

FIRST FINANCIAL CORP /IN/  
Form 10-Q  
November 06, 2013  
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UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

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

For The Quarterly Period Ended September 30, 2013

Commission File Number 0-16759

FIRST FINANCIAL CORPORATION  
(Exact name of registrant as specified in its charter)  
INDIANA  
(State or other jurisdiction  
incorporation or organization)

35-1546989  
(I.R.S. Employer  
Identification No.)

One First Financial Plaza, Terre Haute, IN  
(Address of principal executive office)

47807  
(Zip Code)

(812)238-6000  
(Registrant's telephone number, including area code)

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

Yes  No .

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

Yes  No .

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

Large accelerated filer   
Non-accelerated filer  (Do not check if a smaller reporting company)

Accelerated filer   
Smaller reporting company

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

Yes  No .

As of November 5, 2013, the registrant had outstanding 13,307,498 shares of common stock, without par value.

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## Part I – Financial Information

## Item 1. Financial Statements

## FIRST FINANCIAL CORPORATION

## CONSOLIDATED BALANCE SHEETS

(Dollar amounts in thousands, except per share data)

	September 30, 2013 (unaudited)	December 31, 2012
<b>ASSETS</b>		
Cash and due from banks	\$80,899	\$87,230
Federal funds sold	3,420	20,800
Securities available-for-sale	872,675	691,000
Loans:		
Commercial	1,057,823	1,088,144
Residential	482,477	496,237
Consumer	269,282	268,507
	1,809,582	1,852,888
Less:		
Unearned Income	(977	) (952
Allowance for loan losses	(22,004	) (21,958
	1,786,601	1,829,978
Restricted Stock	21,050	21,292
Accrued interest receivable	11,767	12,024
Premises and equipment, net	51,875	47,308
Bank-owned life insurance	78,679	77,295
Goodwill	39,489	37,612
Other intangible assets	5,253	3,893
Other real estate owned	9,249	7,722
FDIC Indemnification Asset	1,171	2,632
Other assets	55,341	56,622
<b>TOTAL ASSETS</b>	<b>\$3,017,469</b>	<b>\$2,895,408</b>
<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>		
Deposits:		
Non-interest-bearing	\$491,826	\$465,954
Interest-bearing:		
Certificates of deposit of \$100 or more	187,305	213,610
Other interest-bearing deposits	1,807,897	1,596,570
	2,487,028	2,276,134
Short-term borrowings	27,929	40,551
Other borrowings	58,362	119,705
Other liabilities	69,073	86,896
<b>TOTAL LIABILITIES</b>	<b>2,642,392</b>	<b>2,523,286</b>
Shareholders' equity		
Common stock, \$.125 stated value per share;		
Authorized shares-40,000,000		
Issued shares-14,516,113 in 2013 and 14,490,609 in 2012		
Outstanding shares-13,307,498 in 2013 and 13,287,348 in 2012	1,810	1,808

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Additional paid-in capital	70,537	69,989
Retained earnings	354,565	338,342
Accumulated other comprehensive income (loss)	(21,128)	) (7,472 )
Less: Treasury shares at cost-1,208,615 in 2013 and 1,203,261 in 2012	(30,707)	) (30,545 )
TOTAL SHAREHOLDERS' EQUITY	375,077	372,122
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	\$3,017,469	\$2,895,408
See accompanying notes.		

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## FIRST FINANCIAL CORPORATION

## CONSOLIDATED STATEMENTS OF INCOME AND COMPREHENSIVE INCOME (LOSS)

(Dollar amounts in thousands, except per share data)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2013	2012	2013	2012
	(unaudited)	(unaudited)	(unaudited)	(unaudited)
<b>INTEREST INCOME:</b>				
Loans, including related fees	\$22,510	\$24,725	\$68,540	\$75,149
Securities:				
Taxable	5,038	3,308	11,732	10,339
Tax-exempt	1,750	1,827	5,281	5,442
Other	421	568	1,413	1,781
<b>TOTAL INTEREST INCOME</b>	<b>29,719</b>	<b>30,428</b>	<b>86,966</b>	<b>92,711</b>
<b>INTEREST EXPENSE:</b>				
Deposits	1,349	1,881	4,625	6,714
Short-term borrowings	23	33	62	116
Other borrowings	549	1,108	2,570	3,648
<b>TOTAL INTEREST EXPENSE</b>	<b>1,921</b>	<b>3,022</b>	<b>7,257</b>	<b>10,478</b>
<b>NET INTEREST INCOME</b>	<b>27,798</b>	<b>27,406</b>	<b>79,709</b>	<b>82,233</b>
Provision for loan losses	495	2,559	6,476	7,304
<b>NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES</b>	<b>27,303</b>	<b>24,847</b>	<b>73,233</b>	<b>74,929</b>
<b>NON-INTEREST INCOME:</b>				
Trust and financial services	1,402	1,413	4,331	4,332
Service charges and fees on deposit accounts	2,693	2,560	7,341	7,166
Other service charges and fees	2,818	2,506	8,044	7,237
Securities gains/(losses), net	—	17	7	677
Total impairment losses	—	—	—	(11)
Loss recognized in other comprehensive loss	—	—	—	—
Net impairment loss recognized in earnings	—	—	—	(11)
Insurance commissions	1,896	1,736	5,800	5,426
Gain on sales of mortgage loans	583	1,253	2,489	2,970
Other	245	203	1,165	1,159
<b>TOTAL NON-INTEREST INCOME</b>	<b>9,637</b>	<b>9,688</b>	<b>29,177</b>	<b>28,956</b>
<b>NON-INTEREST EXPENSE:</b>				
Salaries and employee benefits	13,773	13,695	41,082	42,005
Occupancy expense	1,544	1,465	4,642	4,370
Equipment expense	1,686	1,335	4,724	4,016
FDIC Expense	500	494	1,559	1,449
Other	7,316	5,975	18,394	17,646
<b>TOTAL NON-INTEREST EXPENSE</b>	<b>24,819</b>	<b>22,964</b>	<b>70,401</b>	<b>69,486</b>
<b>INCOME BEFORE INCOME TAXES</b>	<b>12,121</b>	<b>11,571</b>	<b>32,009</b>	<b>34,399</b>
Provision for income taxes	3,649	3,480	9,398	10,160
<b>NET INCOME</b>	<b>8,472</b>	<b>8,091</b>	<b>22,611</b>	<b>24,239</b>
<b>OTHER COMPREHENSIVE INCOME (LOSS)</b>				
Change in unrealized gains/losses on securities, net of reclassifications	(3,790)	) 3,123	(24,660)	) 3,763
Tax effect	1,468	(1,249)	) 10,112	(1,505)

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	(2,322	) 1,874	(14,548	) 2,258
Change in funded status of post retirement benefits	566	645	1,486	1,932
Tax effect	(226	) (258	) (594	) (773
	340	387	892	1,159
TOTAL OTHER COMPREHENSIVE INCOME (LOSS)	(1,982	) 2,261	(13,656	) 3,417
COMPREHENSIVE INCOME (LOSS)	\$6,490	\$10,352	\$8,955	\$27,656
PER SHARE DATA				
Basic and Diluted Earnings per Share	\$0.64	\$0.61	\$1.70	\$1.83
Dividends per Share	\$—	\$—	\$0.48	\$0.47
Weighted average number of shares outstanding (in thousands)	13,307	13,238	13,305	13,233
See accompanying notes.				

