

STERLING FINANCIAL CORP /WA/

Form 11-K

June 26, 2007

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**UNITED STATES SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549
FORM 11-K**

(Mark One)

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

For the fiscal year ended December 31, 2006

OR

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

For the transition period from _____ to _____ .

Commission File Number 0-20800

A. Full title of the plan and the address of the plan, if different from that of the issuer named below:

STERLING SAVINGS BANK EMPLOYEE SAVINGS AND INVESTMENT PLAN AND TRUST

B. Name of issuer of the securities held pursuant to the plan and the address of its principal executive office:

Sterling Financial Corporation

111 North Wall Street

Spokane, WA 99201

REQUIRED INFORMATION

Item 4. Financial statements and schedules prepared in accordance with the financial reporting requirements of ERISA.

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**Sterling Savings Bank
Employee Savings and Investment Plan and Trust
Financial Statements and Exhibit**

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Report of Independent Registered Public Accounting Firm

To the Participants and Administrative

Committee of the Sterling Savings Bank

Employee Savings and Investment Plan and Trust

We have audited the accompanying statements of net assets available for benefits of the Sterling Savings Bank Employee Savings and Investment Plan and Trust (the Plan) as of December 31, 2006 and 2005, and the related statement of changes in net assets available for benefits for the year ended December 31, 2006. These financial statements are the responsibility of the Plan s management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the 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. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, 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 financial statements referred to above present fairly, in all material respects, the net assets available for benefits of the Plan as of December 31, 2006 and 2005, and the changes in net assets available for benefits for the year ended December 31, 2006, in conformity with accounting principles generally accepted in the United States of America.

Our audits were performed for the purpose of forming an opinion on the basic financial statements taken as a whole. The supplemental schedules of assets (held at end of year) and reportable transactions are presented for the purpose of additional analysis and are not a required part of the basic financial statements, but are supplementary information required by the Department of Labor s Rules and Regulations for Reporting and Disclosure under the Employee Retirement Income Security Act of 1974. These supplemental schedules are the responsibility of the Plan s management. The supplemental schedules have been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, are fairly stated in all material respects in relation to the basic financial statements taken as a whole.

/s/ BDO Seidman, LLP

June 21, 2007

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Sterling Savings Bank
Employee Savings and Investment Plan and Trust
Statements of Net Assets Available for Benefits December 31, 2006 and 2005

| | 2006 | 2005 |
|--|---------------|---------------|
| Assets | | |
| Investments, at fair value | | |
| Mutual funds | \$ 25,826,941 | \$ 19,856,551 |
| Common stock of Sterling Financial Corp. | 27,753,719 | 21,098,497 |
| Collective trust funds | 5,025,543 | 5,465,729 |
| Participant loans | 552,677 | 566,086 |
| | 59,158,880 | 46,986,863 |
| Receivables | | |
| Employer's contribution | 62,053 | 58,805 |
| Participants' contribution | 226,051 | 173,831 |
| Accrued interest | 5,878 | 4,070 |
| | 293,982 | 236,706 |
| Total Assets | 59,452,862 | 47,223,569 |
| Liabilities | (285,247) | 0 |
| Net assets available for benefits at fair value | 59,167,615 | 47,223,569 |
| Adjustment from fair value to contract value for fully benefit responsive investment contracts | 94,528 | 98,253 |
| Net assets available for benefits | \$ 59,262,143 | \$ 47,321,822 |

See accompanying summary of accounting policies and notes to financial statements.

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Sterling Savings Bank
Employee Savings and Investment Plan and Trust
Statements of Changes Net Assets Available for Benefits
Year Ended December 31, 2006

| | 2006 |
|---|---------------|
| Additions to net assets attributed to: | |
| Investment income: | |
| Interest | \$ 40,544 |
| Dividends | 1,273,387 |
| Net appreciation in fair value of investments | 9,583,875 |
| | 10,897,806 |
| Contributions: | |
| Participants | 5,900,796 |
| Rollovers from qualified plans | 443,892 |
| Employer | 1,669,627 |
| Total additions | 18,912,121 |
| Deductions to net assets attributed to: | |
| Benefits paid to participants | 6,941,776 |
| Administration expenses | 30,024 |
| Total deductions | 6,971,800 |
| Net increase in net assets available for benefits | 11,940,321 |
| Net assets available for benefits: | |
| Beginning of year | 47,321,822 |
| End of year | \$ 59,262,143 |

See accompanying summary of accounting policies and notes to financial statements.

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**Sterling Savings Bank
Employee Savings and Investment Plan and Trust
Summary of Accounting Policies**

Basis of Accounting

The financial statements of the Plan are prepared under the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America.

