

NBT BANCORP INC
Form 10-Q
May 12, 2014

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D. C. 20549
FORM 10 Q

(Mark One)

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

For the quarterly period ended March 31, 2014.

OR

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 0-14703

NBT BANCORP INC.
(Exact Name of Registrant as Specified in its Charter)

DELAWARE 16-1268674
(State of Incorporation) (I.R.S. Employer Identification No.)

52 SOUTH BROAD STREET, NORWICH, NEW YORK 13815
(Address of Principal Executive Offices) (Zip Code)

Registrant's Telephone Number, Including Area Code: (607) 337-2265

None

(Former Name, Former Address and Former Fiscal Year, if Changed Since Last Report)

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

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

Indicate by check mark 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. (Check One):

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Large accelerated filer Accelerated filer Non-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 April 30, 2014, there were 43,689,389 shares outstanding of the Registrant's common stock, \$0.01 par value per share.

NBT BANCORP INC.
FORM 10-Q--Quarter Ended March 31, 2014

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Item 1 – FINANCIAL STATEMENTS

NBT Bancorp Inc. and Subsidiaries
Consolidated Balance Sheets (unaudited)

	March 31, 2014	December 31, 2013
(In thousands, except share and per share data)		
Assets		
Cash and due from banks	\$ 182,071	\$ 157,625
Short-term interest bearing accounts	3,493	1,301
Securities available for sale, at fair value	1,377,585	1,364,881
Securities held to maturity (fair value \$114,920 and \$113,276, respectively)	117,896	117,283
Trading securities	6,954	5,779
Federal Reserve and Federal Home Loan Bank stock	41,458	46,864
Loans	5,482,025	5,406,795
Less allowance for loan losses	69,434	69,434
Net loans	5,412,591	5,337,361
Premises and equipment, net	87,647	88,327
Goodwill	263,634	264,997
Intangible assets, net	24,248	25,557
Bank owned life insurance	115,775	114,966
Other assets	119,777	127,234
Total assets	\$7,753,129	\$7,652,175
Liabilities		
Demand (noninterest bearing)	\$ 1,616,612	\$ 1,645,641
Savings, NOW, and money market	3,482,925	3,223,441
Time	969,361	1,021,142
Total deposits	6,068,898	5,890,224
Short-term borrowings	356,878	456,042
Long-term debt	308,679	308,823
Junior subordinated debt	101,196	101,196
Other liabilities	85,276	79,321
Total liabilities	6,920,927	6,835,606
Stockholders' equity		
Preferred stock, \$0.01 par value. Authorized 2,500,000 shares at March 31, 2014 and December 31, 2013	-	-
Common stock, \$0.01 par value. Authorized 100,000,000 shares at March 31, 2014 and December 31, 2013; issued 49,651,494 at March 31, 2014 and December 31, 2013	497	497
Additional paid-in-capital	574,071	574,152
Retained earnings	394,589	385,787
Accumulated other comprehensive loss	(11,550)	(16,765)
Common stock in treasury, at cost, 6,050,806 and 6,138,444 shares at March 31, 2014 and December 31, 2013, respectively	(125,405)	(127,102)
Total stockholders' equity	832,202	816,569
Total liabilities and stockholders' equity	\$7,753,129	\$7,652,175

See accompanying notes to unaudited interim consolidated financial statements.