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CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY

Three Months Ended

September 30, 2013, and 2012

(Dollar amounts in thousands, except per share data)

(Unaudited)

	Common Stock	Additional Capital	Retained Earnings	Accumulated Other Comprehensive Income/(Loss)	Treasury Stock	Total
Balance, July 1, 2012	\$1,807	\$69,571	\$328,056	\$(9,338 )	\$(31,809 )	\$358,287
Net income	—	—	8,091	—	—	8,091
Other comprehensive income	—	—	—	2,261	—	2,261
Omnibus Equity Incentive Plan	1	121	—	—	—	122
Balance, September 30, 2012	\$1,808	\$69,692	\$336,147	\$(7,077 )	\$(31,809 )	\$368,761
Balance, July 1, 2013	\$1,809	\$70,354	\$346,093	\$(19,146 )	\$(30,707 )	\$368,403
Net income	—	—	8,472	—	—	8,472
Other comprehensive income (loss)	—	—	—	(1,982 )	—	(1,982 )
Omnibus Equity Incentive Plan	1	183	—	—	—	184
Balance, September 30, 2013	\$1,810	\$70,537	\$354,565	\$(21,128 )	\$(30,707 )	\$375,077
See accompanying notes.						



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CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY

Nine Months Ended

September 30, 2013, and 2012

(Dollar amounts in thousands, except per share data)

(Unaudited)

	Common Stock	Additional Capital	Retained Earnings	Accumulated Other Comprehensive Income/(Loss)	Treasury Stock	Total
Balance, January 1, 2012	\$1,806	\$69,328	\$318,130	\$(10,494 )	\$(31,809 )	\$346,961
Net income	—	—	24,239	—	—	24,239
Other comprehensive income	—	—	—	3,417	—	3,417
Omnibus Equity Incentive Plan	2	364	—	—	—	366
Cash Dividends, \$.47 per share	—	—	(6,222 )	—	—	(6,222 )
Balance, September 30, 2012	\$1,808	\$69,692	\$336,147	\$(7,077 )	\$(31,809 )	\$368,761
Balance, January 1, 2013	\$1,808	\$69,989	\$338,342	\$(7,472 )	\$(30,545 )	\$372,122
Net income	—	—	22,611	—	—	22,611
Other comprehensive income (loss)	—	—	—	(13,656 )	—	(13,656 )
Treasury stock purchase (5,354 shares)	—	—	—	—	(162 )	(162 )
Omnibus Equity Incentive Plan	2	548	—	—	—	550
Cash Dividends, \$.48 per share	—	—	(6,388 )	—	—	(6,388 )
Balance, September 30, 2013	\$1,810	\$70,537	\$354,565	\$(21,128 )	\$(30,707 )	\$375,077

See accompanying notes.

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FIRST FINANCIAL CORPORATION  
CONSOLIDATED STATEMENTS OF CASH FLOWS  
(Dollar amounts in thousands, except per share data)

	Nine Months Ended September 30,	
	2013	2012
	(Unaudited)	
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>		
Net Income	\$22,611	\$24,239
Adjustments to reconcile net income to net cash provided by operating activities:		
Net amortization (accretion) of premiums and discounts on investments	2,092	2,209
Provision for loan losses	6,476	7,304
Securities (gains) losses	(7	) (677
Securities impairment loss	—	11
(Gain) loss on sale of other real estate	109	46
Restricted stock compensation	550	366
Depreciation and amortization	4,066	3,741
Other, net	1,488	2,345
<b>NET CASH FROM OPERATING ACTIVITIES</b>	<b>37,385</b>	<b>39,584</b>
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>		
Proceeds from sales of securities available-for-sale	5,052	9,015
Redemption of restricted stock	250	1,172
Purchases of restricted stock	(8	) (186
Purchases of customer list	—	(114
Cash received (disbursed) from purchase of branches	177,251	—
Redemption of bank owned life insurance	—	7,319
Purchase of bank owned life insurance	—	(1,551
Calls, maturities and principal reductions on securities available-for-sale	126,395	99,465
Purchases of securities available-for-sale	(339,872	) (96,953
Loans made to customers, net of repayment	36,105	24,248
Proceeds from sales of other real estate owned	1,251	3,210
Net change in federal funds sold	17,380	(44,048
Additions to premises and equipment	(1,850	) (7,318
<b>NET CASH FROM INVESTING ACTIVITIES</b>	<b>21,954</b>	<b>(5,741</b>
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>		
Net change in deposits	20,978	(15,945
Net change in short-term borrowings	(12,622	) (56,025
Proceeds from other borrowings	135,000	—
Maturities of other borrowings	(196,097	) (20,090
Purchase of treasury stock	(162	) —
Dividends paid	(12,767	) (12,425
<b>NET CASH FROM FINANCING ACTIVITIES</b>	<b>(65,670</b>	<b>) (104,485</b>
<b>NET CHANGE IN CASH AND CASH EQUIVALENTS</b>	<b>(6,331</b>	<b>) (70,642</b>
<b>CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD</b>	<b>87,230</b>	<b>134,280</b>
<b>CASH AND CASH EQUIVALENTS, END OF PERIOD</b>	<b>\$80,899</b>	<b>\$63,638</b>
See accompanying notes.		



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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The accompanying September 30, 2013 and 2012 consolidated financial statements are unaudited. The December 31, 2012 consolidated financial statements are as reported in the First Financial Corporation (the "Corporation") 2012 annual report. The information presented does not include all information and footnotes required by U.S. generally accepted accounting principles for complete financial statements. The following notes should be read together with notes to the consolidated financial statements included in the 10-K filed with the Securities and Exchange Commission for the fiscal year ended December 31, 2012.

## 1. Significant Accounting Policies

The significant accounting policies followed by the Corporation and its subsidiaries for interim financial reporting are consistent with the accounting policies followed for annual financial reporting. All adjustments which are, in the opinion of management, necessary for a fair statement of the results for the periods reported have been included in the accompanying consolidated financial statements and are of a normal recurring nature. The Corporation reports financial information for only one segment, banking. Some items in the prior year financials were reclassified to conform to the current presentation.

The Omnibus Equity Incentive Plan is a long-term incentive plan that was designed to align the interests of participants with the interests of shareholders. Under the plan, awards may be made based on certain performance measures. The grants are made in restricted stock units that are subject to a vesting schedule. These shares vest over 3 years in increments of 33%, 33%, and 34% respectively. In 2013 and 2012, 30,219 and 39,643 shares were awarded, respectively. These shares had a grant date value of \$0.9 million and \$1.4 million for 2013 and 2012, vest over three years and their grant is not subject to future performance measures. Outstanding shares are increased at the award date for the total shares awarded.

## 2. Allowance for Loan Losses

The following table presents the activity of the allowance for loan losses by portfolio segment for the three months ended September 30.

Allowance for Loan Losses: (Dollar amounts in thousands)	September 30, 2013				
	Commercial	Residential	Consumer	Unallocated	Total
Beginning balance	\$14,531	\$1,592	\$3,637	\$2,373	\$22,133
Provision for loan losses*	(486 )	(266 )	504	548	300
Loans charged -off	(388 )	(284 )	(840 )	—	(1,512 )
Recoveries	361	398	324	—	1,083
Ending Balance	\$14,018	\$1,440	\$3,625	\$2,921	\$22,004

\* Provision before increase of \$195 thousand in 2013 for decrease in FDIC indemnification asset

Allowance for Loan Losses: (Dollar amounts in thousands)	September 30, 2012				
	Commercial	Residential	Consumer	Unallocated	Total
Beginning balance	\$13,190	\$2,124	\$3,744	\$1,034	\$20,092
Provision for loan losses*	765	1,594	196	85	2,640
Loans charged -off	(715 )	(381 )	(779 )	—	(1,875 )
Recoveries	167	36	397	—	600
Ending Balance	\$13,407	\$3,373	\$3,558	\$1,119	\$21,457

\* Provision before decrease of \$81 thousand in 2012 for increase in FDIC indemnification asset

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The following table presents the activity of the allowance for loan losses by portfolio segment for the nine months ended September 30.

