-4 family residential properties. We seek to make our home equity loans to well-qualified borrowers that satisfy our credit and underwriting standards. Our home equity loans as of December 31, 2017 comprised $195.0 million, or 6%, of loans.

Our multi-family residential loans are primarily secured by multi-family properties, primarily apartment and condominium buildings. We seek to make multi-family residential loans to experienced real estate investors with a proven track record. These loans are primarily repaid from the rental payments generated by the multifamily properties. Our multifamily loans as of December 31, 2017 comprised $62.4 million, or 2% of loans.

We expect to continue to make residential real estate mortgage loans at a similar pace so long as housing values in our markets do not deteriorate from current prevailing levels and we are able to make such loans consistent with our current credit and underwriting standards. Like our commercial real estate loans, our residential real estate loans are secured by real estate, the value of which may fluctuate significantly over a short period of time as a result of market conditions in the area in which the real estate is located. Adverse developments affecting real estate values in our market areas could therefore increase the credit risk associated with these loans, impair the value of property pledged as collateral on loans and affect our ability to sell the collateral upon foreclosure without a loss or additional losses. We primarily make our residential real estate loans to qualified individuals and investors in accordance with our real estate lending policies, which detail maximum loan to value ratios and maturities and, as a result, the repayment of these loans are also affected by adverse personal circumstances.

Construction loans. Our construction real estate loans include commercial construction, land acquisition and land development loans and single-family interim construction loans to small- and medium-sized businesses and individuals. We target experienced local developers primarily focused on multifamily, hospitality, commercial building, retail and warehouse developments. These loans typically are disbursed as construction progresses and carry variable interest rates for commercial loans and fixed rates for consumer loans. As of December 31, 2017, the outstanding balance of our construction loans was $448.3 million, or 14% of our loan portfolio. We expect to continue to make construction loans at a similar pace so long as demand continues and the market for and values of such properties remain stable or continue to improve in our markets.

Construction loans carry a high risk because repayment of these loans is dependent, in part, on the success of the ultimate project or, to a lesser extent, the ability of the borrower to refinance the loan or sell the property upon completion of the project, rather than the ability of the borrower or guarantor to repay principal and interest. Moreover, these loans are typically based on future estimates of value and economic circumstances, which may differ from actual results or be affected by unforeseen events. If the actual circumstances differ from the estimates made at the time of approval of these loans, we face the risk of having inadequate security for the repayment of the loan. Further, these loans are typically secured by the underlying development and, even if we foreclose on the loan, we may be required to fund additional amounts to complete the project and may have to hold the property for an unspecified period of time while we attempt to dispose of it.

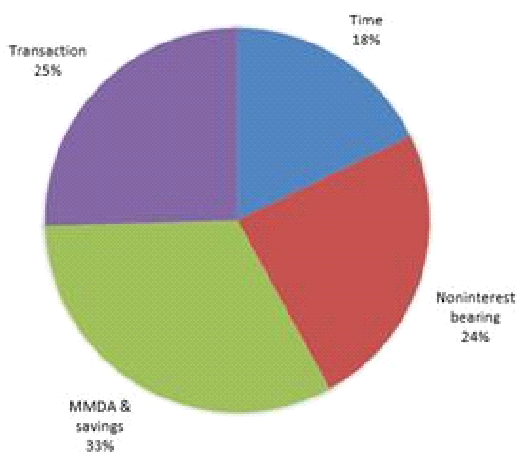
Consumer and other loans. We offer a variety of consumer loans, such as installment loans to individuals for personal, family and household purposes, including car, boat and other recreational vehicle loans and personal lines of credit. Our consumer loans typically are part of an overall client relationship designed to support the individual consumer borrowing needs of our commercial loan and deposit clients, and are well diversified across our markets. As of December 31, 2017, we had outstanding $217.7 million of consumer and other loans, excluding residential real estate loans, representing 7% of our loan portfolio. Consumer loans typically have shorter terms, lower balances, higher yields and higher risks of default than residential real estate mortgage loans. The repayment of consumer loans is dependent on the borrower's continuing financial stability and are therefore more likely to be affected by adverse personal circumstances, such as the loss of employment, unexpected medical costs or divorce. These loans are often secured by the underlying personal property, which typically has insufficient value to satisfy the loan without a loss due to damage to the collateral and general depreciation.

Deposits and other banking services

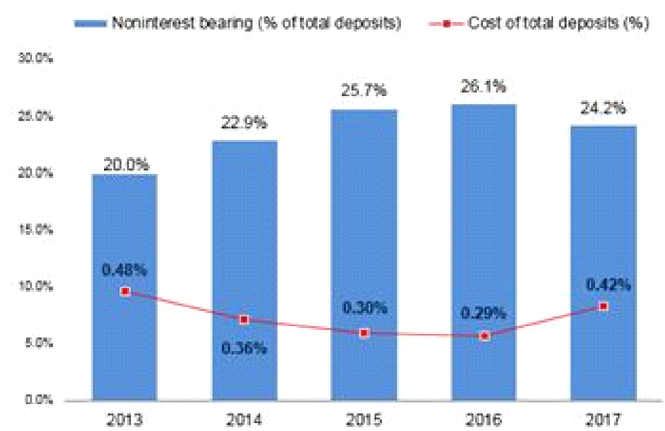
We offer a full range of transaction and interest bearing depository products and services to meet the demands of each segment within our client base. Our target segments include consumer, small business, and corporate entities. We solicit deposits from these target segments through our local bankers, sophisticated product offering and our brand-awareness initiatives, such as our community focused marketing and high-visibility branch locations. We offer demand, negotiable order of withdrawal, money market, certificates of deposit, municipal and savings accounts. To complement our account offerings, we also have in place technology to support electronic banking activities, including consumer online banking and mobile banking. In addition to these electronic banking activities, we make deposit services accessible to our clients by offering direct deposit, wire transfer, night depository, banking-by-mail and remote capture for non-cash items. Our commercial clients are served by a well-developed cash management technology platform.

The following charts show our deposit composition as of December 31, 2017, as well as the growth of our noninterest bearing deposits as a percentage of total deposits and the resulting improvement in our cost of deposits since 2013.

Deposit mix as of December 31, 2017



Noninterest bearing deposit and cost of deposits



The growth of low-cost deposits is an important aspect of our strategic plan, and we believe it is a significant driver of our value. The primary driver of our noninterest bearing deposit growth has been our ability to acquire new commercial clients. This has resulted from the addition of relationship bankers in our Nashville market, improved technology in the cash management area, and the addition of experienced cash management sales and operational specialists. Our cash management product offering includes a well-developed online banking platform complimented by a host of ancillary services including lockbox remittance processing, remote check deposit capture, remote cash capture, fraud protection services, armored car services, commercial and business card products, and merchant processing solutions.

Our consumer offering is anchored on our rewards based checking product where we currently hold over $260 million in deposit balances in approximately 33,000 accounts. The "FirstRewards" checking product incents our clients to use their FirstBank debit card as a primary method of payment at point of sale, utilize online and mobile banking, electronic bill pay, direct deposit, and receive electronic statements. When meeting certain criteria, clients receive a premium interest rate on balances. The Bank benefits from higher interchange revenue, lower expense on a per account basis as compared to traditional products, and better client retention.

The coupling of these strategies delivered through our relationship-based sales model has allowed us to grow noninterest bearing deposits and noninterest income without expanding our account level fee structure. This differentiating approach has set us apart from national and regional competitors and has built loyalty and satisfaction within our client segments.

Mortgage banking services

We offer full-service residential mortgage products and services through our bank branches, our mortgage offices strategically located throughout the southeastern United States both in and outside our community banking footprint and our internet delivery channel. We also offer smaller community banks and mortgage companies a host of diverse, third-party mortgage services. Our mortgage business has a strong track record of profitability and growth driven by our experienced mortgage executive team, diversified distribution channels and correspondent relationships with other community banks and mortgage companies.

While we have always offered, and continue to offer, home mortgage loans to retail customers through our bank branches, we began the expansion and diversification of our mortgage business beyond our traditional bank branch channel in 2010 by opening loan production offices in certain Tennessee markets in an effort to take advantage of attractive opportunities to grow our mortgage revenues and attract new customers to the Bank. We continued this expansion in 2011 with the acquisition of the assets and certain employees of Henger Rast Mortgage, with loan production offices in Alabama and Georgia, and the acquisition of our third party origination group in Greer, South Carolina. We also opened additional mortgage offices outside of our community banking footprint in strategically located markets across the Southeast and continued to hire experienced loan officers across our footprint. In 2014, we started our internet delivery channel to target clients across the nation and to compete against online mortgage providers. Additionally, in 2016 we acquired certain assets of Finance of America Mortgage LLC, further expanding our third party origination channel. As a result of these initiatives, we have expanded our mortgage banking business beyond the traditional home mortgage loans offered by our bank branches and now offer our residential mortgage products and services and third party mortgage services through four diverse delivery channels: (1) Retail Mortgage, which provides residential mortgages to consumers in the Southeast primarily through our bank branches and mortgage offices; (2) Third Party Origination consisting of both correspondent and wholesale lending, which provides mortgage processing and resale services to smaller banks and mortgage companies in Tennessee and other states nationally; (3) ConsumerDirect, which provides residential mortgages on a national basis via internet channels; and (4) Reverse Mortgage, which provides reverse mortgage products to clients in Tennessee, Alabama, Georgia, and other states nationally.

The residential mortgage products and services originated in our community banking footprint and related revenues and expenses are included in our Banking segment while the residential mortgage products and services originated outside of our community banking footprint and related revenues and expenses are included in our Mortgage segment. The Mortgage segment also includes our ConsumerDirect internet delivery channels, our Third Party Origination group and our mortgage servicing activities.

We intend to continue to take advantage of opportunities to grow our mortgage business as they present themselves, including by continuing to expand our mortgage business outside of our community banking footprint, improving the client experience through an enhanced fulfillment process, attracting experienced loan officers and improving profitability through centralized efficiencies and our capital markets execution. We have successfully maintained our ConsumerDirect internet delivery channel over the past year by increasing our marketing of this channel. Additionally, we are continuing to develop our correspondent lending delivery channel, which will be a continued focus of future growth in 2018. We have managed to grow our mortgage business while maintaining a high-degree of scalability to control costs in the event of a downturn in our mortgage business. Our mortgage loan office leases are primarily short-term in nature and approximately 55% of our mortgage-related compensation is in the form of variable compensation. Our mortgage business offers attractive cross-selling opportunities for our consumer banking products through the origination process and our mortgage servicing book.

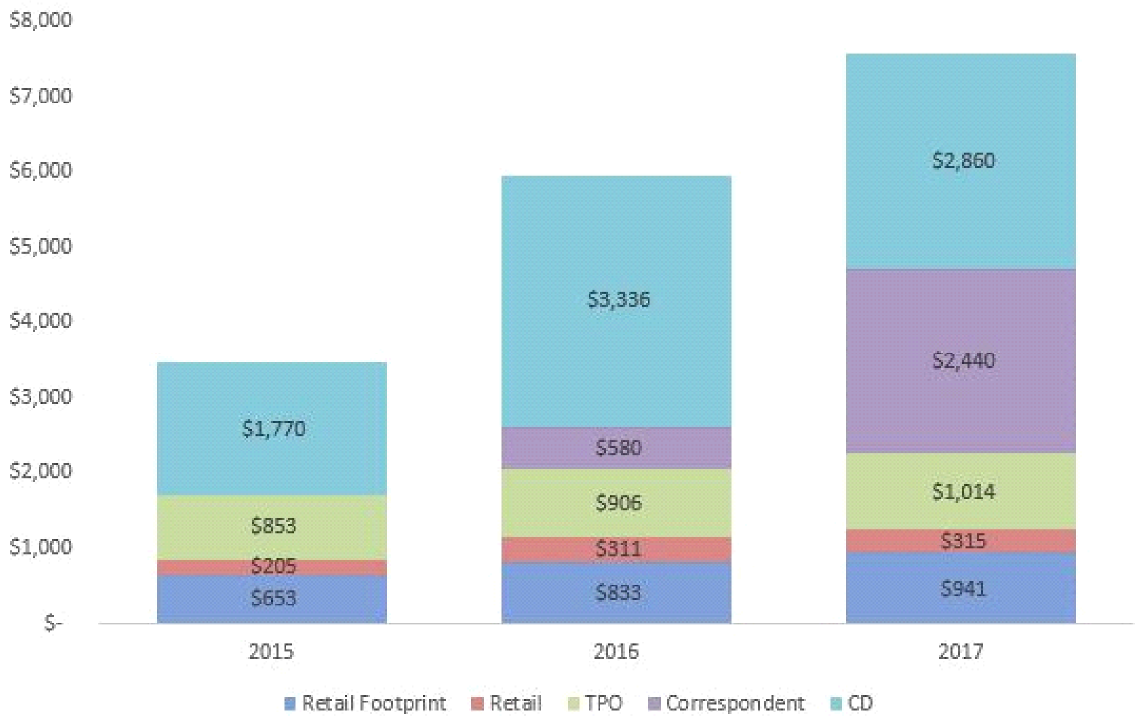
We look to originate quality mortgage loans with a focus on purchase money mortgages. In accordance with our lending policy, each loan undergoes a detailed underwriting process which incorporates uniform underwriting standards and oversight that satisfies secondary market standards as outlined by our investors and our internal policies. Mortgage loans are subject to the same uniform lending policies referenced below and consist primarily of loans with relatively stronger borrower credit scores, with an average FICO score of 731 during the year ended December 31, 2017.

The residential mortgage industry is highly competitive, and we compete with other community banks, regional banks, national banks, credit unions, mortgage companies, financial service companies and online mortgage companies. Due to the highly competitive nature of the residential mortgage industry, we expect to face continued industry-wide competitive pressures related to changing market conditions that will reduce our pricing margins and mortgage revenues generally, especially in a rising rate environment.

Our mortgage banking business is also directly impacted by the interest rate environment, increased regulations, consumer demand, driven in large part by general economic conditions and the real estate markets, and investor demand for mortgage securities. Mortgage production, especially refinancing activity, declines in rising interest rate environments. While we have not yet experienced a slowdown in our mortgage origination volume, due in part to our expansion of our mortgage banking business, our mortgage origination volume could be materially and adversely affected by rising interest rates, and we expect to see declining origination volume in 2018 within the industry.

During the year ended December 31, 2017, we had $7.6 billion in interest rate lock commitment volume, with 58% of these commitments being purchase money mortgage loans. Please see below for a breakdown of our interest rate lock commitment volume by distribution channel since 2015 and by product type in 2017:

Interest rate lock commitment volume by line of business ($ in millions)



Interest rate lock commitment volume by product type (year ended December 31, 2017)

Note: Conv = Conventional; VA = Veterans Affairs; USDA = United States Department of Agriculture Rural Housing Mortgage; FHA = Federal Housing Administration

Investment and trust services

The Bank provides our individual clients access to investment services offered by LPL Financial (formerly INVEST Financial Corporation), an independent third-party broker-dealer that maintains offices in 41 of our bank branches. A full range of investment choices is available through LPL Financial for our clients, including equities, mutual funds, bonds, tax-exempt municipals, and annuities, as well as money management consultation. Life insurance products are also offered to our clients through FirstBank Insurance, Inc., a wholly-owned insurance agency. We also offer our business clients group retirement plan advisory services. We primarily market these services to retirees or pre-retirees with a minimum of $100,000 of investable assets, high income professionals earning more than $200,000 and businesses with group retirements plans that have more than $1 million in assets. We earn noninterest income from the investment and life insurance sales arrangements.

During 2017, the Bank began providing trust administration services as an extension to wealth management through the FirstBank Trust Department through the Clayton Banks acquisition. With $567.4 million assets under management at December 31, 2017, a disciplined investment philosophy and a highly competitive fee schedule, FirstBank Trust primarily serves high-wealth bank relationships and a niche of charitable endowments and foundations.

Risk management

General

Our operating model demands a strong risk culture built to address multiple areas of risk, including credit risk, interest rate risk, liquidity risk, price risk, compliance risk, operational risk, strategic risk and reputational risk. Our risk culture is supported by investments in the right people and technologies to protect our business. Our board of directors and the Bank's board of directors are ultimately responsible for overseeing risk management at the holding company and the Bank, respectively. We have a Chief Risk Officer who oversees risk management across our business (including the Bank) and reports directly to our Chief Executive Officer. Our board, Chief Executive Officer and Chief Risk Officer are supported by the heads of other functional areas at the Bank, including legal, IT, audit, compliance, capital markets and information and physical security. Our comprehensive risk management framework is designed to complement our core strategy of empowering our experienced, local bankers with local-decision making to better serve our clients.

Our credit policies support our goal of maintaining sound credit quality standards while achieving balance sheet growth, earnings growth, appropriate liquidity and other key objectives. We maintain a risk management infrastructure that includes local authority, centralized policymaking and a strong system of checks and balances. The fundamental principles of our credit policy and procedures are to maintain credit quality standards, which enhance our long-term value to our clients, associates, shareholders and communities. Our loan policies provide our bankers with a sufficient degree of flexibility to permit them to deliver responsive and effective lending solutions to our clients while maintaining appropriate credit quality. Furthermore, our bankers and associates are hired for the long-term and they are incentivized to focus on long-term credit quality. Since lending represents credit risk exposure, the Bank's board of directors and its duly appointed committees seek to ensure that the Bank maintains appropriate credit quality standards. We have established oversight committees to administer the loan portfolio and monitor credit risk. These committees include our audit committee and credit committee, and they meet at least quarterly to review the lending activities of the Bank.

Credit concentration

Diversification of risk is a key factor in prudent asset management. Our loan portfolio is balanced between our metropolitan and community markets and by type, thereby diversifying our loan concentration. Our granular loan portfolio reflects a balanced mix of consumer and commercial clients across these markets that we think provides a natural hedge to industry and market cycles. In addition, risk from concentration is actively managed by management and reviewed by the board of directors of the Bank, and exposures relating to borrower, industry and commercial real estate categories are tracked and measured against policy limits. These limits are reviewed as part of our periodic review of the loan policy. Loan concentration levels are monitored by the credit administration department and reported to the board of directors of the Bank.

Loan approval process

The loan approval process at the Bank is characterized by local authority supported by a risk control environment that provides for prompt and thorough underwriting of loans. Our localized decision making is reinforced through a centralized review process supported by technology that monitors credits to ensure compliance with our credit policies. Our loan approval method is based on a hierarchy of individual lending authorities for new credits and renewals granted to our individual bankers, market presidents, credit officers, senior management and credit committee. The Bank's board of directors establishes the maximum lending limits at each level and our senior management team sets individual authorities within these maximum limits to each individual based on demonstrated experience and expertise, and are periodically reviewed and updated. We believe that the ability to have individual loan authority up to specified levels based on experience and track record coupled with appropriate approval limits for our market presidents and credit officers allows us to provide prompt and appropriate responses to our clients while still allowing for the appropriate level of oversight.

As a relationship-oriented lender, rather than transaction-oriented lender, substantially all of our loans are made to borrowers or relationships located or operating in our market area. This provides us with a better understanding of their business, creditworthiness and the economic conditions in their market and industry. Furthermore, our associates are held accountable for all of their decisions, which effectively aligns their incentives to reflect appropriate risk management.

In considering loans, we follow the conservative underwriting principles set forth in our loan policy with a primary focus on the following factors:

- a relationship with our clients that provides us with a thorough understanding of their financial condition and ability to repay the loan;
- verification that the primary and secondary sources of repayment are adequate in relation to the amount of the loan;
- adherence to appropriate loan to value guidelines for real estate secured loans;
- targeted levels of diversification for the loan portfolio, both as to type of borrower and type of collateral; and
- proper documentation of loans, including perfected liens on collateral.

As part of the approval process for any given loan, we seek to minimize risk in a variety of ways, including the following:

- analysis of the borrower's and/or guarantor's financial condition, cash flow, liquidity, and leverage;
- assessment of the project's operating history, operating projections, location and condition;
- review of appraisals, title commitment and environmental reports;
- consideration of the management's experience and financial strength of the principals of the borrower; and
- understanding economic trends and industry conditions.

The board of directors of the Bank reviews and approves loan policy changes, monitors loan portfolio trends and credit trends, and reviews and approves loan transactions that exceed management thresholds as set forth in our loan policies. Loan pricing is established in conjunction with the loan approval process based on pricing guidelines for loans that are set by the Bank's senior management. We believe that our loan approval process provides for thorough internal controls, underwriting, and decision making.

Lending limits

The Bank is limited in the amount it can loan in the aggregate to a single borrower or related borrowers by the amount of our capital. The Bank is a Tennessee chartered bank and therefore all branches, regardless of location, fall under the legal lending limits of the state of Tennessee. Tennessee's legal lending limit is a safety and soundness measure intended to prevent one person or a relatively small and economically related group of persons from borrowing an unduly large amount of a bank's funds. It is also intended to safeguard a bank's depositors by diversifying the risk of loan losses among a relatively large number of creditworthy borrowers engaged in various types of businesses. Generally, under Tennessee law, loans and extensions of credit to a borrower may not exceed 15% of our bank's Tier 1 capital, plus an additional 10% of the bank's Tier 1 capital, with approval of the bank's board. Further, the Bank may elect to conform to similar standards applicable to national banks under federal law, in lieu of Tennessee law. Because the federal law and Tennessee state law standards are determined as a percentage of the Bank's capital, these state and federal limits both increase or decrease as the Bank's capital increases or decreases. Based upon the capitalization of the Bank at December 31, 2017, the Bank's legal lending limits were approximately $66 million (15%) and $111 million (25%). The Bank may seek to sell participations in our larger loans to other financial institutions, which will allow us to manage the risk involved in these loans and to meet the lending needs of our clients requiring extensions of credit in excess of these limits.

In addition to these legally imposed lending limits, we also employ appropriate limits on our overall loan portfolio and requirements with respect to certain types of lending and individual lending relationships. For example, we have lending limits related to maximum borrower, industry and certain types of commercial real estate exposures.

Enterprise risk management

We maintain an enterprise risk management program that helps us to identify, manage, monitor and control potential risks that may affect us, including credit risk, interest rate risk, liquidity risk, price risk, compliance risk, operational risk, strategic risk and reputational risk. Our operating model demands a strong risk culture built to address the multiple areas of risk we face, and our risk management strategy is supported by significant investments in the right people and technologies to protect the organization.

Our comprehensive risk management framework and risk identification is a continuous process and occurs at both the transaction level and the portfolio level. While our local bankers and associates support our day-to-day risk practices, management seeks to identify interdependencies and correlations across portfolios and lines of business that may amplify risk exposure through a thorough centralized review process. Risk measurement helps us to control and monitor risk levels and is based on the sophistication of the risk measurement tools used to reflect the complexity and levels of assumed risk. We monitor risks and ensure compliance with our risk policies by timely reviewing risk positions and exceptions, investing in the technology to monitor credits, requiring senior management authority sign-off on larger credit requests and granting credit authority to bankers and officers based on demonstrated experience and expertise. This monitoring process ensures that management's decisions are implemented for all geographies, products and legal entities.

We control risks through limits that are communicated through policies, standards, procedures and processes that define responsibility and authority. Such limits serve as a means to control exposures to the various risks associated with our activities, and are meaningful management tools that can be adjusted if conditions or risk tolerances change. In addition, we maintain a process to authorize exceptions or changes to risk limits when warranted. These risk management practices help to ensure effective reporting, compliance with all laws, rules and regulations, avoid damage to our reputation and related consequences, and attain our strategic goals while avoiding pitfalls and surprises along the way.

The board of directors of the Bank approves policies that set operational standards and risk limits, and any changes require approval by the Bank's board of directors. Management is responsible for the implementation, integrity and maintenance of our risk management systems ensuring the directives are implemented and administered in compliance with the approved policy. Our Chief Risk Officer supervises the overall management of our risk management program, reports to management and yet also retains independent access to the Bank's board of directors.

Credit risk management

Credit risk management is a key component of our risk management program. We employ consistent analysis and underwriting to examine credit information and prepare underwriting documentation. We monitor and approve exceptions to our credit policies as required, and we also track and address technical exceptions.

Each loan officer has the primary responsibility for appropriately risk rating each commercial loan that is made. In addition, our credit administration department is responsible for the ongoing monitoring of loan portfolio performance through the review of ongoing financial reports, loan officer reports, audit reviews and exception reporting and concentration analysis. This monitoring process also includes an ongoing review of loan risk ratings and management of our allowance for loan losses. We have a Chief Credit Officer responsible for maintaining the integrity of our portfolio within the parameters of the credit policy. We utilize a risk grading system that enables management to differentiate individual loan quality and forecast future profitability and portfolio loss potential.

We assign a credit risk rating at the time a commercial loan is made and adjust it promptly as conditions warrant. Portfolio monitoring systems allow management to proactively assess risk and make decisions that will minimize the impact of negative developments. We promote open communication to minimize or eliminate surprises. Successful credit management is achieved by lenders consistently meeting with clients and reviewing their financial conditions regularly. This enables both the recognition of future opportunities and potential weaknesses early.

The Bank's board of directors supports a strong loan review program and is committed to its effectiveness as part of the independent process of assessing our lending activities. We have communicated to our credit and lending staff that the identification of emerging problem loans begins with the lending personnel knowing their client and, supported by credit personnel, actively monitoring their client relationships. The loan review process is meant to augment this active management of client relationships and to provide an independent and broad-based look into our lending activities. We believe that our strong client relationships support our ability to identify potential deterioration of our credits at an early stage enabling us to address these issues early on to minimize potential losses.

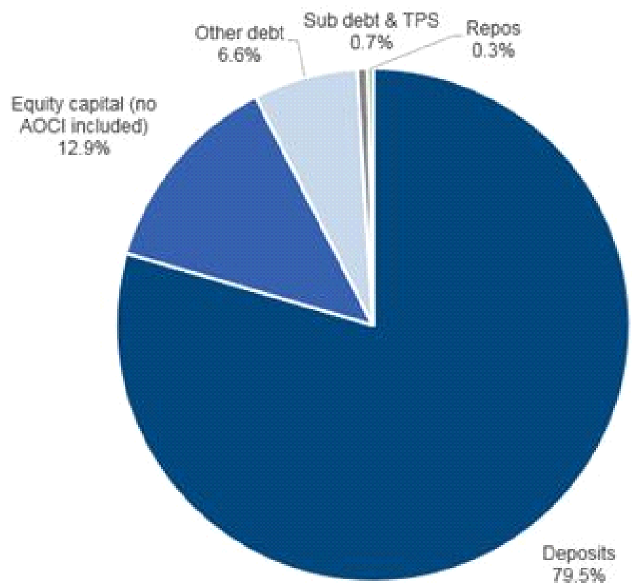
We maintain a robust loan review function by utilizing an internal loan review team as well as third-party loan review firms that report to the board of directors of the Bank to ensure independence and objectivity. The examinations performed by the loan review department are based on risk assessments of individual loan commitments within our loan portfolio over a period of time. At the conclusion of each review, the loan review department provides management and the board of directors with a report that summarizes the findings of the review. At a minimum, the report addresses risk rating accuracy, compliance with regulations and policies, loan documentation accuracy, the timely receipt of financial statements, and any additional material issues.

When delinquencies in our loans exist, we rigorously monitor the levels of such delinquencies for any negative or adverse trends. From time to time, we may modify loans to extend the term or make other concessions to help a borrower with a deteriorating financial condition stay current on their loan and to avoid foreclosure. We generally do not forgive principal or interest on loans or modify the interest rates on loans to rates that are below market rates. Furthermore, we are committed to collecting on all of our loans and, as a result, at times have lower net charge-offs compared to our peer banks. This practice can result in us carrying higher nonperforming assets on our books than our peers, however, our nonperforming assets in recent years have been lower than peers due to strong asset quality. Our commitment to collecting on all of our loans, coupled with our knowledge of our borrowers, sometimes results in higher loan recoveries. We believe that we are well reserved for losses resulting from our non-performing assets.

Liquidity and interest rate risk management

Our liquidity planning framework is focused on ensuring the lowest cost of funding available and planning for unpredictable funding circumstances. To achieve these objectives, we utilize a simple funding and capital structure consisting primarily of deposits and common equity. We remain continually focused on growing our noninterest bearing and other low-cost core deposits while replacing higher cost funding options, including wholesale time deposits and other borrowed debt, to fund our balance sheet growth. The following chart shows our simple funding structure as of December 31, 2017.

Funding structure as of December 31, 2017



In addition, we monitor our liquidity risk by adopting policies to define potential liquidity problems, reviewing and maintaining an updated liquidity contingency plan and providing a prudent capital structure consistent with our credit standing and plans for strategic growth.

Our interest risk management system is overseen by our board of directors, who has the authority to approve acceptable rate risk levels. Our board of directors has established the Asset Liability Committee to ensure appropriate risk appetite by requiring:

- quarterly testing of interest rate risk exposure,
- proactive risk identification and measurement,
- quarterly risk presentations by senior management, and
- independent review of the risk management process.

