

NORTHWEST BANCORPORATION INC  
Form 10KSB/A  
February 01, 2008

**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

**FORM 10-KSB/A**

Amendment No. 1

(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, 2006

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission file number 000-24151

**NORTHWEST BANCORPORATION, INC.**

(Name of small business issuer in its charter)

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Washington  
(State or other jurisdiction of  
incorporation or organization)

91-1574174  
(I.R.S. Employer  
Identification Number)

421 W. Riverside, Spokane, WA  
(Address of principal executive offices)

(Issuer's telephone number) (509) 456-8888

99201-0403  
(Zip Code)

**Securities registered under Section 12(b) of the Act:**

**Title of each class**

None

**Name of each exchange on which registered**

None

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

**Common Stock, No Par Value Per Share**

(Title of Class)

Check whether the issuer is not required to file reports pursuant to Section 13 or 15(d) of the Exchange Act.

Check whether the issuer (1) filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act during the past 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

Check if there is no disclosure of delinquent filers in response to Item 405 of Regulation S-B contained in this form, and no disclosure will 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-KSB or any amendment to this Form 10-KSB.

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

State issuer's revenues for its most recent fiscal year: \$13,451,418.

State the aggregate market value of the voting and non-voting common equity held by non-affiliates computed by reference to the price at which the common equity was sold, or the average bid and asked price of such common equity, as of a specified date within 60 days prior to the end of the Company's fiscal year: \$30,427,716 based on a trade transacted on December 29, 2006.

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State the number of shares outstanding of each of the issuer's classes of common equity, as of the latest practicable date: 2,236,460: as of March 21, 2007.

**DOCUMENTS INCORPORATED BY REFERENCE**

Portions of the definitive Proxy Statement for the registrant's Annual Meeting of Shareholders to be held on May 14, 2007 (the 2007 Proxy Statement ) have been incorporated by reference into Part I, item 4, Part I, item 5 and Part II, item 5 of this Annual Report on Form 10-KSB.

Transitional Small Business Disclosure Format (check one): Yes  No

**Explanatory Note**

This Amendment No. 1 on Form 10-KSB/A ( Amendment ) amends the Form 10-KSB for the year ended December 31, 2006 ( Original Report ) of Northwest Bancorporation, Inc. ( Company ); the Original Report was filed with the U.S. Securities and Exchange Commission on March 21, 2007. This Amendment is being filed to provide five years of data for Items III (Loan Portfolio) and IV (Summary of Loan Loss Experience); the Original Report provided only two years of data. Note 21 has been added to the Notes to Consolidated Financial Statements and details the parent company financial statements. The Report of Independent Registered Public Accounting Firm has been updated to reflect their signature and the modification to Note 21.

These modifications to the Original Report had no effect on the Company s income, financial position, or cash flows.

Except for the modifications described above, this Amendment does not modify or update the Company s previously reported financial statements and other financial disclosures in, or exhibits to, the Original Report, nor does it reflect events occurring after the date of the Original Report. Unaffected items and exhibits have not been repeated in this Amendment.

## PART I

## III. LOAN PORTFOLIO.

The amounts of loans outstanding at the indicated dates are shown in the following table according to type of loan (\$ in thousands):

	2006	December 31			2002
		2005	2004	2003	
	(Dollars in Thousands)				
Commercial	\$ 127,420	\$ 124,611	\$ 121,820	\$ 117,055	\$ 109,948
Real estate	74,496	50,162	25,644	22,127	16,676
Installment	8,090	5,079	4,368	4,625	4,295
Consumer and other	8,102	8,991	7,878	6,983	6,422
	218,108	188,843	159,710	150,790	137,341
Allowance for loan losses	(2,586)	(2,252)	(1,944)	(2,224)	(2,026)
Net deferred loan fees	(400)	(273)	(328)	(307)	(291)
	\$ 215,122	\$ 186,318	\$ 157,438	\$ 148,259	\$ 135,024

The following table shows the amounts and earlier of maturity/re-pricing of commercial, real estate and other loans outstanding as of December 31, 2006 (\$ in thousands):

	Maturing			TOTAL
	Within 1 year maturity	After 1 year but within 5 year maturity	After 5 year maturity	
Commercial	\$ 29,561	\$ 18,053	\$ 79,806	\$ 127,420
Real Estate Loans	52,154	5,844	16,498	74,496
Installment	1,691	787	5,612	8,090
Consumer and Other	6,559	19	1,524	8,102
Totals	\$ 89,965	\$ 24,703	\$ 103,440	\$ 218,108
Loans maturing with:				
Fixed Rates	\$ 11,248	\$ 16,905	\$ 33,094	\$ 61,247
Variable Rates	78,717	7,798	70,346	156,861
Totals	\$ 89,965	\$ 24,703	\$ 103,440	\$ 218,108

Loans are placed in a non-accrual status when they are not adequately collateralized and when, in the opinion of management the collection of interest is questionable. Thereafter, no interest is taken into income unless received in cash or until such time as the borrower demonstrates the ability to resume payments of principal and interest. Interest previously accrued but not collected is reversed and charged against income at the time the loan is placed on non-accrual status.

	December 31	
	2006	2005
	(Dollars in Thousands)	
Loans accounted for on a non-accrual basis	\$ 320	\$ 405
Loans contractually past due ninety days or more as to interest or principal	\$ 0	\$ 19
Gross interest income which would have been recorded under original terms	\$ 11	\$ 18
Gross interest income recorded during the period	\$ 3	\$ 0

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- C.2.** As of the end of the most recent reported period, December 31, 2006, management has no knowledge of additional loans where the financial condition of its borrowers is likely to result in the inability of the borrower to comply with current loan repayment terms. All such credits known to management are identified in the table (above) and any identified potential loss has already been recognized by charge to the Loan Loss Reserve.

**IV. SUMMARY OF LOAN LOSS EXPERIENCE.**

The following table provides an analysis of annualized net losses by loan type for YTD periods over the past five years:

	2006	2005	December 31 2004	2003	2002
	(Dollars in Thousands)				
Total loans net of deferred fees at end of period	\$ 217,708	\$ 188,570	\$ 159,382	\$ 150,483	\$ 137,050
YTD average net loans	\$ 205,388	\$ 174,346	\$ 150,011	\$ 143,985	\$ 137,625
Balance, beginning of period	\$ 2,252	\$ 1,944	\$ 2,224	\$ 2,026	\$ 1,649
Add reserve for probable losses on unused loan commitments and off-balance sheet items (OBS) *	178	206			
Balance, beginning of period, including OBS reserve	2,430	2,150	2,224	2,026	1,649
Loan charge-offs:					
Commercial	28	14	74	13	287
Real Estate		25	128	378	270
Installment & Credit Card	21	68	65	95	153
Total Charge-offs	49	107	267	486	710
Recoveries of loans previously charged-off:					
Commercial		8	4	28	17
Real Estate	17	25	12	1	
Installment & Credit Card	27	30	7	3	5
Total Recoveries	44	63	23	32	22
Net Charge-offs	5	44	244	454	688
Provision charged to expense	360	324	170	652	1,065
Balance, end of year, prior to adjustment for off-balance sheet items	2,785	2,430	2,150	2,224	2,026
Reclassification of reserve for probable losses on unused loan commitments and off-balance sheet items to Other liabilities *	(199)	(178)	(206)		
Balance, end of year	\$ 2,586	\$ 2,252	\$ 1,944	\$ 2,224	\$ 2,026
Ratio of net charge-offs during period to average net loans outstanding	0.00%	0.03%	0.16%	0.32%	0.50%

\* Off-balance sheet reserve was not calculated prior to December 2004.

Breakdown of Allowance for Loan Losses (\$ in thousands):

	December 31, 2006		December 31, 2005	
	Amount	% of allowance to total allowance	Amount	% of allowance to total allowance
Construction and land development (pass)	\$ 627	22.51%	\$ 291	11.98%
Secured by farmland (pass)	1	0.04%	1	0.04%
Home equity loans (pass)	60	2.15%	42	1.73%
Revolving loans secured by 1-4 family residential (pass)	66	2.37%	91	3.74%
Secured by multi-family residential (pass)	50	1.80%	62	2.55%

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Secured by non-farm, non-residential real estate (pass)	401	14.40%	358	14.73%
Commercial and industrial loans (pass)	283	10.16%	270	11.11%
Loans to individuals (pass)	188	6.75%	159	6.54%
Credit card loans	134	4.81%	128	5.27%
All other loans and leases (pass)	3	0.11%	3	0.12%
Mortgage loans held for sale	0	0.00%	0	0.00%
Specifically Identified Potential Loss *	621	22.30%	800	32.93%
Commitments to Lend under Lines/Letters of Credit	199	7.15%	178	7.33%
Supplementary Allowance/Non-specific Factors	152	5.45%	47	1.93%
	\$ 2,785	100.00%	\$ 2,430	100.00%

\* Classified and criticized loans (risk category 7, 8 & 9) loans are individually analyzed at least quarterly to determine loss potential. Allocated reserves related to loans classified 7, 8 & 9 are reported as Specifically Identified Potential Loss.