Allowance for Loan Losses: (Dollar amounts in thousands)	September 30, 2013				
	Commercial	Residential	Consumer	Unallocated	Total
Beginning balance	\$10,987	\$5,426	\$3,879	\$1,666	\$21,958
Provision for loan losses*	2,438	234	1,348	1,255	5,275
Loans charged -off	(2,273)	(4,683)	(2,677)	—	(9,633)
Recoveries	2,866	463	1,075	—	4,404
Ending Balance	\$14,018	\$1,440	\$3,625	\$2,921	\$22,004

\* Provision before increase of \$1.2 million in 2013 for decrease in FDIC indemnification asset

Allowance for Loan Losses: (Dollar amounts in thousands)	September 30, 2012				
	Commercial	Residential	Consumer	Unallocated	Total
Beginning balance	\$12,119	\$2,728	\$3,889	\$505	\$19,241
Provision for loan losses*	3,642	2,859	1,185	614	8,300
Loans charged -off	(2,917)	(2,289)	(2,635)	—	(7,841)
Recoveries	563	75	1,119	—	1,757
Ending Balance	\$13,407	\$3,373	\$3,558	\$1,119	\$21,457

\* Provision before decrease of \$1.0 million in 2012 for increase in FDIC indemnification asset

The following table presents the allocation of the allowance for loan losses and the recorded investment in loans by portfolio segment and based on the impairment method at September 30, 2013 and December 31, 2012.

Allowance for Loan Losses (Dollar amounts in thousands)	September 30, 2013				
	Commercial	Residential	Consumer	Unallocated	Total
Individually evaluated for impairment	\$5,510	\$—	\$—	\$—	\$5,510
Collectively evaluated for impairment	7,698	1,254	3,625	2,921	15,498
Acquired with deteriorated credit quality	810	186	—	—	996
Ending Balance	\$14,018	\$1,440	\$3,625	\$2,921	\$22,004

Loans: (Dollar amounts in thousands)	September 30, 2013			
	Commercial	Residential	Consumer	Total
Individually evaluated for impairment	\$24,741	\$226	\$—	\$24,967
Collectively evaluated for impairment	1,028,446	481,064	270,518	1,780,028
Acquired with deteriorated credit quality	10,142	2,736	—	12,878
Ending Balance	\$1,063,329	\$484,026	\$270,518	\$1,817,873

Allowance for Loan Losses: (Dollar amounts in thousands)	December 31, 2012				
	Commercial	Residential	Consumer	Unallocated	Total
Individually evaluated for impairment	3,453	3,920	—	—	7,373
Collectively evaluated for impairment	7,286	1,506	3,879	1,666	14,337
Acquired with deteriorated credit quality	248	—	—	—	248
Ending Balance	\$10,987	\$5,426	\$3,879	\$1,666	\$21,958

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Loans (Dollar amounts in thousands)	December 31, 2012			
	Commercial	Residential	Consumer	Total
Individually evaluated for impairment	23,721	6,973	—	30,694
Collectively evaluated for impairment	1,056,861	487,486	269,882	1,814,229
Acquired with deteriorated credit quality	13,582	3,421	6	17,009
Ending Balance	\$1,094,164	\$497,880	\$269,888	\$1,861,932

The following tables present loans individually evaluated for impairment by class of loans.

(Dollar amounts in thousands)	September 30, 2013					
	Unpaid Principal Balance	Recorded Investment	Allowance for Loan Losses Allocated	Average Recorded Investment	Interest Income Recognized	Cash Basis Interest Recognized
With no related allowance recorded:						
Commercial						
Commercial & Industrial	\$3,725	\$3,527	\$—	\$1,464	\$—	\$—
Farmland	—	—	—	—	—	—
Non Farm, Non Residential Agriculture	24	24	—	6	—	—
All Other Commercial	—	—	—	—	—	—
Residential						
First Liens	—	—	—	9	—	—
Home Equity	—	—	—	—	—	—
Junior Liens	—	—	—	—	—	—
Multifamily	—	—	—	—	—	—
All Other Residential	—	—	—	—	—	—
Consumer						
Motor Vehicle	—	—	—	—	—	—
All Other Consumer	—	—	—	—	—	—
With an allowance recorded:						
Commercial						
Commercial & Industrial	10,789	10,789	3,353	14,131	—	—
Farmland	—	—	—	446	—	—
Non Farm, Non Residential Agriculture	8,063	7,997	1,361	8,100	—	—
All Other Commercial	4,107	4,107	896	3,458	—	—
Residential						
First Liens	38	38	—	646	—	—
Home Equity	—	—	—	—	—	—
Junior Liens	—	—	—	—	—	—
Multifamily	—	—	—	2,770	—	—
All Other Residential	—	—	—	—	—	—
Consumer						
Motor Vehicle	—	—	—	—	—	—
All Other Consumer	—	—	—	—	—	—
TOTAL	\$26,746	\$26,482	\$5,610	\$31,030	\$—	\$—





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	December 31, 2012					
	Unpaid Principal	Recorded	Allowance for Loan Losses	Average Recorded	Interest Income	Cash Basis Interest Income
(Dollar amounts in thousands)	Balance	Investment	Allocated	Investment	Recognized	Recognized
With no related allowance recorded:						
Commercial						
Commercial & Industrial	\$—	\$—	\$—	\$1,013	\$—	\$—
Farmland	—	—	—	—	—	—
Non Farm, Non Residential	—	—	—	1,679	—	—
Agriculture	—	—	—	—	—	—
All Other Commercial	—	—	—	—	—	—
Residential						
First Liens	—	—	—	150	—	—
Home Equity	—	—	—	—	—	—
Junior Liens	—	—	—	—	—	—
Multifamily	—	—	—	50	—	—
All Other Residential	—	—	—	—	—	—
Consumer						
Motor Vehicle	—	—	—	—	—	—
All Other Consumer	—	—	—	—	—	—
With an allowance recorded:						
Commercial						
Commercial & Industrial	17,262	17,098	3,153	16,738	—	—
Farmland	891	891	191	891	—	—
Non Farm, Non Residential	7,438	7,386	293	5,000	179	—
Agriculture	—	—	—	—	—	—
All Other Commercial	1,209	1,209	52	1,362	—	—
Residential						
First Liens	1,254	1,254	126	1,230	—	—
Home Equity	179	179	—	75	—	—
Junior Liens	—	—	—	176	—	—
Multifamily	5,540	5,540	3,794	2,216	—	—
All Other Residential	—	—	—	—	—	—
Consumer						
Motor Vehicle	—	—	—	—	—	—
All Other Consumer	—	—	—	—	—	—
TOTAL	\$33,773	\$33,557	\$7,609	\$30,580	\$179	\$—

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	Three Months Ended September 30, 2013			Nine Months Ended September 30, 2013		
	Average Recorded	Interest Income	Cash Basis Interest Income	Average Recorded	Interest Income	Cash Basis Interest Income
(Dollar amounts in thousands)	Investment	Recognized	Recognized	Investment	Recognized	Recognized
With no related allowance recorded:						
Commercial						
Commercial & Industrial	\$2,728	\$—	\$—	\$1,464	\$—	\$—
Farmland	—	—	—	—	—	—
Non Farm, Non Residential	12	—	—	6	—	—
Agriculture	—	—	—	—	—	—
All Other Commercial	—	—	—	—	—	—
Residential						
First Liens	17	—	—	9	—	—
Home Equity	—	—	—	—	—	—
Junior Liens	—	—	—	—	—	—
Multifamily	—	—	—	—	—	—
All Other Residential	—	—	—	—	—	—
Consumer						
Motor Vehicle	—	—	—	—	—	—
All Other Consumer	—	—	—	—	—	—
With an allowance recorded:						
Commercial						
Commercial & Industrial	11,627	—	—	14,131	—	—
Farmland	—	—	—	446	—	—
Non Farm, Non Residential	8,185	—	—	8,100	—	—
Agriculture	—	—	—	—	—	—
All Other Commercial	4,148	—	—	3,458	—	—
Residential						
First Liens	39	—	—	646	—	—
Home Equity	—	—	—	—	—	—
Junior Liens	—	—	—	—	—	—
Multifamily	—	—	—	2,770	—	—
All Other Residential	—	—	—	—	—	—
Consumer						
Motor Vehicle	—	—	—	—	—	—
All Other Consumer	—	—	—	—	—	—
TOTAL	\$26,756	\$—	\$—	\$31,030	\$—	\$—