Competition

We conduct our core banking operations primarily in Tennessee and compete in the commercial banking industry solely through our wholly-owned banking subsidiary, FirstBank. The banking industry is highly competitive, and we experience competition in our market areas from many other financial institutions. We compete with commercial banks, credit unions, savings institutions, mortgage banking firms, online mortgage lenders, consumer finance companies, securities brokerage firms, insurance companies, money market funds and other mutual funds, as well as super-regional, national and international financial institutions that operate offices in our market areas and elsewhere. In addition, a number of out-of-state financial intermediaries have opened production offices, or otherwise solicit deposits, in our market areas. Increased competition in our markets may result in reduced loans and deposits, as well as reduced net interest margin and profitability. Furthermore, the Tennessee market has grown increasingly competitive in recent years with a number of banks entering this market, with a primary focus on the state's metropolitan markets. We believe this trend will continue as banks look to gain a foothold in these growing markets. This trend will result in greater competition primarily in our metropolitan markets. However, we firmly believe that our market position and client-focused operating model enhances our ability to attract and retain clients.

See "Our markets" in this section above for a further discussion of the markets we compete in and the competitive landscape in these markets.

Our associates

As of December 31, 2017, we had 1,335 full-time associates and 51 part-time associates. We pride ourselves on maintaining good relations with our associates. None of our employees are represented by any collective bargaining unit or are parties to a collective bargaining agreement.

Information technology systems

We have recently made and continue to make significant investments in our technology platforms. In 2014, we completed an upgrade to our consumer online banking, mobile and voice platforms deploying competitive technology to support consumer self-service banking behavior. During 2015, we completed the installation of a dedicated commercial cash management platform that is configurable at a client segment level supporting a broad range of client needs. We also developed a commercial mobile and tablet app that we launched in late 2016.

During the second quarter of 2016, we successfully converted our core operating platform to the Jack Henry Silverlake platform. This core conversion includes the replacement of our core, teller platform, loan and deposit platforms, as well as a number of other ancillary systems, which we believe helped us achieve a scalable and efficient operations function. Additionally, the core conversion positioned us to offer new products and services that improves our overall customer experience and enhances our ability to attract new households.

Supervision and regulation

The following is a general summary of the material aspects of certain statutes and regulations applicable to us and the Bank. These summary descriptions are not complete, and you should refer to the full text of the statutes, regulations, and corresponding guidance for more information. These statutes and regulations are subject to change, and additional statutes, regulations, and corresponding guidance may be adopted. We are unable to predict these future changes or the effects, if any, that these changes could have on our business, revenues, and financial results.

General

As a registered bank holding company, we are subject to regulation, supervision, and examination by the Board of Governors of the Federal Reserve System, or Federal Reserve, under the Bank Holding Company Act of 1956, as amended (the "BHCA"). In addition, as a Tennessee state-chartered bank that is not a member of the Federal Reserve System, the Bank is subject to primary regulation, supervision, and examination by the Federal Deposit Insurance Corporation, or FDIC, and the Bank's state banking regulator, the Tennessee Department of Financial Institutions, or TDFI. Supervision, regulation, and examination of us and the Bank by the bank regulatory agencies are intended primarily for the protection of consumers, bank depositors and the Deposit Insurance Fund of the FDIC, rather than holders of our capital stock.

Changes as a result of the Dodd-Frank Act

As a result of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, or Dodd-Frank Act, the regulatory framework under which we and the Bank operate has changed. The Dodd-Frank Act brought about a significant overhaul of many aspects of the regulation of the financial services industry, addressing issues including, among others, systemic risk, capital adequacy, deposit insurance assessments, consumer financial protection, interchange fees, lending limits, mortgage lending practices, registration of investment advisers and changes among the bank regulatory agencies. In particular, portions of the Dodd-Frank Act that affected us and the Bank include, but are not limited to:

- The Dodd-Frank Act created the Consumer Financial Protection Bureau, or CFPB, a new federal regulatory body with broad authority to regulate the offering and provision of consumer financial products and services. The authority to examine depository institutions with $10.0 billion or less in assets, such as the Bank, for compliance with federal consumer laws remain largely with the Bank's primary federal regulator, the FDIC. However, the CFPB may participate in examinations of smaller institutions on a "sampling basis" and may refer potential enforcement actions against such institutions to their primary regulators. While the CFPB does not have direct supervisory authority over us or the Bank, it nevertheless has important rulemaking, examination and enforcement authority with regard to consumer financial products and services.

- The Dodd-Frank Act imposed new duties on mortgage lenders, including a duty to determine the borrower's ability to repay the loan, and imposed a requirement on mortgage securitizers to retain a minimum level of economic interest in securitized pools of certain mortgage types.

- The Dodd-Frank Act's Volcker Rule substantially restricted proprietary trading and investments in hedge funds or private equity funds and requires banking entities to implement compliance programs, as described further under "Other Dodd-Frank Act reforms : Volcker Rule" below.

- The Dodd-Frank Act contained other provisions, including but not limited to: new limitations on federal preemption; application of new regulatory capital requirements, including changes to leverage and risk-based capital standards and changes to the components of permissible tiered capital ; changes to the assessment base for deposit insurance premiums; permanently raising the FDIC's standard maximum deposit insurance amount to $250,000 limit for federal deposit insurance; repeal of the prohibition on the payment of interest on demand deposits, thereby permitting depository institutions to pay interest on business transaction and other accounts; a prohibition on incentive-based compensation arrangements that encourage inappropriate risk taking by covered financial institutions and are deemed to be excessive, or that may lead to material losses; requirement that sponsors of asset-backed securities retain a percentage of the credit risk of the assets underlying the securities; requirement that banking regulators remove references to and requirements of reliance upon credit ratings from their regulations and replace them with appropriate alternatives for evaluating credit worthiness.

The list above is not exhaustive. It reflects our current assessment of the Dodd-Frank Act provisions and implementing rules that are reasonably possible to have a substantial impact on us in the future.

Holding company regulation

As a regulated bank holding company, we are subject to various laws and regulations that affect our business. These laws and regulations, among other matters, prescribe minimum capital requirements, limit transactions with affiliates, impose limitations on the business activities in which we can engage, limit the dividend or distributions that the Bank can pay to us, restrict the ability of institutions to guarantee our debt, and impose certain specific accounting requirements on us that may be more restrictive and may result in greater or earlier charges to earnings or reductions in our capital than generally accepted accounting principles, among other things.

Permitted activities

Under the BHCA, as amended, a bank holding company is generally permitted to engage in, or acquire direct or indirect control of more than five percent of any class of the voting shares of any company that is not a bank or bank holding company and that is engaged in, the following activities (in each case, subject to certain conditions and restrictions and prior approval of the Federal Reserve):

- banking or managing or controlling banks:

- furnishing services to or performing services for our subsidiaries:

- any activity that the Federal Reserve determines by regulation or order to be so closely related to banking as to be a proper incident to the business of banking, including:
  - factoring accounts receivable;
  - making, acquiring, brokering or servicing loans and related activities;
  - leasing personal or real property;
  - operating a nonbank depository institution, such as a savings association;
  - performing trust company functions;
  - conducting financial and investment advisory activities;
  - conducting discount securities brokerage activities;
  - underwriting and dealing in government obligations and money market instruments;
  - providing specified management consulting and counseling activities;
  - performing selected data processing services and support services;
  - acting as agent or broker in selling credit life insurance and other types of insurance in connection with credit transactions;
  - performing selected insurance underwriting activities;
  - providing certain community development activities (such as making investments in projects designed primarily to promote community welfare); and
  - issuing and selling money orders and similar consumer-type payment instruments.

While the Federal Reserve has found these activities in the past acceptable for other bank holding companies, the Federal Reserve may not allow us to conduct any or all of these activities, which are reviewed by the Federal Reserve on a case by case basis upon application by a bank holding company.

The Federal Reserve has the authority to order a bank holding company or its subsidiaries to terminate any of these activities or to terminate its ownership or control of any subsidiary when it has reasonable cause to believe that the bank holding company's continued ownership, activity or control constitutes a serious risk to the financial safety, soundness or stability of it or any of its bank subsidiaries.

Acquisitions subject to prior regulatory approval

The BHCA requires the prior approval of the Federal Reserve for a bank holding company to acquire substantially all the assets of a bank or to acquire direct or indirect ownership or control of more than 5% of any class of the voting shares of any bank, bank holding company, savings and loan holding company or savings association, or to increase any such non-majority ownership or control of any bank, bank holding company, savings and loan holding company or savings association, or to merge or consolidate with any bank holding company.

Under the BHCA, if "well capitalized" and "well managed", as defined under the BHCA and implementing regulations, we or any other bank holding company located in Tennessee may purchase a bank located outside of Tennessee. Conversely, a well-capitalized and well-managed bank holding company located outside of Tennessee may purchase a bank located inside Tennessee. In each case, however, restrictions may be placed on the acquisition of a bank that has only been in existence for a limited amount of time or will result in concentrations of deposits exceeding limits specified by statute. For example, Tennessee law currently prohibits a bank holding company from acquiring control of a Tennessee-based financial institution until the target financial institution has been in operation for at least three years.

Bank holding company obligations to bank subsidiaries

Under current law and Federal Reserve policy, a bank holding company is expected to act as a source of financial and managerial strength to its depository institution subsidiaries and to maintain resources adequate to support such subsidiaries, which could require us to commit resources to support the Bank in situations where additional investments in a bank may not otherwise be warranted. These situations include guaranteeing the compliance of an "undercapitalized" bank with its obligations under a capital restoration plan, as described further under "Bank regulation-: Capitalization levels and prompt corrective action" below. As a result of these obligations, a bank holding company may be required to contribute additional capital to its subsidiaries in the form of capital notes or other instruments that qualify as capital under regulatory rules. Any such loan from a holding company to a subsidiary bank is likely to be unsecured and subordinated to the bank's depositors and perhaps to other creditors of the bank. If we were to enter bankruptcy or become subject to the orderly liquidation process established by the Dodd-Frank Act, any commitment by us to a federal bank regulatory agency to maintain the capital of the Bank would be assumed by the bankruptcy trustee or the FDIC, as appropriate, and entitled to a priority of payment.

Restrictions on bank holding company dividends.

The Federal Reserve's policy regarding dividends is that a bank holding company should not declare or pay a cash dividend which would impose undue pressure on the capital of any bank subsidiary or would be funded only through borrowing or other arrangements that might adversely affect a bank holding company's financial position. As a general matter, the Federal Reserve has indicated that the board of directors of a bank holding company should consult with the Federal Reserve and eliminate, defer or significantly reduce the bank holding company's dividends if:

- its 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;
- its prospective rate of earnings retention is not consistent with its capital needs and overall current and prospective financial condition; or
- it will not meet, or is in danger of not meeting, its minimum regulatory capital adequacy ratios.

Should an insured depository institution controlled by a bank holding company be "significantly undercapitalized" under the applicable federal bank capital ratios, or if the bank subsidiary is "undercapitalized" and has failed to submit an acceptable capital restoration plan or has materially failed to implement such a plan, federal banking regulators (in the case of the Bank, the FDIC) may choose to require prior Federal Reserve approval for any capital distribution by the bank holding company. For more information, see "Bank regulation: Capitalization levels and prompt corrective action."

In addition, since our legal entity is separate and distinct from the Bank and does not conduct stand-alone operations, our ability to pay dividends depends on the ability of the Bank to pay dividends to us, which is also subject to regulatory restrictions as described below in "Bank regulation: Bank dividends."

Under Tennessee law, we are not permitted to pay cash dividends if, after giving effect to such payment, we would not be able to pay our debts as they become due in the usual course of business or our total assets would be less than the sum of our total liabilities plus any amounts needed to satisfy any preferential rights if we were dissolving. In addition, in deciding whether or not to declare a dividend of any particular size, our board of directors must consider our current and prospective capital, liquidity, and other needs.

U.S. Basel III capital rules

In July 2013, federal banking regulators, including the Federal Reserve and the FDIC, adopted the U.S. Basel Capital Rules implementing many aspects of the Basel III Capital Standards.

The U.S. Basel III Capital Rules apply to all national and state banks and savings associations and most bank holding companies and savings and loan holding companies, which we collectively refer to herein as "covered" banking organizations. The requirements in the U.S. Basel III Capital Rules started to phase in on January 1, 2015, for many covered banking organizations, including the Company and the Bank. The requirements in the U.S. Basel III Capital Rules will be fully phased in by January 1, 2019.

The U.S. Basel III Capital Rules impose higher risk-based capital and leverage requirements than those previously in place. Specifically, the rules impose the following minimum capital requirements applicable to us and the Bank:

- a common equity Tier 1 risk-based capital ratio of 4.5%;
- a Tier 1 risk-based capital ratio of 6% (increased from the current 4% requirement);
- a total risk-based capital ratio of 8% (unchanged from current requirements); and
- a leverage ratio of 4%.

- a new supplementary leverage ratio of 3%, resulting in a leverage ratio requirement of 7% for such institutions.

Under the U.S. Basel III Capital Rules, Tier 1 Capital is defined to include two components: common equity Tier 1 Capital and additional Tier 1 Capital. The highest form of capital, Common Equity Tier 1 Capital, or CET1 Capital, consists solely of common stock (plus related surplus), retained earnings, accumulated other comprehensive income, and limited amounts of minority interests that are in the form of common stock. Additional Tier 1 Capital includes other perpetual instruments historically included in Tier 1 Capital, such as non-cumulative perpetual preferred stock.

The rules permit bank holding companies with less than $15.0 billion in total consolidated assets, such as us, to continue to include trust-preferred securities and cumulative perpetual preferred stock issued before May 19, 2010, in Tier 1 Capital, but not in CET1 Capital, subject to certain restrictions. Tier 2 Capital consists of instruments that currently qualify in Tier 2 Capital plus instruments that the rule has disqualified from Tier 1 Capital treatment. We have outstanding trust-preferred securities, issued as debt securities. The first issue was for $21,000,000 (21,000 securities priced at $1,000 each) plus $650,000 in the related common securities, and the second issue was for $9,000,000 (9,000 securities priced at $1,000 each) plus $280,000 in the related common securities.

In addition, in order to avoid restrictions on capital distributions or discretionary bonus payments to executives, a covered banking organization must maintain a capital conservation buffer on top of its minimum risk-based capital requirements. This buffer must consist solely of Tier 1 Common Equity, but the buffer applies to all three risk-based measurements (Common Equity Tier 1, Tier 1 Capital and total capital). The capital conservation buffer will be phased in incrementally over time, becoming fully effective on January 1, 2019, and will consist of an additional amount of common equity equal to 2.5% of risk-weighted assets.

The U.S. Basel III Capital Standards require certain deductions from or adjustments to capital. As a result, deductions from CET1 Capital will be required for goodwill (net of associated deferred tax liabilities); intangible assets such as non-mortgage servicing assets and purchased credit card relationships (net of associated deferred tax liabilities); deferred tax assets that arise from net operating loss and tax credit carryforwards (net of any related valuations allowances and net of deferred tax liabilities); any gain on sale in connection with a securitization exposure; any defined benefit pension fund net asset (net of any associated deferred tax liabilities) held by a bank holding company; the aggregate amount of outstanding equity investments (including retained earnings) in financial subsidiaries; and identified losses. Other deductions are required from different levels of capital. The U.S. Basel III Capital Rules also increase the risk weight for certain assets, meaning that more capital must be held against such assets. For example, commercial real estate loans that do not meet certain new underwriting requirements must be risk-weighted at 150% rather than the current 100%.

Additionally, the U.S. Basel III Capital Standards provide for the deduction of three categories of assets: (i) deferred tax assets arising from temporary differences that cannot be realized through net operating loss carrybacks (net of related valuation allowances and of deferred tax liabilities), (ii) mortgage servicing assets (net of associated deferred tax liabilities) and (iii) investments in more than 10% of the issued and outstanding common stock of unconsolidated financial institutions (net of associated deferred tax liabilities). The amount in each category that exceeds 10% of CET1 Capital must be deducted from CET1 Capital. The remaining, non-deducted amounts are then aggregated, and the amount by which this total amount exceeds 15% of CET1 Capital must be deducted from CET1 Capital. Amounts of minority investments in consolidated subsidiaries that exceed certain limits and investments in unconsolidated financial institutions may also have to be deducted from the category of capital to which such instruments belong.

Accumulated other comprehensive income, or AOCI, is presumptively included in CET1 Capital and often would operate to reduce this category of capital. The U.S. Basel III Capital Rules provided a one-time opportunity at the end of the first quarter of 2015 for covered banking organizations to opt out of much of this treatment of AOCI. We elected to opt out. The rules also have the effect of increasing capital requirements by increasing the risk weights on certain assets, including high volatility commercial real estate, mortgage servicing rights not includable in CET1 Capital, equity exposures, and claims on securities firms, which are used in the denominator of the three risk-based capital ratios.

When fully phased in on January 1, 2019, the U.S. Basel III Capital Rules will require us and the Bank to maintain (i) a minimum ratio of CET1 Capital to risk-weighted assets of at least 4.5%, plus the 2.5% capital conservation buffer, effectively resulting in a minimum ratio of CET1 Capital to risk-weighted assets of at least 7.0%, (ii) a minimum ratio of Tier 1 Capital to risk-weighted assets of at least 6.0%, plus the capital conservation buffer, effectively resulting in a minimum Tier 1 Capital ratio of 8.5%, (iii) a minimum ratio of total capital (that is, Tier 1 plus Tier 2) to risk-weighted assets of at least 8.0%, plus the capital conservation buffer, effectively resulting in a minimum total capital ratio of 10.5% and (iv) a minimum leverage ratio of 4%, calculated as the ratio of Tier 1 Capital to average assets. Management believes that we and the Bank would meet all capital adequacy requirements under the U.S. Basel III Capital Rules on a fully phased-in basis if such requirements were currently effective.

The U.S. Basel III Capital Rules also make important changes to the “prompt corrective action” framework discussed below in “Bank regulation: Capitalization levels and prompt corrective action.”

Restrictions on affiliate transactions

See “Bank regulation: Restrictions on transactions with affiliates” below.

Change in control

We are a bank holding company regulated by the Federal Reserve. Subject to certain exceptions, the Change in Bank Control Act, or (“CIBCA”), and its implementing regulations require that any individual or company acquiring “control” of a bank or bank holding company, either directly or indirectly, give the Federal Reserve 60 days’ prior written notice of the proposed acquisition. If within that time period the Federal Reserve has not issued a notice disapproving the proposed acquisition, extended the period for an additional period up to 90 days or requested additional information, the acquisition may proceed. An acquisition may be made before expiration of the disapproval period if the Federal Reserve issues written notice that it intends not to disapprove the acquisition. Acquisition of 25 percent or more of any class of voting securities constitutes control, and it is generally presumed for purposes of the CIBCA that the acquisition of 10 percent or more of any class of voting securities would constitute the acquisition of control, although such a presumption of control may be rebutted.

Also, under the CIBCA, the shareholdings of individuals and companies that are deemed to be “acting in concert” would be aggregated for purposes of determining whether such holders “control” a bank or bank holding company. “Acting in concert” under the CIBCA generally means knowing participation in a joint activity or parallel action towards the common goal of acquiring control of a bank or a bank holding company, whether or not pursuant to an express agreement. The manner in which this definition is applied in individual circumstances can vary and cannot always be predicted with certainty. Many factors can lead to a rebuttable presumption of acting in concert, including where: (i) the shareholders are commonly controlled or managed; (ii) the shareholders are parties to an oral or written agreement or understanding regarding the acquisition, voting or transfer of control of voting securities of a bank or bank holding company; (iii) the shareholders are immediate family members; or (iv) both a shareholder and a controlling shareholder, partner, trustee or management official of such shareholder own equity in the bank or bank holding company.

Furthermore, under the BHCA and its implementing regulations, and subject to certain exceptions, any company would be required to obtain Federal Reserve approval prior to obtaining control of a bank or bank holding company. Control under the BHCA exists where a company acquires 25 percent or more of any class of voting securities, has the ability to elect a majority of a bank holding company’s directors, is found to exercise a “controlling influence” over a bank or bank holding company’s management and policies, and in certain other circumstances. There is a presumption of non-control for any holder of less than 5% of any class of voting securities. In addition, in 2008 the Federal Reserve issued a policy statement on equity investments in banks and bank holding companies, which sets out circumstances under which a minority investor would not be deemed to control a bank or bank holding company for purposes of the BHCA. Among other things, the 2008 policy statement permits a minority investor to hold up to 24.9% (or 33.3% under certain circumstances) of the total equity (voting and non-voting combined) and have at least one representative on the company’s board of directors (with two directors permitted under certain circumstances).

Compensation and risk management

In 2010, the federal banking agencies issued guidance to regulated banks and bank holding companies intended to ensure that incentive compensation arrangements at financial organizations take into account risk and are consistent with safe and sound practices. The guidance is based on three “key principles” calling for incentive compensation plans to: appropriately balance risks and rewards; be compatible with effective controls and risk management; and be backed up by strong corporate governance. Further, in 2016 the federal banking regulators re-proposed rules that would prohibit incentive compensation arrangements that would encourage inappropriate risks by providing excessive compensation or that could lead to a material financial loss, and include certain prescribed standards for governance and risk management for incentive compensation for institutions, such as us, that have over $1 billion in consolidated assets.

Bank regulation

The Bank is a banking institution that is chartered by and headquartered in the State of Tennessee, and it is subject to supervision and regulation by the TDFI and the FDIC. The TDFI and FDIC supervise and regulate all areas of the Bank’s operations including, without limitation, the making of loans, the issuance of securities, the conduct of the Bank’s corporate affairs, the satisfaction of capital adequacy requirements, the payment of dividends, and the establishment or closing of banking offices. The FDIC is the Bank’s primary federal regulatory agency, which periodically examines the Bank’s operations and financial condition and compliance with federal consumer protection laws. In addition, the Bank’s deposit accounts are insured by the FDIC to the maximum extent permitted by law, and the FDIC has certain enforcement powers over the Bank.

As a state-chartered banking institution in the State of Tennessee, the Bank is empowered by statute, subject to the limitations contained in those statutes, to take and pay interest on deposits, to make loans on residential and other real estate, to make consumer and commercial loans, to invest, with certain limitations, in equity securities and in debt obligations of banks and corporations and to provide various other banking services for the benefit of the Bank's clients. Various state consumer laws and regulations also affect the operations of the Bank, including state usury laws, consumer credit and equal credit opportunity laws, and fair credit reporting. In addition, the Federal Deposit Insurance Corporation Improvement Act of 1991, or FDICIA, generally prohibits insured state chartered institutions from conducting activities as principal that are not permitted for national banks. The Bank is also subject to various requirements and restrictions under federal and state law, including but not limited to requirements to maintain reserves against deposits, lending limits, limitations on branching activities, limitations on the types of investments that may be made, activities that may be engaged in, and types of services that may be offered. Various consumer laws and regulations also affect the operations of the Bank. Also, the Bank and certain of its subsidiaries are prohibited from engaging in certain tying arrangements in connection with extensions of credit, leases or sales of property, or furnishing products or services.

Capital adequacy

See "Holding company regulation: U.S. Basel III capital rules."

Capitalization levels and prompt corrective action

Federal law and regulations establish a capital-based regulatory scheme designed to promote early intervention for troubled banks and require the FDIC to choose the least expensive resolution of bank failures. The capital-based regulatory framework contains five categories of regulatory capital requirements, including "well capitalized," "adequately capitalized," "undercapitalized," "significantly undercapitalized," and "critically undercapitalized." A well-capitalized insured depository institution is one (i) having a total risk-based capital ratio of 10 percent or greater, (ii) having a Tier 1 risk-based capital ratio of 8 percent or greater, (iii) having a CET1 capital ratio of 6.5 percent or greater, (iv) having a leverage capital ratio of 5 percent or greater and (v) that is not subject to any order or written directive to meet and maintain a specific capital level for any capital measure.

Generally, a financial institution must be "well capitalized" before the Federal Reserve will approve an application by a bank holding company to acquire a bank or merge with a bank holding company, and the FDIC applies the same requirement in approving bank merger applications.

Immediately upon becoming undercapitalized, a depository institution becomes subject to the provisions of Section 38 of the Federal Deposit Insurance Act, or FDIA, which: (i) restrict payment of capital distributions and management fees; (ii) require that the appropriate federal banking agency monitor the condition of the institution and its efforts to restore its capital; (iii) require submission of a capital restoration plan; (iv) restrict the growth of the institution's assets; and (v) require prior approval of certain expansion proposals. Bank holding companies controlling financial institutions can be called upon to boost the institutions' capital and to partially guarantee the institutions' performance under their capital restoration plans. The appropriate federal banking agency for an undercapitalized institution also may take any number of discretionary supervisory actions if the agency determines that any of these actions is necessary to resolve the problems of the institution at the least possible long-term cost to the deposit insurance fund, subject in certain cases to specified procedures. These discretionary supervisory actions include: (i) requiring the institution to raise additional capital; (ii) restricting transactions with affiliates; (iii) requiring divestiture of the institution or the sale of the institution to a willing purchaser; (iv) requiring the institution to change and improve its management; (iv) prohibiting the acceptance of deposits from correspondent banks; (v) requiring prior Federal Reserve approval for any capital distribution by a bank holding company controlling the institution; and (vi) any other supervisory action that the agency deems appropriate. These and additional mandatory and permissive supervisory actions may be taken with respect to significantly undercapitalized and critically undercapitalized institutions.

As of December 31, 2017, the Bank had sufficient capital to qualify as "well capitalized" under the requirements contained in the applicable regulations, policies and directives pertaining to capital adequacy, and it is unaware of any material violation or alleged material violation of these regulations, policies or directives. Rapid growth, poor loan portfolio performance, or poor earnings performance, or a combination of these factors, could change the Bank's capital position in a relatively short period of time, making additional capital infusions necessary.

It should be noted that the minimum ratios referred to above in this section are merely guidelines, and the bank regulators possess the discretionary authority to require higher capital ratios.

Bank reserves

The Federal Reserve requires all depository institutions, even if not members of the Federal Reserve System, to maintain reserves against some transaction accounts. The balances maintained to meet the reserve requirements imposed by the Federal Reserve may be used to satisfy liquidity requirements. An institution may borrow from the Federal Reserve Bank "discount window" as a secondary source of funds, provided that the institution meets the Federal Reserve Bank's credit standards.

Bank dividends

The FDIC prohibits any distribution that would result in the bank being "undercapitalized" (<4% leverage ratio, <4.5% CET1 Risk-Based ratio, <6% Tier 1 Risk-Based ratio, or <8% Total Risk-Based ratio). Tennessee law places restrictions on the declaration of dividends by state chartered banks to their shareholders, including, but not limited to, that the board of directors of a Tennessee-chartered bank may only make a dividend from the surplus profits arising from the business of the bank, and may not declare dividends in any calendar year that exceeds the total of its retained net income of that year combined with its retained net income of the preceding two (2) years without the prior approval of the TDFI commissioner. Furthermore, the TDFI also has authority to prohibit the payment of dividends by a Tennessee bank when it determines such payment to be an unsafe and unsound banking practice.

Insurance of accounts and other assessments

The Bank pays deposit insurance assessments to the Deposit Insurance Fund, which is determined through a risk-based assessment system. The Bank's deposit accounts are currently insured by the Deposit Insurance Fund, generally up to a maximum of $250,000 per separately insured depositor. The Bank pays assessments to the FDIC for such deposit insurance. Under the current assessment system, the FDIC assigns an institution to a risk category based on the institution's most recent supervisory and capital evaluations, which are designed to measure risk. Under the FDIA, the FDIC may terminate a bank's deposit insurance upon a finding that the institution has engaged in unsafe and unsound practices, is in an unsafe or unsound condition to continue operations, or has violated any applicable law, regulation, rule, order, agreement or condition imposed by the FDIC.

In addition, all FDIC-insured institutions are required to pay assessments to the FDIC to fund interest payments on bonds issued by the Financing Corporation, or FICO, a federal government corporation established to recapitalize the predecessor to the Savings Association Insurance Fund. FICO assessments are set quarterly and the assessment rate was .590 (annual) basis points for all four quarters in 2015, .560 (annual) basis points for all four quarters in 2016, and .520 (annual) basis points for all four quarters in 2017. These assessments will continue until the FICO bonds mature in 2017 through 2019.

Restrictions on transactions with affiliates

The Bank is subject to sections 23A and 23B of the Federal Reserve Act, or FRA, and the Federal Reserve's Regulation W, as made applicable to state nonmember banks by section 18(j) of the FDIA. An affiliate of a bank is any company or entity that controls, is controlled by or is under common control with the Bank, and, in our case, includes, among others, the Company as well as our Executive Chairman, James W. Ayers and the companies he controls. Accordingly, transactions between the Bank, on the one hand, and the Company or Mr. Ayers or any of his affiliates, on the other hand, will be subject to a number of restrictions, including restrictions relating to extensions of credit, contracts, leases and purchases or sale of assets. Such restrictions and limitations prevent the Company or Mr. Ayers or his affiliates from borrowing from the Bank unless the loans are secured by specified collateral of designated amounts. Furthermore, such secured loans by the Bank to the Company or Mr. Ayers and his affiliates are limited, individually, to ten percent (10%) of the Bank's capital and surplus, and such secured loans are limited in the aggregate to twenty percent (20%) of the Bank's capital and surplus.