Investments

The Plan's investments are stated at fair value. Mutual funds are valued at quoted market prices which represent the value of shares held by the Plan at year end. As described in Financial Accounting Standards Board Staff Position, FSP AAG INV-1 and SOP 94-4-1, *Reporting of Fully Benefit-Responsive Investment Contracts Held by Certain Investment Companies Subject to the AICPA Investment Company Guide and Defined-Contribution Health and Welfare and Pension Plans* (the FSP), investment contracts held by a defined-contribution plan are required to be reported at fair value. However, contract value is the relevant measurement attribute for that portion of the net assets available for benefits of a defined-contribution plan attributable to fully benefit-responsive investment contracts because contract value is the amount participants would receive if they were to initiate permitted transactions under the terms of the plan. As required by the FSP, the Statement of Net Assets Available for Benefits presents the fair value of the investment contracts as well as the adjustment of the fully benefit responsive investment contracts from fair value to contract value. The Statement of Changes in Net Assets Available for Benefits is prepared on a contract value basis. Sterling Financial Corporation common stock is valued at its quoted market price.

The Plan presents in the statement of changes in net assets available for benefits the net appreciation or depreciation in the fair value of its investments which consists of the realized gains or losses and the net unrealized appreciation or depreciation on those investments.

Purchases and sales of securities are recorded on a trade-date basis. Interest income is recorded on the accrual basis. Dividends are recorded on the ex-dividend date.

Benefit Payments

Benefits are recorded when paid.

Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make significant estimates and assumptions that affect the reported amounts of net assets available for benefits, disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of changes in net assets available for benefits during the reporting period. Actual results could differ from those estimates.

Risks and Uncertainties

The Plan provides various investment options for participants to choose from in combinations of stocks, mutual funds and other investment securities. These investment options are exposed to various risks, such as interest rate, market and credit. Due to the level of risk associated with certain investments and the level of uncertainty related to changes in the value of such investments, it is at least reasonably possible that changes in risks in the near term would materially affect participants' account balances and the amounts reported in the statements of net assets available for benefits and the statement of changes in net assets available for benefits.

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**Sterling Savings Bank
Employee Savings and Investment Plan and Trust
Notes to Financial Statements**

Reclassifications

Certain amounts in the December 31, 2005 financial statements have been reclassified to conform to the 2006 presentation due to the retroactive application of the FSP.

1. Description of Plan

The following description of the Sterling Savings Bank (Sterling or the Employer) Employee Savings and Investment Plan and Trust (the Plan) provides only general information. Participants should refer to the Plan itself for a more complete description of the Plan s provisions.

General

The Plan is a defined contribution plan, which became effective on July 1, 1985. Employees who have attained the age of 18 may enroll on the first day of the month following one calendar month of employment. The Plan is subject to the provisions of the Employee Retirement Income Security Act of 1974, as amended (ERISA).

Contributions

Participants can contribute from 1% to 75% of their compensation up to the statutory maximum through payroll deductions to the Plan.

Participant contributions are entitled to a discretionary Employer matching contribution. The matching contribution formula provides that Employer will contribute up to a maximum match of 35% of the employee s contribution not to exceed 10% of the participant s compensation. The Employer contributed the maximum match in 2006 and 2005. Additional amounts may be contributed at the option of Sterling as a profit sharing contribution. No discretionary profit sharing contributions were made in 2006 or 2005. All Employer contributions are initially invested in the common stock of Sterling Financial Corporation. Participants who have been employed with Sterling for five years or more have the option of reallocating Employer contributions that have been invested in Sterling Financial Corporation stock into any of the Plan s other investment funds. Subsequent to year end, the Plan has been modified to allow participants to reallocate Employer contributions invested in Sterling Financial Corporation common stock after three years of employment.

Investment Options

Participant contributions are invested in separate investment options as designated by the individual participants. Participants may elect to reallocate the amounts invested in each investment on any business day.

Participant Accounts

Separate accounts are maintained for each participant. Each participant s account is credited with the participant s contribution, an allocation of Sterling s contribution and any Plan earnings, and is debited with any losses and expenses. Allocations of Sterling s contribution and Plan earnings or losses and expenses are based on participant account balances, as defined in the Plan document. The participant s benefit is the amount of any balance that has accumulated in his or her account.

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Sterling Savings Bank

Employee Savings and Investment Plan and Trust

Notes to Financial Statements

Vesting

A participant is 100% vested in his or her voluntary contributions plus actual earnings thereon. Sterling's contributions and earnings thereon are subject to a vesting schedule of 50% after two years and 100% after three years of service.