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	Three Months Ended September 30, 2012			Nine Months Ended September 30, 2012		
	Average Recorded Investment	Interest Income Recognized	Cash Basis Interest Income Recognized	Average Recorded Investment	Interest Income Recognized	Cash Basis Interest Income Recognized
(Dollar amounts in thousands)						
With no related allowance recorded:						
Commercial						
Commercial & Industrial	\$2,531	\$—	\$—	\$1,266	\$—	\$—
Farmland	—	—	—	—	—	—
Non Farm, Non Residential	987	—	—	2,098	—	—
Agriculture	—	—	—	—	—	—
All Other Commercial	—	—	—	—	—	—
Residential						
First Liens	—	—	—	188	—	—
Home Equity	—	—	—	—	—	—
Junior Liens	—	—	—	—	—	—
Multifamily	—	—	—	62	—	—
All Other Residential	—	—	—	—	—	—
Consumer						
Motor Vehicle	—	—	—	—	—	—
All Other Consumer	—	—	—	—	—	—
With an allowance recorded:						
Commercial						
Commercial & Industrial	15,427	—	—	16,648	—	—
Farmland	891	—	—	891	—	—
Non Farm, Non Residential	5,045	—	—	4,404	—	—
Agriculture	—	—	—	—	—	—
All Other Commercial	1,313	—	—	1,400	—	—
Residential						
First Liens	1,234	—	—	1,224	—	—
Home Equity	99	—	—	49	—	—
Junior Liens	—	—	—	220	—	—
Multifamily	2,770	—	—	1,385	—	—
All Other Residential	—	—	—	—	—	—
Consumer						
Motor Vehicle	—	—	—	—	—	—
All Other Consumer	—	—	—	—	—	—
TOTAL	\$30,297	\$—	\$—	\$29,835	\$—	\$—



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The table below presents the recorded investment in non-performing loans.

	September 30, 2013		
	Loans Past Due Over 90 Day Still Accruing	Troubled Debt Restructurings	Nonaccrual
(Dollar amounts in thousands)			
Commercial			
Commercial & Industrial	\$ 10	\$ 10,083	\$ 5,061
Farmland	—	—	179
Non Farm, Non Residential	37	6,215	5,189
Agriculture	—	—	116
All Other Commercial	—	—	4,165
Residential			
First Liens	747	4,276	4,414
Home Equity	22	—	188
Junior Liens	147	—	547
Multifamily	—	—	452
All Other Residential	—	—	135
Consumer			
Motor Vehicle	172	626	186
All Other Consumer	4	17	1,168
TOTAL	\$ 1,139	\$ 21,217	\$ 21,800
	December 31, 2012		
	Loans Past Due Over 90 Day Still Accruing	Troubled Debt Restructurings	Nonaccrual
(Dollar amounts in thousands)			
Commercial			
Commercial & Industrial	\$ 724	\$ 11,573	\$ 9,360
Farmland	231	—	907
Non Farm, Non Residential	491	4,836	6,718
Agriculture	69	—	104
All Other Commercial	—	—	4,811
Residential			
First Liens	1,237	4,126	6,852
Home Equity	24	—	196
Junior Liens	538	—	405
Multifamily	101	—	5,598
All Other Residential	—	—	150
Consumer			
Motor Vehicle	133	685	174
All Other Consumer	3	16	1,519
TOTAL	\$ 3,551	\$ 21,236	\$ 36,794



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Loans covered by loss share agreements with the FDIC included in loans past due over 90 days still on accrual are \$76 thousand at September 30, 2013 and \$630 thousand at December 31, 2012. Covered loans included in non-accrual loans are \$2.7 million at September 30, 2013 and \$4.3 million at December 31, 2012. Covered loans of \$1.7 million at September 30, 2013 and \$2.9 million at December 31, 2012 are deemed impaired and have allowance for loan loss allocated to them of \$100 thousand and \$236 thousand, respectively for September 30, 2013 and December 31, 2012. Non-performing loans include both smaller balance homogeneous loans that are collectively evaluated for impairment and individually classified impaired loans.

The following table presents the aging of the recorded investment in loans by past due category and class of loans.

(Dollar amounts in thousands)	September 30, 2013			Total Past Due	Current	Total
	30-59 Days Past Due	60-89 Days Past Due	Greater than 90 days Past Due			
Commercial						
Commercial & Industrial	\$1,863	\$1,096	\$10,830	\$13,789	\$466,057	\$479,846
Farmland	58	—	123	181	85,479	85,660
Non Farm, Non Residential	204	464	3,080	3,748	255,676	259,424
Agriculture	280	—	1	281	129,151	129,432
All Other Commercial	260	102	—	362	108,605	108,967
Residential						
First Liens	1,701	1,563	1,889	5,153	331,226	336,379
Home Equity	177	9	22	208	42,288	42,496
Junior Liens	248	57	659	964	32,864	33,828
Multifamily	20	—	404	424	60,584	61,008
All Other Residential	—	26	—	26	10,289	10,315
Consumer						
Motor Vehicle	3,250	474	189	3,913	244,281	248,194
All Other Consumer	152	9	4	165	22,159	22,324
TOTAL	\$8,213	\$3,800	\$17,201	\$29,214	\$1,788,659	\$1,817,873

  

(Dollar amounts in thousands)	December 31, 2012			Total Past Due	Current	Total
	30-59 Days Past Due	60-89 Days Past Due	Greater than 90 days Past Due			
Commercial						
Commercial & Industrial	\$1,315	\$861	\$3,616	\$5,792	\$487,160	\$492,952
Farmland	534	—	1,122	1,656	87,270	88,926
Non Farm, Non Residential	5,618	1,004	2,449	9,071	290,023	299,094
Agriculture	137	—	78	215	130,404	130,619
All Other Commercial	568	202	350	1,120	81,453	82,573
Residential						
First Liens	8,359	1,659	4,599	14,617	336,230	350,847
Home Equity	143	15	24	182	43,317	43,499
Junior Liens	555	98	586	1,239	36,535	37,774
Multifamily	52	—	5,641	5,693	49,019	54,712
All Other Residential	214	—	—	214	10,834	11,048
Consumer						
Motor Vehicle	4,164	600	182	4,946	241,303	246,249

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All Other Consumer	225	93	3	321	23,318	23,639
TOTAL	\$21,884	\$4,532	\$18,650	\$45,066	\$1,816,866	\$1,861,932

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Troubled Debt Restructurings:

The Corporation has allocated \$4.1 million and \$1.6 million of specific reserves to customers whose loan terms have been modified in troubled debt restructurings as of September 30, 2013 and December 31, 2012. The Corporation has not committed to lend additional amounts as of September 30, 2013 and December 31, 2012 to customers with outstanding loans that are classified as troubled debt restructurings. Modification of the terms of such loans typically include one or a combination of the following: a reduction of the stated interest rate of the loan; an extension of the maturity date at a stated rate of interest lower than the current market rate for new debt with similar risk. No modification in 2013 or 2012 resulted in permanent reduction of the recorded investment in the loan. There were \$1.6 million in modifications that were troubled debt restructurings in the quarter ended September 30, 2013 and \$5.1 million for the three months ended September 30, 2012, resulting in no impact to the allowance for loan losses. In the third quarter of 2013 and 2012 there were non farm, non residential loans for \$1.5 million and \$4.9 million respectively that were collateralized well enough to expect no loss. The remaining loans added were all other consumer loans. There were no loans that defaulted during the nine months ended September 30, 2013 that had been restructured within the past 12 months. There were \$15 thousand in loans that defaulted during the three and nine months ended September 30, 2012 that had been restructured within the past 12 months.