All such transactions must be on terms that are no less favorable to the Bank than those that would be available from nonaffiliated third parties. Federal Reserve policies also forbid the payment by bank subsidiaries of management fees which are unreasonable in amount or exceed the fair market value of the services rendered or, if no market exists, actual costs plus a reasonable profit.

Loans to insiders

Loans to executive officers, directors or to any person who directly or indirectly, or acting through or in concert with one or more persons, owns, controls or has the power to vote more than 10% of any class of voting securities of a bank, which the Bank refers to as “10% Shareholders,” or to any political or campaign committee the funds or services of which will benefit those executive officers, directors, or 10% Shareholders or which is controlled by those executive officers, directors or 10% Shareholders, are subject to Sections 22(g) and 22(h) of the FRA and their corresponding regulations, which are commonly referred to as Regulation O. Among other things, these loans must be made on terms substantially the same as those prevailing on transactions made to unaffiliated individuals and certain extensions of credit to those persons must first be approved in advance by a disinterested majority of the entire board of directors. Regulation O prohibits loans to any of those individuals where the aggregate amount exceeds an amount equal to 15% of an institution’s unimpaired capital and surplus plus an additional 10% of unimpaired capital and surplus in the case of loans that are fully secured by readily marketable collateral, or when the aggregate amount on all of the extensions of credit outstanding to all of these persons would exceed the Bank’s unimpaired capital and unimpaired surplus. Section 22(g) identifies limited circumstances in which the Bank is permitted to extend credit to executive officers.

Community Reinvestment Act

The Community Reinvestment Act, or CRA, and its corresponding regulations are intended to encourage banks to help meet the credit needs of their service areas, including low and moderate-income neighborhoods, consistent with safe and sound operations. These regulations provide for regulatory assessment of a bank’s record in meeting the credit needs of its service area. Federal banking agencies are required to make public a rating of a bank’s performance under the CRA. The federal banking agencies consider a bank’s CRA rating when a bank submits an application to establish banking centers, merge, or acquire the assets and assume the liabilities of another bank. In the case of a bank holding company, the CRA performance record of all banks involved in the merger or acquisition are reviewed in connection with the filing of an application to acquire ownership or control of shares or assets of a bank or to merge with any other financial holding company. An unsatisfactory record can substantially delay, block or impose conditions on the transaction. The Bank received a satisfactory rating on its most recent CRA assessment.

Branching

The Riegle-Neal Interstate Banking and Branching Efficiency Act of 1994, or Riegle-Neal Act, provides that adequately capitalized and managed bank holding companies are permitted to acquire banks in any state. Previously, under the Riegle-Neal Act, a bank’s ability to branch into a particular state was largely dependent upon whether the state “opted in” to de novo interstate branching. Many states did not “opt-in,” which resulted in branching restrictions in those states. The Dodd-Frank Act amended the Riegle-Neal legal framework for interstate branching to permit national banks and state banks to establish branches in any state if that state would permit the establishment of the branch by a state bank chartered in that state. Under current Tennessee law, our bank may open branch offices throughout Tennessee with the prior approval of the TDFI. All branching remains subject to applicable regulatory approval and adherence to applicable legal requirements.

Anti-money laundering and economic sanctions

The USA PATRIOT Act provides the federal government with additional powers to address terrorist threats through enhanced domestic security measures, expanded surveillance powers, increased information sharing and broadened anti-money laundering requirements. By way of amendments to the BSA, the USA PATRIOT Act imposed new requirements that obligate financial institutions, such as banks, to take certain steps to control the risks associated with money laundering and terrorist financing.

Among other requirements, the USA PATRIOT Act and implementing regulations require banks to establish anti-money laundering programs that include, at a minimum:

- internal policies, procedures and controls designed to implement and maintain the bank’s compliance with all of the requirements of the USA PATRIOT Act, the BSA and related laws and regulations;
- systems and procedures for monitoring and reporting of suspicious transactions and activities;
- designated compliance officer;
- employee training;
- an independent audit function to test the anti-money laundering program;

- procedures to verify the identity of each client upon the opening of accounts; and
- heightened due diligence policies, procedures and controls applicable to certain foreign accounts and relationships.

Additionally, the USA PATRIOT Act requires each financial institution to develop a customer identification program ("CIP") as part of the Bank's anti-money laundering program. The key components of the CIP are identification, verification, government list comparison, notice and record retention. The purpose of the CIP is to enable the financial institution to determine the true identity and anticipated account activity of each client. To make this determination, among other things, the financial institution must collect certain information from clients at the time they enter into the client relationship with the financial institution. This information must be verified within a reasonable time through documentary and non-documentary methods. Furthermore, all clients must be screened against any CIP-related government lists of known or suspected terrorists. Financial institutions are also required to comply with various reporting and recordkeeping requirements. The Federal Reserve and the FDIC consider an applicant's effectiveness in combating money laundering, among other factors, in connection with an application to approve a bank merger or acquisition of control of a bank or bank holding company.

Likewise, the U.S. Department of the Treasury's Office of Foreign Assets Control, or OFAC, is responsible for helping to ensure that United States entities do not engage in transactions with the subjects of U.S. sanctions, as defined by various Executive Orders and Acts of Congress. Currently, OFAC administers and enforces comprehensive U.S. economic sanctions programs against certain specified countries/regions. In addition to the country/region-wide sanctions programs, OFAC also administers complete embargoes against individuals and entities identified on OFAC's list of Specially Designated Nationals and Blocked Persons ("SDN List"). The SDN List includes over 7000 parties that are located in many jurisdictions throughout the world, including in the United States and Europe. The Bank is responsible for determining whether any potential and/or existing clients appear on the SDN List or are owned or controlled by a person on the SDN List. If any client appears on the SDN List or is owned or controlled by a person or entity on the SDN List, such client's account must be placed on hold and a blocking or rejection report, as appropriate and if required, must be filed within 10 business days with OFAC. In addition, if a client is a citizen of, has provided an address in, or is organized under the laws of any country or region for which OFAC maintains a comprehensive sanctions program, the Bank must take certain actions with respect to such clients as dictated under the relevant OFAC sanctions program. The Bank must maintain compliance with OFAC by implementing appropriate policies and procedures and by establishing a recordkeeping system that is reasonably appropriate to administer the Bank's compliance program. The Bank has adopted policies, procedures and controls to comply with the BSA, the USA PATRIOT Act and OFAC regulations.

Regulatory enforcement authority

Federal and state banking laws grant substantial enforcement powers to federal and state banking regulators. This enforcement authority includes, among other things, the ability to assess civil money penalties, to issue cease and desist or removal orders and to initiate injunctive actions against banking organizations and "institution-affiliated parties," such as management, employees and agents. In general, these enforcement actions may be initiated for violations of laws, regulations and orders of regulatory authorities, or unsafe or unsound practices. Other actions or inactions, including filing false, misleading or untimely reports with regulatory authorities, may provide the basis for enforcement action. When issued by a banking regulator, cease-and-desist and similar 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 bank 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 regulatory agency.

Federal home loan bank system

The Bank is a member of the Federal Home Loan Bank of Cincinnati, which is one of 12 regional Federal Home Loan Banks ("FHLBs"). Each FHLB serves as a reserve or central bank for its members within its assigned region. It is funded primarily from funds deposited by member institutions and proceeds from the sale of consolidated obligations of the FHLB system. It makes loans to members (i.e., advances) in accordance with policies and procedures established by the board of directors of the FHLB.

As a member of the FHLB of Cincinnati, the Bank is required to own capital stock in the FHLB in an amount generally at least equal to 0.20% (or 20 basis points) of the Bank's total assets at the end of each calendar year, plus 4.5% of its outstanding advances (borrowings) from the FHLB of Cincinnati under the activity-based stock ownership requirement. These requirements are subject to adjustment from time to time. On December 31, 2017, the Bank was in compliance with this requirement.

Privacy and data security

Under the GLBA, federal banking regulators adopted rules limiting the ability of banks and other financial institutions to disclose nonpublic information about consumers to nonaffiliated third parties. The rules require disclosure of privacy policies to consumers and, in some circumstances, allow consumers to prevent disclosure of certain personal information to nonaffiliated third parties. The GLBA also directed federal regulators, including the FDIC, to prescribe standards for the security of consumer information. The Bank is subject to such standards, as well as standards for notifying clients in the event of a security breach.

Consumer laws and regulations

The Bank is also subject to other federal and state consumer laws and regulations that are designed to protect consumers in transactions with banks. While the list set forth below is not exhaustive, these laws and regulations include the Truth in Lending Act, the Truth in Savings Act, the Electronic Funds Transfer Act, the Expedited Funds Availability Act, the Check Clearing for the 21st Century Act, the Fair Credit Reporting Act, the Fair Debt Collection Practices Act, the Equal Credit Opportunity Act, the Fair Housing Act, the Home Mortgage Disclosure Act, the Fair and Accurate Transactions Act, the Servicemembers Civil Relief Act, the Military Lending Act, the Mortgage Disclosure Improvement Act, and the Real Estate Settlement Procedures Act, among others. These laws and regulations mandate certain disclosure requirements and regulate the manner in which financial institutions must deal with consumers when offering consumer financial products and services.

Rulemaking authority for these and other consumer financial protection laws transferred from the prudential regulators to the CFPB on July 21, 2011. In some cases, regulators such as the Federal Trade Commission and the U.S. Department of Justice also retain certain rulemaking or enforcement authority. The CFPB also has broad authority to prohibit unfair, deceptive and abusive acts and practices (“UDAAP”), and to investigate and penalize financial institutions that violate this prohibition. While the statutory language of the Dodd-Frank Act sets forth the standards for acts and practices that violate the prohibition on UDAAP, certain aspects of these standards are untested, and thus it is currently not possible to predict how the CFPB will exercise this authority. In addition, consumer compliance examination authority remains with the prudential regulators for smaller depository institutions ($10 billion or less in total assets).

The Dodd-Frank Act also authorized the CFPB to establish certain minimum standards for the origination of residential mortgages, including a determination of the borrower’s ability to repay. Under the Dodd-Frank Act, financial institutions may not make a residential mortgage loan unless they make a “reasonable and good faith determination” that the consumer has a “reasonable ability” to repay the loan. The act allows borrowers to raise certain defenses to foreclosure but provides a full or partial safe harbor from such defenses for loans that are “qualified mortgages.” On January 10, 2013, the CFPB published final rules to, among other things, specify the types of income and assets that may be considered in the ability-to-repay determination, the permissible sources for verification, and the required methods of calculating the loan’s monthly payments. Since then the CFPB made certain modifications to these rules. The rules extend the requirement that creditors verify and document a borrower’s “income and assets” to include all “information” that creditors rely on in determining repayment ability. The rules also provide further examples of third-party documents that may be relied on for such verification, such as government records and check-cashing or funds-transfer service receipts. The new rules were effective beginning on January 10, 2014. The rules also define “qualified mortgages,” imposing both underwriting standards—for example, a borrower’s debt-to-income ratio may not exceed 43%—and limits on the terms of their loans. Points and fees are subject to a relatively stringent cap, and the terms include a wide array of payments that may be made in the course of closing a loan. Certain loans, including interest-only loans and negative amortization loans, cannot be qualified mortgages.

Other Dodd-Frank Act reforms

Volcker Rule

The Volcker Rule generally prohibits a “banking entity” (which includes any insured depository institution, such as the Bank, or any affiliate or subsidiary of such depository institution, such as the Company) from (i) engaging in proprietary trading and (ii) acquiring or retaining any ownership interest in, sponsoring, or engaging in certain transactions with, a “covered fund”. Both the proprietary trading and covered fund-related prohibitions are subject to a number of exemptions and exclusions. The final regulations contain exemptions for, among others, market making, risk-mitigating hedging, underwriting, and trading in U.S. government and agency obligations and also permit certain ownership interests in certain types of funds to be retained. They also permit the offering and sponsoring of funds under certain conditions. In addition, the final regulations impose significant compliance and reporting obligations on banking entities.

Banking entities were required to conform their proprietary trading activities and investments in and relationships with covered funds that were in place after December 31, 2013 by July 21, 2015. For those banking entities whose investments in and relationships with covered funds were in place prior to December 31, 2013 ("legacy covered funds"), the Volcker Rule conformance period was recently extended by the Federal Reserve to July 21, 2017 for such legacy covered funds. In addition, the Federal Reserve has also indicated its intention to grant two additional one-year extensions of the conformance period to July 21, 2017, for banking entities to conform ownership interests in and sponsorship of activities of collateralized loan obligations, or CLOs, that are backed in part by non-loan assets and that were in place as of December 31, 2013.

Executive compensation and corporate governance

The Dodd-Frank Act requires public companies to include, at least once every three years, a separate non-binding "say on pay" vote in their proxy statement by which shareholders may vote on the compensation of the public company's named executive officers. In addition, if such public companies are involved in a merger, acquisition, or consolidation, or if they propose to sell or dispose of all or substantially all of their assets, shareholders have a right to an advisory vote on any golden parachute arrangements in connection with such transaction (frequently referred to as "say-on-golden parachute" vote). Other provisions of the act may impact our corporate governance. For instance, the act requires the SEC to adopt rules prohibiting the listing of any equity security of a company that does not have an independent compensation committee; and requiring all exchange-traded companies to adopt clawback policies for incentive compensation paid to executive officers in the event of accounting restatements based on material non-compliance with financial reporting requirements.

Future legislative developments

Various legislative acts are from time to time introduced in Congress and the Tennessee legislature. This legislation may change banking statutes and the environment in which we operate in substantial and unpredictable ways. We cannot determine the ultimate effect that potential legislation, if enacted, or implementing regulations and interpretations with respect thereto, would have our financial condition or results of operations.

Available Information

Our website address is www.firstbankonline.com. We file or furnish to the SEC Annual Reports on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K, proxy statements and annual reports to shareholders, and from time to time, amendments to these documents and other documents called for by the SEC. The reports and other documents filed with or furnished to the SEC are available to investors on or through our website at investors.firstbankonline.com under the heading "Stock & Filings" and then under "SEC Filings." These reports are available on our website free of charge as soon as reasonably practicable after we electronically file them with the SEC.

In addition to our website, you may read and copy any of the materials we file with the SEC at the SEC's Public Reference Room at 100 F Street, NE, Washington, DC 20549. You may obtain information on the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0330. The SEC maintains an internet site that contains our reports, proxy and information statements and other information we file electronically with the SEC at www.sec.gov.

ITEM 1A - Risk Factors

Our operations and financial results are subject to various risks and uncertainties, including, but not limited, to the material risks described below. Many of these risks are beyond our control although efforts are made to manage those risks while simultaneously optimizing operational and financial results. The occurrence of any of the following risks, as well as risks of which we are currently unaware or currently deem immaterial, could materially and adversely affect our assets, business, cash flows, condition (financial or otherwise), liquidity, prospects, results of operations and the trading price of our common stock. It is impossible to predict or identify all such factors and, as a result, you should not consider the following factors to be a complete discussion of the risks, uncertainties and assumptions that could materially and adversely affect our assets, business, cash flows, condition (financial or otherwise), liquidity, prospects, results of operations and the trading price of our common stock.

In addition, certain statements in the following risk factors constitute forward-looking statements. Please refer to the section entitled "Cautionary note regarding forward-looking statements" beginning on page 2 of this Annual Report.

Risks related to our business

Our business concentration in Tennessee imposes risks resulting from any regional or local economic downturn affecting Tennessee.

We conduct our banking operations primarily in Tennessee. As of December 31, 2017, approximately 77% of our loans and approximately 88% of our deposits were made to borrowers or received from depositors who live and/or primarily conduct business in Tennessee. Therefore, our success will depend in large part upon the general economic conditions in this area, which we cannot predict with certainty.

This geographic concentration imposes risks from lack of geographic diversification, as adverse economic developments in Tennessee (including the Nashville MSA, our largest market), among other things, could affect the volume of loan originations, increase the level of nonperforming assets, increase the rate of foreclosure losses on loans, reduce the value of our loans and loan servicing portfolio, reduce the value of the collateral securing our loans and reduce the amount of our deposits. Any regional or local economic downturn that affects Tennessee or existing or prospective borrowers, depositors or property values in this area may affect us and our profitability more significantly and more adversely than our competitors whose operations are less geographically concentrated.

We face strong competition from financial services companies and other companies that offer banking services.

We conduct our banking operations primarily in Tennessee, with our largest market being the Nashville MSA, which is a highly competitive banking market. Many of our competitors offer the same, or a wider variety of, banking services within our market areas, and we compete with them for the same customers. These competitors include banks with nationwide operations, regional banks and community banks. In many instances these national and regional banks have greater resources than we do, and the smaller community banks may have stronger ties in local markets than we do, which may put us at a competitive disadvantage. We also face competition from many other types of financial institutions, including thrift institutions, finance companies, brokerage firms, insurance companies, credit unions, mortgage banks and other financial intermediaries. In addition, a number of out-of-state financial institutions have opened offices and solicit deposits in our market areas. Increased competition in our markets may result in reduced loans and deposits, as well as reduced net interest margin and profitability. If we are unable to attract and retain banking customers, we may be unable to continue to grow our loan and deposit portfolios, and our business, financial condition or results of operations may be adversely affected.

Further, a number of larger banks have recently entered the Nashville MSA, and we believe this trend will continue as banks look to gain a foothold in this growing market. This trend will likely result in greater competition in, and may impair our ability to grow our share of, our largest market.

If we do not effectively manage our asset quality and credit risk, we could experience loan losses.

Making any loan involves various risks, including risks inherent in dealing with individual borrowers, risks of nonpayment, risks resulting from uncertainties as to the future value of collateral and cash flows available to service debt, and risks resulting from changes in economic and market conditions. Our credit risk approval and monitoring procedures may fail to identify or reduce these credit risks, and they cannot completely eliminate all credit risks related to our loan portfolio. If the overall economic climate, including employment rates, real estate markets, interest rates and general economic growth, in the United States, generally, or Tennessee (particularly the Nashville MSA), specifically, experiences material disruption, our borrowers may experience difficulties in repaying their loans, the collateral we hold may decrease in value or become illiquid, and the levels of nonperforming loans, charge-offs and delinquencies could rise and require additional provisions for loan losses, which would cause our net income and return on equity to decrease.

Our provision and allowance for credit losses may not be adequate to cover actual credit losses.

We make various assumptions and judgments about the collectability of our loan and lease portfolio and utilize these assumptions and judgments when determining the provision and allowance for credit losses. The determination of the appropriate level of the provision for credit losses inherently involves a high degree of subjectivity and requires us to make significant estimates of current credit risks and future trends, all of which may undergo material changes. Deterioration in economic conditions affecting borrowers, new information regarding existing loans, identification of additional problem loans and other factors, both within and outside of our control, may require an increase in the amount reserved in the allowance for credit losses. In addition, bank regulatory agencies periodically review our provision and the total allowance for credit losses and may require an increase in the allowance for credit losses or future provisions for credit losses, based on judgments different than those of management. Any increases in the provision or allowance for credit losses will result in a decrease in our net income and, potentially, capital, and may have a material adverse effect on our financial condition or results of operations.

Because a significant portion of our loan portfolio is comprised of real estate loans, negative changes in the economy affecting real estate values and liquidity could impair the value of collateral securing our real estate loans and result in loan and other losses.

As of December 31, 2017, approximately 73% of our loan portfolio was comprised of loans with real estate as a primary or secondary component of collateral. This includes collateral consisting of income producing and residential construction properties, which properties tend to be more sensitive to general economic conditions and downturns in real estate markets. As a result, adverse developments affecting real estate values in our market areas could increase the credit risk associated with our real estate loan portfolio. Adverse changes affecting real estate values and the liquidity of real estate in one or more of our markets could increase the credit risk associated with our loan portfolio and could result in losses that would adversely affect credit quality and our financial condition or results of operations. These adverse changes could significantly impair the value of property pledged as collateral to secure the loans and affect our ability to sell the collateral upon foreclosure without a loss or additional losses. If real estate values decline, it is also more likely that we would be required to increase our allowance for loan losses. Thus, declines in the value of real estate collateral could adversely affect our financial condition, results of operations or cash flows.

We are exposed to higher credit risk by commercial real estate, commercial and industrial, and construction based lending.

Commercial real estate, commercial and industrial, and construction based lending usually involves higher credit risks than 1-4 family residential real estate lending. As of December 31, 2017, the following loan types accounted for the stated percentages of our loan portfolio: commercial real estate (both owner-occupied and non-owner occupied) - 33%; commercial and industrial - 23%; and construction - 14%. These loans expose us to greater credit risk than loans secured by other types of collateral because the collateral securing these loans is typically more difficult to liquidate. Additionally, these types of loans also often involve larger loan balances to a single borrower or groups of related borrowers. These higher credit risks are further heightened when the loans are concentrated in a small number of larger borrowers leading to relationship exposure.

Non-owner occupied commercial real estate loans may be affected to a greater extent than residential loans by adverse conditions in real estate markets or the economy because commercial real estate borrowers’ ability to repay their loans depends on successful development of their properties. These loans also involve greater risk because they generally are not fully amortizing over the loan period, and therefore have a balloon payment due at maturity. A borrower’s ability to make a balloon payment typically will depend on being able to either refinance the loan or sell the underlying property in a timely manner. In addition, banking regulators have been giving commercial real estate lending greater scrutiny, and may require banks with higher levels of commercial real estate loans to implement improved underwriting, internal controls, risk management policies and portfolio stress testing, as well as possibly higher levels of allowances for losses and capital levels as a result of commercial real estate lending growth and exposures.

Commercial and industrial loans and owner-occupied commercial real estate loans are typically based on the borrowers’ ability to repay the loans from the cash flow of their businesses. These loans may involve greater risk because the availability of funds to repay each loan depends substantially on the success of the business itself. In addition, the assets securing the loans depreciate over time, are difficult to appraise and liquidate, and fluctuate in value based on the success of the business.

Risk of loss on a construction loan depends largely upon whether our initial estimate of the property’s value at completion of construction or development equals or exceeds the cost of the property construction or development (including interest), the availability of permanent take-out financing and the builder’s ability to sell the property. During the construction or development phase, a number of factors can result in delays and cost overruns. If estimates of value are inaccurate or if actual construction costs exceed estimates, the value of the property securing the loan may be insufficient to ensure full repayment when completed through a permanent loan or by foreclosure on collateral.

Commercial real estate loans, commercial and industrial loans, and construction loans are more susceptible to a risk of loss during a downturn in the business cycle due to the vulnerability of these sectors during a downturn. Our underwriting, review and monitoring cannot eliminate all of the risks related to these loans.

We also make both secured and unsecured loans to our commercial customers. Unsecured loans generally involve a higher degree of risk of loss than secured loans because, without collateral, repayment is wholly dependent upon the success of the borrowers’ businesses. Because of this lack of collateral, we are limited in our ability to collect on defaulted unsecured loans. Further, the collateral that secures our secured commercial and industrial loans typically includes inventory, accounts receivable and equipment, which usually have a value that is insufficient to satisfy the loan without a loss if the business does not succeed.

Our loan concentration in these sectors and their higher credit risk could lead to increased losses on these loans, which could have a material adverse effect on our financial condition, results of operations or cash flows.

We are exposed to higher credit risk due to relationship exposure with a number of large borrowers.

As of December 31, 2017, we had 43 borrowing relationships in excess of $10 million which accounted for approximately 19% of our loan portfolio. While we are not overly dependent on any one of these relationships and while none of these large relationships have directly impacted our allowance for loan losses in the past, a deterioration of any of these large credits could require us to increase our allowance for loan losses or result in significant losses to us, which could have a material adverse effect on our financial condition, results of operations or cash flows.

We make loans to small-to-medium sized businesses that may not have the resources to weather a downturn in the economy.

We make loans to privately-owned businesses, many of which are considered to be small to medium-sized businesses. Small to medium-sized businesses frequently have smaller market share than their competition, may be more vulnerable to economic downturns, often need substantial additional capital to expand or compete and may experience significant volatility in operating results. Any one or more of these factors may impair the borrower's ability to repay a loan. In addition, the success of a small to medium-sized business often depends on the management talents and efforts of one or two persons or a small group of persons, and the death, disability or resignation of one or more of these persons could have a material adverse impact on the business and its ability to repay a loan. Economic downturns, a sustained decline in commodity prices and other events that negatively impact small businesses in our market areas could cause us to incur substantial credit losses that could negatively affect our results of operations or financial condition.

We may be materially and adversely affected by the creditworthiness and liquidity of other financial institutions.

Financial services institutions are interrelated as a result of trading, clearing, counterparty, or other relationships. We have exposure to many different industries and counterparties, and routinely execute transactions with counterparties in the financial services industry, including commercial banks, brokers and dealers, investment banks and other institutional customers. Many of these transactions expose us to credit risk in the event of a default by, or questions or concerns about the creditworthiness of, a counterparty or client, or concerns about the financial services industry generally. In addition, our credit risk may be exacerbated when the collateral held by us cannot be realized upon or is liquidated at prices not sufficient to recover the full amount of the credit or derivative exposure due to us. Any such losses could have a material adverse effect on us.

A lack of liquidity could adversely affect our operations and jeopardize our liquidity, business, financial condition or results of operations.

We rely on our ability to generate deposits and effectively manage the repayment and maturity schedules of our loans and investment securities to ensure that we have adequate liquidity to fund our operations. In addition to our traditional funding sources, we also may borrow funds from third-party lenders or issue equity or debt securities to investors. Our access to funding sources in amounts adequate to finance or capitalize our activities, or on terms that are acceptable to us, could be impaired by factors that affect us directly or the financial services industry or economy in general, such as disruptions in the financial markets or negative views and expectations about the prospects for the financial services industry. Our liquidity may also be adversely impacted if there is a decline in our mortgage revenues from higher prevailing interest rates. Any decline in available funding could adversely impact our ability to originate loans, invest in securities, meet our expenses, pay dividends to our shareholders, or to fulfill obligations such as repaying our borrowings or meeting deposit withdrawal demands, any of which could have a material adverse impact on our liquidity, business, financial condition or results of operations.

We may not be able to meet our unfunded credit commitments, or adequately reserve for losses associated with our unfunded credit commitments.

A commitment to extend credit is a formal agreement to lend funds to a client as long as there is no violation of any condition established under the agreement. The actual borrowing needs of our customers under these credit commitments have historically been lower than the contractual amount of the commitments. A significant portion of these commitments expire without being drawn upon. Because of the credit profile of our customers, we typically have a substantial amount of total unfunded credit commitments, which is not reflected on our balance sheet. Actual borrowing needs of our customers may exceed our expected funding requirements, especially during a challenging economic environment when our client companies may be more dependent on our credit commitments due to the lack of available credit elsewhere, the increasing costs of credit, or the limited availability of financings from other sources. Any failure to meet our unfunded credit commitments in accordance with the actual borrowing needs of our customers may have a material adverse effect on our business, financial condition, results of operations or reputation.

Changes in interest rates could have an adverse impact on our results of operations and financial condition.

Our earnings and financial condition are dependent to a large degree upon net interest income, which is the difference, or spread, between interest earned on loans, securities and other interest-earning assets and interest paid on deposits, borrowings and other interest-bearing liabilities. When market rates of interest change, the interest we receive on our assets and the interest we pay on our liabilities may fluctuate. This may cause decreases in our spread and may adversely affect our earnings and financial condition.

Interest rates are highly sensitive to many factors including, without limitation:

- The rate of inflation;
- Economic conditions;
- Federal monetary policies; and
- Stability of domestic and foreign markets.

Although we have implemented procedures we believe will reduce the potential effects of changes in interest rates on our net interest income, these procedures may not always be successful. Accordingly, changes in levels of market interest rates could materially and adversely affect our net interest income and our net interest margin, asset quality, loan and lease origination volume, liquidity or overall profitability.

If we are unable to grow our noninterest income, our growth prospects will be impaired.

Taking advantage of opportunities to develop new, and expand existing, streams of noninterest income, including our mortgage business, cash management services, investment services and interchange fees, is a part of our long-term growth strategy. If we are unsuccessful in our attempts to grow our noninterest income, especially in light of the expected decline in mortgage revenues, our long-term growth will be impaired. Further, focusing on these noninterest income streams may divert management's attention and resources away from our core banking business, which could impair our core business, financial condition and operating results. We also derive a meaningful amount of our noninterest income from non-sufficient funds and overdraft fees, and such fees are subject to increased regulatory scrutiny, which could result in an erosion of such fees, and as a result, materially impair our future noninterest income.

Our recent results may not be indicative of our future results.

We may not be able to grow our business at the same rate of growth achieved in recent years or even grow our business at all. In the future, we may not have the benefit of several factors that have been favorable to the growth of our business in past years, such as an interest rate environment where changes in rates occur at a relatively orderly and modest pace and the ability to find suitable expansion opportunities and acquisition targets. Numerous factors, such as weakening or deteriorating economic conditions, regulatory and legislative considerations, and competition may impede or restrict our ability to expand our market presence and build our franchise. Even if we are able to grow our business, we may fail to build the infrastructure sufficient to support such growth, suffer loan losses in excess of reserves for such losses or experience other risks associated with growth.

Our future success is largely dependent upon our ability to successfully execute our business strategy.