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NBT Bancorp Inc. and Subsidiaries Consolidated Statements of Income (unaudited) (In thousands, except per share data)	Three months ended March 31,	
	2014	2013
Interest, fee, and dividend income		
Interest and fees on loans	\$60,015	\$53,695
Securities available for sale	6,757	5,746
Securities held to maturity	768	525
Other	537	403
Total interest, fee, and dividend income	68,077	60,369
Interest expense		
Deposits	3,284	4,150
Short-term borrowings	231	42
Long-term debt	2,507	3,609
Junior subordinated debt	538	428
Total interest expense	6,560	8,229
Net interest income	61,517	52,140
Provision for loan losses	3,596	5,658
Net interest income after provision for loan losses	57,921	46,482
Noninterest income		
Insurance and other financial services revenue	6,737	6,893
Service charges on deposit accounts	4,369	4,323
ATM and debit card fees	4,072	3,242
Retirement plan administration fees	2,918	2,682
Trust	4,446	2,913
Bank owned life insurance	1,382	849
Net securities gains	7	1,145
Other	2,346	3,182
Total noninterest income	26,277	25,229
Noninterest expense		
Salaries and employee benefits	29,534	27,047
Occupancy	6,226	4,977
Data processing and communications	4,001	3,455
Professional fees and outside services	3,415	2,901
Equipment	3,116	2,582
Office supplies and postage	1,685	1,590
FDIC expenses	1,278	1,130
Advertising	739	723
Amortization of intangible assets	1,310	851
Loan collection and other real estate owned	1,040	718
Merger expenses	-	10,681
Other	5,173	4,050
Total noninterest expense	57,517	60,705
Income before income tax expense	26,681	11,006
Income tax expense	8,672	3,357
Net income	\$18,009	\$7,649
Earnings per share		
Basic	\$0.41	\$0.21
Diluted	\$0.41	\$0.21

See accompanying notes to unaudited interim consolidated financial statements.

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NBT Bancorp Inc. and Subsidiaries Consolidated Statements of Comprehensive Income (unaudited) (In thousands)	Three months ended March 31,	
	2014	2013
Net income	\$18,009	\$7,649
Other comprehensive income (loss), net of tax		
Unrealized net holding gains (losses) arising during the period (pre-tax amounts of \$8,623 and (\$1,752))	5,208	(1,058)
Reclassification adjustment for net gains related to securities available for sale included in net income (pre-tax amounts of \$7 and \$1,145)	(4)	(691)
Pension and other benefits:		
Amortization of prior service cost and actuarial gains (pre-tax amounts of \$19 and \$826)	11	503
Total other comprehensive income (loss)	5,215	(1,246)
Comprehensive income	\$23,224	\$6,403

See accompanying notes to unaudited interim consolidated financial statements

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NBT Bancorp Inc. and Subsidiaries

Consolidated Statements of Stockholders' Equity (unaudited)

	Common Stock	Additional Paid-in- Capital	Retained Earnings	Accumulated Other Comprehensive Loss	Common Stock in Treasury	Total
(in thousands, except share and per share data)						
Balance at December 31, 2012	\$ 393	\$ 346,692	\$ 357,558	\$ (5,880)	\$ (116,490)	\$ 582,273
Net income	-	-	7,649	-	-	7,649
Cash dividends - \$0.20 per share	-	-	(6,758)	-	-	(6,758)
Issuance of 10,346,363 shares, net of 408,957 treasury shares, for Alliance acquisition	104	225,447	-	-	(5,779)	219,772
Net issuance of 28,339 shares to employee benefit plans and other stock plans, including tax benefit	-	(965)	-	-	606	(359)
Stock-based compensation	-	1,964	-	-	-	1,964
Other comprehensive loss	-	-	-	(1,246)	-	(1,246)
Balance at March 31, 2013	\$ 497	\$ 573,138	\$ 358,449	\$ (7,126)	\$ (121,663)	\$ 803,295
Balance at December 31, 2013	\$ 497	\$ 574,152	\$ 385,787	\$ (16,765)	\$ (127,102)	\$ 816,569
Net income	-	-	18,009	-	-	18,009
Cash dividends - \$0.21 per share	-	-	(9,207)	-	-	(9,207)
Net issuance of 87,638 shares to employee benefit plans and other stock plans, including tax benefit	-	(1,335)	-	-	1,697	362
Stock-based compensation	-	1,254	-	-	-	1,254
Other comprehensive income	-	-	-	5,215	-	5,215
Balance at March 31, 2014	\$ 497	\$ 574,071	\$ 394,589	\$ (11,550)	\$ (125,405)	\$ 832,202

See accompanying notes to unaudited interim consolidated financial statements.