Credit Quality Indicators:

The Corporation categorizes loans into risk categories based on relevant information about the ability of borrowers to service their debt such as: current financial information, historical payment experience, credit documentation, public information, and current economic trends, among other factors. The Corporation analyzes loans individually by classifying the loans as to credit risk. This analysis includes non-homogeneous loans, such as commercial loans, with an outstanding balance greater than \$100 thousand. Any consumer loans outstanding to a borrower who had commercial loans analyzed will be similarly risk rated. This analysis is performed on a quarterly basis. The Corporation uses the following definitions for risk ratings:

**Special Mention:** Loans classified as special mention have a potential weakness that deserves management's close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the loan or of the institution's credit position at some future date.

**Substandard:** Loans classified as substandard are inadequately protected by the current net worth and debt service capacity of the borrower or of any pledged collateral. These loans have a well-defined weakness or weaknesses which have clearly jeopardized repayment of principal and interest as originally intended. They are characterized by the distinct possibility that the institution will sustain some future loss if the deficiencies are not corrected.

**Doubtful:** Loans classified as doubtful have all the weaknesses inherent in those graded substandard, with the added characteristic that the severity of the weaknesses makes collection or liquidation in full highly questionable or improbable based upon currently existing facts, conditions, and values.

Furthermore, non-homogeneous loans which were not individually analyzed, but are 90+ days past due or on non-accrual are classified as substandard. Loans included in homogeneous pools, such as residential or consumer may be classified as substandard due to 90+ days delinquency, non-accrual status, bankruptcy, or loan restructuring.



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Loans not meeting the criteria above that are analyzed individually as part of the above described process are considered to be pass rated loans. Loans listed as not rated are either less than \$100 thousand or are included in groups of homogeneous loans. As of September 30, 2013 and December 31, 2012, and based on the most recent analysis performed, the risk category of loans by class of loans are as follows:

(Dollar amounts in thousands)	September 30, 2013					
	Pass	Special Mention	Substandard	Doubtful	Not Rated	Total
<b>Commercial</b>						
Commercial & Industrial	\$417,192	\$19,532	\$28,254	\$6,656	\$7,159	\$478,793
Farmland	79,780	3,717	435	—	129	84,061
Non Farm, Non Residential	228,337	8,266	20,812	543	826	258,784
Agriculture	122,541	4,939	80	—	111	127,671
All Other Commercial	93,628	3,639	10,550	47	650	108,514
<b>Residential</b>						
First Liens	115,051	4,217	8,274	1,245	206,439	335,226
Home Equity	13,207	370	1,526	113	27,209	42,425
Junior Liens	9,088	39	631	241	23,708	33,707
Multifamily	56,738	2,473	1,568	48	8	60,835
All Other Residential	3,285	—	33	—	6,966	10,284
<b>Consumer</b>						
Motor Vehicle	11,752	290	358	9	234,689	247,098
All Other Consumer	3,670	76	64	23	18,351	22,184
<b>TOTAL</b>	<b>\$1,154,269</b>	<b>\$47,558</b>	<b>\$72,585</b>	<b>\$8,925</b>	<b>\$526,245</b>	<b>\$1,809,582</b>
<b>December 31, 2012</b>						
(Dollar amounts in thousands)	Pass	Special Mention	Substandard	Doubtful	Not Rated	Total
<b>Commercial</b>						
Commercial & Industrial	\$414,680	\$31,368	\$31,442	\$7,138	\$7,025	\$491,653
Farmland	81,977	2,718	1,616	—	805	87,116
Non Farm, Non Residential	249,614	25,764	22,038	831	42	298,289
Agriculture	119,789	8,921	134	—	62	128,906
All Other Commercial	69,952	132	11,239	54	803	82,180
<b>Residential</b>						
First Liens	113,360	8,986	11,516	689	215,034	349,585
Home Equity	13,035	469	1,631	23	28,267	43,425
Junior Liens	10,419	50	515	70	26,575	37,629
Multifamily	42,719	3,328	8,481	59	—	54,587
All Other Residential	2,840	—	35	—	8,136	11,011
<b>Consumer</b>						
Motor Vehicle	11,695	262	311	25	232,727	245,020
All Other Consumer	4,614	73	104	21	18,675	23,487
<b>TOTAL</b>	<b>\$1,134,694</b>	<b>\$82,071</b>	<b>\$89,062</b>	<b>\$8,910</b>	<b>\$538,151</b>	<b>\$1,852,888</b>



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## 3. Securities

The amortized cost and fair value of the Corporation's investments are shown below. All securities are classified as available-for-sale.

(Dollar amounts in thousands)	September 30, 2013			Fair Value
	Amortized Cost	Unrealized Gains	Unrealized Losses	
U.S. Government agencies	\$1,625	\$6	\$—	\$1,631
Mortgage Backed Securities - Residential	203,624	8,386	(1,783)	) 210,227
Mortgage Backed Securities - Commercial	4,768	1	(246)	) 4,523
Collateralized Mortgage Obligations	466,978	1,918	(12,784)	) 456,112
State and Municipal Obligations	186,632	7,011	(1,647)	) 191,996
Collateralized Debt Obligations	11,007	3,681	(7,164)	) 7,524
Equity Securities	320	342	—	662
TOTAL	\$874,954	\$21,345	\$(23,624)	) \$872,675

(Dollar amounts in thousands)	December 31, 2012			Fair Value
	Amortized Cost	Unrealized Gains	Unrealized Losses	
U.S. Government agencies	\$1,807	\$79	\$—	\$1,886
Mortgage Backed Securities-residential	231,316	13,373	(13)	) 244,676
Mortgage Backed Securities-commercial	5,146	1	(16)	) 5,131
Collateralized mortgage obligations	230,739	2,827	(246)	) 233,320
State and municipal	187,044	12,518	(77)	) 199,485
Collateralized debt obligations	12,243	1,761	(7,882)	) 6,122
Equities	320	60	—	380
TOTAL	\$668,615	\$30,619	\$(8,234)	) \$691,000

Contractual maturities of debt securities at September 30, 2013 were as follows. Securities not due at a single maturity or with no maturity date, primarily mortgage-backed and equity securities are shown separately.

(Dollar amounts in thousands)	Available-for-Sale	
	Amortized Cost	Fair Value
Due in one year or less	\$12,171	\$12,263
Due after one but within five years	35,071	36,659
Due after five but within ten years	83,992	86,735
Due after ten years	535,008	521,606
	666,242	657,263
Mortgage-backed securities and equities	208,712	215,412
TOTAL	\$874,954	\$872,675



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There were \$7 thousand in gains and no losses from investment sales realized by the Corporation for the nine months ended September 30, 2013. For the three months ended September 30, 2013 there were no gains or losses on investment securities. There were \$683 thousand in gains and \$6 thousand in losses from investment sales, and \$11 thousand in losses from OTTI realized by the Corporation for the nine months ended September 30, 2012. The \$11 thousand of OTTI was realized in the second quarter of 2012. For the three months ended September 30, 2012 there were \$19 thousand in gains and \$2 thousand in losses from investment sales.