**PART II**

**NORTHWEST BANCORPORATION, INC. AND SUBSIDIARY**

**REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

**AND**

**FINANCIAL STATEMENTS**

**DECEMBER 31, 2006 AND 2005**

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**REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

To the Board of Directors

Northwest Bancorporation, Inc. and Subsidiary

Spokane, Washington

We have audited the accompanying consolidated statements of financial condition of Northwest Bancorporation, Inc. and subsidiary, Inland Northwest Bank, as of December 31, 2006 and 2005, and the related consolidated statements of income, changes in stockholders' equity, and cash flows for the years then ended. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audit included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing and opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Northwest Bancorporation, Inc. and subsidiary as of December 31, 2006 and 2005, and the results of their operations and their cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

Spokane, Washington

March 19, 2007, except for

the addition of the parent only financial information included in

Note 21 as to which the date is January 31, 2008

**NORTHWEST BANCORPORATION, INC. AND SUBSIDIARY**  
**CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION**

	December 31,	
	2006	2005
<b><u>ASSETS</u></b>		
Cash and due from banks	\$ 12,131,668	\$ 8,336,707
Interest bearing deposits in other institutions	68,630	205,222
Federal funds sold	167,895	2,028,408
Securities available for sale	31,337,393	32,200,153
Securities held to maturity, fair value 2006 \$3,971,944 and 2005 \$4,075,613	3,971,864	4,088,517
Federal Home Loan Bank stock, at cost	645,900	645,900
Loans receivable, net of allowance for loan losses 2006 \$2,586,094; 2005 \$2,252,329	215,122,007	186,317,944
Loans held for sale	1,574,718	148,000
Premises and equipment, net	7,252,448	5,650,373
Accrued interest receivable	1,372,731	1,040,207
Foreclosed real estate and other repossessed assets		16,521
Bank owned life insurance	3,432,503	3,313,771
Other assets	1,868,862	1,473,254
<b>TOTAL ASSETS</b>	<b>\$ 278,946,619</b>	<b>\$ 245,464,977</b>
<b><u>LIABILITIES AND STOCKHOLDERS EQUITY</u></b>		
Deposits	\$ 210,932,995	\$ 192,042,730
Securities sold under agreements to repurchase	25,783,940	17,754,671
Accrued interest payable	765,415	491,977
Federal funds purchased	3,630,000	
Borrowed funds	12,160,171	12,569,338
Other liabilities	1,153,494	919,893
<b>Total liabilities</b>	<b>254,426,015</b>	<b>223,778,609</b>
COMMITMENTS AND CONTINGENCIES (Notes 5 and 10)		
<b>STOCKHOLDERS EQUITY</b>		
Common stock, no par value, authorized 5,000,000 shares; issued and outstanding 2,236,460 and 2,108,864 shares	20,820,819	18,636,573
Retained earnings	3,889,105	3,306,113
Accumulated other comprehensive loss	(189,320)	(256,318)
<b>Total stockholders equity</b>	<b>24,520,604</b>	<b>21,686,368</b>
<b>TOTAL LIABILITIES AND STOCKHOLDERS EQUITY</b>	<b>\$ 278,946,619</b>	<b>\$ 245,464,977</b>

See accompanying notes.

## NORTHWEST BANCORPORATION, INC. AND SUBSIDIARY

## CONSOLIDATED STATEMENT OF INCOME

	Year Ended December 31,	
	2006	2005
<b>Interest Income:</b>		
Loans receivable, including fees	\$ 16,107,894	\$ 12,064,554
<b>Investment securities:</b>		
U.S. government agency securities	1,103,551	1,159,119
U.S. treasury securities	259,283	140,506
Other securities	172,310	150,697
Federal funds sold and interest bearing deposits	241,008	171,868
<b>Total interest income</b>	<b>17,884,046</b>	<b>13,686,744</b>
<b>Interest Expense:</b>		
Deposits	4,998,335	3,393,232
Borrowed funds and securities sold under agreements to repurchase	1,641,690	953,741
<b>Total interest expense</b>	<b>6,640,025</b>	<b>4,346,973</b>
<b>Net interest income</b>	<b>11,244,021</b>	<b>9,339,771</b>
Provision for loan losses	360,000	324,000
<b>Net interest income after provision for loan losses</b>	<b>10,884,021</b>	<b>9,015,771</b>
<b>Noninterest Income:</b>		
Service charges on deposits	885,948	953,605
Net gains from sale of loans	612,206	626,372
Other income	709,242	616,279
	<b>2,207,396</b>	<b>2,196,256</b>
<b>Noninterest Expense:</b>		
Salaries and employee benefits	5,232,840	4,565,934
Occupancy expense	914,148	769,269
Equipment expense	555,277	476,068
Loss on foreclosed real estate and other repossessed assets	5,120	158,991
Other operating expenses	2,253,740	2,061,008
	<b>8,961,125</b>	<b>8,031,270</b>
<b>Net income before income taxes</b>	<b>4,130,292</b>	<b>3,180,757</b>
Income tax expense	1,350,392	1,020,544
<b>NET INCOME</b>	<b>\$ 2,779,900</b>	<b>\$ 2,160,213</b>
<b>Basic earnings per share</b>	<b>\$ 1.24</b>	<b>\$ 0.98</b>
<b>Diluted earnings per share assuming full dilution</b>	<b>\$ 1.22</b>	<b>\$ 0.96</b>

See accompanying notes.



## NORTHWEST BANCORPORATION, INC. AND SUBSIDIARY

## CONSOLIDATED STATEMENT OF CHANGES IN STOCKHOLDERS' EQUITY

	Common Stock		Retained Earnings	Accumulated Other	Total	Comprehensive Income
	Shares	Amount		Comprehensive Income (Loss)		
Balance, December 31, 2004	2,004,901	\$ 16,943,428	\$ 3,063,164	\$ (45,110)	\$ 19,961,482	
Net income			2,160,213		2,160,213	\$ 2,160,213
Stock sold	60	494			494	
Stock issued to directors	3,700	60,347			60,347	
5% stock dividend	100,203	1,632,304	(1,632,304)			
Fractional shares paid in cash			(3,417)		(3,417)	
Cash dividend (\$0.14 per share)			(281,543)		(281,543)	
Net change in unrealized loss on available for sale securities, net of taxes				(211,208)	(211,208)	(211,208)
Comprehensive income						\$ 1,949,005
Balance, December 31, 2005	2,108,864	18,636,573	3,306,113	(256,318)	21,686,368	
Net income			2,779,900		2,779,900	\$ 2,779,900
Stock repurchased	(200)	(3,522)			(3,522)	
Stock sold	18,652	167,162			167,162	
Stock issued to directors	3,700	68,339			68,339	
Equity-based compensation		97,507			97,507	
5% stock dividend	105,444	1,854,760	(1,854,760)			
Fractional shares paid in cash			(4,000)		(4,000)	
Cash dividend (\$0.16 per share)			(338,148)		(338,148)	
Net change in unrealized loss on available for sale securities, net of taxes				66,998	66,998	66,998
Comprehensive income						\$ 2,846,898
Balance, December 31, 2006	2,236,460	\$ 20,820,819	\$ 3,889,105	\$ (189,320)	\$ 24,520,604	

See accompanying notes.

## NORTHWEST BANCORPORATION, INC. AND SUBSIDIARY

## CONSOLIDATED STATEMENT OF CASH FLOWS

	Year Ended December 31,	
	2006	2005
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Net income	\$ 2,779,900	\$ 2,160,213
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	562,193	458,610
Provision for loan losses	360,000	324,000
Provision for losses on foreclosed real estate and other repossessed assets	5,120	125,406
Accretion of securities discounts	(195,706)	(74,232)
Amortization of securities premiums	24,044	2,475
Increase in cash surrender value of bank owned life insurance	(118,732)	(121,049)
Loss on disposal of assets	3,812	1,074
Net loss (gain) on sale of foreclosed real estate and other repossessed assets		33,585
Stock dividends received		(2,600)
Deferred income taxes	(53,192)	(139,200)
Equity-based compensation expense	41,183	
Change in assets and liabilities:		
Accrued interest receivable	(332,524)	(209,059)
Other assets	(376,929)	(769,033)
Loans held for sale	(1,426,718)	475,263
Accrued interest payable	273,438	132,113
Other liabilities	233,601	(3,893)
Net cash provided by operating activities	1,779,490	2,393,673
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Net (increase) decrease in federal funds sold	1,860,513	(974,563)
Securities available for sale:		
Proceeds from maturities and principal payments	20,749,104	15,531,545
Purchases	(19,591,567)	(9,698,592)
Securities held to maturity:		
Proceeds from maturities and principal payments	535,000	335,000
Purchases	(439,951)	(1,737,185)
Purchases of premises and equipment	(2,168,080)	(1,153,923)
Proceeds from sale of premises and equipment		2,250
Proceeds from sale of foreclosed real estate and other repossessed assets	11,401	584,023
Net increase in loans	(29,164,063)	(29,240,703)
Net cash used by investing activities	(28,207,643)	(26,352,148)

See accompanying notes.



## NORTHWEST BANCORPORATION, INC. AND SUBSIDIARY

## CONSOLIDATED STATEMENT OF CASH FLOWS (Continued)

	Year Ended December 31,	
	2006	2005
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>		
Net increase in deposits	\$ 18,890,265	\$ 15,006,075
Net increase (decrease) in securities sold under agreements to repurchase	8,029,269	4,758,858
Proceeds from issuance of common stock	235,501	60,841
Excess tax benefit, equity-based compensation	56,324	
Payment of fractional shares	(4,000)	(3,417)
Repurchase of common stock	(3,522)	
Payment of cash dividends	(338,148)	(281,543)
Proceeds from issuance of borrowed funds	3,000,000	7,000,000
Proceeds from issuance of junior subordinated debentures		5,155,000
Repayment of borrowed funds	(3,409,167)	(5,400,336)
Net decrease in structured notes		(3,980,391)
Net increase in fed funds purchased	3,630,000	
Net cash provided by financing activities	30,086,522	22,315,087
<b>NET CHANGE IN CASH AND CASH EQUIVALENTS</b>		
Cash and cash equivalents, beginning of year	8,541,929	10,185,317
Cash and cash equivalents, end of year	\$ 12,200,298	\$ 8,541,929
<b>SUPPLEMENTAL CASH FLOWS INFORMATION</b>		
Cash paid during the year for:		
Interest	\$ 6,366,587	\$ 4,214,860
Income taxes	\$ 1,528,653	\$ 1,126,308
<b>SUPPLEMENTAL SCHEDULE OF NONCASH INVESTING ACTIVITIES</b>		
Net change in unrealized loss on securities available for sale	\$ 101,512	\$ (320,012)
Acquisition of real estate and other repossessed assets in settlement of loans	\$	\$ 37,000
<b>SUPPLEMENTAL SCHEDULE OF NONCASH FINANCING ACTIVITIES</b>		
Premises acquired through capital lease obligation	\$	\$ 600,404

See accompanying notes.