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	Three Months Ended	
	March 31,	
	2014	2013
NBT Bancorp Inc. and Subsidiaries		
Consolidated Statements of Cash Flows (unaudited)		
(In thousands, except per share data)		
Operating activities		
Net income	\$18,009	\$7,649
Adjustments to reconcile net income to net cash provided by operating activities		
Provision for loan losses	3,596	5,658
Depreciation and amortization of premises and equipment	2,046	1,791
Net accretion on securities	921	1,091
Amortization of intangible assets	1,310	851
Stock based compensation	1,254	1,964
Increase in surrender value of bank owned life insurance	(968)	(849)
Purchases of trading securities	(1,043)	(744)
Unrealized gains in trading securities	(132)	(100)
Deferred income tax benefit	(18)	(309)
Proceeds from sales of loans held for sale	439	15,417
Originations and purchases of loans held for sale	(1,418)	(17,307)
Net gains on sales of loans held for sale	(3)	(480)
Net security gains	(7)	(1,145)
Net gain on sales of other real estate owned	(102)	(151)
Proceeds from settlement of bank owned life insurance	573	-
Gains on bank owned life insurance settlement	(414)	-
Net decrease in other assets	7,136	915
Net increase (decrease) in other liabilities	1,156	(9,336)
Net cash provided by operating activities	32,335	4,915
Investing activities		
Net cash provided by acquisitions	-	81,049
Securities available for sale:		
Proceeds from maturities, calls, and principal paydowns	67,341	109,986
Proceeds from sales	-	2,607
Purchases	(70,339)	(119,749)
Securities held to maturity:		
Proceeds from maturities, calls, and principal paydowns	5,107	6,940
Purchases	(5,217)	(3,131)
Proceeds from FHLB stock redemption	15,306	1,989
Net increase in loans	(78,304)	(17,791)
Net increase in Federal Reserve and FHLB stock	(9,900)	-
Purchases of premises and equipment	(1,114)	(1,006)
Proceeds from sales of other real estate owned	902	1,023
Net cash (used in) provided by investing activities	(76,218)	61,917
Financing activities		
Net increase in deposits	178,674	118,194
Net (decrease) increase in short-term borrowings	(99,164)	1,326
Repayments of long-term debt	(144)	(43,757)
Proceeds from the issuance of shares to employee benefit plans and other stock plans	362	(359)
Cash dividends and payment for fractional shares	(9,207)	(6,758)
Net cash provided by financing activities	70,521	68,646
Net increase in cash and cash equivalents	26,638	135,478
Cash and cash equivalents at beginning of period	158,926	163,668

Cash and cash equivalents at end of period

\$185,564 \$299,146

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	Three Months	
Supplemental disclosure of cash flow information	Ended March 31,	
Cash paid during the period for:	2014	2013
Interest	\$6,829	\$8,000
Income taxes paid	2,745	344
Noncash investing activities:		
Loans transferred to other real estate owned	\$460	\$959
Acquisitions:		
Fair value of assets acquired	\$-	\$1,503,448
Fair value of liabilities assumed	-	1,283,676

See accompanying notes to unaudited interim consolidated financial statements.

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NBT BANCORP INC. and Subsidiaries

NOTES TO UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS

March 31, 2014

Note 1. Description of Business

NBT Bancorp Inc. (the “Registrant” or the “Company”) is a registered financial holding company incorporated in the state of Delaware in 1986, with its principal headquarters located in Norwich, New York. The principal assets of the Registrant consist of all of the outstanding shares of common stock of its subsidiaries, including: NBT Bank, National Association (the “Bank”), NBT Financial Services, Inc. (“NBT Financial”), NBT Holdings, Inc. (“NBT Holdings”), Hathaway Agency, Inc., and CNBF Capital Trust I, NBT Statutory Trust I and NBT Statutory Trust II (collectively, the “Trusts”). The Company’s principal sources of revenue are the management fees and dividends it receives from the Bank, NBT Financial and NBT Holdings.