Our future success, including our ability to achieve our growth and profitability goals, is dependent on the ability of our management team to execute on our long-term business strategy, which requires them to, among other things:

- maintain and enhance our reputation;
- attract and retain experienced and talented bankers in each of our markets;
- maintain adequate funding sources, including by continuing to attract stable, low-cost deposits;
- enhance our market penetration in our metropolitan markets and maintain our leadership position in our community markets;
- improve our operating efficiency;
- implement new technologies to enhance the client experience and keep pace with our competitors;
- identify attractive acquisition targets, close on such acquisitions on favorable terms and successfully integrate acquired businesses;
- attract and maintain business banking relationships with well-qualified businesses, real estate developers and investors with proven track records in our market areas;

- attract sufficient loans that meet prudent credit standards;
- originate conforming residential mortgage loans for resale into secondary markets to provide mortgage banking income;
- maintain adequate liquidity and regulatory capital and comply with applicable federal and state banking laws and regulations;
- manage our credit, interest rate and liquidity risk;
- develop new, and grow our existing, streams of noninterest income;
- oversee the performance of third-party vendors that provide material services to our business; and
- control expenses in line with their current projections.

Failure of management to execute our business strategy could negatively impact our business, growth prospects, financial condition or results of operations. Further, if we do not manage our growth effectively, our business, financial condition, results of operations and future prospects could be negatively affected, and we may not be able to continue to implement our business strategy and successfully conduct our operations.

We follow a relationship-based operating model, and our ability to maintain our reputation is critical to the success of our business.

We are a community bank, and our reputation is one of the most valuable components of our business. As such, we strive to conduct our business in a manner that enhances our reputation. This is done, in part, by recruiting, hiring and retaining bankers and other associates who share our core values of being an integral part of the communities we serve, delivering superior service to our customers and caring about our customers and associates. Further, maintaining our reputation also depends on our ability to protect our brand and associated intellectual property. If our reputation is negatively affected by the actions of our associates or otherwise, our business and, therefore, our operating results may be materially and adversely affected.

We depend on our executive officers and other key individuals to continue the implementation of our long-term business strategy and could be harmed by the loss of their services and our inability to make up for such loss with qualified replacements.

We believe that our continued growth and future success will depend in large part on the skills of our senior management team and our ability to motivate and retain these individuals and other key individuals. The loss of any member of our senior management team could reduce our ability to successfully implement our long-term business strategy, our business could suffer and the value of our common stock could be materially and adversely affected.

The success of our operating model is largely dependent on our ability to attract and retain talented bankers in each of our markets.

We strive to attract and retain talented bankers in each of our markets by fostering an entrepreneurial environment, empowering them with local decision making authority and providing them with sufficient infrastructure and resources to support their growth while also providing management with appropriate oversight. However, the competition for bankers in each of our markets is intense. We compete for talent with both smaller banks that may be able to offer bankers more responsibility, autonomy and local relationships and larger banks that may be able to offer bankers higher compensation, resources and support. As a result, we may not be able to effectively compete for talent across our markets. Further, our bankers may leave us to work for our competitors and, in some instances, may take important banking relationships with them. If we are unable to attract and retain talented bankers in our markets, our business, growth prospects or financial results could be materially and adversely affected.

We may fail to realize all of the anticipated benefits from previously acquired financial institutions or institutions that we may acquire in the future, or those benefits may take longer to realize than expected. We may also encounter significant difficulties in integrating financial institutions that we acquire.

Our ability to realize the anticipated benefits of any acquisition of other financial institutions, bank branches and/or mortgage operations in target markets will depend, to a large extent, on our ability to successfully integrate the acquired businesses. Such an acquisition strategy will involve significant risks, including the following:

- finding suitable markets for expansion;
- finding suitable candidates for acquisition;

- finding suitable financing sources to fund acquisitions;
- attracting and retaining qualified management;
- maintaining adequate regulatory capital;
- obtaining federal and state regulatory approvals; and
- closing on suitable acquisitions on terms that are favorable to us.

The integration and combination of the acquired businesses is a complex, costly and time-consuming process. As a result, we may be required to devote significant management attention and resources to integrating business practices and operations. The integration process may disrupt our business and the business of the acquired bank and, if implemented ineffectively, would restrict the full realization of the anticipated benefits of the acquisition. The failure to meet the challenges involved in integrating acquired businesses and to fully realize the anticipated benefits of acquisitions could adversely impact our business, financial condition or results of operations.

Our lending limit may restrict our growth and prevent us from effectively implementing our business strategy.

We are limited by law in the amount we can loan in the aggregate to a single borrower or related borrowers by the amount of our capital. Tennessee's legal lending limit is intended to prevent one person or a relatively small and economically related group of persons from borrowing an unduly large amount of a bank's funds. It is also intended to safeguard a bank's depositors by diversifying the risk of loan losses among a relatively large number of creditworthy borrowers engaged in various types of businesses. Based upon our capitalization at December 31, 2017, our legal lending limits were approximately $66 million (15% of capital and surplus) and $111 million (25% of capital and surplus). Therefore, based upon our current capital levels, the amount we may lend may be significantly less than that of many of our larger competitors and may discourage potential borrowers who have credit needs in excess of our lending limit from doing business with us. We may accommodate larger loans by selling participations in those loans to other financial institutions, but this strategy may not always be available. In addition to these legally imposed lending limits, we also employ appropriate limits on our overall loan portfolio and requirements with respect to certain types of lending and individual lending relationships. If we are unable to compete effectively for loans from our target customers, we may not be able to effectively implement our business strategy, which could have a material adverse effect on our business, financial condition, results of operations or prospects.

Our funding sources may prove insufficient to support our future growth.

Deposits, cash flows from operations (including from our mortgage business) and investment securities for sale are the primary sources of funds for our lending activities and general business purposes. However, from time to time we also obtain advances from the Federal Home Loan Bank, purchase federal funds, engage in overnight borrowing from the Federal Reserve and correspondent banks and sell loans**.** While we believe our current funding sources to be adequate, our future growth may be severely constrained if we are unable to maintain our access to funding or if adequate financing is not available on acceptable terms to accommodate future growth, which could have a material adverse effect on our financial condition, results of operations or cash flows.

The performance of our investment securities portfolio is subject to fluctuation due to changes in interest rates and market conditions, including credit deterioration of the issuers of individual securities.

Changes in interest rates may negatively affect both the returns on and market value of our investment securities. Interest rate volatility can reduce unrealized gains or increase unrealized losses in our portfolio. Interest rates are highly sensitive to many factors including monetary policies, domestic and international economic and political issues, and other factors beyond our control. Additionally, actual investment income and cash flows from investment securities that carry prepayment risk, such as mortgage-backed securities and callable securities, may materially differ from those anticipated at the time of investment or subsequently as a result of changes in interest rates and market conditions. These occurrences could have a material adverse effect on our net interest income or our results of operations.

Decreased residential mortgage origination volume and pricing decisions of competitors may adversely affect our profitability.

Our mortgage operation originates and sells residential mortgage loans, services residential mortgage loans, and provides third-party origination services to other community banks and mortgage companies. Changes in interest rates, housing prices, applicable government regulations and pricing decisions by our loan competitors may adversely affect demand for our residential mortgage loan products, the revenue realized on the sale of loans, the revenues received from servicing such loans for others and, ultimately, reduce our net income. New regulations, increased regulatory reviews, and/or changes in the structure of the secondary mortgage markets which we utilize to sell mortgage loans may increase costs and make it more difficult to operate a residential mortgage origination business. Our revenue from the mortgage banking business was $116.9 million in 2017. This revenue could significantly decline in future periods if interest rates were to continue rising and the other risks highlighted in this paragraph were realized, which may adversely affect our profitability.

Our mortgage banking profitability could significantly decline if we are not able to originate and resell a high volume of mortgage loans and securities.

Mortgage production, especially refinancing activity, declines in rising interest rate environments. Our mortgage origination volume could be materially and adversely affected by rising interest rates. We expect to see declining origination volume in 2018 across the industry. Moreover, when interest rates increase further, there can be no assurance that our mortgage production will continue at current levels. Further, nearly half of our mortgages are originated through our consumer direct internet delivery channel, which targets national customers. As a result, loan originations through this channel are particularly susceptible to the interest rate environment and the national housing market. Because we sell a substantial portion of the mortgage loans we originate, the profitability of our mortgage banking business also depends in large part on our ability to aggregate a high volume of loans and sell them in the secondary market at a gain. In fact, as rates rise, we expect increasing industry-wide competitive pressures related to changing market conditions to reduce our pricing margins and mortgage revenues generally. If our level of mortgage production declines, our continued profitability will depend upon our ability to reduce our costs commensurate with the reduction of revenue from our mortgage operations. If we are unable to do so, our continued profitability may be materially and adversely affected.

We may incur costs, liabilities, fines and other sanctions if we fail to satisfy our mortgage loan servicing obligations.

We act as servicer for approximately $6.5 billion of mortgage loans owned by third parties as of December 31, 2017. As a servicer for those loans, we have certain contractual obligations to third parties. If we commit a material breach of our obligations as servicer, we may be subject to termination if the breach is not cured within a specified period of time following notice, causing us to lose servicing income. For certain investors and/or transactions, we may be contractually obligated to repurchase a mortgage loan or reimburse the investor for credit losses incurred on the loan as a remedy for origination errors with respect to the loan. If we have increased repurchase obligations because of claims that we did not satisfy our obligations as a servicer, or if we have increased loss severity on such repurchases, we may have a significant reduction to net servicing income within our mortgage banking noninterest income. In addition, we may be subject to fines and other sanctions imposed by federal or state regulators as a result of actual or perceived deficiencies in our foreclosure practices. Any of these actions may harm our reputation or negatively affect our residential lending or servicing business and, as a result, our profitability.

We may be required to repurchase mortgage loans or indemnify buyers against losses in some circumstances.

In 2017, we sold nearly all of the $6.3 billion of mortgage loans held for sale that we originated and purchased. When mortgage loans are sold, whether as whole loans or pursuant to a securitization, we are required to make customary representations and warranties to purchasers, guarantors and insurers about the mortgage loans and the manner in which they were originated. We may be required to repurchase or substitute mortgage loans, or indemnify buyers against losses, in the event we breach certain representations or warranties in connection with the sale of such loans. If repurchase and indemnity demands increase, are valid claims and are in excess of our provision for potential losses, our liquidity, results of operations or financial condition may be materially and adversely affected.

We depend on third-party service providers in the operation of our business.

We depend on a third-party service providers in the operation of our business. In particular, we have engaged one such third party, Cenlar, to provide servicing of our mortgage loan business. In the event that this service provider, or any other third-party service provider that we may use in the future, fails to perform its servicing duties or performs those duties inadequately, we could experience a temporary interruption in collecting principal and interest on mortgage loans, sustain credit losses on our loans or incur additional costs to obtain a replacement servicer. There can be no assurance that a replacement servicer could be retained in a timely manner or at similar rates. Further, our servicing rights could be terminated or we may be required to repurchase mortgage loans or reimburse investors as a result of such failures of our third-party service providers, any of which could adversely affect our reputation, results of operations or financial condition.

We also receive core systems processing, essential web hosting and other Internet systems, deposit processing 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, particularly on a timely basis, our operations could be interrupted. If an interruption were to continue for a significant period of time, our business, financial condition or results of operations could be adversely affected, perhaps materially. Even if we are able to replace third-party service providers, it may be at a higher cost to us, which could adversely affect our business, financial condition or results of operations.

Our risk management framework may not be effective in mitigating risks and/or losses to us.

Our risk management framework is comprised of various processes, systems and strategies, and is designed to manage the types of risk to which we are subject, including, among others, credit, market, liquidity, interest rate and compliance risks. Our framework also includes financial or other modeling methodologies that involve management assumptions and judgment. Our risk management framework may not be effective under all circumstances and may not adequately mitigate any risk or loss to us. If our framework is not effective, we could suffer unexpected losses and our business, financial condition, results of operations or prospects could be materially and adversely affected.

System failure or breaches of our network security, including as a result of cyber-attacks or data security breaches, could subject us to increased operating costs as well as litigation and other liabilities.

The computer systems and network infrastructure we use may be vulnerable to physical theft, fire, power loss, telecommunications failure or a similar catastrophic event, as well as security breaches, denial of service attacks, viruses, worms and other disruptive problems caused by hackers. Any damage or failure that causes breakdowns or disruptions in our client relationship management, general ledger, deposit, loan and other systems could damage our reputation, result in a loss of client business, subject us to additional regulatory scrutiny, or expose us to civil litigation and possible financial liability, any of which could have a material adverse effect on us.

Computer break-ins, phishing and other disruptions could also jeopardize the security of information stored in and transmitted through our computer systems and network infrastructure. Information security risks have generally increased in recent years in part because of the proliferation of new technologies, the use of the internet and telecommunications technologies to conduct financial transactions, and the increased sophistication and activities of organized crime, hackers, terrorists, and other external parties. Our operations rely on the secure processing, transmission and storage of confidential information in our computer systems and networks. Although we believe we have robust information security procedures and controls, our technologies, systems, networks, and our customers' devices may become the target of cyber-attacks or information security breaches that could result in the unauthorized release, gathering, monitoring, misuse, loss or destruction of our or our customers' confidential, proprietary and other information, or otherwise disrupt our or our customers' business operations. As cyber threats continue to evolve, we may be required to expend significant additional resources to continue to modify or enhance our protective measures or to investigate and remediate any information security vulnerabilities.

We are under continuous threat of loss due to hacking and cyber-attacks especially as we continue to expand client capabilities to utilize internet and other remote channels to transact business. While we are not aware of any successful hacking or cyber-attacks into our computer or information technology systems, there can be no assurance that we will not be the victim of successful hacking or cyber-attacks in the future that could cause us to suffer material losses. The occurrence of any cyber-attack or information security breach could result in significant potential liabilities to customers and other third parties, reputational damage, the disruption of our operations and regulatory concerns, all of which could materially and adversely affect our business, financial condition or results of operations.

The financial services industry is undergoing rapid technological changes and, we may not have the resources to implement new technology to stay current with these changes.

The financial services industry is undergoing rapid technological changes with frequent introductions of new technology-driven products and services. In addition to better serving customers, the effective use of technology increases efficiency and enables financial institutions to reduce costs. Our future success will depend in part upon our ability to address the needs of our customers by using technology to provide products and services that will satisfy client demands for convenience as well as to provide secure electronic environments as we continue to grow and expand our market area. Many of our larger competitors have substantially greater resources to invest, and have invested significantly more than us, in technological improvements. As a result, they may be able to offer additional or more convenient products compared to those that we will be able to provide, which would put us at a competitive disadvantage. Accordingly, we may not be able to effectively implement new technology-driven products and services or be successful in marketing such products and services to our customers, which could impair our growth and profitability.

We are subject to certain operational risks, including, but not limited to, client or employee fraud.

Employee errors and employee and client misconduct could subject us to financial losses or regulatory sanctions and seriously harm our reputation. Misconduct by our employees could include hiding unauthorized activities from us, improper or unauthorized activities on behalf of our customers or improper use of confidential information. It is not always possible to prevent employee errors and misconduct, and the precautions we take to prevent and detect this activity may not be effective in all cases. Employee errors could also subject us to financial claims for negligence. We maintain a system of internal controls and insurance coverage to mitigate against these operational risks. If our internal controls fail to prevent or detect an occurrence, or if any resulting loss is not insured or exceeds applicable insurance limits, it could have a material adverse effect on our business, financial condition or results of operations.

In addition, we rely heavily upon information supplied by third parties, including the information contained in credit applications, property appraisals, title information, equipment pricing and valuation and employment and income documentation, in deciding which loans we will originate, as well as the terms of those loans. If any of the information upon which we rely is misrepresented, either fraudulently or inadvertently, and the misrepresentation is not detected prior to asset funding, the value of the asset may be significantly lower than expected, or we may fund a loan that we would not have funded or on terms we would not have extended.

We may need to raise additional capital in the future.

We are required to meet certain regulatory capital requirements and maintain sufficient liquidity. We may need to raise additional capital in the future to provide us with sufficient capital resources and liquidity to meet our commitments and business needs, which could include the possibility of financing acquisitions. Our ability to raise additional capital depends on conditions in the capital markets, economic conditions and a number of other factors, including investor perceptions regarding the banking industry, market conditions, governmental activities, and our financial condition and performance. Accordingly, we may be unable to raise additional capital if needed or on terms acceptable to us. Further, such additional capital could result in dilution to our existing shareholders. If we fail to maintain capital to meet regulatory requirements, our financial condition, liquidity, results of operations, as well as our ability to maintain compliance with regulatory capital requirements, would be materially and adversely affected.

Our FDIC deposit insurance premiums and assessments may increase.

Our deposits are insured by the FDIC up to legal limits and, accordingly, subjects us to the payment of FDIC deposit insurance premiums and assessments. High levels of bank failures since the financial crisis and increases in the statutory deposit insurance limits have increased resolution costs to the FDIC and put significant pressure on the Deposit Insurance Fund. In order to maintain a strong funding position and restore the reserve ratios of the Deposit Insurance Fund following the financial crisis, the FDIC increased deposit insurance assessment rates and charged special assessments to all FDIC-insured financial institutions. Further increases in assessment rates or special assessments may occur in the future, especially if there are significant additional failures of financial institutions. Any future special assessments, increases in assessment rates or required prepayments in FDIC insurance premiums could reduce our profitability or limit our ability to pursue certain business opportunities, which could have a material adverse effect on our assets, business, cash flow, condition (financial or otherwise), liquidity, prospects or results of operations.

Our financial condition may be affected negatively by the costs of litigation.

We may be involved from time to time in a variety of litigation, investigations or similar matters arising out of our business. From time to time, and particularly during periods of economic stress, customers may make claims or otherwise take legal action pertaining to performance of our responsibilities. These claims are often referred to as “lender liability” claims. Whether customer claims and legal action related to the performance of our responsibilities are founded or unfounded, if such claims and legal actions are not resolved in a favorable manner, they may result in significant financial liability and/or adversely affect our market perception, products and services, as well as potentially affecting customer demand for those products and services. In many cases, we may seek reimbursement from our insurance carriers to cover such costs and expenses. Our insurance may not cover all claims that may be asserted against us, and any claims asserted against us, regardless of merit or eventual outcome, may harm our reputation. Should the ultimate judgments or settlements in any litigation or investigation significantly exceed our insurance coverage, they could have a material adverse effect on our business, financial condition or results of operations.

Prior to our initial public offering, we were treated as an S-corporation, and claims of taxing authorities or our former sole shareholder related to our prior status as an S-corporation, could harm us.

Prior to our initial public offering, we were an S-corporation for U.S. federal income tax purposes. While we were an S-corporation, Mr. Ayers, our sole shareholder at the time, was taxed on our income. Following our initial public offering in 2016, our status as an S-corporation was terminated and we became a “C-corporation” under the provisions of the Internal Revenue Code. If the unaudited, open tax years in which we were an S-corporation are audited by the Internal Revenue Service (the “IRS”) and we are determined not to have qualified for, or to have violated, our S-corporation status, we will be obligated to pay back tax, interest and penalties. The amounts that we would be obligated to pay could include tax on all of our taxable income while we were an S-corporation. Any such claims could result in additional costs to us and could have a material adverse effect on our results of operations or financial condition.

In addition, in the event of an adjustment to our reported taxable income for periods prior to termination of our S-corporation status, it is possible that Mr. Ayers would be liable for additional income taxes for those prior periods. Therefore, we entered into a tax sharing agreement with Mr. Ayers. Pursuant to this agreement, upon our filing any tax return (amended or otherwise), in the event of any restatement of our taxable income or pursuant to a determination by, or a settlement with, a taxing authority, for any period during which we were an S-corporation, we may be required to make a payment to Mr. Ayers in an amount equal to Mr. Ayers' incremental tax liability. In addition, we have agreed to indemnify Mr. Ayers with respect to unpaid income tax liabilities to the extent that such unpaid income tax liabilities are attributable to an adjustment to our taxable income for any period after our S-corporation status terminates. In both cases the amount of the payment will be based on the assumption that Mr. Ayers is taxed at the highest rate applicable to individuals for the relevant periods. We will also indemnify Mr. Ayers for any interest, penalties, losses, costs or expenses arising out of any claim under the agreement. Any such payments to or on behalf of Mr. Ayers would result in additional costs to us and could have a material adverse effect on our results of operations or financial condition.

We could be subject to environmental risks and associated costs on our other real estate owned assets.

A significant portion of our loan portfolio is comprised of loans collateralized by real estate. There is a risk that hazardous or toxic waste could be discovered on the properties that secure our loans. If we acquire such properties as a result of foreclosure, we could be held responsible for the cost of cleaning up or removing this waste, and this cost could exceed the value of the underlying properties and materially and adversely affect us.

Risks related to our regulatory environment

The Dodd-Frank Act and related rules and regulations may adversely affect our business, financial condition or results of operations.

The Dodd-Frank Act contains a variety of far-reaching changes and reforms for the financial services industry and directs federal regulatory agencies to study the effects of, and issue implementing regulations for, these reforms. Many of the provisions of the Dodd-Frank Act could have a direct effect on our performance and, in some cases, impact our ability to conduct business. Examples of these provisions include, but are not limited to:

- Increased capital requirements and changes to the quality of capital required to be held by banking organizations;
- Changes to deposit insurance assessments;
- Regulation of proprietary trading;
- Repeal of the federal prohibitions on the payment of interest on demand deposits, thereby permitting depository institutions to pay interest on business transaction and other accounts;
- Establishment of the Consumer Financial Protection Bureau (the "CFPB") with broad authority to implement new consumer protection regulations and, for banks with $10 billion or more in assets, to examine and enforce compliance with federal consumer laws;
- Implementation of risk retention rules for loans (excluding qualified residential mortgages) that are sold by a bank;
- Implementation of annual stress tests for all banks with assets exceeding $10 billion;
- Regulation of debit-card interchange fees; and
- Regulation of lending and the requirements for "qualified mortgages", "qualified residential mortgages" and the assessment of "ability to repay" requirements.

Many of these provisions have already been the subject of proposed and final rules by regulatory authorities. Many other provisions, however, remain subject to regulatory rulemaking and implementation, the effects of which are not yet known. The provisions of the Dodd-Frank Act and any rules adopted to implement those provisions as well as any additional legislative or regulatory changes may impact the profitability of our business, require that we change certain of our business practices, materially affect our business model or affect retention of key personnel, require us to raise additional capital and expose us to additional costs (including increased compliance costs). These and other changes may also require us to invest significant management attention and resources to make any necessary changes and may adversely affect our ability to conduct our business as previously conducted or our financial condition or results of operations.

Monetary policies and economic factors may limit our ability to attract deposits or make loans.

The monetary policies of federal regulatory authorities, particularly the Federal Reserve, and economic conditions in our service area and the United States generally, affect our ability to attract deposits and extend loans. We cannot predict either the nature or timing of any changes in these monetary policies and economic conditions, including the Federal Reserve's interest rate policies, or their impact on our financial performance. Adverse conditions in the economic environment could also lead to a potential decline in deposits and demand for loans, which could have a material and adverse effect on our financial condition, results of operations or cash flows.

As the parent company of FirstBank, the Federal Reserve may require us to commit capital resources to support the Bank.

The Federal Reserve requires us to act as a source of strength to the Bank and to commit capital and financial resources to support the Bank. This support may be required at times when we might otherwise determine not to provide it. In addition, if we commit to a federal bank regulator that we will maintain the capital of the Bank, whether in response to the Federal Reserve's invoking its source-of-strength authority or in response to other regulatory measures, that commitment will be assumed by a bankruptcy trustee and, as a result, the Bank will be entitled to priority payment in respect of that commitment, ahead of our other creditors. Thus, any borrowing that must be done by us in order to support the Bank may adversely impact our cash flow, financial condition, results of operations or prospects.

Federal and state regulators periodically examine our business and may require us to remediate adverse examination findings or may take enforcement action against us.

The Federal Reserve, the FDIC and the TDFI periodically examine our business, including our compliance with laws and regulations. If, as a result of an examination, the Federal Reserve or the TDFI were to determine that our financial condition, capital resources, asset quality, earnings prospects, management, liquidity or other aspects of any of our operations had become unsatisfactory, or that we were in violation of any law or regulation, they may take a number of different remedial actions as they deem appropriate. These actions may include the power to require us to remediate any such adverse examination findings.

In addition, these agencies have the power to take enforcement action against us to enjoin "unsafe or unsound" practices, to require affirmative action to correct any conditions resulting from any violation of law or regulation or unsafe or unsound practice, to issue an administrative order that can be judicially enforced, to direct an increase in our capital, to direct the sale of subsidiaries or other assets, to limit dividends and distributions, to restrict our growth, to assess civil monetary penalties against us or our officers or directors, to remove officers and directors or, if it is concluded that such conditions cannot be corrected or there is an imminent risk of loss to depositors, to terminate our deposit insurance and place us into receivership or conservatorship. Any regulatory enforcement action against us could have a material adverse effect on our assets, business, cash flow, condition (financial or otherwise), liquidity, prospects or results of operations.

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

Federal, state and local laws and regulations have been adopted that are intended to eliminate certain lending practices considered "predatory." The origination of loans with certain terms and conditions and that otherwise meet the definition of a "qualified mortgage" may protect us from liability to a borrower for failing to make the necessary determinations. In either case, we may find it necessary to tighten our mortgage loan underwriting standards in response to applicable regulations, which may constrain our ability to make loans consistent with our business strategies. It is our policy not to make predatory loans and to determine borrowers' ability to repay, but the law and related rules create the potential for increased liability with respect to our lending and loan investment activities. They increase our cost of doing business and, ultimately, may prevent us from making certain loans and cause us to reduce the average percentage rate or the points and fees on loans that we do make, which in turn could have a material adverse effect on our business, cash flow, condition (financial or otherwise), liquidity, prospects or results of operations.

We are subject to numerous fair lending laws designed to protect consumers and failure to comply with these laws could lead to a wide variety of sanctions.

The Equal Credit Opportunity Act, the Fair Housing Act and other fair lending laws and regulations prohibit discriminatory lending practices by financial institutions. The U.S. Department of Justice, federal banking agencies and other federal agencies are responsible for enforcing these laws and regulations. A successful regulatory challenge to an institution's compliance with fair lending laws and regulations could result in a wide variety of sanctions, including damages and civil money penalties, injunctive relief, restrictions on mergers and acquisitions, restrictions on expansion and restrictions on entering new lines of business. Private parties may also have the ability to challenge an institution's performance under fair lending laws in private class action litigation. Such actions could have a material adverse effect on our assets, business, cash flow, condition (financial or otherwise), liquidity, prospects or results of operations.

We could face a risk of noncompliance and enforcement action with the Bank Secrecy Act of 1970 (the "Bank Secrecy Act") and other anti-money laundering statutes and regulations.

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

Risks related to our common stock

We are controlled by James W. Ayers, whose interests in our business may be different than our other shareholders, and, as a "controlled company" within the meaning of the rules of NYSE, our other shareholders will not have the same protections afforded to shareholders of companies that are subject to certain corporate governance requirements.

Mr. Ayers, our Executive Chairman, currently owns approximately 56.3% of our common stock. Further, pursuant to the shareholder's agreement that was entered into with Mr. Ayers in connection with our initial public offering, Mr. Ayers has the right to designate up to a majority of our board of directors. As a result, Mr. Ayers or his nominees to our board of directors will have the ability to control the appointment of our management, the entering into of mergers, material acquisitions and dispositions and other extraordinary transactions and to influence amendments to our charter, bylaws and other corporate governance documents. So long as Mr. Ayers continues to own a majority of our common stock, he will have the ability to control the vote in any election of directors and will have the ability to prevent any transaction that requires shareholder approval regardless of whether others believe the transaction is in our best interests. In any of these matters, the interests of Mr. Ayers may differ from or conflict with the interests of our other shareholders. Moreover, this concentration of stock ownership may also adversely affect the trading price for our common stock to the extent investors perceive disadvantages in owning stock of a company with a controlling shareholder.

In addition, because Mr. Ayers controls a majority of the voting power of our outstanding common stock, we are a "controlled company" within the meaning of the corporate governance standards of NYSE. Under these rules, a company of which more than 50% of the voting power is held by an individual, group or another company is a "controlled company" and may elect not to comply with certain corporate governance requirements, including the requirements that a majority of the board of directors consist of independent directors and the requirements that the executive compensation committee and nominating and corporate governance committee each be comprised entirely of independent directors. We may take advantage of certain of these exemptions for as long as we continue to qualify as a "controlled company," and, historically, we have relied on the exemption that we have a nominating and corporate governance committee. While exempt, we may also choose not to have a majority of independent directors or a compensation committee that consists entirely of independent directors. Accordingly, our shareholders may not have the same protections afforded to shareholders of companies that are subject to all of the corporate governance requirements of NYSE.

Our corporate organization documents contain certain provisions that could have an anti-takeover effect and may delay, make more difficult or prevent an attempted acquisition of us that our shareholders may favor.