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**NORTHWEST BANCORPORATION, INC. AND SUBSIDIARY**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**Note 1 Summary of Significant Accounting Policies**

**Basis of presentation and consolidation:**

The consolidated financial statements include the accounts of Northwest Bancorporation, Inc. (the Company) and its wholly-owned subsidiary, Inland Northwest Bank (the Bank). All significant intercompany balances and transactions have been eliminated in consolidation.

**Nature of business:**

The Bank is a state chartered commercial bank under the laws of the state of Washington, and provides banking services primarily in eastern Washington and northern Idaho. The Bank is subject to competition from other financial institutions, as well as nonfinancial intermediaries. The Company and the Bank are also subject to the regulations of certain federal and state agencies and undergo periodic examinations by those regulatory agencies.

**Use of estimates:**

In preparing the consolidated financial statements in conformity with accounting principles generally accepted in the United States of America, management is required to make estimates and assumptions that affect the reported amounts of certain assets and liabilities as of the date of the consolidated statements of financial condition and certain revenues and expenses for the period. Actual results could differ, either positively or negatively, from those estimates.

Material estimates that are particularly susceptible to significant change in the near-term relate to the determination of deferred taxes, the allowance for loan losses, the valuation of real estate acquired in connection with foreclosures, or in satisfaction of loans, and stock options.

Management believes that the allowance for loan losses and other real estate owned is adequate. While management uses currently available information to recognize losses on loans and other real estate (when owned), future additions to the allowances may be necessary based on changes in economic conditions. In addition, various regulatory agencies, as an integral part of their examination process, periodically review the Bank's allowance for loan losses and other real estate owned. Such agencies may require the Bank to recognize additions to the allowances based on their judgments of information available to them at the time of their examination.

**Cash and cash equivalents:**

For the purpose of presentation in the consolidated statement of cash flows, cash and cash equivalents are defined as those amounts included in the statement of financial condition captioned cash and due from banks and interest-bearing deposits in other institutions, which mature within 90 days. Cash and cash equivalents on deposit with other financial institutions periodically exceed the federal insurance limit.

**Securities held to maturity:**

Bonds for which the Bank has the positive intent and ability to hold to maturity are reported at cost, adjusted for premiums and discounts that are recognized in interest income using the interest method over the period to maturity or call date if it is probable that the security will be called.

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**NORTHWEST BANCORPORATION, INC. AND SUBSIDIARY**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**Note 1 Summary of Significant Accounting Policies (Continued)**

**Securities available for sale:**

Securities available for sale consist of bonds, notes and mortgage-backed securities not classified as securities held to maturity or trading securities. Unrealized holding gains and losses, net of tax, on securities available for sale are reported as a net amount in accumulated comprehensive income. Gains and losses on the sale of securities available for sale are determined using the specific-identification method. Premiums and discounts are recognized in interest income using the interest method over the period to maturity or call date if it is probable that the security will be called.

Declines in the fair value of individual held to maturity and available for sale securities below their cost that are other than temporary result in write-downs of the individual securities to their fair value. No such write-downs have occurred.

**Loans held for sale:**

Mortgage loans originated and intended for sale in the secondary market are carried at the lower of cost or estimated market value in the aggregate. Net unrealized losses, if any, are recognized in a valuation allowance by charges to income. Gains or losses on the sale of such loans are based on the specific identification method.

**Loans:**

The Bank grants mortgage, commercial, installment and consumer loans to its customers. A substantial portion of the loan portfolio is represented by loans throughout eastern Washington and northern Idaho. The ability of the Bank's debtors to honor their contracts is dependent upon the real estate and general economic conditions in this area.

Loans that management has the intent and ability to hold for the foreseeable future or until maturity or pay-off generally are reported at their outstanding unpaid principal balances adjusted for charge-offs, the allowance for loan losses, and any deferred fees or costs on originated loans. Interest income is accrued on the unpaid principal balance. Loan origination fees, net of certain direct origination costs, are deferred and recognized as an adjustment of the related loan yield using the interest method.

The accrual of interest on loans is discontinued at the time the loan is 90 days delinquent unless the credit is well-secured and in process of collection. Management may also discontinue accrual of interest if management feels the borrower may be unable to meet payments as they become due. When interest accrual is discontinued, all unpaid accrued interest is reversed against interest income, with interest income subsequently recognized only to the extent cash payments are received. The interest on these loans is accounted for on the cash-basis or cost-recovery method, until qualifying for return to accrual. Loans are returned to accrual status when all the principal and interest amounts contractually due are brought current and future payments are reasonably assured.

In the ordinary course of business, the Bank has entered into commitments to extend credit, including commitments under credit card arrangements, commercial letters of credit and standby letters of credit. Such financial instruments are recorded when they are funded.

**Allowance for loan losses:**

The allowance for loan losses is established as losses are estimated to have occurred through a provision for loan losses charged to earnings. Loan losses are charged against the allowance when management believes the uncollectibility of a loan balance is confirmed. Subsequent recoveries, if any, are credited to the allowance.

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**NORTHWEST BANCORPORATION, INC. AND SUBSIDIARY**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**Note 1 Summary of Significant Accounting Policies (Continued)**

The allowance for loan losses is evaluated on a regular basis by management and is based upon management's periodic review of the collectibility of the loans in light of historical experience, the nature and volume of the loan portfolio, adverse situations that may affect the borrower's ability to repay, estimated value of any underlying collateral and prevailing economic conditions. This evaluation is inherently subjective as it requires estimates that are susceptible to significant revision as more information becomes available.

A loan is considered impaired when, based on current information and events, it is probable that the Bank will be unable to collect the scheduled payments, principal, or interest when due according to the contractual terms of the loan agreement. Factors considered by management in determining impairment include payment status, collateral value, and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower's prior payment record, and the amount of the shortfall in relation to the principal and interest owed. Impairment is measured on a loan by loan basis for commercial and construction loans by either the present value of expected future cash flows discounted at the loan's effective interest rate, the loan's obtainable market price, or the fair value of the collateral if the loan is collateral dependent.

Large groups of smaller balance homogeneous loans are collectively evaluated for impairment. Accordingly, the Bank does not separately identify individual consumer and residential loans for impairment disclosures.

**Premises and equipment:**

Buildings, furniture and equipment, and leasehold improvements are carried at cost, less accumulated depreciation and amortization over estimated useful lives or the related lease terms of the assets, which range from 3 to 39 years. Land is carried at cost. Depreciation and amortization expense is calculated using the straight-line method for financial statement purposes. Normal costs of maintenance and repairs are charged to expense as incurred.

**Foreclosed real estate and other repossessed assets:**

Real estate properties acquired through, or in lieu of, loan foreclosure are to be sold and are initially recorded at fair value at the date of foreclosure establishing a new carrying value. After foreclosure, valuations are periodically performed by management and the real estate is carried at the lower of carrying amount or fair value less selling cost. An allowance for impairment losses is used for declines in estimated fair value.

**Income taxes:**

Deferred income tax assets and liabilities are determined using the liability (or balance sheet) method. Under this method, the net deferred tax asset or liability is determined based on the tax effects of the temporary differences between the book and tax bases of the various balance sheet assets and liabilities and gives current recognition to changes in tax rates and laws.

**Stock compensation plan:**

At December 31, 2005, the Bank had a nonqualified stock option plan for key employees, which has subsequently been amended and which is described more fully in Note 14. Prior to January 1, 2006, the Company

## NORTHWEST BANCORPORATION, INC. AND SUBSIDIARY

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

## Note 1 Summary of Significant Accounting Policies (Continued)

and the Bank accounted for this plan under the recognition and measurement principles of Accounting Principles Board ( APB ) Opinion No. 25, *Accounting for Stock Issued to Employees* and related Interpretations. For the year ended December 31, 2005, no stock-based compensation cost is reflected in net income, as all options granted under the plan had an exercise price equal to the market value of the underlying common stock on the date of the grant. The following table illustrates the effect on net income and earnings per share if the Company and the Bank had applied the fair value recognition provisions of Financial Accounting Standards Board ( FASB ) Statement No. 123R *Accounting for Stock-Based Compensation*, to stock-based employee compensation.

The fair value assumptions for options granted in 2005 are based on a risk-free interest rate of 3.94%, 7 year expected life, 21.68% expected volatility and a 1.00% expected dividend rate.

	December 31, 2005
Net income, as reported	\$ 2,160,213
Deduct total stock-based employee compensation expense determined under fair value based method for all awards, net of related tax effects	(26,816)
Pro forma net income	\$ 2,133,397
Earnings per share:	
Basic, as reported	\$ 0.98
Basic, pro forma	\$ 0.96
Diluted, as reported	\$ 0.96
Diluted, pro forma	\$ 0.94

**Earnings per share:**

Earnings per share represents income available to common stockholders divided by the weighted-average number of common shares outstanding during the period. Earnings per share assuming full dilution reflects additional common shares that would have been outstanding if dilutive potential common shares had been issued, as well as any adjustment to income that would result from the assumed issuance. Potential common shares that may be issued by the Company related solely to outstanding stock options, and are determined using the treasury stock method (see Note 19).