The Company’s business, primarily conducted through the Bank but also through its other subsidiaries, consists of providing commercial banking and financial services to customers in its market area, which includes central and upstate New York, northeastern Pennsylvania, southern New Hampshire, western Massachusetts and the greater Burlington, Vermont area. The Company has been, and intends to continue to be, a community-oriented financial institution offering a variety of financial services. The Company’s business philosophy is to operate as a community bank with local decision-making, principally in non-metropolitan markets, providing a broad array of banking and financial services to retail, commercial, and municipal customers.

Note 2. Basis of Presentation

The accompanying unaudited interim consolidated financial statements include the accounts of the Registrant and its wholly owned subsidiaries, the Bank, NBT Financial and NBT Holdings. Collectively, the Registrant and its subsidiaries are referred to herein as “the Company.” The interim data includes all adjustments, consisting only of normal recurring adjustments, necessary for a fair statement of the results for the interim periods in accordance with generally accepted accounting principles (“GAAP”). These consolidated financial statements should be read in conjunction with the audited consolidated financial statements and notes thereto included in our 2013 Annual Report on Form 10-K. The results of operations for the interim periods are not necessarily indicative of the results that may be expected for the full year or any other interim period. All intercompany transactions have been eliminated in consolidation. Amounts in the prior period financial statements are reclassified whenever necessary to conform to current period presentation. The Company has evaluated subsequent events for potential recognition and/or disclosure and there were none identified.

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Note 3. Securities

The amortized cost, estimated fair value, and unrealized gains and losses of securities available for sale are as follows:

(In thousands)	Amortized cost	Unrealized gains	Unrealized losses	Estimated fair value
March 31, 2014				
U.S. Treasury	\$33,204	\$ 269	\$ -	\$33,473
Federal Agency	305,245	430	5,517	300,158
State & municipal	111,583	1,967	855	112,695
Mortgage-backed:				
Government-sponsored enterprises	351,748	6,164	1,404	356,508
U.S. government agency securities	20,781	940	71	21,650
Collateralized mortgage obligations:				
Government-sponsored enterprises	501,563	2,080	13,411	490,232
U.S. government agency securities	46,876	656	117	47,415
Other securities	12,839	2,851	236	15,454
Total securities available for sale	\$1,383,839	\$ 15,357	\$ 21,611	\$1,377,585
December 31, 2013				
U.S. Treasury	\$43,279	\$ 337	\$ -	\$43,616
Federal Agency	285,880	343	7,308	278,915
State & municipal	113,435	1,842	1,612	113,665
Mortgage-backed:				
Government-sponsored enterprises	337,666	5,788	2,131	341,323
U.S. government agency securities	21,924	1,002	85	22,841
Collateralized mortgage obligations:				
Government-sponsored enterprises	521,257	1,777	18,141	504,893
U.S. government agency securities	43,943	794	102	44,635
Other securities	12,367	2,854	228	14,993
Total securities available for sale	\$1,379,751	\$ 14,737	\$ 29,607	\$1,364,881

Other securities primarily represent marketable equity securities.

There were no sales of securities available for sale during the three months ended March 31, 2014. Proceeds from the sales of securities available for sale were \$2.6 million during the three months ended March 31, 2013, and gains on the sales were \$1.1 million. There were no losses on the sales during 2013.

Securities with amortized costs totaling \$1.5 billion at March 31, 2014 and \$1.4 billion at December 31, 2013 were pledged to secure public deposits and for other purposes required or permitted by law. Additionally, at March 31, 2014 and December 31, 2013, securities with an amortized cost of \$224.9 million and \$218.4 million, respectively, were pledged as collateral for securities sold under repurchase agreements.