Our governing documents and certain agreements to which we are a party contain provisions that make a change-in-control difficult to accomplish, and may discourage a potential acquirer. These include a provision that directors cannot be removed except for cause and a provision that requires the affirmative vote of eighty percent (80%) of the shares outstanding to amend certain provisions of our charter. These anti-takeover provisions may have an adverse effect on the market for our common stock.

We have the ability to incur debt and pledge our assets, including our stock in the Bank, to secure that debt.

Absent special and unusual circumstances, a holder of any indebtedness for borrowed money has rights that are superior to those of holders of any common stock. For example, interest must be paid to the lender before dividends can be paid to any shareholders, and loans must be paid off before any assets can be distributed to any shareholders if we were to liquidate. Further, we would have to make principal and interest payments on our indebtedness, which could reduce our profitability or result in net losses on a consolidated basis even if the Bank were profitable.

The price of our common stock could be volatile.

The market price of our common stock may be volatile and could be subject to wide fluctuations in price in response to various factors, some of which are beyond our control. In addition, if the market for stocks in our industry, or the stock market in general, experiences a loss of investor confidence, the trading price of our common stock could decline for reasons unrelated to our business, financial condition or results of operations. If any of the foregoing occurs, it could cause our stock price to fall and may expose us to lawsuits that, even if unsuccessful, could be costly to defend and a distraction to management which could materially adversely affect our business, financial condition or results of operations.

Future sales of our common stock or securities convertible into our common stock may dilute our shareholders' ownership in us and may adversely affect us or the market price of our common stock.

We are generally not restricted from issuing additional shares of our common stock up to the authorized number of shares set forth in our charter. We may issue additional shares of our common stock or securities convertible into our common stock in the future pursuant to current or future employee stock option plans, employee stock grants, upon exercise of warrants or in connection with future acquisitions or financings. In addition, Mr. Ayers has registration rights that allow him to sell additional shares of common stock in subsequent offerings. We cannot predict the size of any such future issuances or the effect, if any, that any such future issuances will have on the trading price of our common stock. Any such future issuances of shares of our common stock or securities convertible into common stock may have a dilutive effect on the holders of our common stock and could have a material negative effect on the trading price of our common stock.

Future sales of our common stock in the public market could lower our share price, and any additional capital raised by us through the sale of equity or convertible debt securities may dilute our shareholders ownership in us and may adversely affect us or the market price of our common stock.

We or Mr. Ayers, may sell additional shares of common stock in subsequent public offerings. We may also issue additional shares of common stock or convertible securities to finance future acquisitions. We cannot predict the size of future issuances of our common stock or the effect, if any, that future issuances and sales of our common stock will have on the market price of our common stock. Sales of substantial amounts of our common stock (including sales that may occur pursuant to registration rights and shares that may be issued in connection with acquisitions), or the perception that such sales could occur, may adversely affect prevailing market prices for our common stock.

Applicable laws and regulations restrict both the ability of the Bank to pay dividends to us and our ability to pay dividends to our shareholders.

We and the Bank are subject to various regulatory restrictions relating to the payment of dividends. In addition, the Federal Reserve has the authority to prohibit bank holding companies from engaging in unsafe or unsound practices in conducting their business. These federal and state laws, regulations and policies are described in greater detail in "Business: Supervision and regulation: Bank regulation: Bank dividends" and "Business: Supervision and regulation: Holding company regulation: Restriction on bank holding company dividends," and generally consider previous results and net income, capital needs, asset quality, existence of enforcement or remediation proceedings, and overall financial condition in determining whether a dividend payment is appropriate. For the foreseeable future, the majority, if not all, of our revenue will be from any dividends paid to us by the Bank. Accordingly, our ability to pay dividends also depends on the ability of the Bank to pay dividends to us. Further, the present and future dividend policy of the Bank is subject to the discretion of its board of directors. We cannot guarantee that we or the Bank will be permitted by financial condition or applicable regulatory restrictions to pay dividends, that the board of directors of the Bank will elect to pay dividends to us, or the timing or amount of any dividend actually paid. See "Dividend policy." If we do not pay dividends, market perceptions of our common stock may be adversely affected, which could in turn create downward pressure on our stock price.

We identified a material weakness in our internal control over financial reporting related to reconciliations of our mortgage loans held for sale and related clearing accounts in the year ended December 31, 2016 and if we are unable to establish and maintain effective internal controls in accordance with Section 404 of the Sarbanes-Oxley Act of 2002 (the "Sarbanes-Oxley Act") it could have a material adverse effect on our business and stock price.

We are required to comply with the SEC's rules implementing Section 302 and 404 of the Sarbanes-Oxley Act, that require management to certify financial and other information in our quarterly and annual reports and, beginning with this Annual Report on Form 10-K, provide an annual management report on the effectiveness of control over financial reporting. Pursuant to the Jumpstart Our Business Startups Act (the "JOBS Act"), our independent registered public accounting firm will not be required to attest to the effectiveness of our internal control over financial reporting until the later of the year following our first annual report required to be filed with the SEC or the date we are no longer an emerging growth company, which may be up to five full fiscal years following our initial public offering.

In connection with the preparation of our consolidated financial statements in our Annual Report on Form 10-K for the year ended December 31, 2016, our management determined that as of December 31, 2016, we had a material weakness in our internal control over financial reporting resulting from deficiencies around the recording of mortgage banking transactions and reconciliations of mortgage loans held for sale and related clearing accounts on a timely basis. A "material weakness" is a deficiency, or a combination of deficiencies, in internal control over financial reporting such that there is a reasonable possibility that a material misstatement of our annual or interim financial statements will not be prevented or detected on a timely basis. Specifically, we did not have effective processes and procedures in place to ensure that all transactions involving the origination, purchase, transfer or sales of our mortgage loans held for sale were properly recorded and reflected on our financial statements and, as a result, failed to properly record certain transactions in the proper interim periods in 2016. While this deficiency did not result in a restatement of any previously reported interim consolidated financial statements for 2016, our management concluded there was a reasonable possibility that a material misstatement of the Company's annual or interim financial statements might not be prevented or detected on a timely basis. See "Controls and Procedures" included in Item 9A of our Annual Report on Form 10-K for the year ended December 31, 2016 for a further discussion of this material weakness. Our management believes that the conversion to the system, which was completed during 2016, and the revised policies and procedures for reconciling applicable accounts put in place during 2016 have been sufficient to remediate this material weakness. As of December 31, 2017, management considers the material weakness to be remediated based on their evaluation of the controls.

While we believe that we have taken appropriate steps to remediate the material weakness, we cannot be certain that other material weaknesses and control deficiencies will not be discovered in the future. If additional material weaknesses or significant deficiencies in our internal control over financial reporting are discovered or occur in the future, our consolidated financial statements may contain material misstatements and we could be required to restate our financial results. In addition, if additional material weaknesses or significant deficiencies in our internal control over financial reporting are discovered or occur in the future, or if we are unable to produce accurate and timely financial statements, our stock price may be adversely affected and we may be unable to maintain compliance with applicable stock exchange listing requirements.

We are an emerging growth company, and we cannot be certain if the reduced disclosure requirements applicable to emerging growth companies will make our common stock less attractive to investors.

We are an "emerging growth company," as defined in the JOBS Act, and we intend to take advantage of certain exemptions from various regulatory and reporting requirements that are applicable to public companies that are emerging growth companies, including, but not limited to, exemptions from being required to comply with the auditor attestation requirements of Section 404 of the Sarbanes-Oxley Act, reduced disclosure obligations regarding executive compensation in our periodic reports and proxy statements, and exemptions from the requirements of holding a nonbinding advisory vote on executive compensation and shareholder approval of any golden parachute payments not previously approved. In addition, even if we comply with the greater obligations of public companies that are not emerging growth companies, we may avail ourselves of the reduced requirements applicable to emerging growth companies from time to time in the future, so long as we are an emerging growth company. We will remain an emerging growth company for up to five years, though we will cease to be an emerging growth company earlier if we have more than $1 billion in annual gross revenues, have more than $700 million in market value of our common stock held by non-affiliates, or issue more than $1 billion of non-convertible debt in a three-year period. Investors and securities analysts may find it more difficult to evaluate our common stock because we will rely on one or more of these exemptions and, as a result, investor confidence or the market price of our common stock may be materially and adversely affected.

Securities that we issue, including our common stock, are not FDIC insured.

Securities that we issue, including our common stock, are not savings or deposit accounts or other obligations of any bank, insured by the FDIC, any other governmental agency or instrumentality, or any private insurer, and are subject to investment risk, including the possible loss of our shareholders' investments.

ITEM 1B - Unresolved Staff Comments

None.

ITEM 2 - Properties

Our principal executive offices and FirstBank's main office are located at 211 Commerce Street, Suite 300, Nashville, Tennessee 37201. We currently operate 56 full-service bank branches and 9 other banking locations throughout our geographic market areas as well as 18 mortgage offices throughout the southeastern United States. We have banking locations in the metropolitan markets of Nashville, Chattanooga, Knoxville, Memphis, Jackson (TN) and Huntsville (AL) in addition to 12 community markets. See "ITEM 1. Business – Our Markets" for more detail. We own 44 of these banking locations and lease our other banking locations, nearly all of our mortgage offices and our principal executive office. We believe that our offices and banking locations are in good condition, are suitable to our needs and, for the most part, are relatively new or refurbished.

ITEM 3 - Legal Proceedings

Various legal proceedings to which FB Financial Corporation or a subsidiary of FB Financial Corporation is party arise from time to time in the normal course of business. As of the date hereof, there are no material pending legal proceedings to which FB Financial Corporation or any of its subsidiaries is a party or of which any of its or its subsidiaries' assets or properties are subject.

ITEM 4 - Mine Safety Disclosures

Not applicable.

PART II

ITEM 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities.

Market Information and Holders of Record

FB Financial Corporation's common stock is traded on the New York Stock Exchange under the symbol "FBK" and has traded on that market since September 16, 2016. Prior to that time, there was no established public trading market for our stock.

The following table shows the high and low sales price information for the Company's common stock for each full quarter in 2017 and 2016 as reported on the New York Stock Exchange.

	Price per share of common stock	
	High	Low
2017		
First quarter	$ 35.50	$ 23.71
Second quarter	$ 38.59	$ 32.49
Third quarter	$ 38.24	$ 32.84
Fourth quarter	$ 44.81	$ 37.91
2016		
First quarter	N/A	N/A
Second quarter	N/A	N/A
Third quarter	$ 21.27	$ 20.00
Fourth quarter	$ 26.45	$ 19.81

The Company had approximately 735 stockholders of record as of March 12, 2018.

Stock Performance Graph

The performance graph and table below compares the cumulative total stockholder return on the common stock of the Company with the cumulative total return on the equity securities included in the Standard & Poor's 500 Index (S&P 500), which reflects overall stock market performance and the KBW Bank Index, which is a modified cap-weighted index consisting of 24 exchange-listed National Market stocks. The graph assumes an initial $100 investment on December 30, 2016 through December 29, 2017. Data for the S&P 500 and KBW Regional Bank Index assumes reinvestment of dividends. Returns are shown on a total return basis. The performance graph represents past performance and should not be considered to be an indication of future performance. The information in this paragraph and the following stock performance graph shall not be deemed to be "soliciting material" or to be "filed" with the SEC or subject to Regulation 14A or 14C, other than as provided in Item 201 of Regulation S-K, or to the liabilities of Section 18 of the Exchange Act, except to the extent that we specifically request that such information be treated as soliciting material or specifically incorporate it by reference into a filing under the Securities Act or the Exchange Act.

	Index		
	FB Financial Corporation	S&P 500 Total Return Index	KBW Bank Total Return Index
12/30/2016	100.00	100.00	100.00
1/27/2017	99.00	102.60	101.23
2/24/2017	124.20	106.09	104.71
3/24/2017	121.89	105.20	99.33
4/21/2017	135.49	105.54	98.17
5/19/2017	145.90	107.24	98.77
6/16/2017	139.88	109.74	103.00
7/14/2017	133.95	111.05	105.96
8/11/2017	127.17	110.40	103.39
9/8/2017	131.25	111.51	99.59
10/6/2017	146.47	115.67	111.44
11/3/2017	156.72	117.50	113.15
12/1/2017	165.28	120.25	116.19
12/31/2017	161.81	121.83	118.59

Dividend Policy

Prior to our initial public offering, we were an S corporation for U.S. federal income tax purposes. As an S Corporation, we historically made distributions to our sole shareholder to provide him with funds to pay U.S. federal income tax on our taxable income that was "passed through" to him. We also historically paid additional dividends to our shareholder as a return on his investment from time to time. Following our initial public offering and after our conversion to a C corporation, our dividend policy and practice changed, and we will no longer pay distributions to provide our shareholders with funds to pay U.S. federal income tax on their pro rata portion of our taxable income.

We currently intend to retain our future earnings, if any, to fund the development and growth of our business, and we currently do not anticipate paying any dividends to the holders of our common stock. Any future determination relating to our dividend policy will be made by our board of directors and will depend on a number of factors, including general and economic conditions, industry standards, our financial condition and operating results, our available cash and current and anticipated cash needs, capital requirements, banking regulations, contractual, legal, tax and regulatory restrictions and implications on the payment of dividends by us to our shareholders or by the Bank to us, and such other factors as our board of directors may deem relevant.

The following table shows the dividends that have been declared on our common stock with respect to the periods indicated below. Per share amounts are presented to the nearest cent.

(dollars in thousands, except share amounts and per share data) Quarterly period		Amount per share		Total cash dividend
First Quarter 2016	$	0.29	$	5,000
Second Quarter 2016	$	0.25	$	4,300
Third Quarter 2016	$	3.49	$	60,000
Fourth Quarter 2016	$	—	$	—
First Quarter 2017	$	—	$	—
Second Quarter 2017	$	—	$	—
Third Quarter 2017	$	—	$	—
Fourth Quarter 2017	$	—	$	—

As a bank holding company, any dividends paid by us are subject to various federal and state regulatory limitations and also may be subject to the ability of the Bank to make distributions or pay dividends to us. The Bank is also subject to various legal, regulatory and other restrictions on its ability to pay dividends and make other distributions and payments to us. Our ability to pay dividends is limited by minimum capital and other requirements prescribed by law and regulation. Furthermore, we are generally prohibited under Tennessee corporate law from making a distribution to a shareholder to the extent that, at the time of the distribution, after giving effect to the distribution, we would not be able to pay our debts as they become due in the usual course of business or our total assets would be less than the sum of its total liabilities plus (unless the charter permits otherwise) the amount that would be needed, if we were to be dissolved at the time of the distribution, to satisfy the preferential rights upon dissolution of any shareholders who may have preferential rights superior to those receiving the distribution. In addition, financing arrangements that we may enter into in the future may include restrictive covenants that may limit our ability to pay dividends.

Sale of Equity Securities and Use of Proceeds

Initial Public Offering

On September 15, 2016, our registration statement on Form S-1 (Registration No. 333-213210) was declared effective by the SEC for our underwritten initial public offering in which we sold a total of 6,764,704 shares of our common stock at a price to the public of $19.00 per share. J.P. Morgan Securities LLC, UBS Securities LLC, and Keefe, Bruyette & Woods, Inc., acted as the joint book-running managers for the offering, and Raymond James & Associates, Inc., Sandler O'Neill & Partners, L.P., and Stephens Inc. acted as co-managers.

The offering commenced on September 15, 2016 and closed on September 21, 2016. All of the shares registered pursuant to the registration statement were sold at an aggregate offering price of $128.5 million. We received net proceeds of approximately $115.5 million after deducting underwriting discounts and commissions of $9.0 million and other offering expenses of $4.0 million. No payments with respect to expenses were made by us to directors, officers or persons owning ten percent or more of either class of our common stock or to their associates, or to our affiliates. However, $55.0 million of the net proceeds from the offering were used to fund a cash distribution to James W. Ayers, our majority shareholder and executive chairman, which was intended to be non-taxable to Mr. Ayers, and $10.1 million of the net proceeds from the offering were used to fund the repayment of all amounts outstanding under our subordinated notes held by Mr. Ayers. During the third quarter of 2017, approximately $7.8 million was used to fund the merger with the Clayton Banks. Remaining proceeds of approximately $27.1 million from the offering remain in interest bearing deposits in other financial institutions and may be used to support our growth, including to fund our organic growth and implement our strategic initiatives, which may include the potential expansion of our business through opportunistic acquisitions of depository institutions and other complementary businesses, and selective acquisitions of assets, deposits and branches that we believe present attractive risk-adjusted returns or provide a strategic benefit to our growth strategy, for working capital and for other general corporate purposes, and to strengthen our regulatory capital. There has been no material change in the planned use of proceeds from our initial public offering as described in our prospectus filed with the SEC on September 19, 2016 pursuant to Rule 424(b)(4) under the Securities Act.

Private Placement

As previously reported in our Current Report on Form 8-K that was filed with the SEC on May 26, 2017, we sold 4,806,710 shares of our common stock (the "Private Placement Shares") to accredited investors in a private placement that closed on June 1, 2017. We received net proceeds of approximately $152.7 million from the sale of the Private Placement Shares after deducting placement agent fees of approximately $5.5 million and other offering expenses of approximately $0.4 million. The net proceeds were used to fund a portion of the payment of approximately $184.2 million cash consideration to Clayton HC, Inc. in connection with our acquisition of Clayton Bank and Trust and American City Bank, which closed on July 31, 2017. The Private Placement Shares were not registered under the Securities Act in reliance on the exemption from registration in Section 4(a)(2) of the Securities Act and Regulation D promulgated under the Securities Act.

ITEM 6 - Selected Financial Data

The following selected historical consolidated financial data of the Company should be read in conjunction with, and are qualified by reference to, “Management’s discussion and analysis of financial condition and results of operations” and the consolidated financial statements and notes thereto included elsewhere herein. Our historical results for any prior period are not necessarily indicative of results to be expected in any future period.

	As of or for the year ended December 31,				
	2017	2016	2015	2014	2013
Statement of Income Data					
Total interest income	$ 169,613	$ 120,494	$ 102,782	$ 92,889	$ 87,082
Total interest expense	16,342	9,544	8,910	9,513	11,606
Net interest income	153,271	110,950	93,872	83,376	75,476
Provision for loan losses	(950)	(1,479)	(3,064)	(2,716)	(1,519)
Total noninterest income	141,581	144,685	92,380	50,802	41,386
Total noninterest expense	222,317	194,790	138,492	102,163	89,584
Net income before income taxes	73,485	62,324	50,824	34,731	28,797
Income tax expense	21,087	21,733	2,968	2,269	1,894
Net income	52,398	40,591	47,856	32,462	26,903
Net interest income (tax—equivalent basis)	156,094	113,311	95,887	85,487	77,640
Per Common Share					
Basic net income	1.90	2.12	2.79	1.89	1.57
Diluted net income	1.86	2.10	2.79	1.89	1.57
Book value(1)	19.54	13.71	13.78	12.53	11.04
Tangible book value(5)	14.56	11.58	10.66	9.59	8.01
Pro Forma Statement of Income and Per Common Share Data(4)					
Pro forma provision for income tax	21,087	22,902	17,829	12,375	10,185
Pro forma net income	52,398	39,422	32,995	22,356	18,612
Pro forma net income per common share—basic	1.90	2.06	1.92	1.30	1.08
Pro forma net income per common share—diluted	1.86	2.04	1.92	1.30	1.08
Selected Balance Sheet Data					
Cash and due from banks	29,831	50,157	53,893	40,093	41,943
Loans held for investment	3,166,911	1,848,784	1,701,863	1,415,896	1,341,347
Allowance for loan losses	(24,041)	(21,747)	(24,460)	(29,030)	(32,353)
Loans held for sale	526,185	507,442	273,196	194,745	61,062
Available-for-sale securities, fair value	543,992	582,183	649,387	652,601	685,547
Other real estate owned, net	16,442	7,403	11,641	7,259	8,796
Total assets	4,727,713	3,276,881	2,899,420	2,428,189	2,258,387
Customer deposits	3,578,694	2,670,031	2,432,843	1,918,635	1,803,567
Brokered and internet time deposits	85,701	1,531	5,631	4,934	5,579
Total deposits	3,664,395	2,671,562	2,438,474	1,923,569	1,803,567
Borrowings	333,302	194,892	74,616	143,850	137,861
Total shareholders' equity	596,729	330,498	236,674	215,228	189,687
Selected Ratios					
Return on average:					
Assets(2)	1.37%	1.35%	1.86%	1.40%	1.22%
Shareholders' equity(2)	11.24%	14.68%	20.91%	15.94%	13.98%
Average shareholders' equity to average assets	12.23%	9.22%	8.88%	8.81%	8.73%
Net interest margin (tax-equivalent basis)	4.46%	4.10%	3.97%	3.93%	3.75%
Efficiency ratio	75.40%	76.20%	74.36%	76.14%	76.66%
Adjusted efficiency ratio (tax-equivalent basis)(5)	67.31%	70.59%	73.10%	73.93%	75.24%
Loans held for investment to deposit ratio	86.42%	69.20%	69.79%	73.61%	74.37%
Yield on interest-earning assets	4.93%	4.45%	4.34%	4.37%	4.31%
Cost of interest-bearing liabilities	0.66%	0.48%	0.49%	0.56%	0.70%
Cost of total deposits	0.42%	0.29%	0.30%	0.36%	0.48%
Pro Forma Selected Ratios					
Pro forma return on average assets(2)(4)	1.37%	1.31%	1.28%	0.97%	0.84%
Pro forma return on average equity(2)(4)	11.24%	14.25%	14.47%	10.98%	9.67%
Credit Quality Ratios					
Allowance for loan losses to loans, net of unearned income	0.76%	1.18%	1.50%	2.05%	2.41%
Allowance for loan losses to nonperforming loans	238.10%	216.22%	211.10%	168.75%	113.83%
Nonperforming loans to loans, net of unearned income	0.32%	0.54%	0.68%	1.21%	2.12%
Capital Ratios (Company)					
Shareholders' equity to assets	12.62%	10.09%	8.16%	8.86%	8.40%
Tier 1 capital (to average assets)	10.46%	10.05%	7.64%	8.10%	7.97%
Tier 1 capital (to risk-weighted assets)(3)	11.43%	12.19%	9.58%	11.32%	11.47%
Total capital (to risk-weighted assets)(3)	12.01%	13.03%	11.15%	13.18%	13.41%
Tangible common equity to tangible assets(5)	9.72%	8.65%	6.43%	6.93%	6.24%
Common Equity Tier 1 (to risk-weighted assets) (CET1)(3)	10.71%	11.04%	8.23%	N/A	N/A
Capital Ratios (Bank)					
Shareholders' equity to assets	12.61%	9.94%	9.17%	10.09%	9.73%
Tier 1 capital (to average assets)	9.77%	8.95%	7.65%	8.10%	7.98%
Tier 1 capital (to risk-weighted assets)(3)	10.72%	10.88%	9.63%	11.34%	11.54%
Total capital to (risk-weighted assets)(3)	11.30%	11.72%	11.02%	12.96%	13.20%
Common Equity Tier 1 (to risk-weighted assets) (CET1)(3)	10.72%	10.88%	9.63%	N/A	N/A

(1) Book value per share equals our total shareholders’ equity as of the date presented divided by the number of shares of our common stock outstanding as of the date presented. The

number of shares of our common stock outstanding was 30,535,517 and 24,107,660 as of December 31, 2017 and 2016, respectively, and 17,180,000 as of December 31, 2015, 2014 and 2013.

(2) We have calculated our return on average assets and return on average equity for a period by dividing net income for that period by our average assets and average equity, as the case may be, for that period. We have calculated our pro forma return on average assets and pro forma return on average equity for a period by calculating our pro forma net income for that period as described in footnote 4 below and dividing that by our average assets and average equity, as the case be, for that period. We calculate our average assets and average equity for a period by dividing the sum of our total asset balance or total stockholder's equity balance, as the case may be, as of the close of business on each day in the relevant period and dividing by the number of days in the period.

(3) We calculate our risk-weighted assets using the standardized method of the Basel III Framework as of December 31, 2017, 2016 and 2015 and the Basel II Framework for all previous periods, as implemented by the Federal Reserve and the FDIC.

(4) We have calculated our pro forma net income, pro forma net income per share, pro forma returns on average assets and pro forma return on average equity for each period shown by calculating a pro forma provision for federal income tax using a combined effective income tax rate of 36.75%, 35.08% 35.63% and 35.37% for the years ended December 31, 2016, 2015, 2014 and 2013, respectively, and adjusting our historical net income for each period to give effect to the pro forma provision for U.S. federal income tax for such period.

(5) These measures are not measures recognized under generally accepted accounting principles (United States) ("GAAP"), and are therefore considered to be non-GAAP financial measures. See "GAAP reconciliation and management explanation of non-GAAP financial measures" for a reconciliation of these measures to their most comparable GAAP measures.

GAAP reconciliation and management explanation of non-GAAP financial measures

We identify certain of the financial measures discussed in our selected historical consolidated financial data as being "non-GAAP financial measures." In accordance with the SEC's rules, we classify a financial measure as being a non-GAAP financial measure if that financial measure excludes or includes amounts, or is subject to adjustments that have the effect of excluding or including amounts, that are included or excluded, as the case may be, in the most directly comparable measure calculated and presented in accordance with generally accepted accounting principles as in effect from time to time in the United States in our statements of income, balance sheets or statements of cash flows.

The non-GAAP financial measures that we discuss in our selected historical consolidated financial data should not be considered in isolation or as a substitute for the most directly comparable or other financial measures calculated in accordance with GAAP. Moreover, the manner in which we calculate the non-GAAP financial measures that we discuss in our selected historical consolidated financial data may differ from that of other companies reporting measures with similar names. You should understand how such other banking organizations calculate their financial measures similar or with names similar to the non-GAAP financial measures we have discussed in our selected historical consolidated financial data when comparing such non-GAAP financial measures. The following reconciliation tables provide a more detailed analysis of these, and reconciliation for, each of non-GAAP financial measures

Adjusted efficiency ratio

The adjusted efficiency ratio is a non-GAAP measure that excludes securities gains (losses), merger-related and conversion expenses, one time IPO equity grants and other selected items. Our management uses this measure in its analysis of our performance. Our management believes this measure provides a greater understanding of ongoing operations and enhances comparability of results with prior periods, as well as demonstrates the effects of significant gains and charges. The most directly comparable financial measure calculated in accordance with GAAP is the efficiency ratio.

The following table presents, as of the dates set forth below, the calculation of our efficiency ratio on a tax-equivalent basis.

	Year ended December 31,				
(dollars in thousands, except per share data)	**2017**	**2016**	**2015**	**2014**	**2013**
Adjusted efficiency ratio (tax-equivalent basis)					
Total noninterest expense	$ 222,317	$ 194,790	$ 138,492	$ 102,163	$ 89,584
Less vesting of one time equity grants	—	2,960	—	3,000	—
Less variable compensation charge related to cash settled equity awards previously issued	635	1,254	—	—	—
Less merger and conversion expenses	19,034	3,268	3,543	—	—
Less impairment of MSRs	—	4,678	194	—	—
Less loss on sale of MSRs	249	4,447	—	—	—
Adjusted noninterest expense	$ 202,399	$ 178,183	$ 134,755	$ 99,163	$ 89,584
Net interest income (tax-equivalent basis)	$ 156,094	$ 113,311	$ 95,887	$ 85,487	$ 77,640
Total noninterest income	141,581	144,685	92,380	50,802	41,386
Less bargain purchase gain	—	—	2,794		
Less change in fair value on MSRs	(3,424)	—	—	—	—
Less gain on sales of other real estate	774	1,282	(317)	132	—
Less (loss) gain on other assets	(664)	(103)	(393)	19	(67)
Less gain on securities	285	4,407	1,844	2,000	34
Adjusted noninterest income	$ 144,610	$ 139,099	$ 88,452	$ 48,651	$ 41,419
Adjusted operating revenue	$ 300,704	$ 252,410	$ 184,339	$ 134,138	$ 119,059
Efficiency ratio (GAAP)	75.40%	76.20%	74.36%	76.14%	76.66%
Adjusted efficiency ratio (tax-equivalent basis)	67.31%	70.59%	73.10%	73.93%	75.24%

Tangible book value per common share and tangible common equity to tangible assets

Tangible book value per common share and tangible common equity to tangible assets are non-GAAP measures that exclude the impact of goodwill and other intangibles used by the Company's management to evaluate capital adequacy. Because intangible assets such as goodwill and other intangibles vary extensively from company to company, we believe that the presentation of this information allows investors to more easily compare the Company's capital position to other companies. The most directly comparable financial measure calculated in accordance with GAAP is book value per common share and our total shareholders' equity to total assets.