**Comprehensive income:**

Accounting principles generally require that recognized revenue, expenses, gains and losses be included in net income. Although certain changes in assets and liabilities, such as unrealized gains and losses on available for sale securities, are reported as separate components of the equity section of the balance sheet, such items, along with net income are components of comprehensive income.

## NORTHWEST BANCORPORATION, INC. AND SUBSIDIARY

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

## Note 1 Summary of Significant Accounting Policies (Continued)

The components of other comprehensive income and related tax effects are as follows:

	Years Ended December 31	
	2006	2005
Unrealized holding gains/(losses) on available for sale securities	\$ 101,512	\$ (320,012)
Reclassification adjustment for gains realized in income		
Net unrealized losses	101,512	(320,012)
Tax effect	(34,514)	108,804
<b>NET OF TAX AMOUNT</b>	<b>\$ 66,998</b>	<b>\$ (211,208)</b>

**Reclassifications:**

Certain reclassifications have been made in the December 31, 2005 consolidated financial statements in order to conform to the December 31, 2006 presentation, with no effect on previously reported net income or stockholders' equity.

**New accounting pronouncements:**

**SFAS 157, Fair Value Measurements** In September 2006, the FASB issued SFAS No. 157, Fair Value Measurements. This Statement defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements. This Statement applies under other accounting pronouncements that require or permit fair value measurements. Accordingly, this Statement does not require any new fair value measurements. This Statement is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. SFAS No. 157 is not expected to have a material impact on the Company.

In September 2006, the SEC's Office of the Chief Accountant and Divisions of Corporation Finance and Investment Management released SAB No. 108, *Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements* (SAB No. 108), that provides interpretive guidance on how the effects of the carryover or reversal of prior year misstatements should be considered in quantifying a current year misstatement. The SEC staff believes that registrants should quantify errors using both a balance sheet and an income statement approach and evaluate whether either approach results in quantifying a misstatement that, when all relevant quantitative and qualitative factors are considered, is material. This pronouncement is effective for fiscal years ending after November 15, 2006. The Company has adopted SAB No. 108 and has found there to be no material impact on its financial position or results of operations.

**FIN No. 48, Accounting for Uncertainty in Income Taxes** On July 13, 2006, FASB issued Interpretation (FIN) No. 48, Accounting for Uncertainty in Income Taxes An Interpretation of FASB Statement No. 109. FIN 48 clarifies the accounting for uncertainty in income taxes recognized in an enterprise's financial statements in accordance with SFAS No. 109, Accounting for Income Taxes. FIN 48 also prescribes a consistent recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. FIN No. 48 also provides guidance on de-recognition, classification, interest and penalties, accounting in interim periods, disclosure, and transition. The provisions of FIN 48 are effective for fiscal years beginning after December 15, 2006. FIN 48 is not expected to have a material impact on the Company.

## NORTHWEST BANCORPORATION, INC. AND SUBSIDIARY

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

## Note 1 Summary of Significant Accounting Policies (Continued)

## Advertising costs:

Advertising costs are charged to operations when incurred. Advertising expense for the years ended December 31, 2006 and 2005 was \$120,700 and \$139,218, respectively.

## Note 2 Investments in Securities

Securities held by the Bank have been classified in the consolidated statement of financial condition according to management's intent. The amortized cost of securities and their approximate fair values at December 31, 2006 and 2005, were as follows:

	Amortized Cost	December 31, 2006		Fair Value
		Gross Unrealized Gains	Gross Unrealized Losses	
<b>Securities available for sale:</b>				
U.S. government agency securities	\$ 23,195,000	\$ 4,370	\$ (275,583)	\$ 22,923,787
U.S. treasury securities	6,959,627	10,476	(7,283)	6,962,820
Corporate debt obligations	500,000		(44,740)	455,260
Mortgage backed securities	969,616	25,910		995,526
	\$ 31,624,243	\$ 40,756	\$ (327,606)	\$ 31,337,393

	Amortized Cost	December 31, 2005		Fair Value
		Gross Unrealized Gains	Gross Unrealized Losses	
<b>Securities available for sale:</b>				
U.S. government agency securities	\$ 25,695,000	\$ 1,312	\$ (390,073)	\$ 25,306,239
U.S. treasury securities	5,129,924		(10,304)	5,119,620
Corporate debt obligations	494,357		(39,167)	455,190
Mortgage backed securities	1,269,232	49,872		1,319,104
	\$ 32,588,513	\$ 51,184	\$ (439,544)	\$ 32,200,153

	Amortized Cost	December 31, 2006		Fair Value
		Gross Unrealized Gains	Gross Unrealized Losses	
<b>Securities held to maturity:</b>				
State and municipal securities	\$ 3,971,864	\$ 25,655	\$ (25,575)	\$ 3,971,944

	Amortized Cost	December 31, 2005		Fair Value
		Gross Unrealized Gains	Gross Unrealized Losses	
<b>Securities held to maturity:</b>				
State and municipal securities	\$ 4,088,517	\$ 22,999	\$ (35,903)	\$ 4,075,613





## NORTHWEST BANCORPORATION, INC. AND SUBSIDIARY

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

## Note 2 Investments in Securities (Continued)

The following table shows the investments' gross unrealized losses and fair values, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position at December 31, 2006.

	December 31, 2006					
	Impaired Less Than 12 Months		Impaired 12 Months or More		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
U.S. government agency securities	\$ 399,236	\$ (764)	\$ 21,520,182	\$ (274,819)	\$ 21,919,418	\$ (275,583)
U.S. treasury securities	3,165,480	(7,283)			3,165,480	(7,283)
Corporate debt obligations	455,260	(44,740)			455,260	(44,740)
State and municipal securities	2,595,264	(24,486)	198,911	(1,089)	2,794,175	(25,575)
	\$ 6,615,240	\$ (77,273)	\$ 21,719,093	\$ (275,908)	\$ 28,334,333	\$ (353,181)

Management has evaluated the above securities and does not believe that any individual unrealized loss as of December 31, 2006, represents an other-than-temporary impairment. The decline in fair market value of these securities is generally due to changes in interest rates since purchase and is not related to any known decline in the creditworthiness of the issuer. At December 31, 2006, forty-four securities have unrealized losses.

At December 31, 2006 and 2005, securities available for sale with an amortized cost of \$23,847,055 and \$21,697,664, respectively, were pledged to secure the Bank's performance of its obligations under repurchase agreements. The market value of these securities was \$23,585,965 and \$21,387,660 at December 31, 2006 and 2005, respectively. Securities held to maturity with an amortized cost of \$3,971,864 and \$521,660 at December 31, 2006 and 2005, respectively, were pledged to secure the Bank's performance of its obligations under repurchase agreements. The market value of these securities was \$3,971,944 and \$514,861 at December 31, 2006 and 2005, respectively. Securities available for sale with an amortized cost of \$2,064,557 and \$2,110,925 at December 31, 2006 and 2005, respectively, were pledged to secure public deposits for purposes required or permitted by law. The market value of these securities was \$2,038,438 and \$2,094,230 at December 31, 2006 and 2005, respectively. Securities available for sale with an amortized cost of \$5,712,630 and \$5,879,924 at December 31, 2006 and 2005, respectively, were pledged to the Federal Reserve Bank. The market value of these securities was \$5,712,990 and \$5,857,433 at December 31, 2006 and 2005, respectively.

For the years ended December 31, 2006 and 2005, there were no sales of securities available for sale.

The scheduled maturities of securities held to maturity and securities available for sale at December 31, 2006, are as follows:

	Held to maturity		Available for sale	
	Amortized	Fair Value	Amortized	Fair Value
	Cost		Cost	
Due in one year or less	\$ 275,243	\$ 274,971	\$ 7,959,627	\$ 7,956,570
Due from one year to five years	904,409	896,065	6,000,000	5,959,210
Due from five to ten years	2,061,482	2,060,860	11,890,000	11,737,665
Due after ten years	730,730	740,048	4,805,000	4,688,423
Mortgage backed securities			969,616	995,525
	\$ 3,971,864	\$ 3,971,944	\$ 31,624,243	\$ 31,337,393



## NORTHWEST BANCORPORATION, INC. AND SUBSIDIARY

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

**Note 3 Federal Home Loan Bank Stock (FHLB)**

The Bank's investment in the Federal Home Loan Bank of Seattle (class B stock) is carried at par value (\$100 per share), which reasonably approximates its fair value. As a member of the FHLB system, the Bank is required to maintain a minimum level of investment in FHLB stock based on specified percentages of its outstanding FHLB advances. The Bank may request redemption at par value of any stock in excess of the amount the Bank is required to hold. Stock redemptions are at the discretion of the FHLB and generally require five years prior written notice to FHLB.

The Seattle FHLB is regulated by the Federal Housing Finance Board (the Finance Board). In connection with a 2004 examination, the Seattle FHLB presented a three-year business and capital management plan to the Finance Board's Office of Supervision. In a Written Agreement with the Seattle FHLB, the Finance Board accepted the plan subject to certain restrictions on stock repurchases and dividend payments. The Seattle FHLB did not pay dividends on its stock in 2005. On January 12, 2007, the Finance Board terminated the Written Agreement. According to the Seattle FHLB, the termination of the agreement was because it is now in full compliance with the terms of the agreement and that it has made significant progress in implementing its business and capital management plan. The Seattle FHLB did pay a small dividend in late 2006, based on third-quarter 2006 earnings. Future dividend payments are subject to a formula outlined in the Seattle FHLB's Form 8-K filing with the Securities and Exchange Commission, dated October 11, 2006.