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The amortized cost, estimated fair value, and unrealized gains and losses of securities held to maturity are as follows:

(In thousands)	Amortized cost	Unrealized gains	Unrealized losses	Estimated fair value
March 31, 2014				
Mortgage-backed	\$ 881	\$ 120	\$ -	\$ 1,001
Collateralized mortgage obligations	60,973	-	3,444	57,529
State & municipal	56,042	361	13	56,390
Total securities held to maturity	\$ 117,896	\$ 481	\$ 3,457	\$ 114,920
December 31, 2013				
Mortgage-backed	\$ 953	\$ 128	\$ -	\$ 1,081
Collateralized mortgage obligations	62,025	-	4,569	57,456
State & municipal	54,305	442	8	54,739
Total securities held to maturity	\$ 117,283	\$ 570	\$ 4,577	\$ 113,276

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The following table sets forth information with regard to investment securities with unrealized losses at March 31, 2014 and December 31, 2013:

Security Type:	Less than 12 months			12 months or longer			Total		
	Fair Value	Unrealized losses	Number of Positions	Fair Value	Unrealized losses	Number of Positions	Fair Value	Unrealized losses	Number of Positions
March 31, 2014									
Investment securities available for sale:									
Federal agency	\$245,397	\$(5,221)	21	\$9,704	\$(296)	1	\$255,101	\$(5,517)	22
State & municipal	48,377	(839)	171	934	(16)	3	49,311	(855)	174
Mortgage-backed Collateralized mortgage obligations	1,110,605	(1,465)	58	960	(10)	4	1,111,565	(1,475)	62
Other securities	295,408	(10,516)	31	60,681	(3,012)	4	356,089	(13,528)	35
Total securities with unrealized losses	5,507	(186)	2	198	(50)	1	5,705	(236)	3
	\$1,705,294	\$(18,227)	283	\$72,477	\$(3,384)	13	\$1,777,771	\$(21,611)	296
March 31, 2014									
Investment securities held to maturity:									
Collateralized mortgage obligations									
State & municipal	\$57,528	\$(3,444)	5	\$-	\$-	-	\$57,528	\$(3,444)	5
Total securities with unrealized losses	2,120	(13)	3	-	-	-	2,120	(13)	3
	\$59,648	\$(3,457)	8	\$-	\$-	-	\$59,648	\$(3,457)	8
December 31, 2013									
Investment securities available for sale:									
Federal agency	\$233,935	\$(6,927)	20	\$9,619	\$(381)	1	\$243,554	\$(7,308)	21
State & municipal	50,328	(1,612)	177	-	-	-	50,328	(1,612)	177
Mortgage-backed Collateralized mortgage obligations	143,080	(2,216)	79	-	-	-	143,080	(2,216)	79
Other securities	379,273	(18,243)	36	-	-	-	379,273	(18,243)	36
Total securities with unrealized losses	5,490	(203)	2	223	(25)	1	5,713	(228)	3
	\$812,106	\$(29,201)	314	\$9,842	\$(406)	2	\$821,948	\$(29,607)	316
December 31, 2013									
Investment securities held to maturity:									
Collateralized mortgage obligations									
State & municipal	\$57,456	\$(4,569)	5	\$-	\$-	-	\$57,456	\$(4,569)	5
Total securities with unrealized losses	1,012	(8)	1	-	-	-	1,012	(8)	1
	\$58,468	\$(4,577)	6	\$-	\$-	-	\$58,468	\$(4,577)	6

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Declines in the fair value of held-to-maturity and available-for-sale securities below their cost that are deemed to be other than temporary are reflected in earnings as realized losses or in other comprehensive income, depending on whether the Company intends to sell the security or more likely than not will be required to sell the security before recovery of its amortized cost basis less any current-period credit loss. If the Company intends to sell the security or more likely than not will be required to sell the security before recovery of its amortized cost basis less any current-period credit loss, the other-than-temporary impairment 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 the Company 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 credit loss, the other-than-temporary impairment shall be separated into (a) the amount representing the credit loss and (b) the amount related to all other factors. The amount of the total other-than-temporary impairment related to the credit loss shall be recognized in earnings. The amount of the total other-than-temporary impairment related to other factors shall be recognized in other comprehensive income, net of applicable taxes.

In estimating other-than-temporary impairment losses, management considers, among other things, (i) the length of time and the extent to which the fair value has been less than cost, (ii) the financial condition and near-term prospects of the issuer, and (iii) the historical and implied volatility of the fair value of the security.