Forfeitures

Forfeitures totaled \$132,406 and \$55,483 at December 31, 2006 and 2005, respectively. Forfeitures of Sterling contributions will reduce future matching contributions. Forfeitures in the amount of \$46,494 were used to offset Employer contributions for the year ended December 31, 2006. The remaining forfeitures were allocated to a suspense account for use in future years to offset Employer contributions.

Payment of Benefits

Distributions are made upon termination, death, disability or retirement. Participants or their beneficiaries will receive payment of benefits as follows: (a) balances of \$5,000 or less will be distributed in a lump sum, or (b) balances greater than \$5,000 will be distributed in various optional forms of distribution. The Plan allows for automatic rollover of participant balances between \$1,000 and \$5,000 to an IRA, in the event the participant does not elect otherwise.

Participant Loans

A participant may borrow from his or her fund account up to a maximum of 50% of his or her vested account balance. However, participant loans can be no more than \$50,000 minus the participant's highest outstanding loan amount during the prior twelve months. The loans are secured by the vested balance in the participant's account and bear interest at the Federal Reserve prime rate plus 1%, calculated at the end of each month and applied to all loans funded during the next month. Principal and interest are paid ratably through regular payroll deductions over a period not to exceed five years. Participants pay a loan origination fee, as well as an annual loan maintenance fee.

Administrative Expenses

Both Sterling and Plan participants pay the costs of the Plan. Plan participants pay a portion of the trustee fee in the amount of \$15 per participant per year. Additionally, each share of Sterling Financial Corporation common stock that is purchased by the Plan on the open market is subject to a fee of \$0.10 per share, which is paid by the participants. Sterling pays the remaining portion of the trustee fee charged by Merrill Lynch as trustee and all other fees, expenses and commissions.

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Sterling Savings Bank
Employee Savings and Investment Plan and Trust
Notes to Financial Statements

2. Investments

The following table presents the fair value of investments, including those that represent 5% or more of the Plan's net assets at December 31, 2006 and 2005.

| | 2006 | 2005 |
|--|----------------------|----------------------|
| Corporate Stocks: | | |
| Common Stock of Sterling Financial Corporation | \$ 27,753,719 | \$ 21,098,497 |
| Collective Trust Funds: | | |
| Merrill Lynch Retirement Preservation Trust | 5,025,543 | 5,465,729 |
| Mutual Funds: | | |
| American Growth Fund | 6,584,624 | 5,577,653 |
| MFS Value Fund | 5,137,659 | 3,929,070 |
| Munder Midcap Core Growth | 3,441,940 | 2,696,601 |
| American Balanced Fund | 3,161,529 | 1,734,034 |
| Blackrock S&P 500 Index | 2,447,524 | 2,121,572 |
| Thornburg International Value Fund | 2,088,616 | 1,209,339 |
| Blackrock Bond Fund | 1,968,928 | 1,807,139 |
| Blackrock Global Allocation Fund | 996,121 | 779,255 |
| Delaware Group Trend Fund | 0 | 1,888 |
| Participant Loans | 552,677 | 566,086 |
| | \$ 59,158,880 | \$ 46,986,863 |

During the year ended December 31, 2006, the Plan's investments (including gains and losses on investments bought and sold, as well as held during the year) appreciated (depreciated) in value as follows:

| | 2006 |
|--|---------------------|
| Mutual funds | \$ 2,129,391 |
| Common stock of Sterling Financial Corporation | 7,454,484 |
| Total | \$ 9,583,875 |

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Table of Contents**Sterling Savings Bank****Employee Savings and Investment Plan and Trust****Notes to Financial Statements**

Investment in the Plan is participant-directed, except that the Employer's matching contributions are generally invested in Sterling Financial Corporation common stock. As described in Note 1, a participant who has been an Employee for at least five years may reinvest the matching contribution into other investment options. Subsequent to year end, a participant with three years of service may reinvest the matching contribution. Participants at their discretion may also direct investments to Sterling Financial Corporation common stock. Information about the net assets in Sterling Financial Corporation common stock as of December 31, 2006 and 2005, and the change from 2006 to 2005 in non-participant directed investment balances are as follows:

| | 2006 | 2005 |
|--|---------------|---------------|
| Net assets in Sterling Financial Corporation common stock: | | |
| Non-participant directed | \$ 17,127,665 | \$ 12,817,519 |
| Participant directed | 10,626,054 | 8,280,978 |
| Total | \$ 27,753,719 | \$ 21,098,497 |