**Note 4 Loans Receivable and Allowance for Loan Losses**

The components of loans in the consolidated statement of financial condition were as follows:

	December 31,	
	2006	2005
Commercial	\$ 127,420,075	\$ 124,611,102
Real estate	74,496,452	50,162,043
Installment	8,089,752	5,079,144
Consumer and other	8,101,648	8,990,996
	<b>218,107,927</b>	188,843,285
Allowance for loan losses	<b>(2,586,094)</b>	(2,252,329)
Net deferred loan fees	<b>(399,826)</b>	(273,012)
	<b>\$ 215,122,007</b>	\$ 186,317,944

An analysis of the change in the allowance for loan losses follows:

	December 31,	
	2006	2005
Balance, beginning of year	\$ 2,252,329	\$ 1,943,760
Reverse prior year reclassification of reserve for probable losses on unused loan commitments and off-balance sheet items	178,190	206,080
Balance, beginning of year, including OBS reserve	2,430,519	2,149,840
Provision charged to operations	360,000	324,000
Loans charged off, net of recoveries	<b>(4,899)</b>	(43,321)
Balance, end of year, prior to adjustment for off-balance sheet items	2,785,620	2,430,519

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Reclassification of reserve for probable losses on unused loan commitments and off-balance sheet items to Accrued interest payable and other liabilities	(199,526)	(178,190)
Balance, end of year	<b>\$ 2,586,094</b>	\$ 2,252,329

## NORTHWEST BANCORPORATION, INC. AND SUBSIDIARY

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

## Note 4 Loans Receivable and Allowance for Loan Losses (Continued)

The loans fall into the following fixed and variable components:

	December 31,	
	2006	2005
Fixed rate loans	\$ 61,246,767	\$ 53,476,753
Variable rate loans	156,861,160	135,366,532
	<b>\$ 218,107,927</b>	<b>\$ 188,843,285</b>

Impairment of loans having recorded investments of \$467,278 and \$634,876 at December 31, 2006 and 2005, respectively, has been recognized in conformity with FASB Statement No. 114 as amended by FASB Statement No. 118. The total allowance for loan losses related to these loans was \$265,760 and \$309,290 at December 31, 2006 and 2005, respectively. The Bank is not committed to lend additional funds to debtors whose loans have been modified. The average recorded investment in impaired loans during the years ended December 31, 2006 and 2005, was \$533,743 and \$678,399, respectively. Interest income on impaired loans of \$2,725 and \$7,923 was recognized for cash payments received in 2006 and 2005, respectively. The Company had \$319,922 and \$405,168 of loans placed on nonaccrual at December 31, 2006 and 2005, respectively. Loans over 90 days past due and still on accrual status were \$-0- and \$19,333 at December 31, 2006 and 2005, respectively.

## Note 5 Premises and Equipment

Components of premises and equipment included in the consolidated statement of financial condition at December 31, 2006 and 2005, were as follows:

	December 31,	
	2006	2005
Premises	\$ 2,314,849	\$ 1,588,103
Furniture, fixtures and equipment	4,255,825	3,921,946
Leasehold improvements	2,252,280	1,880,341
	<b>8,822,954</b>	7,390,390
Less accumulated depreciation and amortization	<b>(4,395,170)</b>	<b>(4,000,743)</b>
	<b>4,427,784</b>	3,389,647
Land	2,809,542	1,816,334
Construction in progress	15,122	444,392
Premises and equipment, net	<b>\$ 7,252,448</b>	<b>\$ 5,650,373</b>

Depreciation and amortization expense was \$562,193 and \$458,610 for the years ended December 31, 2006 and 2005, respectively.

The Bank has operating leases on a number of its branches that expire on various dates through 2026. The lease agreements have various renewal options.

## NORTHWEST BANCORPORATION, INC. AND SUBSIDIARY

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

## Note 5 Premises and Equipment (Continued)

The following is a schedule by year of future minimum rental payments required under operating leases that have initial or remaining noncancellable lease terms in excess of one year as of December 31, 2006:

<b>Year ending December 31,</b>	
2007	\$ 424,695
2008	294,678
2009	193,338
2010	89,340
2011	96,171
Thereafter	1,454,578
<b>TOTAL MINIMUM PAYMENTS REQUIRED</b>	<b>\$ 2,552,800</b>

Total lease payments under the above mentioned operating leases and other month-to-month rentals for the years ended December 31, 2006 and 2005, were \$437,910 and \$389,781, respectively.

The Bank acquired \$600,404 in land under a capital lease agreement that expires in 2031. The minimum annual lease commitments under this capital lease agreement are summarized as follows:

<b>Year ending December 31,</b>	
2007	\$ 48,000
2008	48,000
2009	48,000
2010	49,500
2011	54,000
Thereafter	1,051,417
	1,298,917
Less amount representing interest	699,513
<b>PRESENT VALUE OF LEASE PAYMENTS</b>	<b>\$ 599,404</b>

In 2006, the Bank entered into an agreement with the Spokane Public Facilities District (PFD) for the purchase of naming rights to the Spokane Opera House; now known as the INB Performing Arts Center. Under the agreement, the Bank will pay the PFD \$150,000 per year for a period of ten years, with the final payment due in 2015.

## Note 6 Foreclosed Real Estate and Other Repossessed Assets

An allowance for losses on foreclosed real estate and other repossessed assets has been established. Activity in the account is as follows:

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	2006	2005
Balance, beginning of year	\$	\$ 125,000
Charge offs	(5,120)	(250,406)
Provision charged to income	5,120	125,406
Balance, end of year	\$	\$

## NORTHWEST BANCORPORATION, INC. AND SUBSIDIARY

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

**Note 6 Foreclosed Real Estate and Other Repossessed Assets (Continued)**

Included in the losses on foreclosed real estate and other repossessed assets in the consolidated statement of income for the years ending December 31, 2006 and 2005, are impairment losses of \$5,120 and \$125,406, respectively, on real estate and other repossessed assets held for sale. Realized gains (losses) of \$0 and \$(33,585) are included in (gain) loss on foreclosed real estate and other repossessed assets for the years ended December 31, 2006 and 2005, respectively.

**Note 7 Deposits**

Major classifications of deposits at December 31, 2006 and 2005, were as follows:

	2006	2005
Non-interest bearing demand deposits	\$ 49,436,083	\$ 49,107,178
Money market	36,322,976	44,899,228
NOW accounts	13,222,069	13,037,717
Savings deposits	8,825,525	8,245,679
Time deposits, \$100,000 and over	38,658,512	29,310,784
Other time deposits	64,467,830	47,442,144
	<b>\$ 210,932,995</b>	<b>\$ 192,042,730</b>

Maturities for time deposits at December 31, 2006, are summarized as follows:

Maturing one year or less	\$ 48,417,071
Maturing one to five years	54,709,271
Maturing five to ten years	
	\$ 103,126,342

Overdraft deposit accounts with balances of \$73,506 and \$49,611 at December 31, 2006 and 2005, respectively, were reclassified as loans receivable.

**Note 8 Borrowed Funds**

In June 2005, the Company issued junior subordinated debentures aggregating \$5,155,000 to Northwest Bancorporation Capital Trust I, with interest fixed at 5.95% through June 30, 2010, thereafter re-pricing quarterly at three-month LIBOR plus 1.70%. The Trust issued \$155,000 of common securities to the Company and capital securities with an aggregate liquidation amount of \$5,000,000 (\$1,000 per capital security) to third-party investors. The common securities are included in Other assets on the statement of financial condition; the subordinated debentures are included in Borrowed funds. The subordinated debentures are includable as Tier I capital for regulatory purposes. The subordinated debentures and the capital securities pay interest and dividends, respectively, on a quarterly basis, which are included in interest expense. The subordinated debentures will mature on June 30, 2035, at which time the capital securities must be redeemed. The subordinated debentures and capital securities can be redeemed, in whole or in part, beginning June 30, 2010, at a redemption price of \$1,000 per capital security. The Company has provided a full and unconditional guarantee of the obligations of the Trust under the capital securities in the event of default. Northwest Bancorporation Capital Trust I is not consolidated in these financial statements. Pursuant to FIN 46R, the Company reports the junior subordinated debentures within the liabilities section of the statement of financial condition.





## NORTHWEST BANCORPORATION, INC. AND SUBSIDIARY

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

## Note 8 Borrowed Funds (Continued)

Other borrowed funds reported by the Bank consist primarily of Federal Home Loan Bank advances and overnight Federal Funds Purchased from a correspondent bank. Federal Home Loan Bank advances are secured by a blanket pledge on Bank assets and specifically by loans with a carrying value of \$65,928,304 at December 31, 2006. Federal Funds Purchased are borrowed on an unsecured basis.

Total borrowed funds consist of the following at December 31:

Advance Date	Maturity Date	Interest Rate	2006	2005
07/29/97	07/29/27	6.60%	\$ 43,664	\$ 45,778
04/20/98	04/19/13	6.15%	1,033,554	1,151,415
05/11/98	05/11/28	6.28%	98,698	100,372
08/19/98	08/18/28	6.09%	101,450	103,253
02/11/02	02/09/07	5.05%	2,500,000	2,500,000
02/11/02	02/11/09	4.94%	628,401	914,116
04/11/05	04/09/10	4.64%	2,000,000	2,000,000
Total Federal Home Loan Bank advances			6,405,767	6,814,934
Junior subordinated debentures			5,155,000	5,155,000
Capital lease obligation (see Note 5)			599,404	599,404
<b>TOTAL BORROWED FUNDS</b>			<b>\$ 12,160,171</b>	<b>\$ 12,569,338</b>

The scheduled maturities of the Federal Home Loan Bank advances at December 31, 2006, are as follows:

Years Ending	Weighted-Average Interest Rate	Amount
December 31, 2007	5.09%	\$ 2,919,863
2008	5.35%	431,503
2009	5.84%	215,429
2010	4.76%	2,172,239
2011	6.16%	187,238
Thereafter	6.19%	479,495
		\$ 6,405,767

## Note 9 Securities Sold Under Repurchase Agreements

Securities sold under agreements to repurchase generally mature within one to four days from the transaction date. For the year, securities sold under agreements to repurchase averaged \$21,124,599; the high balance during the year was \$27,474,692. The average rate paid during the year was 4.29%. Securities underlying the agreements are presented in Note 2. Securities sold under agreements to repurchase are reflected at the amount of cash received in connection with the transaction. The Bank may be required to provide additional collateral based on the fair value of the underlying securities.