The following table presents, as of the dates set forth below, tangible common equity compared with total shareholders' equity, tangible book value per common share compared with our book value per common share and common equity to tangible assets compared to total shareholders' equity to total assets:

	As of December 31,				
(dollars in thousands, except per share data)	**2017**	**2016**	**2015**	**2014**	**2013**
Tangible Assets					
Total assets	$ 4,727,713	$ 3,276,881	$ 2,899,420	$ 2,428,189	$ 2,258,387
Adjustments:					
Goodwill	(137,190)	(46,867)	(46,904)	(46,904)	(46,904)
Core deposit and other intangibles	(14,902)	(4,563)	(6,695)	(3,495)	(5,108)
Tangible assets	$ 4,575,621	$ 3,225,451	$ 2,845,821	$ 2,377,790	$ 2,206,375
Tangible Common Equity					
Total shareholders' equity	$ 596,729	$ 330,498	$ 236,674	$ 215,228	$ 189,687
Adjustments:					
Goodwill	(137,190)	(46,867)	(46,904)	(46,904)	(46,904)
Core deposit and other intangibles	(14,902)	(4,563)	(6,695)	(3,495)	(5,108)
Tangible common equity	$ 444,637	$ 279,068	$ 183,075	$ 164,829	$ 137,675
Common shares outstanding	30,535,517	24,107,660	17,180,000	17,180,000	17,180,000
Book value per common share	$ 19.54	$ 13.71	$ 13.78	$ 12.53	$ 11.04
Tangible book value per common share	14.56	11.58	10.66	9.59	8.01
Total shareholders' equity to total assets	12.62%	10.09%	8.16%	8.86%	8.40%
Tangible common equity to tangible assets	9.72%	8.65%	6.43%	6.93%	6.24%

ITEM 7 – Management's discussion and analysis of financial condition and results of operations

The following is a discussion of our financial condition at December 31, 2017 and 2016 and our results of operations for each of the three years in the three year period ended December 31, 2017, and should be read in conjunction with our audited consolidated financial statements included elsewhere herein. This discussion and analysis contains forward-looking statements that are subject to certain risks and uncertainties and are based on certain assumptions that we believe are reasonable but may prove to be inaccurate. Certain risks, uncertainties and other factors, including those set forth in the "Cautionary note regarding forward-looking statements" and "Risk Factors" sections of this Annual Report, may cause actual results to differ materially from those projected results discussed in the forward-looking statements appearing in this discussion and analysis. We assume no obligation to update any of these forward-looking statements.

Critical accounting policies

Our financial statements are prepared in accordance with U.S. generally accepted accounting principles ("GAAP") and general practices within the banking industry. Within our financial statements, certain financial information contain approximate measurements of financial effects of transactions and impacts at the consolidated balance sheet dates and our results of operations for the reporting periods. We monitor the status of proposed and newly issued accounting standards to evaluate the impact on our financial condition and results of operations. Our accounting policies, including the impact of newly issued accounting standards, are discussed in further detail in Note 1, "Summary of Significant Accounting Policies," in the notes to our consolidated financial statements. The following discussion presents some of the more significant judgments and estimates used in preparing our financial statements.

Allowance for loan losses

The allowance for loan losses is established through a provision for loan losses charged to expense. Management periodically reviews the allowance for loan losses. Loans are charged against the allowance for loan losses when management believes that the collectability of principal is unlikely. Recoveries of amounts previously charged off are credited to the allowance. In the event management concludes that the allowance for loan losses is more than adequate to absorb potential loan losses, a reverse provision may be recorded whereby a credit is made to the expense account.

The allowance for loan losses is maintained at a level that management considers adequate to absorb probable incurred credit losses on outstanding loans. Factors considered in management's evaluation of the adequacy of the allowance are current and anticipated economic conditions, previous loan loss experience, changes in the nature, volume and composition of the loan portfolio, industry or other concentrations of credit, review of specific problem loans, the level of classified and nonperforming loans, the results of regulatory examinations, the estimated fair value of underlying collateral and overall quality of the loan portfolio. The allowance consists of specific and general components. The specific component relates to loans that are classified as impaired. For such loans, an allowance is established when the discounted cash flows or the collateral value, less estimated selling costs, of the impaired loan is lower than the carrying value of that loan. The general component covers non-impaired loans and is based on historical loss experience with the overall level, adjusted for qualitative, economic and other factors impacting the future collectability of the loan portfolio.

Certain loans acquired in acquisitions or mergers are accounted for under ASC 310-30 "Loans and Debt Securities Acquired with Deteriorated Credit Quality," which prohibits the carryover of an allowance for loan losses for loans acquired in which the acquirer concludes that it will not collect the contractual amount. As a result, these loans are carried at values which represent management's estimate of the future cash flows of these loans. Increases in expected cash flows to be collected from the contractual cash flows are required to be recognized as an adjustment to the loan's yield over its remaining life, while decreases in expected cash flows are required to be recognized as an impairment.

Investment securities

Debt securities are classified as held to maturity and carried at amortized cost when management has the positive intent and ability to hold them to maturity. Debt securities are classified as available-for-sale when they might be sold before maturity. Equity securities with readily determinable fair values are classified as available-for-sale. Securities available-for-sale are carried at fair value, with unrealized holding gains and losses reported in other comprehensive income (loss), net of applicable taxes.

Interest income includes the amortization and accretion of purchase premium and discount. Premiums and discounts on securities are amortized on the level-yield method anticipating prepayments based upon the prior three month average monthly prepayments when available. Gains and losses on sales are recorded on the trade date and determined using the specific identification method as no ready market exists for this stock and it has no quoted market value.

We evaluate securities for other-than-temporary impairment ("OTTI") at least on a quarterly basis, and more frequently when economic or market concerns warrant such evaluation. For securities in an unrealized loss position, consideration is given to the length of time and the extent to which the fair value has been less than cost, the financial condition and near-term prospects of the issuer, and our intent and ability to retain our investment in the issuer for a period of time sufficient to allow for any anticipated recovery in fair value. In analyzing an issuer's financial condition, we consider whether the securities are issued by the federal government or its agencies, whether downgrades by bond rating agencies have occurred, and the results of reviews of the issuer's financial condition.

When OTTI is determined to have occurred, the amount of the OTTI recognized in earnings depends on whether we intend to sell the security or it is more likely than not that we will be required to sell the security before recovery of its amortized cost basis, less any current-period credit loss. If we intend to sell the security or it is more likely than not that we will be required to sell the security before recovery of its amortized cost basis, less any current-period credit loss, the OTTI recognized in earnings is equal to the entire difference between its amortized cost basis and its fair value at the balance sheet date. If we do not intend to sell the security and it is not more likely than not that we will be required to sell the security before recovery of its amortized cost basis less any current-period loss, the OTTI is separated into the amount representing the credit loss and the amount related to all other factors. The amount of the total related to the credit loss is determined based on the present value of cash flows expected to be collected and is recognized as a charge to earnings. The amount of the OTTI related to other factors is recognized in other comprehensive income (loss), net of applicable taxes. The previous amortized cost basis less the OTTI recognized in earnings becomes the new amortized cost basis of the investment.

Loans held for sale

Loans originated and intended for sale in the secondary market, primarily mortgage loans, are carried at fair value as permitted under the guidance in ASC 825, "Financial Instruments." Gains and losses are recognized in income at the time the loan is closed. These gains and losses are classified under the line item "Mortgage banking income" in our consolidated financial statements. Pass through origination costs and related loan fees are also included in "Mortgage banking income." Other expenses are classified in the appropriate noninterest expense accounts.

Other real estate owned

Other real estate owned ("OREO") includes real estate acquired through, or in lieu of, loan foreclosure and excess land and facilities held for sale. OREO is initially recorded at fair value less the estimated cost to sell at the date of foreclosure which may establish a new cost basis. After foreclosure, valuations are periodically performed by management and the asset is carried at the lower of carrying amount or fair value less costs to sell. Revenue and expenses from operations are included in other noninterest income and noninterest expenses. Losses due to the valuation of the property are included in loss on sales or write-downs of other real estate owned.

Mortgage servicing rights

We began retaining the right to service certain mortgage loans in 2014 that we sell to secondary market investors. These mortgage servicing rights are recognized as a separate asset on the date the corresponding mortgage loan is sold.

In periods prior to 2017, mortgage servicing rights were carried at amortized cost less impairment mortgage servicing rights were amortized in proportion to and over the period of estimated net servicing income. Fair value was determined using an income approach with various assumptions including expected cash flows, prepayment speeds, market discount rates, servicing costs, and other factors. Impairment losses on mortgage servicing rights were recognized to the extent by which the unamortized cost exceeded fair value.

As of January 1, 2017, the Company elected to account for its mortgage servicing rights under the fair value option as permitted under ASC 860-50-35, Transfers and Servicing. The change in accounting policy resulted in a one-time adjustment to retained earnings for the after-tax increase in fair value above book value at January 1, 2017. Subsequent changes in fair value are recorded in earnings in Mortgage banking income.

Goodwill and other intangible assets

Goodwill represents the excess of the cost of an acquisition over the fair value of the net assets acquired. Goodwill impairment testing is performed annually or more frequently if events or circumstances indicate possible impairment. Goodwill is assigned to the Company's reporting units, which are determined based on geography and may include one or more individual branches. Fair values of reporting units are determined using either discounted cash flow analyses based on internal financial forecasts or, if available, market-based valuation multiples for comparable businesses. If the estimated implied fair value of goodwill is less than the carrying amount, an impairment loss would be recognized as noninterest expense to reduce the carrying amount to the estimated implied fair value which could be material to our operating results for any particular reporting period.

Other intangible assets consist of core deposit intangible assets arising from whole bank and branch acquisitions in addition to an operating lease intangible, customer base trust intangible and a loan servicing intangible related to a manufactured housing recorded in conjunction with the merger with the Clayton Banks completed on July 31, 2017. All intangible assets are initially measured at fair value and then amortized over their estimated useful lives.

Rate-lock commitments and forward loan sale contracts

We enter into commitments to originate and purchase loans whereby the interest rate on the loan is determined prior to funding (rate-lock commitments). Rate-lock commitments on mortgage loans that are intended to be sold are considered to be derivatives. Accordingly, such commitments, along with any related fees received from potential borrowers, are recorded at fair value in other assets or liabilities, with changes in fair value recorded in mortgage banking income. Fair value is based on fees currently charged to enter into similar agreements, and for fixed-rate commitments, the difference between current levels of interest rates and the committed rates is also considered.

We utilize forward loan sale contracts to mitigate the interest rate risk inherent in our mortgage loan pipeline and held-for-sale portfolio. Forward loan sale contracts are contracts for delayed delivery of mortgage loans. We agree to deliver on a specified future date, a specified instrument, at a specified price or yield. However, the contract may allow for cash settlement. The credit risk inherent to us arises from the potential inability of counterparties to meet the terms of their contracts. In the event of non-acceptance by the counterparty, we would be subject to the credit and inherent (or market) risk of the loans retained. Such contracts are accounted for as derivatives and, along with related fees paid to investor are recorded at fair value in derivative assets or liabilities, with changes in fair value recorded in mortgage banking income. Fair value is based on the estimated amounts that we would receive or pay to terminate the commitment at the reporting date.

Business combinations, Accounting for Acquired Loans and related Assets

We account for our acquisitions under ASC 805, “Business Combinations”, which requires the use of the purchase method of accounting. All identifiable assets acquired, including loans, are recorded at fair value. No allowance for loan losses related to the acquired loans is recorded on the acquisition date because the fair value measurements incorporate assumptions regarding the credit risk. The fair value measurements of acquired loans are based on the estimates related to expected prepayments and the amount of timing of undiscounted expected principal, interest and other cash flows.

Over the life of the acquired loans, we continue to estimate cash flows expected to be collected on individual loans or on pools of loans sharing common risk characteristics. We evaluate, as of the end of each fiscal quarter, the present value of the acquired loans determined using the effective interest rates. If the cash flows expected to be collected have decreased, we recognize a provision for loan loss in our consolidated statement of income; for any increases in cash flows expected to be collected, the Company adjusts the amount of acceptable yield recognized on a prospective basis over the loans’ or the pool’s remaining life.

Overview

We are a bank holding company headquartered in Nashville, Tennessee. We operate primarily through our wholly-owned bank subsidiary, FirstBank, the third largest bank headquartered in Tennessee, based on total assets. FirstBank provides a comprehensive suite of commercial and consumer banking services to clients in select markets in Tennessee, North Alabama, and North Georgia. Our footprint includes 56 full-service bank branches and 9 other banking locations serving the following MSAs Nashville, Chattanooga (including North Georgia), Knoxville, Memphis, Jackson, and Huntsville (AL) and 12 community markets throughout Tennessee. FirstBank also provides mortgage banking services utilizing its bank branch network and mortgage banking offices strategically located throughout the southeastern United States and a national internet delivery channel.

We operate through two segments, Banking and Mortgage. We generate most of our revenue in our Banking segment from interest on loans and investments, loan-related fees, mortgage originations in our banking footprint, investment services and deposit-related fees and, in our Mortgage segment, from origination fees and gains on sales in the secondary market of mortgage loans that we originate outside our Banking footprint or through our internet delivery channels and from servicing. Our primary source of funding for our loans is customer deposits, and to a lesser extent Federal Home Loan Bank advances and other borrowings.

Mergers and acquisitions

Clayton Bank and Trust and American City Bank

Effective July 31, 2017, the Company and FirstBank completed the previously-announced merger with Clayton Bank and Trust ("CBT") and American City Bank ("ACB" and together with CBT, the "Clayton Bank"), pursuant to the Stock Purchase Agreement dated February 8, 2017, as amended on May 26, 2017, with Clayton HC, Inc., a Tennessee Corporation ("Seller"), and James L. Clayton, the majority shareholder of Seller. The transaction was valued at approximately $236.5 million. The Company issued 1,521,200 share of common stock and paid approximately $184.2 million to purchase all of the outstanding shares of the Clayton Banks. At closing, the Clayton Banks merged with and into FirstBank, with FirstBank continuing as the surviving banking corporation. After finalizing purchase accounting adjustments, the Clayton Banks merger added approximately $1,215.8 million in total assets, $1,059.7 million in loans, and $979.5 million in deposits. Operating results for 2017 include the operating results of the acquired assets and assumed liabilities of the Clayton Banks subsequent to the acquisition date. Substantially all of the operations of the Clayton Banks are included in the Banking Segment. We incurred merger and conversion expenses connected with this transaction amounting to $19.0 million during the year ended December 31, 2017.

Northwest Georgia Bank

On September 18, 2015, we completed our acquisition of Northwest Georgia Bank ("NWGB"), pursuant to an Agreement and Plan of Merger dated April 27, 2015. We acquired the stock of NWGB for $1.5 million in cash. NWGB was a 110-year old institution with six branches, primarily serving clients in the Chattanooga MSA, including parts of northern Georgia. We acquired net assets with a fair value of approximately $272.3 million, which includes a bargain purchase gain of $2.8 million, loans with a fair value of approximately $78.6 million, and assumed liabilities of approximately $268.1 million, including deposits with a fair value of approximately $246.2 million. At the acquisition date, $4.9 million of core deposit intangible assets were recorded. Additionally, we recorded merger and conversion related charges totaling $3.3 million and $3.5 million for the years ended December 31, 2016 and 2015, respectively.

Key factors affecting our business

Economic conditions

Our business and financial performance are affected by economic conditions generally in the United States and more directly in the markets where we primarily operate. The significant economic factors that are most relevant to our business and our financial performance include the general economic conditions in the U.S. and in our markets, unemployment rates, real estate markets and interest rates.

The United States economy expanded by 2.6% at an annual rate in the fourth quarter of 2017, due primarily to increases in consumer spending, business investment, exports, housing investment as well as state and local government spending. This expansion follows the growth experienced in 2014 through 2016, which followed modest growth in 2013. Unemployment rates decreased slightly, following a pattern of continuous decline. According to the U.S. Bureau of Labor Statistics, the seasonally adjusted unemployment rate at December 31, 2017 was 4.1% compared to 4.7% at December 31, 2016 and 5.0% at December 31, 2015. The Federal Reserve Board increased its federal funds target range by 25 basis points in December 2017 to 125-150 basis points, the third increase to its target range since December 2016. Interest rates remain extraordinarily low by historical standards, but are expected to increase over time, and general economic conditions are supportive of growth.

Existing home sales in the United States, as indicated by the National Association of Realtors, grew to a seasonally adjusted annual rate of 5.6 million units in December 2017, compared to 5.5 million units in December 2016 and 5.3 million units in December 2015. New home sales showed continued solid growth to a seasonally adjusted annual rate of 625 thousand units in December 2017, up from 548 thousand units in December 2016, and 536 thousand units in December 2015. Home values, as indicated by the seasonally adjusted S&P CoreLogic Case-Shiller 20-City Composite Home Price Index, showed an increase of 6.2% from December 31, 2016 to December 31, 2017. Bankruptcy filings, per the U.S. Court Statistics, also improved with total filings down 0.7% for the year ended December 31, 2017, compared to the same period in 2016, with business filings down 4.0% and personal filings down 0.6%, for the year ending December 31, 2017, compared to the same period in 2016.

According to the Beige Book published by the Federal Reserve Board in January 2018, overall economic activity in the Sixth Federal Reserve District (which includes Florida, Georgia, Tennessee, Alabama and parts of Mississippi and Louisiana) remains positive with most noting that economic conditions were improving at a modest pace over the reporting period. Most contacts expect continued slow and steady growth in the near-term. Business contacts experienced on-going labor market tightness but limited wage growth. Non-labor input costs increased slightly from the previous report. Contacts reported that holiday retail sales exceeded expectations, but auto sales softened. Reports from the hospitality sector were positive, reflecting strong advance bookings. Residential real estate brokers and builders noted mixed sales activity for both existing and new homes. Home prices rose and inventory levels were described as flat or down. Commercial real estate contacts reported increased demand in nonresidential construction, especially industrial and warehousing. Manufacturers indicated that new orders picked up since the previous report.

The economy in the state of Tennessee continued to see improvements as well, according to the U.S. Bureau of Economic Analysis. The unemployment rate, as indicated by the U.S. Bureau of Labor Statistics, improved to 3.2% as of December 31, 2017, down from 5.1% of December 31, 2016. Nashville achieved a historically low unemployment rate of 2.4% as of December 31, 2017, down from 3.8% as of December 31, 2016.

Interest rates

Net interest income is the largest contributor to our net income and is the difference between the interest and fees earned on interest-earning assets (usually loans and investment securities) and the interest expense incurred in connection with interest-bearing liabilities (usually deposits and borrowings). The level of net interest income is primarily a function of the average balance of interest-earning assets, the average balance of interest-bearing liabilities and the spread between the contractual yield on such assets and the contractual cost of such liabilities. These factors are influenced by both the pricing and mix of interest-earning assets and interest-bearing liabilities which, in turn, are impacted by external factors such as local economic conditions, competition for loans and deposits, the monetary policy of the Federal Reserve Board and market interest rates.

The cost of our deposits and short-term wholesale borrowings is largely based on short-term interest rates, which are primarily driven by the Federal Reserve Board’s actions. The yields generated by our loans and securities are typically driven by short-term and long-term interest rates, which are set by the market and are, at times, heavily influenced by the Federal Reserve Board’s actions. The level of net interest income is therefore influenced by movements in such interest rates and the pace at which such movements occur. Since 2012, short-term and long-term interest rates have remained at very low levels by historical standards, with many benchmark rates, such as the federal funds rate and one- and three-month LIBOR, near zero. Subsequent declines in the yield curve or a decline in longer-term yields relative to short-term yields (a flatter yield curve) would have an adverse impact on our net interest margin and net interest income. Although short-term interest rates have risen since the Federal Reserve Board increased the federal funds target range by 75 basis points in 2017, from a historical perspective the Federal Reserve continues to maintain an accommodative monetary policy, and we expect interest rates to continue to increase gradually throughout 2018. However, the low interest rate environment likely will not continue in the long-term .Continued rate increases may have the effect of decreasing our mortgage origination and our general mortgage banking profitability. For additional information regarding our interest rate risks factors and management, see “Business: Risk management: Liquidity and interest rate risk management” and “Risk factors: Risks related to our business.”

Credit trends

We focus on originating quality loans and have established loan approval policies and procedures to assist us in upholding the overall credit quality of our loan portfolio. However, credit trends in the markets in which we operate and in our loan portfolio can materially impact our financial condition and performance and are primarily driven by the economic conditions in our markets.

Underlying credit quality improved during 2017 compared to 2016 largely driven by the improvement in the macro-economic factors discussed above. This improvement in credit quality led to an improvement in our nonperforming loans and classified loans, although the aggregate amounts of nonperforming and classified loans increased due to our acquisition of the Clayton Banks. The percentage of total nonperforming loans to loans held for investment decreased to 0.32% for the year ended December 31, 2017, compared against 0.54% for 2016. Our loans classified as substandard declined 1.75% of loans held for investment for the year ended December 31, 2017, compared to 2.09% for 2016. Our nonperforming assets for the year ended December 31, 2017 were $71.9 million, or 1.52% of assets, increasing from $19.1 million, or 0.58% of assets for the year ended December 31, 2016. Excluding $43.0 million of rebooked GNMA loans (for which the Bank has the right to repurchase, but does not intend to repurchase) and $5.9 million of excess facilities acquired from the Clayton Banks, our adjusted nonperforming assets represented 0.49% of assets for the year ended December 31, 2017.

Although we have recently experienced favorable credit trends through 2017 and currently expect these trends to continue through 2018, we are sensitive to credit quality risks in our commercial real estate, commercial and industrial, and construction loan portfolios due to our concentration of loans in these categories. For additional information regarding credit quality risk factors for our Company, see “Business: Risk management: Credit risk management” and “Risk factors: Risks related to our business.”

Competition

Our profitability and growth are affected by the highly competitive nature of the financial services industry. We compete with commercial banks, savings banks, credit unions, non-bank financial services companies, online mortgage providers and other financial institutions operating within the areas we serve, particularly with national and regional banks that often have more resources than we do to invest in growth and technology and community banks with strong local ties, all of which target the same clients we do. Recently, we have seen increased competitive pressures on loan rates and terms and increased competition for deposits. Continued loan pricing pressure may continue to affect our financial results in the future.

For additional information, see "Business: Our markets," "Business: Competition" and "Risk factors: Risks related to our business."

Regulatory trends and changes in laws

We are subject to extensive regulation and supervision, which continue to evolve as the legal and regulatory framework governing our operations continues to change. The current operating environment also has heightened supervisory expectations in areas such as consumer compliance, the Bank Secrecy Act and anti-money laundering compliance, risk management and internal audit. As a result of these heightened expectations, we expect to incur additional costs for additional compliance, risk management and audit personnel or professional fees associated with advisors and consultants.

As described further under "Business: Supervision and regulation," we are subject to a variety of laws and regulations, including the Dodd-Frank Act. The Dodd-Frank Act is complex, and many aspects of it are subject to final rulemaking that continues to emerge. Implementation of the Dodd-Frank Act will continue to impact our earnings through higher compliance costs and imposition of new restrictions on our business. The Dodd-Frank Act may also continue to have a material adverse impact on the value of certain assets and liabilities held on our balance sheet. The ultimate impact of the Dodd-Frank Act on our business will depend on regulatory interpretation and rulemaking as well as the success of any of our actions to mitigate the negative impacts of certain provisions. Key parts of the Dodd-Frank Act that will specifically impact our business include the repeal of a previous prohibition against payment of interest on demand deposits, the implementation of the Basel III capital adequacy standards, a change in the basis for FDIC deposit insurance assessments, substantial revisions to the regulatory regime applicable to the mortgage market, and enhanced emphasis on consumer protection generally.

See also "Risk factors: Risks related to our regulatory environment."

Factors affecting comparability of financial results

S Corporation status

From our formation in 2001 through September 16, 2016, we elected to be taxed for federal income tax purposes as a "Subchapter S corporation" under the provisions of Section 1361 through 1379 of the Internal Revenue Code of 1986, as amended (the "Code"). As a result, our net income was not subject to, and we have not paid, U.S. federal income taxes, and we have not been required to make any provision or recognize any liability for federal income tax in our financial statements for the periods ending on or prior to September 16, 2016. We terminated our status as a "Subchapter S" corporation in connection with our initial public offering as of September 16, 2016. We commenced paying federal income taxes on our pre-tax net income, and our net income for each fiscal year and each interim period commencing on or after September 16, 2016 will reflect a provision for federal income taxes. As a result of that change in our status under the federal income tax laws during 2016, the net income and earnings per share data presented in our historical financial statements set forth elsewhere in this report, which do not include any provision for federal income taxes, will not be comparable with our 2016 results or future net income and earnings per share in periods in which we are taxed as a C corporation, which will be calculated by including a provision for federal income taxes. Unaudited pro forma amounts for income tax expense and basic and diluted earnings per share are presented in the consolidated statements of income assuming the Company's pro forma tax rates of 36.75% for the year ended December 31, 2016 and 35.08% for the year ended December 31, 2015 as if it had been a C corporation during those periods. The unaudited pro forma results for the year ended December 31, 2016 excludes the effect of recognition of the increase in the deferred tax liability of $13.2 million attributable to the conversion in our taxable status as discussed in Note 15 in the notes to our consolidated financial statements.

Although we have not historically paid federal income tax, in the past, we have made periodic cash distributions to our majority (and formerly sole) shareholder in amounts estimated to be necessary for him to pay his estimated individual U.S. federal income tax liabilities related to our taxable income that was "passed through" to him. However, these distributions have not been consistent, as sometimes the distributions have been lower than or in excess of the shareholder's estimated individual U.S. federal income tax rates which may differ from the rates imposed on the income of C Corporations. Our historical cash flows and financial condition have been affected by such cash distributions.

Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of the change in tax rates resulting from becoming a C Corporation was recognized in income in the third quarter of 2016 in which such change took place. On September 16, 2016, the Company recorded an additional net deferred tax liability of $13.2 million to recognize the difference between the financial statement carrying amounts of assets and liabilities and their respective tax bases as of the date that the Company became a taxable corporate entity. In recording the impact of the conversion to a C Corporation, the Company recorded a deferred income tax expense of $3.0 million related to the unrealized gain on available for sale securities through the income statement; therefore, the amount shown in other comprehensive income has not been reduced by the above expense. This difference will remain in OCI until the underlying securities are sold or mature.

Public company costs

On August 19, 2016, we filed a Registration Statement on Form S-1 with the SEC. That Registration Statement was declared effective by the SEC on September 15, 2016. We sold and issued 6,764,704 shares of common stock at $19 per share pursuant to that Registration Statement. Total proceeds received, net of offering costs, were approximately $115.5 million. The proceeds were used to fund a $55.0 million distribution to the majority shareholder representing undistributed earnings previously taxed to him under subchapter S, and used to repay all $10.1 million aggregate principal amount of subordinated notes held by the majority shareholder, plus any accrued and unpaid interest thereon**.** We qualify as an “emerging growth company” as defined by the Jumpstart Our Business Startups Act (JOBS Act).

There are additional costs associated with operating as a public company, hiring additional personnel, enhancing technology and expanding additional operational and administrative capabilities. We expect that these costs will include legal, regulatory, accounting, investor relations and other expenses that we did not incur as a private company. Sarbanes-Oxley, as well as rules adopted by the U.S. Securities and Exchange Commission, or SEC, the FDIC and national securities exchanges also requires public companies to implement specified corporate governance practices. In addition, due to regulatory changes in the banking industry and the implementation of new laws, rules and regulations, we are now subject to higher regulatory compliance costs. These additional rules and regulations also increase our legal, regulatory, accounting and financial compliance costs and make some activities more time-consuming.

Tax legislation changes

In addition, on December 22, 2017, the Tax Cuts and Jobs Act (the “Tax Reform Act”) was enacted into law. The Tax Reform Act provides for significant changes to the U.S. tax code that impact businesses. Effective January 1, 2018, the Tax Reform Act reduces the U.S. federal tax rate for corporations from 35% to 21% for U.S. taxable income and requires a one-time remeasurement of deferred taxes to reflect their value at a lower tax rate of 21%. The Tax Reform Act includes other changes, including, but not limited to, immediate deductions for certain new investments instead of deductions for depreciation expense over time, additional limitations on the deductibility of executive compensation and limitations on the deductibility of interest. For more information regarding the impact of the Tax Reform Act on the Company, see Note 15, “Income Taxes” in the notes to our consolidated financial statements.

Overview of recent financial performance

Results of operation

Our financial performance over the last three years primarily reflects the success of our growth strategies and the continued economic improvement in our markets, as described above. As a result, we have improved our pre-tax and pro forma net income and profitability over each of the last three years. Our net income increased by 29.1% in 2017 to $52.4 million from $40.6 million in 2016. Pre-tax net income increased by 11.2 million, or 17.9%, from $62.3 million for the year ended December 31, 2016 to $73.5 million for the year ended December 31, 2017. Our unaudited pro forma net income for the year ended 2016 was $39.4 million, up by $6.4 million, compared to the year ended December 31, 2015. Pre-tax net income and unaudited pro forma net income for the year ended December 31, 2015 were $50.8 million and $33.0 million, respectively. There was a 15.2% decrease in net income in 2016 from net income of $47.9 million in 2015 due to our conversion to a C corporation, which included a $13.2 million charge to income related to our conversion to a C corporation in connection with our initial public offering in the third quarter of 2016. Our net income represented a return on average assets, or ROAA, of 1.37%, 1.35% and 1.86% in 2017, 2016 and 2015, respectively, and a return on average shareholders’ equity, or ROAE, of 11.24%, 14.68% and 20.91% in 2017, 2016 and 2015, respectively. Our ratio of average shareholders’ equity to average assets in 2017, 2016 and 2015 was 12.23%, 9.22% and 8.88% respectively.