The following tables show the securities' gross unrealized losses and fair value, aggregated by investment category and length of time that individual securities have been in continuous unrealized loss position, at September 30, 2013 and December 31, 2012.

(Dollar amounts in thousands)	September 30, 2013					
	Less Than 12 Months		More Than 12 Months		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Mortgage Backed Securities - Residential	\$60,541	\$(1,783)	\$—	\$—	\$60,541	\$(1,783)
Mortgage Backed Securities - Commercial	4,486	(246)	—	—	4,486	(246)
Collateralized mortgage obligations	333,189	(12,258)	8,791	(526)	341,980	(12,784)
State and municipal obligations	38,538	(1,553)	991	(94)	39,529	(1,647)
Collateralized Debt Obligations	—	—	3,843	(7,164)	3,843	(7,164)
Total temporarily impaired securities	\$436,754	\$(15,840)	\$13,625	\$(7,784)	\$450,379	\$(23,624)

  

(Dollar amounts in thousands)	December 31, 2012					
	Less Than 12 Months		More Than 12 Months		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Mortgage Backed Securities - Residential	\$7,245	\$(13)	\$—	\$—	\$7,245	\$(13)
Mortgage Backed Securities - Commercial	5,086	(16)	—	—	5,086	(16)
Collateralized mortgage obligations	46,121	(246)	—	—	46,121	(246)
State and municipal obligations	8,611	(77)	—	—	8,611	(77)
Collateralized Debt Obligations	—	—	4,032	(7,882)	4,032	(7,882)
Total temporarily impaired securities	\$67,063	\$(352)	\$4,032	\$(7,882)	\$71,095	\$(8,234)

Management evaluates securities for other-than-temporary impairment (“OTTI”) at least on a quarterly basis, and more frequently when economic or market conditions warrant such an evaluation. The investment securities portfolio is evaluated for OTTI by segregating the portfolio into two general segments and applying the appropriate OTTI model. Investment securities are generally evaluated for OTTI under FASB ASC 320, Investments - Debt and Equity Securities. However, certain purchased beneficial interests, including non-agency mortgage-backed securities, asset-backed securities, and collateralized debt obligations, that had credit ratings at the time of purchase of below AA are evaluated using the model outlined in FASB ASC 325-40, Beneficial Interests in Securitized Financial Assets.

In determining OTTI under the FASB ASC 320 model, management considers many factors, including: (1) the length of time and the extent to which the fair value has been less than cost, (2) the financial condition and near-term prospects of the issuer, (3) whether the market decline was affected by macroeconomic conditions, and (4) whether

the entity has the intent to sell the security or more likely than not will be required to sell the security before its anticipated recovery. The assessment of whether an other-than-temporary decline exists involves a high degree of subjectivity and judgment and is based on the information available to management at a point in time.

The second segment of the portfolio uses the OTTI guidance provided by FASB ASC 325 that is specific to purchased beneficial interests that, on the purchase date, were rated below AA. Under the FASB ASC 325 model, the Company compares the present value of the remaining cash flows as estimated at the preceding evaluation date to the current expected remaining cash flows. An OTTI is deemed to have occurred if there has been an adverse change in the remaining expected future cash flows.



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When OTTI occurs under either model, the amount of the OTTI recognized in earnings depends on whether an entity intends to sell the security or it is more likely than not it will be required to sell the security before recovery of its amortized cost basis, less any current-period credit loss. If an entity intends to sell or it is more likely than not it will be required to sell the security before recovery of its amortized cost basis, less any current-period credit loss, the OTTI shall be recognized in earnings equal to the entire difference between the investment's amortized cost basis and its fair value at the balance sheet date. If an entity does not intend to sell the security and it is not more likely than not that the entity will be required to sell the security before recovery of its amortized cost basis less any current-period loss, the OTTI shall be separated into the amount representing the credit loss and the amount related to all other factors. The amount of the total OTTI related to the credit loss is determined based on the present value of cash flows expected to be collected and is recognized in earnings. The amount of the total OTTI related to other factors is recognized in other comprehensive income, net of applicable taxes. The previous amortized cost basis less the OTTI recognized in earnings becomes the new amortized cost basis of the investment.

Gross unrealized losses on investment securities were \$23.6 million as of September 30, 2013 and \$8.2 million as of December 31, 2012. A majority of these losses represent negative adjustments to market value relative to the interest rate environment reflecting the increase in market rates in 2013 and not losses related to the creditworthiness of the issuer. Based upon our review of the issuers, we do not believe these investments to be other than temporarily impaired. Management does not intend to sell these securities and it is not more likely than not that we will be required to sell them before their anticipated recovery.

A significant portion of the securities in an unrealized loss position for more than 12 months relate to collateralized debt obligations that were separately evaluated under FASB ASC 325-40, Beneficial Interests in Securitized Financial Assets. Based upon qualitative considerations, such as a down grade in credit rating or further defaults of underlying issuers during the quarter, and an analysis of expected cash flows, we have determined that three of the CDO's included in collateralized debt obligations were other-than-temporarily impaired, though no impairment was identified during 2013. Those three CDO's have a contractual balance of \$26.7 million at September 30, 2013 which has been reduced to \$7.0 million by \$1.4 million of interest payments received, \$14.9 million of cumulative OTTI charges recorded through earnings to date, and \$3.4 million recorded in other comprehensive income (\$2.1 million after tax effect). The severity of the OTTI recorded varies by security, based on the analysis described below, and ranges at September 30, 2013 from 28% to 94%. The losses recorded in other comprehensive income represents temporary impairment due to factors other than credit loss, mainly current market illiquidity. The issuers in these securities are primarily banks, but some of the pools do include a limited number of insurance companies. The market for these securities has become very illiquid, there are very few new issuances of trust preferred securities and the credit spreads implied by current prices have increased dramatically and remain very high, resulting in significant non-credit related impairment. The Company uses the OTTI evaluation model to compare the present value of expected cash flows to the previous estimate to ensure there are no adverse changes in cash flows during the quarter. The OTTI model considers the structure and term of the CDO and the financial condition of the underlying issuers. Specifically, the model details interest rates, principal balances of note classes and underlying issuers, the timing and amount of interest and principal payments of the underlying issuers, and the allocation of the payments to the note classes. Cash flows are projected using a forward rate LIBOR curve, as these CDOs are variable rate instruments. An average rate is then computed using this same forward rate curve to determine an appropriate discount rate (3 month LIBOR plus margin ranging from 160 to 180 basis points). The current estimate of expected cash flows is based on the most recent trustee reports and any other relevant market information including announcements of interest payment deferrals or defaults of underlying trust preferred securities. Assumptions used in the model include expected future default rates and prepayments. In addition we use the model to "stress" each CDO, or make assumptions more severe than expected activity, to determine the degree to which assumptions could deteriorate before the CDO could no longer fully support repayment of the Company's note class.

In the third quarter of 2013, the Corporation received a \$1.3 million payment on a CDO that had a book value of \$0.2 million. The payment in excess of book value is recognized as interest income. This CDO had the highest severity of recorded impairment and while a payment by the issuer was expected, such payment was not projected until maturity in the OTTI evaluation at June 30, 2013. The future payments, if any, on this CDO cannot be predicted with enough accuracy that such future payments will be recorded as interest income when received.

Collateralized debt obligations include an investment in a CDO consisting of pooled trust preferred securities in which the issuers are primarily banks. This CDO with an amortized cost of \$606 thousand and a fair value of \$548 thousand is rated BAA3 and is the senior tranche, is not in the scope of FASB ASC 325, as it was rated high investment grade at purchase, and is not considered to be other-than-temporarily impaired based on its credit quality. Its fair value is negatively impacted by the factors described above.