Management has the intent to hold the securities classified as held to maturity until they mature, at which time it is believed the Company will receive full value for the securities. Furthermore, as of March 31, 2014, management also had the intent to hold, and will not be required to sell, the securities classified as available for sale for a period of time sufficient for a recovery of cost, which may be until maturity. The unrealized losses are due to increases in market interest rates over the yields available at the time the underlying securities were purchased. When necessary, the Company has performed a discounted cash flow analysis to determine whether or not it will receive the contractual principal and interest on certain securities. The fair value is expected to recover as the bonds approach their maturity date or repricing date or if market yields for such investments decline. As of March 31, 2014, management believes the impairments detailed in the table above are temporary and no other-than-temporary impairment losses have been realized in the Company's consolidated statements of income.

The following tables set forth information with regard to contractual maturities of debt securities at March 31, 2014:

(In thousands)	Amortized cost	Estimated fair value
Debt securities classified as available for sale		
Within one year	\$27,461	\$27,627
From one to five years	302,113	301,603
From five to ten years	259,225	259,821
After ten years	782,201	773,080
	\$1,371,000	\$1,362,131
Debt securities classified as held to maturity		
Within one year	\$24,714	\$24,765
From one to five years	21,654	21,957
From five to ten years	8,401	8,395
After ten years	63,127	59,803
	\$117,896	\$114,920

Maturities of mortgage-backed, collateralized mortgage obligations and asset-backed securities are stated based on their estimated average lives. Actual maturities may differ from estimated average lives or contractual maturities because, in certain cases, borrowers have the right to call or prepay obligations with or without call or prepayment

penalties.

Except for U.S. Government securities, there were no holdings, when taken in the aggregate, of any single issuer that exceeded 10% of consolidated stockholders' equity at March 31, 2014.

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Note 4. Allowance for Loan Losses and Credit Quality of Loans

Allowance for Loan Losses

The allowance for loan losses is maintained at a level estimated by management to provide adequately for risk of probable losses inherent in the current loan portfolio. The adequacy of the allowance for loan losses is continuously monitored. It is assessed for adequacy using a methodology designed to ensure the level of the allowance reasonably reflects the loan portfolio’s risk profile. It is evaluated to ensure that it is sufficient to absorb all reasonably estimable credit losses inherent in the current loan portfolio.

To develop and document a systematic methodology for determining the allowance for loan losses, the Company has divided the loan portfolio into three segments, each with different risk characteristics and methodologies for assessing risk. Those segments are further segregated between our loans accounted for under the amortized cost method (referred to as “originated” loans) and loans acquired in a business combination (referred to as “acquired” loans). Each portfolio segment is broken down into class segments where appropriate. Class segments contain unique measurement attributes, risk characteristics and methods for monitoring and assessing risk that are necessary to develop the allowance for loan losses. Unique characteristics such as borrower type, loan type, collateral type, and risk characteristics define each class segment. The following table illustrates the portfolio and class segments for the Company’s loan portfolio:

Portfolio	Class
Commercial Loans	Commercial
	Commercial Real Estate
	Agricultural
	Agricultural Real Estate
	Business Banking
Consumer Loans	Indirect
	Home Equity
	Direct

Residential Real Estate Mortgages

Commercial Loans

The Company offers a variety of commercial loan products including commercial (non-real estate), commercial real estate, agricultural, agricultural real estate, and business banking loans. The Company’s underwriting analysis for commercial loans typically includes credit verification, independent appraisals, a review of the borrower’s financial condition, and a detailed analysis of the borrower’s underlying cash flows.

Commercial – The Company offers a variety of loan options to meet the specific needs of our commercial customers including term loans, time notes and lines of credit. Such loans are made available to businesses for working capital needs such as inventory and receivables, business expansion and equipment purchases. Generally, a collateral lien is placed on equipment or other assets owned by the borrower. These loans carry a higher risk than commercial real estate loans due to the nature of the underlying collateral, which can be business assets such as equipment and accounts receivable. To reduce the risk, management also attempts to secure real estate as collateral and obtain personal guarantees of the borrowers.