Changes in non-participant directed net assets in Sterling Financial Corporation common stock for the years ended December 31:

| | 2006 | 2005 |
|---|--------------|--------------|
| Contributions | \$ 1,728,432 | \$ 1,362,712 |
| Interest and dividends | 128,138 | 30,640 |
| Net appreciation | 4,542,555 | (582,145) |
| Benefits paid to participants | (1,609,015) | (660,230) |
| Administrative expenses | (8,712) | (10,556) |
| Transfers to participant-directed investments | (471,252) | (212,510) |
| Total | \$ 4,310,146 | \$ (72,089) |

3. Plan Termination

Although it has not expressed an intent to do so, Sterling has the right to discontinue its contributions to the Plan at any time and to terminate the Plan subject to the provisions of ERISA. In the event of plan termination, participants accounts will become fully vested and non-forfeitable. All assets remaining in the Plan after payment of any expenses properly chargeable against the Plan shall be paid to participants in accordance with the terms of the Plan.

4. Tax Status

On October 18, 2004, the Employer received a letter from the Internal Revenue Service informing the Employer that the Plan is qualified and exempt under Sections 401 and 501 of the Internal Revenue Code of 1986, as amended. Although the Plan has been amended since receiving the determination letter, the Plan administrator and the Plan's tax counsel believe that the Plan is designed and is currently being operated in compliance with the applicable requirements of the Internal Revenue Code.

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Sterling Savings Bank

Employee Savings and Investment Plan and Trust

Notes to Financial Statements

5. Related Party Transactions

Certain Plan investments are shares of mutual funds and collective trust funds managed by Merrill Lynch, which is the trustee of the Plan. These investments include the Merrill Lynch Retirement Preservation Trust, Blackrock Bond Fund, Blackrock Global Allocation Fund, and Blackrock S&P 500 Index Fund. No transaction fees or commissions were paid, or are payable by the Plan through the Trust relating to these funds in 2006 and 2005.

Certain Plan investments are shares in Sterling Financial Corporation common stock, as detailed in Note 2. Sterling Financial Corporation is the parent company of Sterling Savings Bank and therefore these transactions also qualify as party-in-interest transactions.

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Sterling Savings Bank
Employee Savings and Investment Plan and Trust
Schedule of Assets (Held at End of Year)
December 31, 2006
EIN: 91-1166044 Plan Number: 001

| (a) | (b) | (c) | (d) | (e) |
|--|--|---|------------------|---------------|
| Identity of Issuer, Borrower, Lessor or Similar Party | Description of Investment, Including Maturity Date, Rate of Interest Collateral, Par or Maturity Value | Cost** | Current Value | |
| Common Stock | | | | |
| * | Sterling Financial Corporation | Common stock, 820,873 shares at \$1 par value | \$ 11,280,296 | \$ 27,753,719 |
| Collective Trust Funds | | | | |
| * | Merrill Lynch Retirement Preservation Trust | 5,120,071 units | | 5,025,543 |
| Mutual Funds | | | | |
| | American Growth Fund | Mutual fund, 202,916 shares | | 6,584,624 |
| | MFS Value Fund | Mutual fund, 191,919 shares | | 5,137,659 |
| | Munder Midcap Core Growth | Mutual fund, 136,911 shares | | 3,441,940 |
| | American Balanced Fund | Mutual fund, 166,221 shares | | 3,161,529 |
| * | Blackrock S&P 500 Index | Mutual fund, 140,662 shares | | 2,447,524 |
| | Thornburg International Value Fund | Mutual fund, 73,336 shares | | 2,088,616 |
| * | Blackrock Bond Fund | Mutual fund, 171,062 shares | | 1,968,928 |
| * | Blackrock Global Allocation Fund | Mutual fund, 54,852 shares | | 996,121 |
| | | | | 25,826,941 |
| | Participant Loans | Interest ranging from 5.00% to 9.25%, maturing through December 2011 | | 552,677 |
| | | | | \$ 59,158,880 |

* Represents party-in-interest to the Plan.

** Cost information is omitted with respect to participant or beneficiary directed transactions.

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**Sterling Savings Bank
Employee Savings and Investment Plan and Trust
Signatures**

SIGNATURES

The Plan. Pursuant to the requirements of the Securities Exchange Act of 1934, the trustees (or other persons who administer the employee benefit plan) have duly caused this annual report to be signed on its behalf by the undersigned hereunto duly authorized.

Sterling Savings Bank Employee Savings
and
Investment Plan and Trust

Date: June 26, 2007

/s/ Robert G. Butterfield
Robert G. Butterfield
Senior Vice President, Principal
Accounting Officer and Controller

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INDEX TO EXHIBITS

| Exhibit No. | Description |
|-------------|--|
| 23 | Consent of Independent Registered Public Accounting Firm |