Management has consistently used Standard & Poors pricing to value these investments. There are a number of other pricing sources available to determine fair value for these investments. These sources utilize a variety of methods to determine fair value. The result is a wide range of estimates of fair value for these securities. The Standard & Poors pricing ranges from 4.4 to 90.3

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while Moody Investor Service pricing ranges from .32 to 90.5, with others falling somewhere in between. We recognize that the Standard & Poors pricing utilized is an estimate, but have been consistent in using this source and its estimate of fair value.

Equity securities relate to investments in a bank stock held at the holding company. In the second quarter of 2012 the Corporation recognized other-than-temporary impairment on this equity security in the amount of \$11 thousand. On October 1, 2013 it was announced that another bank was acquiring this security and the Corporation intends to sell acquiring bank's security when the acquisition has been completed.

The table below presents a rollforward of the credit losses recognized in earnings for the three and nine month periods ended September 30, 2013 and 2012:

(Dollar amounts in thousands)	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2013	2012	2013	2012
Beginning balance	\$ 14,983	\$ 14,983	\$ 14,983	\$ 15,180
Increases to the amount related to the credit				
Loss for which other-than-temporary was previously recognized	—	—	—	11
Reductions for increases in cash flows collected	(581	) —	(581	) —
Amounts realized for securities sold during the period	—	—	—	(208
Ending balance	\$ 14,402	\$ 14,983	\$ 14,402	\$ 14,983

## 4. Fair Value

FASB ASC No. 820-10 establishes a fair value hierarchy which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The standard describes three levels of inputs that may be used to measure fair value:

Level 1: Quoted prices (unadjusted) of identical assets or liabilities in active markets that the entity has the ability to access as of the measurement date.

Level 2: Significant other observable inputs other than Level I prices such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data.

Level 3: Significant unobservable inputs that reflect a reporting entity's own assumptions about the assumptions that market participants would use in pricing an asset or liability.

The fair value of most securities available for sale is determined by obtaining quoted prices on nationally recognized securities exchanges (Level 1 inputs) or matrix pricing, which is a mathematical technique widely used in the industry to value debt securities without relying exclusively on quoted prices for the specific securities but rather by relying on the securities' relationship to other benchmark quoted securities (Level 2 inputs).

For those securities that cannot be priced using quoted market prices or observable inputs a Level 3 valuation is determined. These securities are primarily trust preferred securities, which are priced using Level 3 due to current market illiquidity and certain investments in state and municipal securities. The fair value of the trust preferred securities is obtained from a third party provider without adjustment. As described previously, management obtains values from other pricing sources to validate the Standard & Poors pricing that they currently utilize. The fair value of state and municipal obligations are derived by comparing the securities to current market rates plus an appropriate credit spread to determine an estimated value. Illiquidity spreads are then considered. Credit reviews are performed on

each of the issuers. The significant unobservable inputs used in the fair value measurement of the Corporation's state and municipal obligations are credit spreads related to specific issuers. Significantly higher credit spread assumptions would result in significantly lower fair value measurement. Conversely, significantly lower credit spreads would result in a significantly higher fair value measurements.

The fair value of derivatives is based on valuation models using observable market data as of the measurement date (Level 2 inputs).

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	September 30, 2013			
	Fair Value Measurements Using Significant Unobservable Inputs (Level 3)			
(Dollar amounts in thousands)	Level 1	Level 2	Level 3	Total
U.S. Government agencies	\$—	\$1,631	\$—	\$1,631
Mortgage Backed Securities-residential	—	210,227	—	210,227
Mortgage Backed Securities-commercial	—	4,523	—	4,523
Collateralized mortgage obligations	—	456,112	—	456,112
State and municipal	—	187,472	4,524	191,996
Collateralized debt obligations	—	—	7,524	7,524
Equities	662	—	—	662
TOTAL	\$662	\$859,965	\$12,048	\$872,675
Derivative Assets		1,381		
Derivative Liabilities		(1,381	)	

	December 31, 2012			
	Fair Value Measurements Using Significant Unobservable Inputs (Level 3)			
(Dollar amounts in thousands)	Level 1	Level 2	Level 3	Total
U.S. Government agencies	\$—	\$1,886	\$—	\$1,886
Mortgage Backed Securities-residential	—	244,676	—	244,676
Mortgage Backed Securities-commercial	—	5,131	—	5,131
Collateralized mortgage obligations	—	233,320	—	233,320
State and municipal	—	189,574	9,911	199,485
Collateralized debt obligations	—	—	6,122	6,122
Equities	380	—	—	380
TOTAL	\$380	\$674,587	\$16,033	\$691,000
Derivative Assets		2,053		
Derivative Liabilities		(2,053	)	

There were no transfers between Level 1 and Level 2 during 2013 and 2012.

The table below presents a reconciliation and income statement classification of gains and losses for all assets measured at fair value on a recurring basis using significant unobservable inputs (Level 3) for the three and nine months ended September 30, 2013 and the year ended December 31, 2012.

	Fair Value Measurements Using Significant Unobservable Inputs (Level 3)		
	Three Months Ended September 30, 2013		
	State and municipal obligations	Collateralized debt obligations	Total
Beginning balance, July 1	\$6,502	\$8,177	\$14,679
Total realized/unrealized gains or losses			
Included in earnings	—	—	—
Included in other comprehensive income	—	(305	) (305
Transfers	(1,187	) —	(1,187
Settlements	(790	) (349	) (1,139

Ending balance, September 30	\$4,525	\$7,523	\$12,048
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	Fair Value Measurements Using Significant Unobservable Inputs (Level 3) Nine Months Ended September 30, 2013		
	State and municipal obligations	Collateralized debt obligations	Total
Beginning balance, January 1	\$9,911	\$6,122	\$16,033
Total realized/unrealized gains or losses Included in earnings	—	—	—
Included in other comprehensive income	—	2,499	2,499
Transfers	(1,187	) —	(1,187
Settlements	(4,199	) (1,098	) (5,297
Ending balance, September 30	\$4,525	\$7,523	\$12,048

The transfers out of level 3 is due to securities that previously were not priced independently are now priced as other level 2 securities.

	Fair Value Measurements Using Significant Unobservable Inputs (Level 3) Balance at December 31, 2012			
	Equities	State and municipal obligations	Collateralized debt obligations	Total
Beginning balance, January 1	\$1,711	\$9,525	\$4,771	\$16,007
Total realized/unrealized gains or losses Included in earnings	(446	) —	(96	) (542
Included in other comprehensive income	—	—	1,556	1,556
Purchases	—	1,186	—	1,186
Settlements	(1,265	) (800	) (109	) (2,174
Ending balance, December 31	\$—	\$9,911	\$6,122	\$16,033

The following table presents quantitative information about recurring and non-recurring Level 3 fair value measurements at September 30, 2013.

	Fair Value	Valuation Technique(s)	Unobservable Input(s)	Range
State and municipal obligations	\$4,525	Discounted cash flow	Discount rate Probability of default	3.05%-5.50%
Other real estate	\$9,249	Sales comparison/income approach	Discount rate for age of appraisal and market conditions	5.00%-20.00%
Impaired Loans	17,324	Sales comparison/income approach	Discount rate for age of appraisal and market conditions	0.00%-50.00%

All impaired loans disclosed in footnote 2 that have no allowance for loan loss allocation are valued at Level 3 and are carried at a fair value of \$17.3 million, net of a valuation allowance of \$5.6 million at September 30, 2013. At December 31, 2012 impaired loans valued at Level 3 were carried at a fair value of \$26.0 million, net of a valuation allowance of \$7.6 million. The impact to the provision for loan losses was \$(0.2) and \$2.2 million for the three and nine months ended September 30, 2013, and was \$4.2 million for the year ended December 31, 2012. Other real estate owned is valued at Level 3. Other real estate owned at September 30, 2013, with a value of \$9.2 million was reduced \$1.3 million for fair value adjustment. Other real estate owned at December 31, 2012, with a value of \$7.7 million was

reduced \$234 thousand for fair value adjustment.