Commercial Real Estate – The Company offers commercial real estate loans to finance real estate purchases, refinancings, expansions and improvements to commercial properties. Commercial real estate loans are made to

finance the purchases of real estate, generally with completed structures. These commercial real estate loans are secured by first liens on the real estate, which may include apartments, commercial structures, housing businesses, healthcare facilities, and other non owner-occupied facilities. These loans are typically less risky than commercial loans, since they are secured by real estate and buildings, and are generally originated in amounts of no more than 80% of the appraised value of the property.

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Agricultural – The Company offers a variety of agricultural loans to meet the needs of our agricultural customers including term loans, time notes, and lines of credit. These loans are made to purchase livestock, purchase and modernize equipment, and finance seasonal crop expenses. Generally, a collateral lien is placed on the livestock, equipment, produce inventories, and/or receivables owned by the borrower. These loans may carry a higher risk than commercial and agricultural real estate loans due to the industry price volatility, and in some cases, the perishable nature of the underlying collateral. To reduce these risks, management may attempt to secure these loans with additional real estate collateral, obtain personal guarantees of the borrowers, or obtain government loan guarantees to provide further support.

Agricultural Real Estate – The Company offers real estate loans to our agricultural customers to finance farm related real estate purchases, refinancings, expansions, and improvements to agricultural properties such as barns, production facilities, and land. The agricultural real estate loans are secured by first liens on the farm real estate. Because they are secured by land and buildings, these loans may be less risky than agricultural loans. These loans are typically originated in amounts of no more than 75% of the appraised value of the property. Government loan guarantees may be obtained to provide further support.

Business Banking - The Company offers a variety of loan options to meet the specific needs of our business banking customers including term loans, business banking mortgages and lines of credit. Such loans are generally less than \$0.5 million and are made available to businesses for working capital such as inventory and receivables, business expansion, equipment purchases, and agricultural needs. Generally, a collateral lien is placed on equipment or other assets owned by the borrower such as inventory and/or receivables. These loans carry a higher risk than commercial loans due to the smaller size of the borrower and lower levels of capital. To reduce the risk, the Company obtains personal guarantees of the owners for a majority of the loans.

Consumer Loans

The Company offers a variety of consumer loan products including indirect, home equity, and direct loans.

Indirect – The Company maintains relationships with many dealers primarily in the communities that we serve. Through these relationships, the company primarily finances the purchases of automobiles and recreational vehicles (such as campers, boats, etc.) indirectly through dealer relationships. Approximately 75% of the indirect relationships represent automobile financing. Most of these loans carry a fixed rate of interest with principal repayment terms typically ranging from three to six years, based upon the nature of the collateral and the size of the loan. The majority of indirect consumer loans are underwritten on a secured basis using the underlying collateral being financed.

Home Equity – The Company offers fixed home equity loans as well as home equity lines of credit to consumers to finance home improvements, debt consolidation, education and other uses. Consumers are able to borrow up to 85% of the equity in their homes. The Company originates home equity lines of credit and second mortgage loans (loans secured by a second junior lien position on one-to-four-family residential real estate). These loans carry a higher risk than first mortgage residential loans as they are in a second position with respect to collateral. Risk is reduced through underwriting criteria, which include credit verification, appraisals, a review of the borrower's financial condition, and personal cash flows. A security interest, with title insurance when necessary, is taken in the underlying real estate.

Direct – The Company offers a variety of consumer installment loans to finance vehicle purchases, mobile home purchases and personal expenditures. Most of these loans carry a fixed rate of interest with principal repayment terms typically ranging from one to ten years, based upon the nature of the collateral and the size of the loan. The majority of consumer loans are underwritten on a secured basis using the underlying collateral being financed or a customer's deposit account. In addition to installment loans, the Company also offers personal lines of credit and overdraft protection. A minimal amount of loans are unsecured, which carry a higher risk of loss.