The improvement in pre-tax net income has resulted primarily from growth in our net interest income, which has been enhanced by consistently improved net interest margins. Net interest income increased to $154.2 million in 2017 compared to $112.4 million in 2016 and $96.9 million for 2015. The increase in net interest income was attributable to the success of our growth initiatives. Continued strong demand for our loan products in the metropolitan markets, the hiring of additional lenders, and a concerted effort to increase customer deposits has fueled our organic growth while the merger with the Clayton Banks on July 31, 2017 has significantly increased our presence in the Knoxville MSA and surrounding community markets.

Noninterest income for 2017 compared to 2016 decreased by $3.1 million, or 2.1%, primarily due to a decrease in gain on sale of securities of approximately $4.1 million during the period. This followed a 56.6% increase in noninterest income in 2016 from noninterest income of $92.4 million in 2015 primarily due to the significant increase in mortgage banking income in 2016 which was partially offset by a bargain purchase gain of $2.8 million in 2015. Our net interest margin, on a tax-equivalent basis, has consistently improved over the last three years, increasing to 4.46% in 2017 as compared to 4.10% in 2016 and 3.97% in 2015. The increase in 2017 was primarily a result of the impact of the product mix acquired from the Clayton Banks, an increase in accretion from the Clayton Banks' loan mark increased loan rates and fees and the collection of nonaccrual interest income during the same period in addition to our continued efforts to maintain our cost of funds, loan growth and increased volume in loans held for sale.

Noninterest expense increased to $222.3 million for 2017 compared to $194.8 million and $138.5 million for 2016 and 2015, respectively. The increases were a result of merger and conversion costs resulting from the Clayton Banks transaction and continued increases in personnel costs associate with our growth offset by the impact of the change to fair value election on MSRs as of January 1, 2017.

Financial condition

Our total assets grew by 44.3% in 2017 to $4.73 billion at December 31, 2017 as compared to $3.28 billion at December 31, 2016. The significant increase resulted from the merger with the Clayton Banks which increased loans approximately $1,060 million, goodwill approximately $90 million, and other intangibles approximately $12 million when the merger was completed on July 31, 2017. Additionally, we continued to see strong organic loan growth of approximately 13.9% during 2017.

In 2017, we grew total deposits by 37.2% to $3.66 billion and noninterest bearing deposits by 27.4% to $888.2 million at December 31, 2017 from $2.67 billion and $697.1 million, respectively, at December 31, 2016. Most of the increase resulted from the merger with the Clayton Banks which increased deposits approximately $979.5 million when the merger was completed on July 31, 2017.

Business segment highlights

We operate our business in two business segments: Banking and Mortgage. See Note 21, "Segment Reporting," in the notes to our consolidated financial statements for a description of these business segments.

During the first quarter of 2016, management evaluated the current composition of its operating segments – Banking and Mortgage. The primary focus of the evaluation was on capturing all of the revenue and expenses from all customer activities within the Banking segment's geographic footprint. Specifically, the primary product and service that was not previously captured by the Banking segment related to our retail mortgage origination activities occurring within our banking geographic footprint and typically within our existing branch network. Therefore, we have reclassified the revenue and associated expenses from the retail mortgage origination activities within the banking geographic footprint into the Banking segment from the Mortgage segment for all periods presented. Based on the review and evaluation of the revised information, our chief executive officer believes that this presentation better presents the results of each segment to enhance overall resource allocation and evaluation of the Company's performance. Additionally, we believe that the revised results of the Banking segment become more comparable to other banking organizations for analysis and understanding of the Banking segment operating results.

As discussed above, the mortgage retail origination activities within the Banking segment contributed the following to Banking segment results:

	Year Ended December 31,		
	2017	**2016**	**2015**
Mortgage banking income	$ 26,737	$ 25,542	$ 18,718
Noninterest expense	21,714	16,095	13,189

Banking

Income before taxes increased by $4.7 million, or 8.4% in the year ended December 31, 2017 to $60.4 million as compared to $55.7 million in the year ended December 31, 2016. The increase reflects an improvement of $40.7 million in net interest income due to an increase of $667.5 million in average loan balances driven by our merger with the Clayton Banks in addition to 13.9% organic loan growth combined with favorable interest rates and an improved credit environment. Noninterest expense increased $34.4 million, primarily due to increased merger and conversion costs of $15.8 million attributed to our merger with the Clayton Banks in addition to increases in salaries and other costs associated with our growth.

Income before taxes increased by $11.8 million, or 26.8% in the year ended December 31, 2016 to $55.7 million as compared to $43.9 million in the year ended December 31, 2015. The increase reflects an improvement of $20.0 million in net interest income due to increase of $222.1 million in average loan balances driven primarily by interest rates and an improved credit environment, the overall economic climate and the implementation of our growth initiatives in addition to our acquisition of NWGB. Noninterest expense increased $18.2 million, primarily due to increases in salaries, other costs associated with our growth and operating of NWGB for the entire year of 2016 compared with approximately three and a half months in 2015

Mortgage

Income before taxes from the mortgage segment increased $6.5 million in the year ended December 31, 2017 to $13.1 million as compared to $6.6 million in the year ended December 31, 2016. This increase is primarily attributable to increased interest rate lock commitments. Interest rate lock commitment volume increased $1,604.7 million for the year ended December 31, 2017 to $7,570.4 million as compared to $5,965.7 million for the year ended December 31, 2016. The increase in interest rate lock commitment volume is primarily due to increased activity in our correspondent delivery channel, which was established in the second quarter of 2016. Noninterest income decreased $2.0 million to $90.2 million for the year ended December 31, 2017 as compared to $92.2 for the year ended December 31, 2016, driven by the change in delivery channel mix of interest rate lock commitment volume during the year. Additionally, on January 1, 2017, fair value accounting was elected on MSRs; the change in fair value is now included in mortgage banking income and amounted to a $4.0 million charge offset by a hedging gain of $0.6 million during the year ended December 31, 2017. Previous to this change, amortization and impairment of MSRs was included in noninterest expense and amounted to $13.0 million for the year ended December 31, 2016. This decline in amortization and impairment was partially offset by an increase in other mortgage noninterest expense of $6.2 million related to the correspondent channel and overall increased production. Interest rate lock commitments in the pipeline at December 31, 2017 were $504.2 million compared with $532.9 million at December 31 2016.

Income before taxes from the mortgage segment decreased $0.3 million in the year ended December 31, 2016 to $6.6 million as compared to $6.9 million in the year ended December 31, 2015. This decrease is primarily attributable to increased impairment on mortgage servicing rights during the year ended December 31, 2016 in addition to a loss on sale of mortgage servicing rights of $4.4 million. Interest rate lock commitment volume increased $2,485.6 million for the year ended December 31, 2016 to $5,965.7 million as compared to $3,480.1 million for the year ended December 31, 2015. The increase in volume was the result of the expansion of the consumer direct delivery and correspondent delivery channels and a favorable interest rate environment through the majority of 2016. During the fourth quarter of 2016, mortgage rates increased. The combination of this increase in rates and the overall seasonal nature of historical mortgage production caused a decline in the level of interest rate lock commitments during the fourth quarter. Noninterest income increased $40.7 million to $92.2 million for the year ended December 31, 2016 as compared to $51.5 for the year ended December 31, 2015, reflecting the significant increased activity in mortgage loan volume. The increase in noninterest income was partially offset by a $38.1 million increase in noninterest expense, which includes an impairment of mortgage servicing rights of $4.7 million in addition to increased personnel and occupancy costs associated with our growth.

Results of operation

Throughout the following discussion of our operating results, we present our net interest income, net interest margin and efficiency ratio on a fully tax-equivalent basis. The fully tax-equivalent basis adjusts for the tax-favored status of net interest income from certain loans and investments. We believe this measure to be the preferred industry measurement of net interest income, which enhances comparability of net interest income arising from taxable and tax-exempt sources. The adjustment to convert certain income to a tax-equivalent basis consists of dividing tax exempt income by one minus the combined federal and state statutory income tax rate of 39.225%.

Net interest income

Our net interest income is primarily affected by the interest rate environment, and by the volume and the composition of our interest-earning assets and interest-bearing liabilities. We utilize net interest margin, or NIM, which represents net interest income divided by average interest-earning assets, to track the performance of our investing and lending activities. We earn interest income from interest, dividends and fees earned on interest-earning assets, as well as from amortization and accretion of discounts on acquired loans. Our interest-earning assets include loans, time deposits in other financial institutions and securities available for sale. We incur interest expense on interest-bearing liabilities, including interest-bearing deposits, borrowings and other forms of indebtedness as well as from amortization of premiums on purchased deposits. Our interest-bearing liabilities include deposits, advances from the FHLB, other borrowings and other liabilities.

Year ended December 31, 2017 compared to year ended December 31, 2016

Net interest income before the provision for loan losses increased 38.1% to $153.3 million in the year ended December 31, 2017 compared to $111.0 million in the year ended December 31, 2016. On a tax-equivalent basis, net interest income increased $42.8 million to $156.1 million in the year ended December 31, 2017 as compared to $113.3 million in the year ended December 31, 2016. The increase in tax-equivalent net interest income in the year ended December 31, 2017 was primarily driven by higher loan balances, due to the success of our growth initiatives, including our merger with the Clayton Banks.

Interest income, on a tax-equivalent basis, was $172.4 million for the year ended December 31, 2017, compared to $122.9 million for the year ended December 31, 2016, an increase of $49.6 million. The two largest components of interest income are loan income and investment income. Loan income consists primarily of interest earned on our loans held for investment portfolio. Investment income consists primarily of interest earned on our investment portfolio. Loan income related to loans held for investment in addition to loans held for sale, on a tax-equivalent basis, increased $42.2 million to $137.0 million from $94.8 million for the year ended December 31, 2016 primarily due to increased average loan balances of $667.5 million in addition to $5.4 million in accretion on loans purchased in our acquisitions. The tax-equivalent yield on loans was 5.66%, up 25 basis points from the year ended December 31, 2016. The increase in yield was primarily due to the contractual interest rate on loans held for investment, which yielded 4.95% for the year ended December 31, 2017.

The components of our loan yield, a key driver to our NIM for the December 31, 2017, 2016 and 2015 were as follows:

	Year Ended December 31,					
	2017		2016		2015	
(dollars in thousands)	Interest income	Average yield	Interest income	Average yield	Interest income/ expense	Average yield/ rate
Loan yield components:						
Contractual interest rate on loans held for investment (1)	$ 119,617	4.95%	$ 82,136	4.69%	$ 73,021	4.78%
Origination and other loan fee income	7,638	0.32%	7,208	0.41%	4,310	0.28%
Accretion on purchased loans	5,419	0.22%	3,538	0.20%	254	0.02%
Nonaccrual interest collections	3,266	0.14%	1,075	0.06%	—	0.00%
Syndicated loan fee income	1,010	0.04%	825	0.05%	690	0.05%
Total loan yield	$ 136,950	5.66%	$ 94,782	5.41%	$ 78,275	5.12%

(1) Includes tax equivalent adjustment

Accretion on purchased loans contributed 15 and 13 basis points to the NIM for the year ended December 31, 2017 and 2016, respectively. Additionally, syndicated loan fees contributed 3 basis points to the NIM for each of the year ended December 31, 2017 and 2016, and nonaccrual interest collections contributed 9 and 4 basis points to the NIM for the same periods, respectively.

For the year ended December 31, 2017, interest income on loans held for sale increased $6.0 million compared to the year ended December 31, 2016. This resulted from a $3.7 million increase in interest income from higher interest rates and a $2.3 million increase in interest income from growth in volume. For the year ended December 31, 2017, investment income, on a tax-equivalent basis, increased to $16.7 million compared to $16.2 million for the year ended December 31, 2016. The average balance in the investment portfolio in the year ended December 31, 2017 was $558.0 million compared to $576.9 million in the year ended December 31, 2016. The decline in the balance is driven by the use of investment cash flow to fund loan growth.

Interest expense was $16.3 million for the year ended December 31, 2017, an increase of $6.8 million, or 71.2%, as compared to the year ended December 31, 2016. The increase in interest expense was primarily due to an increase in deposit interest expense driven by overall increased interest rates and growth in deposit volume driven by our merger with the Clayton Banks. Interest expense on deposits was $13.0 million and $7.3 million for the year ended December 31, 2017 and 2016, respectively. The cost of total deposits was 0.42% and 0.29% for the year ended December 31, 2017 and 2016, respectively. The cost of interest-bearing deposits was 0.56% and 0.40% for the same periods, respectively. The primary driver for the increase in total interest expense is the increase in money market and time deposit interest expense. Money market interest expense increased to $5.4 million from $2.3 million for the year ended December 31, 2017 and 2016, respectively, driven by an increase in rate and balances. The rate on money markets was 0.61%, up 24 basis points from year ended December 31, 2016. Time deposit interest expense increased $1.8 million to $3.8 million from the year ended December 31, 2016, driven by an increase in rate and balances. The rate on time deposits was 0.73%, up 25 basis points from the year ended December 31, 2016 due to the higher renewal rate of maturing accounts. Average time deposit balances increased $110.3 million to $511.7 million from $401.5 million during the year ended December 31, 2017. The increase is due to a change in product mix attributable to our merger with the Clayton Banks, which increased average brokered and internet time deposits by $42.2 million for the year ended December 31, 2017 compared to the same period in 2016. The rate on brokered and internet time deposits carried an inherently higher rate at 1.54% for the year ended December 31, 2017 compared to the same period in 2016. The rate on brokered and internet time deposits carried an inherently higher rate at 1.54% for the year ended December 31, 2017 than traditional customer time deposits, which carried a rate of 0.66% for the year ended December 31,2017 compared to 0.48% for the year ended December 31, 2016, reflecting rate increases. Interest expense on borrowings was $3.3 million and $2.2 million for the year ended December 31, 2017 and 2016, respectively, while the cost of total borrowings was 2.09% and 1.49% for the year ended December 31, 2017 and 2016, respectively. The increase in expense on borrowing was due primarily to an increase in interest expense on FHLB advances which increased to $1.7 million from $0.7 for the year ended December 31, 2017 and 2016, respectively, driven by increased balances primarily related to our funding strategy for the merger with the Clayton Banks in addition to increased rates during the year.

Our net interest margin, on a tax-equivalent basis, increased to 4.46% during the year ended December 31, 2017 from 4.10% in the year ended December 31, 2016, primarily as a result of increased loan yield driven primarily by increased volume as a result of our merger with the Clayton Banks in addition to increased contractual rates, accretion on loans purchased from the Clayton Banks and nonaccrual interest income.

Year ended December 31, 2016 compared to year ended December 31, 2015

Net interest income increased 18.2% to $111.0 million for the year ended December 31, 2016 compared to $93.9 million for the year ended December 31, 2015. On a tax-equivalent basis, net interest income increased $17.4 million to $113.3 million for the year ended December 31, 2016 as compared to $95.9 million for the year ended December 31, 2015. The increase in tax equivalent net interest income in year ended December 31, 2016 was primarily driven by higher loan balances, partially due to the success of our acquisition of NWGB, including recognized accretion of the credit discount taken in purchase accounting of $3.5 million in the year ended December 31, 2016.

Interest income, on a tax-equivalent basis, was $122.9 million for the year ended December 31, 2016, compared to $104.8 million for the year ended December 31, 2015, an increase of $18.1 million. The two largest components of interest income are loan income and investment income. Loan income consists primarily of interest earned on our loan portfolio. Investment income consists primarily of interest earned on our investment portfolio. Loan income, on a tax-equivalent basis, increased $16.5 million to $94.8 million from $78.3 million for the year ended December 31, 2015 primarily due to increased average loan balances of $222.1 million in addition to $3.5 million in accretion on loans purchased in our acquisition of NWGB. The tax-equivalent yield on loans was 5.41%, up 29 basis points from the year ended December 31, 2015. The increase in yield was primarily due to accretion on loans purchased from NWGB, which yielded 0.20%, in addition to increased origination fees which yielded 0.46%.

Accretion on purchased loans contributed 13 and 1 basis points to the NIM for each of the year ended December 31, 2016 and 2015, respectively. Additionally, during the year ended December 31, 2016 and 2015, nonaccrual interest collections contributed 4 basis points and 0 basis points to the NIM, respectively, while syndicated loan fees contributed 3 basis points and 3 basis points to the NIM during the same periods.

Interest expense was $9.5 million for the year ended December 31, 2016, an increase of $0.6 million, or 7.1%, as compared to the year ended December 31, 2015. The increase in interest expense was due primarily to an increase in deposit interest expense due to the growth in deposits, which includes our acquisition of NWGB. Interest expense on deposits was $7.3 million and $6.3 million for the years ended December 31, 2016 and 2015, respectively. The cost of total deposits was 0.29% and 0.30% for the years ended December 31, 2016 and 2015, respectively. The cost of interest-bearing deposits was 0.40% and 0.40% for the same periods. The primary driver for the increase in total interest expense is the increase in money market interest expense to $2.3 million from $1.5 for the year ended December 31, 2016 and 2015, respectively, driven by an increase in rate and balances. The rate on money markets was 0.37%, up 5 basis points from the year ended December 31, 2015. Time deposit interest expense also increased $0.4 million to $1.9 million from the year ended December 31, 2015, primarily as a result of increased balances. The rate on time deposits was 0.48%, down 3 basis points from the year ended December 31, 2015 due to the lower renewal rate of maturing accounts. Average time deposit balances increased $98.1 million to $401.5 million from $303.4 million during the year ended December 31, 2016. A primary driver of the increase in time deposits during the year ended December 31, 2016 is a result of restructuring an IRA savings product to a time deposit product during the second quarter of 2016, the average balance of which was $75.7 million. Interest expense on borrowings was $2.2 million and $2.6 million for the years ended December 31, 2016 and 2015, respectively, while the cost of total borrowings was 1.49% and 1.06% for the years ended December 31, 2016 and 2015, respectively.

Our net interest margin, on a tax-equivalent basis, increased to 4.10% for the year ended December 31, 2016 from 3.97% for the year ended December 31, 2015, primarily as a result of our continued efforts to reduce our cost of funds, growing loans and benefiting from our acquisition of NWGB.

Average balance sheet amounts, interest earned and yield analysis

The table below shows the average balances, income and expense and yield rates of each of our interesting-earning assets and interest-bearing liabilities on a tax-equivalent basis, if applicable, for the periods indicated.

									Year Ended December 31,
			2017			2016			2015
(dollars in thousands on tax-equivalent basis)	**Average balances [1]**	**Interest income/ expense**	**Average yield/ rate**	**Average balances [1]**	**Interest income/ expense**	**Average yield/ rate**	**Average balances [1]**	**Interest income/ expense**	**Average yield/ rate**
Interest-earning assets:									
Loans[2][4]	$2,418,261	$ 136,950	5.66%	$1,750,796	$ 94,782	5.41%	$1,528,719	$ 78,275	5.12%
Loans held for sale	419,290	17,256	4.12%	362,518	11,268	3.11%	250,237	9,651	3.86%
Securities:									
Taxable	441,568	10,084	2.28%	485,083	10,646	2.19%	537,762	11,783	2.19%
Tax-exempt[4]	116,384	6,592	5.66%	91,863	5,548	6.04%	73,871	4,620	6.25%
Total Securities[4]	557,952	16,676	2.99%	576,946	16,194	2.81%	611,633	16,403	2.68%
Federal funds sold	20,175	140	0.69%	12,686	64	0.50%	8,969	51	0.57%
Interest-bearing deposits with other financial institutions	75,567	954	1.26%	51,861	285	0.55%	10,508	155	1.48%
FHLB stock	8,894	460	5.17%	6,630	262	3.95%	6,692	262	3.92%
Total interest earning assets[4]	3,500,139	172,436	4.93%	2,761,437	122,855	4.45%	2,416,758	104,797	4.34%
Noninterest Earning Assets:									
Cash and due from banks	53,653			46,523			45,987		
Allowance for loan losses	(22,967)			(23,986)			(28,688)		
Other assets[3]	280,333			217,301			143,838		
Total noninterest earning assets	311,019			239,838			161,137		
Total assets	$3,811,158			$3,001,275			$2,577,895		
Interest-bearing liabilities:									
Interest bearing deposits:									
Customer time deposits	$ 467,507	$ 3,077	0.66%	$ 399,207	$ 1,926	0.48%	$ 297,723	$ 1,550	0.52%
Broker and internet time deposits	44,234	682	1.54%	2,276	3	0.13%	5,631	9	0.16%
Time deposits	511,741	3,759	0.73%	401,483	1,929	0.48%	303,354	1,559	0.51%
Money market	888,258	5,387	0.61%	614,804	2,292	0.37%	455,271	1,477	0.32%
Negotiable order of withdrawals	762,918	3,640	0.48%	699,907	2,643	0.38%	621,630	2,327	0.37%
Savings deposits	156,328	245	0.16%	129,544	478	0.37%	183,307	929	0.51%
Total interest bearing deposits	2,319,245	13,031	0.56%	1,845,738	7,342	0.40%	1,563,562	6,292	0.40%
Other interest-bearing liabilities:									
FHLB advances	110,764	1,778	1.61%	64,309	688	1.07%	17,885	608	3.40%
Other borrowings	16,968	42	0.25%	45,691	121	0.26%	187,630	318	0.17%
Long-term debt	30,930	1,491	4.82%	38,207	1,393	3.65%	41,003	1,692	4.13%
Total other interest-bearing liabilities	158,662	3,311	2.09%	148,207	2,202	1.49%	246,518	2,618	1.06%
Total Interest-bearing liabilities	2,477,907	16,342	0.66%	1,993,945	9,544	0.48%	1,810,080	8,910	0.49%
Noninterest bearing liabilities:									
Demand deposits	814,643			695,765			519,273		
Other liabilities	52,389			34,978			19,698		
Total noninterest-bearing liabilities	867,032			730,743			538,971		
Total liabilities	3,344,939			2,724,688			2,349,051		
Shareholders' equity	466,219			276,587			228,844		
Total liabilities and shareholders' equity	$3,811,158			$3,001,275			$2,577,895		
Net interest income (tax-equivalent basis)		$ 156,094			$ 113,311			$ 95,887	
Interest rate spread (tax-equivalent basis)			4.36%			4.05%			3.93%
Net interest margin (tax-equivalent basis)[5]			4.46%			4.10%			3.97%
Average interest-earning assets to average interest-bearing liabilities			141.3%			138.5%			133.5%

(1) *Calculated using daily averages.*

(2) *Average balances of nonaccrual loans are included in average loan balances. Loan fees of $7.6 million, $7.2 million and $4.3 million, accretion of $5.4 million, $3.5 million and $0.3 million, nonaccrual interest collections of $3.3 million, $1.1 million and $0, and syndicated loan fees of $1.0 million, $0.8 million and $0.7 million are included in interest income in the years ended December 31, 2017, 2016 and 2015, respectively.*

(3) *Includes investments in premises and equipment, foreclosed assets, interest receivable, MSRs, core deposit and other intangibles, goodwill and other miscellaneous assets.*

(4) *Interest income includes the effects of taxable-equivalent adjustments using a U.S. federal income tax rate and, where applicable, state income tax to increase tax-exempt interest income to a tax-equivalent basis. The net taxable-equivalent adjustment amounts included in the above table were $2.8 million, $2.4 million and $2.0 million for the years ended December 31, 2017, 2016 and 2015, respectively.*

Rate/volume analysis

The tables below present the components of the changes in net interest income for the year ended December 31, 2017 and 2016. For each major category of interest-earning assets and interest-bearing liabilities, information is provided with respect to changes due to average volumes and changes due to rates, with the changes in both volumes and rates allocated to these two categories based on the proportionate absolute changes in each category.

Year ended December 31, 2017 compared to year ended December 31, 2016

	Year ended December 31, 2017 compared to year ended December 31, 2016 due to changes in		
(dollars in thousands on a tax-equivalent basis)	**volume**	**rate**	**Net increase (decrease)**
Interest-earning assets:			
Loans[1][2]	$ 37,800	$ 4,368	$ 42,168
Loans held for sale	2,336	3,652	5,988
Securities available for sale and other securities:			
Taxable	(994)	432	(562)
Tax Exempt[2]	1,389	(345)	1,044
Federal funds sold and balances at Federal Reserve Bank	52	24	76
Time deposits in other financial institutions	299	370	669
FHLB stock	117	81	198
Total interest income[2]	40,999	8,582	49,581
Interest-bearing liabilities:			
Time deposits	810	1,020	1,830
Money market	1,658	1,437	3,095
Negotiable order of withdrawal accounts	301	696	997
Savings deposits	42	(275)	(233)
FHLB advances	746	344	1,090
Other borrowings	(71)	(8)	(79)
Long-term debt	(351)	449	98
Total interest expense	3,135	3,663	6,798
Change in net interest income[2]	$ 37,864	$ 4,919	$ 42,783

(1) *Average loans are gross, including nonaccrual loans and overdrafts (before deduction of net fees and allowance for loan losses). Loan fees of $7.6 million and $7.2 million and accretion of $5.4 million and $3.5 million, nonaccrual interest collections of $3.3 million and $1.1 million, and syndicated loan fee income of $1.0 million and $0.8 million are included in interest income in the year ended December 31, 2017 and 2016, respectively.*

(2) *Interest income includes the effects of the tax-equivalent adjustments to increase tax-exempt interest income to a tax-equivalent basis*.

As discussed above, the $48.2 million increase in loan and loans held for sale interest income during the year ended December 31, 2017 compared to year ended December 31, 2016 was the primary driver of the $42.8 increase in net interest income. The increase in loan interest income on loans held for investment of $42.2 million was driven by an increase in average loan balances of $667.5 million, or 38.1%, to $2.4 billion as of December 31, 2017, as compared to $1.8 billion as of year ended December 31, 2016, which was driven by our merger with the Clayton Banks and strong loan growth in our metropolitan markets. The increase in interest income on loans held for sale of $6.0 million was driven by both increases in volume and rates. Average loans held for sale increased $56.8 million or 15.7% over the previous year driven by strong demand throughout our delivery channels and the expansion of our correspondent delivery channel.

Year ended December 31, 2016 compared to year ended December 31, 2015

(dollars in thousands on a tax-equivalent basis)	Year ended December 31, 2016 compared to year ended December 31, 2015 due to changes in volume	rate	Net increase (decrease)
Interest-earning assets:			
Loans(1)	$ 12,022	$ 4,485	$ 16,507
Loans held for sale	3,490	(1,873)	1,617
Securities available for sale and other securities:			
Taxable	(1,156)	19	(1,137)
Tax Exempt(2)	1,087	(159)	928
Federal funds sold and balances at Federal Reserve Bank	19	(6)	13
Time deposits in other financial institutions	227	(97)	130
FHLB stock	(2)	2	—
Total interest income(2)	15,687	2,371	18,058
Interest-bearing liabilities:			
Time deposits	471	(101)	370
Money market	595	220	815
Negotiable order of withdrawal accounts	296	20	316
Savings deposits	(198)	(253)	(451)
FHLB advances	(147)	227	80
Other borrowings	(217)	20	(197)
Long-term debt	(102)	(197)	(299)
Total interest expense	698	(64)	634
Change in net interest income(2)	$ 14,989	$ 2,435	$ 17,424

(1) Average loans are gross, including nonaccrual loans and overdrafts (before deduction of net fees and allowance for loan losses). Loan fees of $7.2 million and $4.3 million and accretion of $3.5 million and $0.3 million, nonaccrual interest collections of $1.1 million and $0, and syndicated loan fee income of $0.8 million and $0.7 million are included in interest income in the year ended December 31, 2016 and 2015, respectively.

(2) Interest income includes the effects of the tax-equivalent adjustments to increase tax-exempt interest income to a tax-equivalent basis.

As discussed above, the $18.1 million increase in loans and loans held for sale interest income for the year ended December 31, 2016 compared to the year ended December 31, 2015 was the primary driver of the $17.4 million increase in net interest income. The increase in loan interest income was driven by an increase in average loan balances of $222.1 million, or 14.5%, to $1.8 billion as of December 31, 2016, as compared to $1.5 billion as of December 31, 2015. Our loan growth during the period was driven by growth in our metropolitan markets, primarily in the Nashville MSA, resulting from the investment in new locations and banking teams and improving economic conditions in addition to the acquisition of NWGB. The increase in loans held for sale of $112.3 million was the result of increased volume driven by lower interest rates, an increase in mortgage loan officers and the growth of our internet delivery channel.

Provision for loan losses

The provision for loan losses charged to operating expense is an amount which, in the judgment of management, is necessary to maintain the allowance for loan losses at a level that is believed to be adequate to meet the inherent risks of losses in our loan portfolio. Factors considered by management in determining the amount of the provision for loan losses include the internal risk rating of individual credits, historical and current trends in net charge-offs, trends in nonperforming loans, trends in past due loans, trends in the market values of underlying collateral securing loans and the current economic conditions in the markets in which we operate. The determination of the amount is complex and involves a high degree of judgment and subjectivity. See "Critical Accounting Policies – Allowance for Loan Losses."