## Note 10 Commitments and Contingencies

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The Bank is a party to various legal collection actions normally associated with financial institutions, the aggregate effect of which, in management's and legal counsel's opinion, would not be material to the financial condition of Northwest Bancorporation.

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**NORTHWEST BANCORPORATION, INC. AND SUBSIDIARY**
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)****Note 10 Commitments and Contingencies (Continued)**

The Bank has three unsecured operating lines of credit with KeyBank of Washington for \$10,200,000, with two lines totaling \$10,100,000, maturing July 1, 2007, and the remaining \$100,000 line maturing on July 1, 2008. In addition, the Bank maintains lines of credit with Pacific Coast Bankers Bank for \$5,000,000, maturing June 30, 2007; U.S. Bank for \$1,500,000, maturing July 31, 2007; and, Zions Bank for \$1,500,000, with no stated maturity. There was \$3,630,000 outstanding on the KeyBank line at December 31, 2006 (detailed in the Consolidated Statements of Financial Condition as Federal funds purchased ) and zero outstanding on any of the lines at December 31, 2005. The Bank also has a line of credit with Federal Home Loan Bank for \$41,740,000 at December 31, 2006, with \$35,335,000 available in overnight funds and long-term funds. This line is collateralized by a general pledge of all assets of the Bank. There were \$6,405,768 and \$6,814,934 of outstanding long-term advances on the Federal Home Loan Bank line at December 31, 2006 and 2005, respectively (see Note 8). There was zero outstanding on overnight funds on the FHLB line at December 31, 2006 and 2005.

In the ordinary course of business the Bank makes various commitments and incurs certain contingent liabilities, which are not reflected in the accompanying financial statements. The Bank uses the same credit policies in making such commitments as they do for instruments that are included in the consolidated statement of financial condition. These commitments and contingent liabilities include various commitments to extend credit and standby letters of credit. At December 31, 2006 and 2005, commitments under standby letters of credit were \$1,276,927 and \$844,625, respectively, and firm loan commitments were \$99,724,243 and \$86,568,925, respectively. Substantially all of the commitments provide for repayment at a variable rate of interest. The Bank does not anticipate any material losses as a result of these commitments.

**Note 11 Concentrations of Credit Risk**

The majority of the Bank's loans, commitments, and standby letters of credit have been granted to customers in the Bank's market area, which is the eastern Washington and northern Idaho area. Substantially all such customers are depositors of the Bank. The concentrations of credit by type of loan are set forth in Note 4. The distribution of commitments to extend credit approximates the distribution of loans outstanding. Outstanding commitments and standby letters of credit were granted primarily to commercial borrowers.

The Bank places its cash with high credit quality institutions. The amount on deposit fluctuates, and at times exceeds the insured limit by the U.S. Federal Deposit Insurance Corporation, which potentially subjects the Bank to credit risk.

**Note 12 Income Taxes**

The components of income tax expense are as follows:

	2006	2005
Current tax expense	\$ 1,403,584	\$ 1,159,744
Deferred tax benefit	(53,192)	(139,200)
<b>INCOME TAX EXPENSE</b>	<b>\$ 1,350,392</b>	<b>\$ 1,020,544</b>

## NORTHWEST BANCORPORATION, INC. AND SUBSIDIARY

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

## Note 12 Income Taxes (Continued)

The components of the deferred tax assets and deferred tax liabilities are as follows:

	2006	2005
Deferred tax assets:		
Allowance for loan losses	\$ 763,455	\$ 637,455
Net unrealized loss on securities available for sale	97,529	132,042
Deferred compensation	153,361	125,754
Stock options	13,978	
Goodwill amortization	35,642	40,273
Nonaccrual loan interest	3,740	3,397
Other	4,910	5,835
	<b>1,072,615</b>	<b>944,756</b>
Deferred tax liabilities:		
Fixed asset basis differentials	434,720	438,452
Federal Home Loan Bank stock	95,092	95,092
Deferred loan fees and costs	148,227	81,696
Prepaid expenses	101,827	55,446
	<b>779,866</b>	<b>670,686</b>
NET DEFERRED TAX ASSET	<b>\$ 292,749</b>	<b>\$ 274,070</b>

The effective tax rate differs from the statutory federal tax rate for the years presented as follows:

	2006	2005
Federal income tax at statutory rate	\$ 1,404,299	\$ 1,081,458
Effect of tax-exempt interest income	(50,248)	(49,356)
Effect of nondeductible interest expense	8,354	5,033
Effect of state income taxes	35,231	22,559
Other	(47,244)	(39,150)
INCOME TAX EXPENSE	<b>\$ 1,350,392</b>	<b>\$ 1,020,544</b>

At December 31, 2006, an income tax receivable of \$271,971 and a net deferred tax asset of \$292,749 were included in other assets on the consolidated statement of financial condition; a state income tax payable of \$18,511 was included in other liabilities. At December 31, 2005, an income tax receivable of \$87,286 and a net deferred tax asset of \$274,070 were included in other assets on the consolidated statement of financial condition; a state income tax payable of \$15,219 is included in other liabilities.

## Note 13 Employee Benefits

The Bank maintains a 401(k) profit sharing plan covering all employees who meet certain eligibility requirements. The plan provides for employees to elect up to 50% of their compensation to be paid into the plan. The Bank's policy is to match contributions equal to 50% of the participant's contribution, not to exceed 2.5% of the participant's compensation. Vesting occurs over a six-year graded vesting schedule. Expenses

associated with the plan were \$99,492 and \$94,960 for the years ended December 31, 2006 and 2005, respectively.

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**NORTHWEST BANCORPORATION, INC. AND SUBSIDIARY**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**Note 13 Employee Benefits (Continued)**

The Bank maintains a nonqualified deferred compensation plan under which eligible participants may elect to defer a portion of their compensation, with prior annual approval of the Board of Directors. The Bank does not match contributions to this plan, but does credit interest on amounts deferred based on the tax-equivalent rate earned on its bank owned life insurance products. Expenses associated with the plan were \$10,489 and \$7,331 for the years ended December 31, 2006 and 2005, respectively. Accrued liabilities associated with the plan were \$220,283 and \$154,593 for December 31, 2006 and 2005, respectively. To fund benefits under this plan, the Bank is the owner and beneficiary of single premium life insurance policies on certain current and past employees. At December 31, 2006 and 2005, the cash value of these policies was \$3,432,503 and \$3,313,771, respectively.

The Bank maintains unfunded, nonqualified executive income and retirement plans for certain of its current and retired senior executives under which participants designated by the Board of Directors are entitled to supplemental income or retirement benefits. Expenses associated with these plans were \$37,826 and \$37,207 for the years ended December 31, 2006 and 2005, respectively. Accrued liabilities associated with these plans were \$217,892 and \$204,704 for December 31, 2006 and 2005, respectively.

**Note 14 Stock Based Compensation**

On May 15, 2006, stockholders approved the Inland Northwest Bank 2006 Share Incentive Plan and the issuance of shares of common stock of the Company pursuant to the Plan. This Plan is an amendment and restatement of the Inland Northwest Bank Non-Qualified Stock Option Plan originally effective July 21, 1992, as revised December 21, 1993, December 21, 1999 and April 16, 2002. The Plan allows the Board of Directors of Inland Northwest Bank to grant stock options and restricted stock awards to key employees of the Bank. At a meeting of the Board of Directors in July 2006, the Directors delegated the administration of the Plan to the Compensation and Insurance Committee. As of January 1, 2006, the Company adopted SFAS No. 123(R), Share Based Payment, which requires the recognition of compensation costs relating to share-based payment transactions in the financial statements. The Company has elected the modified prospective application method of reporting, which provides for no restatement of prior periods and no cumulative adjustment to equity accounts. Prior to the adoption of SFAS No. 123(R), the Company elected to account for stock-based compensation using the intrinsic value-based method of recognizing compensation costs outlined in APB Opinion No. 25, Accounting for Stock Issued to Employees, and adopted the disclosure-only provisions under SFAS No. 123, Accounting for Stock-Based Compensation.

The decision as to whether to award restricted stock grants or options may vary from time-to-time or from employee to employee, at the discretion of the Bank's Compensation and Insurance Committee; however, it is anticipated that restricted stock will be awarded, primarily, to promote the long-term interests of the Company by retaining key Bank employees and stock options will be awarded, primarily, to attract key Bank employees. The maximum number of stock options and restricted shares that may be awarded under the Plan, as adjusted for stock dividends, is 366,583. At December 31, 2006, 200,080 shares and/or options were available for award to employees.

Restricted stock awards cliff-vest after a three-year period and, therefore, the fair value of these awards will be recognized ratably over a three-year period as compensation expense. Stock options vest over a five-year period and expire at the end of ten-years. The fair value of these awards will be recognized ratably over the vesting period as compensation expense. At December 31, 2006, restricted stock awards of 10,150 shares of common stock and stock options representing 120,136 shares of common stock were outstanding. None of the restricted stock awards outstanding have vested as of December 31, 2006. Options representing 100,932 shares have vested as of December 31, 2006.

## NORTHWEST BANCORPORATION, INC. AND SUBSIDIARY

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

## Note 14 Stock Based Compensation (Continued)

Restricted stock-award activity is summarized in the following table:

	Number of shares	Weighted average fair value at date of grant
Outstanding at December 31, 2005		\$
Granted	10,150	17.97
Forfeited		
Exercised		
Outstanding at December 31, 2006	10,150	\$ 17.97

Stock options vest over a five-year period and expire ten years from the date of the grant. The exercise price of each option equals the fair market value of the Company's stock on the date of grant.