Fair value is measured based on the value of the collateral securing those loans, and is determined using several methods. Generally the fair value of real estate is determined based on appraisals by qualified licensed appraisers. Appraisals for real estate generally use three methods to derive value: cost, sales or market comparison and income approach. The cost method bases value on the

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cost to replace current property. The market comparison evaluates the sales price of similar properties in the same market area. The income approach considers net operating income generated by the property and the investor's required return. The final fair value is based on a reconciliation of these three approaches. If an appraisal is not available, the fair value may be determined by using a cash flow analysis, a broker's opinion of value, the net present value of future cash flows, or an observable market price from an active market. Fair value of other real estate is based upon the current appraised values of the properties as determined by qualified licensed appraisers and the Company's judgment of other relevant market conditions. Appraisals are obtained annually and reductions in value are recorded as a valuation through a charge to expense. The primary unobservable input used by management in estimating fair value are additional discounts to the appraised value to consider the age of the appraisal and market conditions, which are based on management's past experience in resolving these types of properties. These discounts range from 5% to 20%. Other real estate and impaired loans carried at fair value are primarily comprised of smaller balance properties. One impaired loan has an estimated fair value of \$3.9 million. The collateral securing this loan is a hotel and was appraised based on income and sales comparison approaches. Given the current distressed market, it was difficult for the appraiser to identify recent and relevant comparable sales, therefore the value was based predominantly on the income method which applied a 9.5% capitalization rate to projected net operating income.

The following tables presents loans identified as impaired by class of loans as of September 30, 2013 and December 31, 2012, which are all considered Level 3.

(Dollar amounts in thousands)	September 30, 2013		Fair Value
	Carrying Value	Allowance for Loan Losses Allocated	
Commercial			
Commercial & Industrial	\$10,792	\$3,353	\$7,439
Farmland	—	—	—
Non Farm, Non Residential	7,997	1,361	6,636
Agriculture	—	—	—
All Other Commercial	4,107	896	3,211
Residential			
First Liens	38	—	38
Home Equity	—	—	—
Junior Liens	—	—	—
Multifamily	—	—	—
All Other Residential	—	—	—
Consumer			
Motor Vehicle	—	—	—
All Other Consumer	—	—	—
TOTAL	\$22,934	\$5,610	\$17,324

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(Dollar amounts in thousands)	December 31, 2012		Fair Value
	Carrying Value	Allowance for Loan Losses Allocated	
Commercial			
Commercial & Industrial	\$17,098	\$3,153	\$13,945
Farmland	891	191	700
Non Farm, Non Residential Agriculture	7,386	293	7,093
All Other Commercial	1,209	52	1,157
Residential			
First Liens	1,254	126	1,128
Home Equity	179	—	179
Junior Liens	—	—	—
Multifamily	5,540	3,794	1,746
All Other Residential	—	—	—
Consumer			
Motor Vehicle	—	—	—
All Other Consumer	—	—	—
TOTAL	\$33,557	\$7,609	\$25,948

The carrying amounts and estimated fair value of financial instruments at September 30, 2013 and December 31, 2012, are shown below. Carrying amount is the estimated fair value for cash and due from banks, federal funds sold, short-term borrowings, accrued interest receivable and payable, demand deposits, short-term debt and variable-rate loans or deposits that reprice frequently and fully. Security fair values were described previously. For fixed-rate, non-impaired loans or deposits, variable rate loans or deposits with infrequent repricing or repricing limits, and for longer-term borrowings, fair value is based on discounted cash flows using current market rates applied to the estimated life and considering credit risk. The valuation of impaired loans was described previously. Loan fair value estimates do not necessarily represent an exit price. Fair values of loans held for sale are based on market bids on the loans or similar loans. It was not practicable to determine the fair value of Federal Home Loan Bank stock due to restrictions placed on its transferability. For the FDIC indemnification asset the carrying value is the estimated fair value as it represents amounts to be received from the FDIC in the near term. Fair value of debt is based on current rates for similar financing. The fair value of off-balance sheet items is not considered material.

(Dollar amounts in thousands)	September 30, 2013				Total
	Carrying Value	Fair Value Level 1	Level 2	Level 3	
Cash and due from banks	\$80,899	\$20,404	\$60,495	\$—	\$80,899
Federal funds sold	3,420	—	3,420	—	3,420
Securities available—for—sale	872,675	662	859,965	12,048	872,675
Restricted stock	21,050	—	—	—	—
Loans, net	1,786,601	—	—	1,845,392	1,845,392
FDIC Indemnification Asset	1,171	—	1,171	—	1,171
Accrued interest receivable	11,767	—	3,475	8,292	11,767
Deposits	(2,487,028 )	—	(2,489,329 )	—	(2,489,329 )
Short—term borrowings	(27,929 )	—	(27,929 )	—	(27,929 )
Federal Home Loan Bank advances	(58,362 )	—	(60,721 )	—	(60,721 )
Accrued interest payable	(770 )	—	(770 )	—	(770 )



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(Dollar amounts in thousands)	December 31, 2012				
	Carrying Value	Fair Value Level 1	Level 2	Level 3	Total
Cash and due from banks	\$87,230	\$21,333	\$65,897	\$—	\$87,230
Federal funds sold	20,800	—	20,800	—	20,800
Securities available—for—sale	691,000	380	674,587	16,033	691,000
Restricted stock	21,292	—	—	—	—
Loans, net	1,829,978	—	—	1,916,256	1,916,256
FDIC Indemnification Asset	2,632	—	2,632	—	2,632
Accrued interest receivable	12,024	—	2,980	9,044	12,024
Deposits	(2,276,134 )	—	(2,280,910 )	—	(2,280,910 )
Short—term borrowings	(40,551 )	—	(40,551 )	—	(40,551 )
Federal Home Loan Bank advances	(119,705 )	—	(124,933 )	—	(124,933 )
Accrued interest payable	(1,163 )	—	(1,163 )	—	(1,163 )

## 5. Short-Term Borrowings

Period-end short-term borrowings were comprised of the following:

	(000 's)	
	September 30, 2013	December 31, 2012
Federal Funds Purchased	\$160	\$2,750
Repurchase Agreements	27,769	37,801
	\$27,929	\$40,551

## 6. Other Borrowings

Other borrowings at period-end are summarized as follows:

	(000 's)	
	September 30, 2013	December 31, 2012
FHLB Advances	\$58,362	\$119,705
	\$58,362	\$119,705



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## 7. Components of Net Periodic Benefit Cost

	Three Months Ended September 30, (000's)				Nine Months Ended September 30, (000's)			
	Pension Benefits		Post-Retirement Health Benefits		Pension Benefits		Post-Retirement Health Benefits	
	2013	2012	2013	2012	2013	2012	2013	2012
Service cost	\$559	\$1,218	\$17	\$15	\$1,678	\$3,654	\$51	\$82
Interest cost	846	917	43	43	2,537	2,750	130	180
Expected return on plan assets	(827 )	(815 )	—	—	(2,482 )	(2,444 )	—	—
Amortization of transition obligation	—	—	15	15	—	—	44	45
Net amortization of prior service cost	(4 )	41	—	—	(12 )	124	—	—
Net amortization of net (gain) loss	523	567	—	—	1,568	1,702	—	—