Year ended December 31, 2017 compared to year ended December 31, 2016

Our reversal of the provision for loan losses for the year ended December 31, 2017 was $1.0 million as compared to $1.5 million for the year ended December 31, 2016, reflecting continued improving credit quality throughout the year ended December 31, 2017, including net recoveries of $3.2 million compared to net charge-offs of $1.2 million in the previous year.

Year ended December 31, 2016 compared to year ended December 31, 2015.

Our reversal of the provision for loan losses for the year ended December 31, 2016 was $1.5 million as compared $3.1 million for the year ended December 31, 2015, reflecting our improved credit quality and a decrease in troubled loans throughout 2015 and 2016.

Noninterest income

Our noninterest income includes gains on sales of mortgage loans, fees on mortgage loan originations, loan servicing fees, hedging results, fees generated from deposit services, securities gains and all other noninterest income.

The following table sets forth the components of noninterest income for the periods indicated:

	Year Ended December 31,		
(dollars in thousands)	**2017**	**2016**	**2015**
Mortgage banking income	$ 116,933	$ 117,751	$ 70,190
Service charges on deposit accounts	7,787	8,009	7,389
ATM and interchange fees	8,784	7,791	6,536
Investment services and trust income	3,949	3,337	3,260
Bargain purchase gain	—	—	2,794
Gain from securities, net	285	4,407	1,844
Gain on sales or write-downs of other real estate owned	774	1,282	(317)
Other	3,069	2,108	684
Total noninterest income	$ 141,581	$ 144,685	$ 92,380

Year ended December 31, 2017 compared to year ended December 31, 2016

Noninterest income was $141.6 million for the year ended December 31, 2017, a decrease of $3.1 million, or 2.1%, as compared to $144.7 million for the year ended December 31, 2016. Noninterest income to average assets (excluding any gains or losses from sale of securities) was 3.7% in the year ended December 31, 2017 as compared to 4.7% in the year ended December 31, 2016.

Mortgage banking income primarily includes origination fees on mortgage loans including from wholesale and third party origination services and gains and losses on the sale of mortgage loans, change in fair value of mortgage loans and derivatives, changes in the fair value of MSRs, and mortgage servicing fees. Mortgage banking income was $116.9 million and $117.8 million for the year ended December 31, 2017 and 2016, respectively.

During the year ended December 31, 2017, the Bank’s mortgage operations had closings of $6,331.5 million which generated $107.2 million in gains and related fair value charges included in mortgage banking income. This compares to $4,671.6 million and $105.7 million for the year ended December 31, 2016. During the fourth quarter of 2016, mortgage rates increased above prevailing rates experienced during the first three quarters of 2016. This increase in rates has caused the level of interest rate lock commitments in the pipeline to decline to approximately $504.2 million at December 31, 2017 from its height of $850.5 million at September 30, 2016 and $532.9 million at December 31, 2016. The increase in gains on sale were driven by an increase in interest rate lock volume of $1,604.7 million or 26.9%, to $7,570.4 million for the year ended December 31, 2017 from the year ended December 31, 2016, due to growth in the correspondent delivery channel, which was established during the second quarter of 2016, offset by declining interest rate lock volume in the consumer direct delivery channel. With the increasing rates and change in mix of sales volume, including a lower contribution margin from the newly established correspondent delivery channel, the Company is currently experiencing a decline in mortgage sales margins from the year ended December 31, 2016. Income from mortgage servicing was $13.2 million and $12.1 million for the years ended December 31, 2017 and 2016, respectively. This increase was offset by a decline in fair value on MSRs for the year ended December 31, 2017 of $3.4 million. The change in fair value included a gain related to the change in fair value of MSR hedging instruments of $0.6 million. The fair value adjustment during the year ended December 31, 2017 was the result of our change in accounting policy to elect fair value on MSRs as of January 1, 2017. As such, there is no such fair value adjustment reflected in mortgage banking income for the year ended December 31, 2016.

The components of mortgage banking income for the December 31, 2017, 2016 and 2015 were as follows:

(in thousands)	Year Ended December 31, 2017	2016	2015
Mortgage banking income:			
Origination and sales of mortgage loans	$ 103,735	$ 94,472	$ 64,319
Net change in fair value of loans held for sale and derivatives	3,454	11,216	$ 2,257
Change in fair value on MSRs	(3,424)	—	—
Mortgage servicing income	13,168	12,063	3,614
Total mortgage banking income	$ 116,933	$ 117,751	$ 70,190
Closing volume	$ 6,331,458	$ 4,671,561	$ 2,757,463
Interest rate lock commitment volume	$ 7,570,387	$ 5,965,709	$ 3,480,069
Outstanding principal balance of mortgage loans serviced	$ 6,529,431	$ 2,833,958	$ 2,545,449

Mortgage banking income attributable to our Banking segment was $26.7 million and $25.5 million for the years ended December 31, 2017 and 2016, respectively, and mortgage banking income attributable to our Mortgage segment was $90.2 million and $92.2 million for the years ended December 31, 2017 and 2016, respectively.

Service charges on deposit accounts include analysis and maintenance fees on accounts, per item charges, non-sufficient funds and overdraft fees. Service charges on deposit accounts were $7.8 million, a decrease of $0.2 million, or 2.8%, for the year ended December 31, 2017, compared to $8.0 million for the year ended December 31, 2016.

ATM and interchange fees include debit card interchange, ATM and other consumer fees. These fees increased 12.7% to $8.8 million during the year ended December 31, 2017 as compared to $7.8 million for the year ended December 31, 2016 as a result of increased debit card fees from continued growth in client usage of debit cards experienced by most financial institutions in addition to our merger with the Clayton Banks.

Investment services and trust income increased 18.3% during the year ended December 31, 2017 to $3.9 million compared to $3.3 million for the year ended December 31, 2016 due to our merger with the Clayton Banks, which added revenue from trust operations for the last five months of 2017.

Gains on securities for the year ended December 31, 2017 were $0.3 million, resulting from the sale of approximately $94.7 million in securities, compared to gains on sales of securities of $4.4 million, resulting from the sale of approximately $271.2 million for the year ended December 31, 2016. Also included in gain from securities is a change for other-than-temporary impairment of $0.9 million during the year ended December 31, 2017 related to one of the equity securities held which we do not intend to hold long-term. The gains are attributable to management taking advantage of portfolio structuring opportunities to lock in current gains while maintaining comparable interest rates and maturities and to fund current loan growth in addition to overall asset liability management.

Net gain on sales or write-downs of foreclosed assets for the year ended December 31, 2017 was $0.8 million compared to a net gain of $1.3 million for the year ended December 31, 2016. This change was the result of specific sales and valuation transactions of other real estate.

Other noninterest income for the year ended December 31, 2017 increased $1.0 million to $3.1 million as compared to other noninterest income of $2.1 million for the year ended December 31, 2016, reflecting the contribution from the Clayton Banks during the last five months of 2017.

Year ended December 31, 2016 compared to year ended December 31, 2015

Noninterest income was $144.7 million for the year ended December 31, 2016, an increase of $52.3 million, or 56.6%, as compared to $92.4 million for the year ended December 31, 2015. Noninterest income to average assets (excluding any gains or losses from sale of securities) was 4.7% in the year ended December 31, 2016 as compared to 3.5% in the year ended December 31, 2015.

Mortgage banking income primarily includes origination fees on mortgage loans, gains and losses on the sale of mortgage loans, fees from wholesale and third party origination services provided to community banks and mortgage companies, and mortgage servicing fees. Mortgage banking income was $117.8 million and $70.2 million for the year ended December 31, 2016 and 2015, respectively. Originations of mortgage loans to be sold totaled $4,671.6 million for the year ended December 31, 2016 as compared to $2,757.5 million for the year ended December 31, 2015. The increase in originations of mortgage loans to be sold is due to increased overall volume as well as the expansion of the consumer direct delivery and correspondent delivery channels and a favorable interest rate environment through the third quarter of 2016. During the fourth quarter of 2016, mortgage rates increased above prevailing rates experienced during the first three quarters of 2016. The combination of this increase in rates and the overall seasonal nature of historical mortgage production caused a decline in the level of interest rate lock commitments during the fourth quarter of 2016.

Service charges on deposit accounts were $8.0 million, an increase of $0.6 million or 8.4% for the year ended December 31, 2016, compared to $7.4 million for the year ended December 31, 2015. The increase in service charges on deposit accounts in the year ended December 31, 2016 was primarily the result of deposit account growth driven by our acquisition of NWGB.

ATM and interchange fees include debit card interchange, ATM and other consumer fees. These fees increased 19.2% to $7.8 million during the year ended December 31, 2016 as compared to $6.5 million for the year ended December 31, 2015 as a result of increased debit card fees from continued growth in client usage of debit cards experienced by most financial institutions in addition to our acquisition of NWGB.

Investment services income remained flat for the year ended December 31, 2016 at $3.3 million compared to $3.3 million for the year ended December 31, 2015.

Bargain purchase gain of $2.8 million for the year ended December 31, 2015 represents the excess fair value of net assets acquired over the purchase price in our acquisition of NWGB.

Gains on sales of securities for the year ended December 31, 2016 were $4.4 million, resulting from the sale of approximately $271.1 million in securities, compared to gains on sales of securities for the year ended December 31, 2015 of $1.8 million. The gains are attributable to management taking advantage of portfolio structuring opportunities to lock in current gains while maintaining comparable interest rates and maturities and to fund current loan growth.

Net gain on sales or write-downs of foreclosed assets for the year ended December 31, 2016 was $1.3 million compared to a net loss of $317 thousand for the year ended December 31, 2015. This change was the result of specific sales and valuation transactions of other real estate.

Other noninterest income for the year ended December 31, 2016 was $2.1 million as compared to other noninterest income of $0.7 million for the year ended December 31, 2015. This $1.4 million increase in other noninterest income was due to recoveries on acquired loans of $0.8 million that were charged off prior to the acquisition of NWGB in addition to increased miscellaneous income items associated with our overall growth.

Noninterest expense

Our noninterest expense includes primarily salaries and employee benefits expense, occupancy expense, legal and professional fees, data processing expense, amortization of intangibles, regulatory fees and deposit insurance assessments, software license and maintenance fees, advertising and other real estate owned expense, among others. We monitor the ratio of noninterest expense to the sum of net interest income plus noninterest income, which is commonly known as the efficiency ratio.

The following table sets forth the components of noninterest expense for the periods indicated:

	Year Ended December 31,		
(dollars in thousands)	**2017**	**2016**	**2015**
Salaries and employee benefits	$ 130,355	$ 113,992	$ 84,214
Occupancy and fixed asset expense	13,836	12,611	10,777
Legal and professional fees	5,737	3,514	3,355
Data processing expense	6,488	4,181	2,053
Merger and conversion expenses	19,034	3,268	3,543.0
Amortization of intangibles	1,995	2,132	1,731
Amortization of mortgage servicing rights	—	8,321	2,601
Impairment of mortgage servicing rights	—	4,678	194
Loss on sale of mortgage servicing rights	249	4,447	—
Regulatory fees and deposit insurance assessments	2,049	1,952	2,190
Other real estate owned expense	916	907	643
Software license and maintenance fees	1,873	2,874	1,986
Advertising	12,957	10,608	8,062
Other	26,828	21,305	17,143
Total noninterest expense	222,317	$ 194,790	$ 138,492

Year ended December 31, 2017 compared to year ended December 31, 2016

Noninterest expense increased by $27.5 million during the year ended December 31, 2017 to $222.3 million as compared to $194.8 million in the year ended December 31, 2016. This increase resulted primarily from the $15.8 million increase in merger and conversion expenses during the year ended December 31, 2017 in addition to increased costs associated with our growth and merger with the Clayton Banks, including higher salaries and employee benefits expenses

Salaries and employee benefits expense was the largest component of noninterest expenses representing 58.6% and 58.5% of total noninterest expense in the year ended December 31, 2017 and 2016, respectively. During the year ended December 31, 2017, salaries and employee benefits expense increased $16.4 million, or 14.4%, to $130.4 million as compared to $114.0 million for the year ended December 31, 2016. The increase was primarily due to increased costs associated with our growth and merger with the Clayton Banks and the $7.8 million increase in mortgage banking salaries and benefits resulting from the increase in mortgage loan interest rate lock commitment volume and expansion in our correspondent delivery channel.

Salaries and employee benefits expense also reflects $3.2 million accrued for equity compensation grants during the year ended December 31, 2017 that were made in conjunction with our initial public offering to all full-time associates. This compares to $4.3 million in stock-related grant expense during the year ended December 31, 2016. On December 29, 2017, additional restricted stock units with a total value of $0.8 million were granted to employees of the Clayton Banks and other legacy bank employees that joined the Company after the completion of the IPO. Additionally, salaries and benefits expense includes amounts accrued under our three management incentive plans (prior to the IPO) that were based on our total assets, tangible book value of consolidated equity and contractually-defined after-tax earnings. As of September 16, 2016, the date of the initial public offering, participants in these plans were given the option to convert their equity based incentive plan units to shares of restricted stock units at the IPO price of $19 per share. Aggregate salaries and employee benefits expense recognized under these incentive plans totaled $3.5 million and $5.4 million for the year ended December 31, 2017 and 2016, respectively.

Occupancy and fixed asset expense in the year ended December 31, 2017 was $13.8 million, an increase of $1.2 million, compared to $12.6 million for the year ended December 31, 2016, reflecting the impact of the Clayton Banks.

Legal and professional fees were $5.7 million for the year ended December 31, 2017 as compared to $3.5 million for the year ended December 31, 2016. The increase in legal and professional fees is attributable to additional professional services related to being a publicly traded company in addition to our growth and volume of business.

Data processing costs increased $2.3 million, or 55.2%, to $6.5 million for the year ended December 31, 2017 from $4.2 million for the year ended December 31, 2016. The increase for the year ended December 31, 2017 was attributable to our growth and volume of transaction processing, partially attributable to our merger with the Clayton Banks.

Merger and conversion expenses related to the merger with the Clayton Banks that closed on July 31, 2017 were $19.0 million for the year ended December 31, 2017 as compared to $3.3 million related to the acquisition of NWGB for the year ended December 31, 2016. Also included in merger and conversion expenses for the year ended December 31, 2017 is a $10 million charitable contribution to a foundation established to invest in the communities across the markets of the Clayton Banks. We completed the core conversion of the Clayton Banks onto our core system and consolidated five branch locations on December 1, 2017. We do not expect to incur any additional significant costs related to the merger with the Clayton Banks.

Amortization of core deposit and other intangible assets totaled $2.0 million for the year ended December 31, 2017 compared to $2.1 million for the year ended December 31, 2016. This amortization relates to the core deposit intangible recognized in connection with the merger with the Clayton Banks and the acquisition of NWGB and the leasehold intangible, customer base trust intangible and manufactured housing servicing intangible recognized in the merger with the Clayton Banks. These intangibles are being amortized over their useful lives (see Note 8 in the notes to Consolidated Financial Statements).

MSRs are recognized as a separate asset on the date the corresponding mortgage loan is sold. Prior to January 1, 2017, MSRs were amortized in proportion to and over the period of estimated net servicing income. The amortization of MSRs was determined using the level yield method based on the expected life of the loan and these servicing rights were carried at the lower of amortized cost or fair value. As of January 1, 2017, we elected to transition our accounting policy to carry MSRs at fair value as permitted under ASC-860-50-35, *Transfers and Servicing*, which positions us to hedge our MSR portfolio. Fair value is determined using an income approach with various assumptions including expected cash flows, prepayment speeds, market discount rates, servicing costs and other factors. MSRs were carried at fair value at December 31, 2017 and amortized cost less impairment at December 31, 2016. Therefore, there was no amortization expense or impairment losses for the year ended December 31, 2017 as fair value changes under fair value accounting are included in noninterest income as mortgage banking income. Amortization expense amounted to $8.3 million for the year ended December 31, 2016. Impairment losses on MSRs are recognized to the extent by which the unamortized cost exceeds fair value. Impairment losses on MSRs of $4.7 million were recognized in earnings in the year ended December 31, 2016.

Regulatory fees and deposit insurance assessments were relatively flat, amounting to $2.0 million for year ended December 31, 2017.

Expenses related to other real estate owned for the year ended December 31, 2017 were $0.9 million, flat compared to $0.9 million for the year ended December 31, 2016. Legal fees related to other real estate owned sold is the primary driver of this activity.

Software license and maintenance fees for the year ended December 31, 2017 were $1.9 million, a decrease of $1.0 million compared to $2.9 million for the year ended December 31, 2016. This decrease is due to costs associated with the conversion of our core system to Jack Henry Silverlake during the second quarter of 2016.

Advertising costs for the year ended December 31, 2017 were $13.0 million, an increase of $2.3 million compared to $10.6 million for the year ended December 31, 2016. This increase was largely driven by the mortgage segment and expansion in the correspondent channel established in the second quarter of 2016 in addition to the addition of the Clayton Banks.

Other noninterest expense for the year ended December 31, 2017 was $26.8 million, an increase of $5.3 million from the year ended December 31, 2016, reflecting an increase of various expenses associated with our overall growth, including the impact of the merger with the Clayton Banks in addition to increases in mortgage banking activities.

Year ended December 31, 2016 compared to year ended December 31, 2015

Noninterest expense increased by $56.3 million during the year ended December 31, 2016 to $194.8 million as compared to $138.5 million in the year ended December 31, 2015. This increase resulted primarily from higher salaries and employee benefits expenses (including in connection with one time IPO awards described below) in addition to impairment of mortgage servicing rights and increased costs associated with our growth, especially in mortgage and from our acquisition of NWGB.

Salaries and employee benefits expense is the largest component of noninterest expenses representing 58.5% and 60.8% of total noninterest expense in the year ended December 31, 2016 and 2015, respectively. During the year ended December 31, 2016, salaries and employee benefits expense increased $29.8 million, or 35.4%, to $114.0 million as compared to $84.2 million for the year ended December 31, 2015. The increase was primarily due to the $26.8 million increase in mortgage banking salaries and benefits resulting from the increase in mortgage production, expansion and growth of our senior management team. This also included equity compensation grants that were made in conjunction with our initial public offering to all full-time associates. Salaries and employee benefits expense includes amounts earned under our three management incentive plans that are based on our total assets, tangible book value of consolidated equity and contractually-defined after-tax earnings. Aggregate salaries and employee benefits expense recognized under these incentive plans totaled $5.4 million and $3.2 million for the year ended December 31, 2016 and 2015, respectively. As of September 16, 2016, the date of the initial public offering, participants in these plans were given the option to convert their equity based incentive plan units to shares of restricted stock units at the IPO price of $19 per share. Additionally, we granted certain employees and executive officers restricted stock units in a total grant value of $18.2 million. Expense related to these grants amounted to $4.3 million in the year ended December 31, 2016. As of December 31, 2016, there was $15.7 million in total unrecognized expense related to these grants and the conversion of the equity based incentive plan units to be recognized over the remaining vesting period.

Occupancy and fixed asset expense in the year ended December 31, 2016 was $12.6 million, an increase of $1.8 million, compared to $10.8 million for the year ended December 31, 2015. This increase was attributable to expansion in mortgage, the addition of our new branch in the Nashville MSA and the acquisition of NWGB, which would have been included for the full year in 2016.

Legal and professional fees were $3.5 million for the year ended December 31, 2016 as compared to $3.4 million for the year ended December 31, 2015. The increase in legal and professional fees is attributable to additional professional services related to our growth and volume of business.

Data processing costs increased $2.1 million, or 103.7%, to $4.2 million for the year ended December 31, 2016 from $2.1 million for the year ended December 31, 2015. The increase for the year ended December 31, 2016 was attributable to costs associated with the conversion of our core system to Jack Henry Silverlake during the second quarter of 2016.

Merger and conversion expenses related to the acquisition of NWGB and conversion of our core processing system were $3.3 million for the year ended December 31, 2016 as compared to $3.5 million for the year ended December 31, 2015. We do not anticipate incurring additional costs related to our acquisition of NWGB or our core processor conversion from Cardinal to Jack Henry Silverlake.

Amortization of intangible assets totaled $2.1 million for the year ended December 31, 2016 compared to $1.7 million for the year ended December 31, 2015. This amortization relates to core deposit intangible assets, which are being amortized over their useful lives. As of December 31, 2016, these intangible assets have remaining estimated useful lives of approximately 9 years.

Prior to 2014, all of our mortgage loan sales transferred servicing rights to the buyer. Beginning in the first quarter of 2014, we began retaining some servicing rights. These MSRs are recognized as a separate asset on the date the corresponding mortgage loan is sold. MSRs are amortized in proportion to and over the period of estimated net servicing income. The amortization of MSRs is determined using the level yield method based on the expected life of the loan. These MSRs are carried at the lower of amortized cost or fair value. Fair value is determined using an income approach with various assumptions including expected cash flows, prepayment speeds, market discount rates, servicing costs and other factors. MSRs were carried at amortized cost less impairment of $32.1 million and $29.7 million at December 31, 2016 and 2015, respectively, and amortization expense amounted to $8.3 million and $2.6 million for the years ended December 31, 2016 and 2015, respectively. Impairment losses on MSRs are recognized to the extent by which the unamortized cost exceeds fair value. Impairment losses on MSRs of $4.7 million and $194 thousand were recognized in earnings in the years ended December 31, 2016 and 2015, respectively.

Regulatory fees and deposit insurance assessments were relatively flat, amounting to $2.0 million and $2.2 million for year ended December 31, 2016 and 2015, respectively.

Expenses related to foreclosed assets for the year ended December 31, 2016 were $907 thousand, an increase of $264 thousand compared to $643 thousand for the year ended December 31, 2015. Legal fees related to foreclosed real estate sold was the primary driver for the increase.

Software license and maintenance fees for the year ended December 31, 2016 were $2.9 million, an increase of $0.9 million compared to $2.0 million for the year ended December 31, 2015. This increase is due to our growth and customization costs associated with the conversion of our core system to Jack Henry Silverlake during the second quarter of 2016.

Advertising costs for the year ended December 31, 2016 were $10.6 million, an increase of $2.5 million compared to $8.1 million for the year ended December 31, 2015. This increase was largely driven by the mortgage segment's internet delivery channel and communications surrounding our second quarter conversion to Jack Henry Silverlake.

Other noninterest expense for year ended December 31, 2016 was $21.3 million, an increase of $4.2 million from the year ended December 31, 2015, reflecting an increase of various expenses in mortgage banking activities and overall growth, including from the acquisition of NWGB.

Efficiency ratio

The efficiency ratio is one measure of productivity in the banking industry. This ratio is calculated to measure the cost of generating one dollar of revenue. That is, the ratio is designed to reflect the percentage of one dollar which must be expended to generate that dollar of revenue. We calculate this ratio by dividing noninterest expense by the sum of net interest income and noninterest income. For an adjusted efficiency ratio, we exclude certain gains and expenses we do not consider core to our business.

Our efficiency ratio was 75.40%, 76.20% and 74.36% for the years ended December 31, 2017, 2016 and 2015, respectively. Our adjusted efficiency ratio, on a tax-equivalent basis, was 67.31%, 70.59% and 73.10% for the years ended December 31, 2017, 2016 and 2015, respectively. See "GAAP reconciliation and management explanation of non-GAAP financial measures" for a discussion of the adjusted efficiency ratio.

Return on equity and assets

The following table sets forth our ROAA, ROAE, dividend payout ratio and average shareholders' equity to average assets ratio for the periods indicated:

	Year Ended December 31,		
	2017	2016	2015
Return on average total assets	1.37%	1.35%	1.86%
Return on average shareholders' equity	11.24%	14.68%	20.91%
Dividend payout ratio	—	170.73%	49.31%
Average shareholders' equity to average assets	12.23%	9.22%	8.88%

Income tax

Income tax expense was $21.1 million, $21.7 million and $3.0 million for the years ended December 31, 2017, 2016 and 2015, respectively. Income tax expense for the year ended December 31, 2017 reflects a $5.9 million adjustment to reduce the deferred tax liability resulting from the Tax Cuts and Jobs Act reduction in federal tax rate from 35.0% to 21.0% enacted on December 22, 2017. Income tax expense for the year ended December 31, 2016 includes the $13.2 million increase in deferred tax liability associated with our conversion to a C corporation. From our formation in 2001 through September 16, 2016, we elected to be taxed for federal income tax purposes as a “Subchapter S corporation” under the provisions of Section 1361 through 1379 of the Internal Revenue Code. As a result, our net income was not subject to, and we did not pay, U.S. federal income taxes and we were not required to make any provision or recognize any liability for federal income tax in our financial statements for the periods ending on or prior to June 30, 2016. We terminated our status as an S Corporation in connection with our initial public offering as of September 16, 2016. We commenced paying federal income taxes on our pre-tax net income in the third quarter of 2016 and our net income for each fiscal year and each interim period commencing on or after September 16, 2016 and each such period reflect a provision for federal income taxes. See “Pro forma income tax expense and net income” below for a discussion on what our income tax expense and net income would have been had we been taxed as a C Corporation for the full periods.

Pro forma income tax expense and net income

We have determined that had we been taxed as a C Corporation and paid U.S. federal income tax for the years ended December 31, 2016 and 2015, our combined effective income tax rate would have been 36.75% and 35.08% respectively. These pro forma effective rates reflect a U.S. federal income statutory tax rate of 35.00% on corporate income and the fact that a portion of our net income in each of these periods was derived from nontaxable investment income, a bargain purchase gain in the third quarter of 2015, and other nondeductible expenses. Our net income for the years ended December 31, 2016 and 2015 was $40.6 million and $47.9 million, respectively, and our tax-equivalent net interest income for the same periods was $113.3 million and $95.9 million, respectively. Had we been subject to U.S. federal income tax during these periods, on a pro forma basis, our provision for combined federal and state income tax would have been $22.9 million and $17.8 million for the years ended December 31, 2016 and 2015, respectively. The increases in such pro forma provision for U.S. federal income tax would have resulted primarily from the increase in our net income for such periods. As a result of the foregoing factors, our unaudited pro forma net income (after U.S. federal income tax) for the years ended December 31, 2016 and 2015 would have been $39.4 million and $33.0 million, respectively.

Financial condition

The following discussion of our financial condition compares for the year ended December 31, 2017 with the year ended December 31, 2016.

Total assets

Our total assets were $4.73 billion at December 31, 2017. This compares to total assets of $3.28 billion as of December 31, 2016. The increase in total assets is primarily attributable to the merger with the Clayton Banks as well as strong organic loan growth in our metropolitan markets.

Loan portfolio

Our loan portfolio is our most significant earning asset, comprising 67.0% and 56.4% of our total assets as of December 31, 2017 and 2016, respectively. Our strategy is to grow our loan portfolio by originating quality commercial and consumer loans that comply with our credit policies and that produce revenues consistent with our financial objectives. Our overall lending approach is primarily focused on providing credit to our customers directly rather than purchasing loan syndications and loan participations from other banks (collectively, “Purchased loans”). At December 31, 2017 and December 31, 2016, loans held for investment included approximately $62.9 million and $29.7 million, respectively, related to Purchased loans. Currently, our loan portfolio is diversified relative to industry concentrations across the various loan portfolio categories. At December 31, 2017 and December 31, 2016, our outstanding loans to the broader healthcare industry made up less than 5% of our total outstanding loans and are spread across nursing homes, assisted living facilities, outpatient mental health and substance abuse centers, home health care services, and medical practices within our geographic markets. We believe our loan portfolio is well-balanced, which provides us with the opportunity to grow while monitoring our loan concentrations.

Loans

Loans increased $1.32 billion, or 71.3%, to $3.17 billion as of December 31, 2017 as compared to $1.85 billion as of December 31, 2016. Our loan growth during the year ended December 31, 2017 has been composed of increases of $328.8 million, or 85.1%, in commercial and industrial loans, $202.4 million or, 82.3%, in construction loans, $138.5 million, or 38.8%, in owner occupied commercial real estate loans, $283.7 million, or 105.9%, in non-owner occupied commercial real estate loans, $221.3 million, or 42.8%, in residential real estate loans and $143.4 million, or 193.0%, in consumer and other loans, respectively. The increase in loans during the year ended December 31, 2017 is attributable to the merger with the Clayton Banks, which contributed loans with a fair value of $1,059.7 million on July 31, 2017 in addition to continued strong demand in our metropolitan markets, building customer relationships and continued favorable economic conditions throughout much of our geographic footprint.

Loans by type

The following table sets forth the balance and associated percentage of each major category in our loan portfolio of loans as of the dates indicated:

	As of December 31,									
	2017		2016		2015		2014		2013	
(dollars in thousands)	**Amount**	**% of total**	**Amount**	**% of total**	**Amount**	**% of total**	**Amount**	**% of total**	**Amount**	**% of total**
Loan Type:										
Commercial and industrial	$715,075	23%	$386,233	21%	$318,791	19%	$265,818	18%	$251,557	19%
Construction	448,326	14%	245,905	13%	238,170	14%	165,957	12%	112,060	8%
Residential real estate:										
1-to-4 family	480,989	15%	294,924	16%	290,704	17%	266,641	19%	251,271	19%
Line of credit	194,986	6%	177,190	10%	171,526	10%	159,868	11%	158,111	12%
Multi-family	62,374	2%	44,977	2%	59,510	3%	52,238	4%	45,497	3%
Commercial real estate:										

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