The fair value of each option award is estimated on the date of grant using the Black-Scholes option pricing model that uses the assumptions noted in the following table. The risk-free rate is based on the U.S. Treasury yield curve in effect at the time of grant. The expected life of options granted represents the period of time that options granted are expected to be outstanding. Expected volatilities are based on historical volatility of the Company's stock. Historical forfeiture rate is nominal. Expected dividend yield reflects the Company's expected future dividend rates.

	Risk free interest rate	Expected life (years)	Expected volatility	Expected forfeiture rate	Expected dividend yield
Options granted in 2005	3.94%	7	21.86%	0.00%	1.00%
Options granted in 2006	4.49%	7	25.56%	0.00%	0.88%

Stock option activity is summarized in the following table:

	2006		2005	
	Shares actual	Weighted-average exercise price	Shares actual	Weighted-average exercise price
Outstanding options, beginning of year	139,079	\$ 9.69	137,072	\$ 9.62
Granted	3,675	\$ 17.35	2,205	\$ 12.74
Exercised	(18,702)	\$ 8.94	(63)	\$ 7.47
Forfeited	(3,916)	\$ 11.81	(134)	\$ 7.47
Outstanding options, end of year	120,136	\$ 9.95	139,079	\$ 9.69
Options exercisable at year end	100,932		108,338	
Weighted-average fair value of options granted during the year	\$ 6.18		\$ 4.25	





## NORTHWEST BANCORPORATION, INC. AND SUBSIDIARY

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

## Note 14 Stock Based Compensation (Continued)

Options outstanding at December 31, 2006 were as follows:

Price ranges	Options outstanding			Exercisable options			
	Number outstanding at end of year	Weighted-average contractual life	Weighted-average exercise price	Intrinsic value of stock options	Number exercisable at end of year	Weighted-average exercise price	Intrinsic value of stock options
(\$7.46)	20,637	3.96	\$ 7.46	\$ 223,294	20,637	\$ 7.46	\$ 223,289
(\$7.47 through \$11.36)	39,027	4.35	\$ 8.09	\$ 397,641	36,475	\$ 8.08	\$ 372,191
(\$11.37 through \$17.57)	60,472	5.00	\$ 12.00	\$ 380,032	43,820	\$ 11.51	\$ 296,776
<b>TOTAL</b>	<b>120,136</b>	<b>4.61</b>	<b>\$ 9.95</b>	<b>\$ 1,000,967</b>	<b>100,932</b>	<b>\$ 9.44</b>	<b>\$ 892,256</b>

For the year ended December 31, 2006 cash proceeds of \$167,162 were received from the exercise of options. It is the Company's policy to issue new shares for the exercise of stock options.

The pre-tax compensation expense yet to be recognized for stock-based awards that have been awarded but not vested is as follows:

	Stock options	Restricted stock	Total awards
2007	\$ 15,569	\$ 59,441	\$ 75,010
2008	8,099	58,443	66,542
2009	3,329	45,469	48,798
2010	993		993
2011	88		88
Total	\$ 28,078	\$ 163,353	\$ 191,431

The following table illustrates the effect of the change, from applying the original provisions of SFAS No. 123, to the adoption of SFAS No. 123(R), on the Company's results of operations for the year ended December 31, 2006.

	Using previous accounting	Equity-based compensation adjustments	As reported
Income before income taxes	\$ 4,171,475	\$ (41,183)	\$ 4,130,292
Income taxes	\$ 1,363,857	\$ (13,465)	\$ 1,350,392
Net income	\$ 2,807,618	\$ (27,718)	\$ 2,779,900
Basic earnings per share	\$ 1.26	\$ (0.02)	\$ 1.24
Diluted earnings per share	\$ 1.23	\$ (0.01)	\$ 1.22

## Note 15 Common Stock

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On April 19, 2005, the Board of Directors announced a 5% stock dividend on all common stock, effective to stockholders of record May 16, 2005, and issued June 15, 2005. All amounts per share and weighted-average shares outstanding for all periods presented have been retroactively adjusted to reflect the stock dividends. The Company recorded a transfer from retained earnings to common stock for the market value of the additional shares issued at May 16, 2005.

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**NORTHWEST BANCORPORATION, INC. AND SUBSIDIARY**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**Note 15 Common Stock (Continued)**

On April 18, 2006, the Board of Directors announced a 5% stock dividend on all common stock, effective to stockholders of record May 15, 2006, and issued June 15, 2006. All amounts per share and weighted-average shares outstanding for all periods presented have been retroactively adjusted to reflect the stock dividends. The Company recorded a transfer from retained earnings to common stock for the market value of the additional shares issued at May 15, 2006.

During 2006 and 2005, the Board of Directors voted to issue 3,700 shares of Company stock to nonemployee Directors pursuant to the Company's Director Compensation Plan.

**Note 16 Related Party Transactions**

The Company, through its Bank subsidiary, has had, and may be expected to have in the future, banking transactions in the ordinary course of business with directors, principal officers, their immediate families, and affiliated companies in which they are principal stockholders. Aggregate loan balances with related parties at December 31, 2006 and 2005, were \$2,363,141 and \$2,053,487, respectively. During the years ended December 31, 2006 and 2005, total principal additions were \$673,262 and \$1,994,109 and total principal payments were \$363,608 and \$2,250,859, respectively. Aggregate deposit balances with related parties at December 31, 2006 and 2005, were \$2,200,330 and \$1,552,675, respectively. All related party loans and deposits which have been made, in the opinion of management, are on the same terms, including interest rates and collateral, as those prevailing at the time for comparable transactions with others.

**Note 17 Restrictions on Dividends and Retained Earnings**

Federal and state banking regulations place certain restrictions on dividends paid by the Bank to the Company. The total amount of dividends, which may be paid at any date, is generally limited to the retained earnings of the Bank, which was \$13,556,684 at December 31, 2006. Accordingly, \$12,864,293 of the Company's equity in the net assets of the Bank was restricted at December 31, 2006.

In addition, dividends paid by the Bank to the Company would be prohibited if the effect thereof would cause the Bank's capital to be reduced below applicable minimum capital requirements.

**Note 18 Regulatory Capital Requirements**

The Bank is subject to various regulatory capital requirements administered by the federal banking agencies. Failure to meet minimum capital requirements can initiate certain mandatory and possibly additional discretionary actions by regulators that, if undertaken, could have a direct material effect on the Bank's financial statements. Under capital adequacy guidelines on the regulatory framework for prompt corrective action, the Bank must meet specific capital adequacy guidelines that involve quantitative measures of the Bank's assets, liabilities, and certain off-balance-sheet items as calculated under regulatory accounting practices. The Bank's capital classification is also subject to qualitative judgments by the regulators about components, risk weightings, and other factors.

Quantitative measures established by regulation to ensure capital adequacy require the Bank to maintain minimum amounts and ratios (set forth in the following table) of Tier 1 capital (as defined in the regulations) to total average assets (as defined), and minimum ratios of Tier 1 and total capital (as defined) to risk-weighted assets (as defined). Under the regulatory framework for prompt corrective action, the Bank must maintain minimum Tier 1 leverage, Tier 1 risk-based, and total risk-based ratios as set forth in the table.

## NORTHWEST BANCORPORATION, INC. AND SUBSIDIARY

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

## Note 18 Regulatory Capital Requirements (Continued)

As of December 31, 2006, the most recent notification from the Bank's regulator categorized the Bank as well capitalized under the regulatory framework for prompt corrective action. To be categorized as well capitalized, the Bank must maintain minimum capital ratios as set forth in the following table. There are no conditions or events since that notification that management believes have changed the institution's category.

The Company's and Bank's actual December 31, 2006 and 2005, capital amounts and ratios are also presented in the table:

	Actual		Capital Adequacy Purposes		To Be Well Capitalized Under Prompt Corrective Action Provisions	
	Amount	Ratio	Amount	Ratio	Amount	Ratio
<b>December 31, 2006</b>						
Total capital (to risk-weighted assets):						
Northwest Bancorporation	\$ 32,496,000	13.95%	\$ 18,633,360	≥ 8%	NA	NA
Inland Northwest Bank	29,396,000	12.66%	18,576,240	≥ 8%	\$ 23,220,300	≥ 10%
Tier 1 capital (to risk-weighted assets):						
Northwest Bancorporation	29,710,000	12.76%	9,316,680	≥ 4%	NA	NA
Inland Northwest Bank	26,610,000	11.46%	9,288,120	≥ 4%	13,932,180	≥ 6%
Tier 1 capital (to average assets):						
Northwest Bancorporation	29,710,000	10.82%	10,980,200	≥ 4%	NA	NA
Inland Northwest Bank	26,610,000	9.69%	10,980,200	≥ 4%	13,725,250	≥ 5%
<b>December 31, 2005</b>						
Total capital (to risk-weighted assets):						
Northwest Bancorporation	\$ 29,373,000	14.70%	\$ 15,988,480	≥ 8%	NA	NA
Inland Northwest Bank	23,987,000	12.03%	15,945,760	≥ 8%	\$ 19,932,200	≥ 10%
Tier 1 capital (to risk-weighted assets):						
Northwest Bancorporation	26,943,000	13.48%	7,994,240	≥ 4%	NA	NA
Inland Northwest Bank	21,557,000	10.82%	7,972,880	≥ 4%	11,959,320	≥ 6%
Tier 1 capital (to average assets):						
Northwest Bancorporation	26,943,000	10.97%	9,828,480	≥ 4%	NA	NA
Inland Northwest Bank	21,557,000	8.77%	9,828,480	≥ 4%	12,285,600	≥ 5%

## NORTHWEST BANCORPORATION, INC. AND SUBSIDIARY

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

**Note 19 Earnings Per Share**

Earnings per share and the calculated effect of dilutive securities on earnings per share is as follows:

	Year Ended December 31, 2006		
	Income (Numerator)	Shares (Denominator)	Per Share Amount
<b>Basic EPS</b>			
Income available to common stockholders	\$ 2,779,900	2,236,460	\$ 1.24
<b>Effect of Dilutive Securities</b>			
Stock options		40,463	
<b>Diluted EPS</b>			
Income available to common stockholders plus assumed conversions	\$ 2,779,900	2,276,923	\$ 1.22
<b>Year Ended December 31, 2005</b>			
	Income (Numerator)	Shares (Denominator)	Per Share Amount
<b>Basic EPS</b>			
Income available to common stockholders	\$ 2,160,213	2,213,051	\$ 0.98
<b>Effect of Dilutive Securities</b>			
Stock options		48,531	
<b>Diluted EPS</b>			
Income available to common stockholders plus assumed conversions	\$ 2,160,213	2,261,582	\$ 0.96

The Company's stock (stock symbol: NBCT) is quoted on various Internet listing services, including the OTC Bulletin Board ([www.otcbb.com](http://www.otcbb.com)) where a list of market makers is also detailed. The average market price per share used in the determination of the dilutive effect of stock options was the average price of daily closing market values throughout the year.

## NORTHWEST BANCORPORATION, INC. AND SUBSIDIARY

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

**Note 20 Fair Value of Financial Instruments**

The estimated fair values of the Bank's financial instruments were as follows at December 31:

	2006		2005	
	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
<b>Financial Assets:</b>				
Cash and cash equivalents	\$ 12,200,298	\$ 12,200,298	\$ 8,541,929	8,541,929
Federal funds sold	167,895	167,895	2,028,408	2,028,408
Securities available for sale	31,337,393	31,337,393	32,200,153	32,200,153
Securities held to maturity	3,971,864	3,971,944	4,088,517	4,075,613
Federal Home Loan Bank stock	645,900	645,900	645,900	645,900
Loans and loans held for sale, net	216,696,725	215,643,179	186,465,944	185,610,905
Bank owned life insurance	3,432,503	3,432,503	3,313,771	3,313,771
<b>Financial Liabilities:</b>				
Federal funds purchased	3,630,000	3,630,000		
Borrowed funds	12,160,171	12,148,494	12,569,338	12,576,963
Deposits	210,932,995	210,810,717	192,042,730	192,294,552
Securities sold under agreements to repurchase	25,783,940	25,783,940	17,754,671	17,754,671

The following methods and assumptions were used to estimate the fair value of each class of financial instruments:

**Cash and cash equivalents, and funds sold:**

The carrying amount approximates fair value because of the short maturity of these investments.

**Securities available for sale, securities held to maturity, and other investments:**

The fair values of marketable securities are based on quoted market prices or dealer quotes. If a quoted market price is not available, fair value is estimated using quoted market prices for similar securities.

**Loans receivable:**

Fair values are estimated for portfolios of loans with similar financial characteristics. Loans are segregated by type such as commercial, real estate, consumer, credit card, and other. Each loan category is further segmented into fixed and adjustable rate interest terms. The fair values for fixed-rate loans are estimated by discounting the future cash flows using the current rates at which similar loans would be made to borrowers with similar credit ratings and for the same remaining maturities. For variable rate loans that reprice frequently and have no significant change in credit risk, fair values are based on carrying values.

**Federal funds purchased:**

The carrying amount approximates fair value.

**Bank owned life insurance:**

The carrying amount (the cash surrender value) approximates fair value.





**NORTHWEST BANCORPORATION, INC. AND SUBSIDIARY**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)**

**Note 20 Fair Value of Financial Instruments (Continued)**

**Deposits and securities sold under agreements to repurchase:**

The fair value of demand deposits, savings accounts, NOW, securities sold under agreements to repurchase and money market deposits is the amount payable on demand at the reporting date. The fair value of fixed-maturity time deposits is estimated using the rates currently offered for deposits of similar remaining maturities.

**Borrowed funds:**

The fair values of the Bank's long-term debt are estimated using discounted cash flow analyses based on the Bank's current incremental borrowing rates for similar types of borrowing arrangements.

The junior subordinated debentures detailed in Note 8 carry a fixed rate of interest of 5.95% through June 30, 2010. Subsequent to that date, assuming the Company does not redeem the debentures, the rate of interest is reset quarterly to equal three-month LIBOR plus 1.70%.

**Off-balance-sheet instruments:**

Fair values for off-balance-sheet lending commitments are based on fees currently charged to enter into similar agreements, taking into account the remaining terms of the agreements and the counterparties' credit standings. The fair value of the fees at December 31, 2006 and 2005, were insignificant. See Note 10 for the notional amount of the commitments to extend credit.

## NORTHWEST BANCORPORATION, INC. AND SUBSIDIARY

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

**Note 21: Northwest Bancorporation, Inc. (NBCT)**

(PARENT COMPANY ONLY)

Summary financial information is as follows (in thousands):

NBCT Statements of Financial Condition	December 31,		
	2006	2005	2004
<b>ASSETS</b>			
Cash	\$ 2,541	\$ 5,006	\$ 106
Investment in trust equities	155	155	
Investment in subsidiaries	26,420	21,302	19,754
Deferred tax asset	36	40	45
Other equity securities	250	250	
Other assets	273	88	102
<b>TOTAL ASSETS</b>	<b>29,675</b>	<b>26,841</b>	<b>20,007</b>
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>			
Other liabilities			46
Junior subordinated debentures	5,155	5,155	
Stockholders' equity	24,520	21,686	19,961
<b>TOTAL LIABILITIES AND EQUITY CAPITAL</b>	<b>\$ 29,675</b>	<b>\$ 26,841</b>	<b>\$ 20,007</b>
<b>NBCT</b>			
<b>Statements of Income</b>			
	<b>For the year ended December 31,</b>		
	<b>2006</b>	<b>2005</b>	<b>2004</b>
<b>INTEREST INCOME:</b>			
Interest bearing deposits	\$ 114	\$ 60	\$ 2
<b>OTHER INCOME (EXPENSE):</b>			
Dividend income from subsidiaries		530	230
Equity in undistributed income of subsidiaries	2,954	1,757	1,790
Interest on other borrowings	(313)	(163)	
Other income			1
Other expense	(69)	(90)	(88)
	2,686	2,094	1,935
<b>PROVISION FOR (BENEFIT FROM) INCOME TAXES</b>	<b>(94)</b>	<b>(66)</b>	<b>(29)</b>
<b>NET INCOME</b>	<b>\$ 2,780</b>	<b>\$ 2,160</b>	<b>\$ 1,964</b>

## NORTHWEST BANCORPORATION, INC. AND SUBSIDIARY

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

NBCT Statements of Cash Flows	For the year ended December 31,		
	2006	2005	2004
<b>OPERATING ACTIVITIES:</b>			
Net income	\$ 2,780	\$ 2,160	\$ 1,964
Adjustments to reconcile net income to net cash provided by operating activities:			
Equity in undistributed earnings of subsidiaries	(2,954)	(1,757)	(1,790)
Amortization, shareholder accounting software	2	2	
(Increase) decrease in deferred taxes	4	5	5
Equity-based compensation expense	41		
(Increase) decrease in other assets	(187)	12	20
Increase (decrease) in other liabilities		(46)	(149)
Net cash provided (used) by operating activities	(314)	376	50
<b>INVESTING ACTIVITIES:</b>			
Funds invested in equity securities		(250)	
Funds invested in trust equities		(155)	
Additional funds invested in subsidiaries	(2,100)		
Net cash provided (used) by investing activities	(2,100)	(405)	
<b>FINANCING ACTIVITIES:</b>			
Proceeds from issuance of junior subordinated debentures		5,155	
Issuance of stock	69	61	54
Stock repurchase	(3)		
Net proceeds from exercise of stock options	167		55
Excess tax benefits, equity-based compensation	56		
Other	2	(2)	1
Cash dividends paid, including fractional shares paid in cash	(342)	(285)	(232)
Net cash provided (used) by financing activities	(51)	4,929	(122)
<b>NET INCREASE (DECREASE) IN CASH</b>	<b>(2,465)</b>	<b>4,900</b>	<b>(72)</b>
CASH, BEGINNING OF PERIOD	5,006	106	178
CASH, END OF PERIOD	\$ 2,541	\$ 5,006	\$ 106
<b>SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:</b>			
Interest paid	\$ 313	\$ 163	\$
Taxes paid	\$ 1,479	\$ 1,116	\$ 688

**PART III**

**Signatures**

In accordance with Section 13 of the Securities Exchange Act of 1934, the Registrant has caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

NORTHWEST BANCORPORATION, INC.

By */s/* RANDALL L. FEWEL  
Randall L. Fewel, President and

Chief Executive Officer

Date: February 1, 2008

In accordance with Section 13 of the Securities Exchange Act of 1934, the Registrant has caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

By */s/* CHRISTOPHER C. JUREY  
Christopher C. Jurey, Chief Financial Officer

Date: February 1, 2008

**Index to Exhibits**

**Exhibit**

<b>No.</b>	<b>Description</b>
31.1	Certification of Randall L. Fewel, President and Chief Executive Officer, pursuant to Rule 13a-14(a) under the Securities and Exchange Act of 1934
31.2	Certification of Christopher C. Jurey, Chief Financial Officer, pursuant to Rule 13a-14(a) under the Securities and Exchange Act of 1934
32.1	Certification of Randall L. Fewel, President and Chief Executive Officer, pursuant to 18 U.S.C. 1350
32.2	Certification of Christopher C. Jurey, Chief Financial Officer, pursuant to 18 U.S.C. 1350