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Residential Real Estate Mortgages

Residential real estate loans consist primarily of loans secured by first or second deeds of trust on primary residences. We originate adjustable-rate and fixed-rate, one-to-four-family residential real estate loans for the construction, purchase or refinancing of a mortgage. These loans are collateralized by owner-occupied properties located in the Company's market area. Loans on one-to-four-family residential real estate are generally originated in amounts of no more than 85% of the purchase price or appraised value (whichever is lower), or have private mortgage insurance. The Company's underwriting analysis for residential mortgage loans typically includes credit verification, independent appraisals, and a review of the borrower's financial condition. Mortgage title insurance and hazard insurance are normally required. Construction loans have a unique risk, because they are secured by an incomplete dwelling. This risk is reduced through periodic site inspections, including one at each loan draw period.

For purposes of evaluating the adequacy of the allowance, the Company considers a number of significant factors that affect the collectability of the portfolio. For individually analyzed loans, these include estimates of loss exposure, which reflect the facts and circumstances that affect the likelihood of repayment of such loans as of the evaluation date. For homogeneous pools of loans, estimates of the Company's exposure to credit loss reflect a current assessment of a number of factors, which could affect collectability. These factors include: past loss experience; size, trend, composition, and nature of loans; changes in lending policies and procedures, including underwriting standards and collection, charge-offs and recoveries; trends experienced in nonperforming and delinquent loans; current economic conditions in the Company's market; portfolio concentrations that may affect loss experienced across one or more components of the portfolio; the effect of external factors such as competition, legal and regulatory requirements; and the experience, ability, and depth of lending management and staff. In addition, various regulatory agencies, as an integral component of their examination process, periodically review the Company's allowance for loan losses. Such agencies may require the Company to make loan grade changes as well as recognize additions to the allowance based on their examinations.

After a thorough consideration of the factors discussed above, any required additions or reductions to the allowance for loan losses are made periodically by charges or credits to the provision for loan losses. These charges or credits are necessary to maintain the allowance at a level which management believes is reasonably reflective of overall inherent risk of probable loss in the portfolio. While management uses available information to recognize losses on loans, additions and reductions of the allowance may fluctuate from one reporting period to another. These fluctuations are reflective of changes in risk associated with portfolio content and/or changes in management's assessment of any or all of the determining factors discussed above.

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The following tables illustrate the changes in the allowance for loan losses by our portfolio segments for the three months ended March 31, 2014 and 2013:

Three months ended March 31	Commercial Loans	Consumer Loans	Residential		Total
			Real Estate Mortgages	Unallocated	
Balance as of December 31, 2013	\$ 35,090	\$ 27,694	\$ 6,520	\$ 130	\$69,434
Charge-offs	(479)	(4,032)	(319)	-	(4,830)
Recoveries	399	741	94	-	1,234
Provision	(573)	4,033	(70)	206	3,596
Ending Balance as of March 31, 2014	\$ 34,437	\$ 28,436	\$ 6,225	\$ 336	\$69,434
Balance as of December 31, 2012	\$ 35,624	\$ 27,162	\$ 6,252	\$ 296	\$69,334
Charge-offs	(3,322)	(3,723)	(671)	-	(7,716)
Recoveries	467	977	14	-	1,458
Provision	2,589	1,869	1,113	87	5,658
Ending Balance as of March 31, 2013	\$ 35,358	\$ 26,285	\$ 6,708	\$ 383	\$68,734

For acquired loans, to the extent that we experience deterioration in borrower credit quality resulting in a decrease in our expected cash flows subsequent to acquisition of the loans, an allowance for loan losses would be established based on our estimate of future credit losses over the remaining life of the loans. As of March 31, 2014 and 2013, there was no allowance for loan losses for the acquired loan portfolio. Net charge-offs related to acquired loans totaled approximately \$0.2 million during the three months ended March 31, 2014 and 2013, and are included in the table above.

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The following tables illustrate the allowance for loan losses and the recorded investment by portfolio segments as of March 31, 2014 and December 31, 2013:

Allowance for Loan Losses and Recorded Investment in Loans
(in thousands)

	Commercial Loans	Consumer Loans	Residential Real Estate Mortgages	Unallocated	Total
As of March 31, 2014					
Allowance for loan losses	\$ 34,437	\$ 28,436	\$ 6,225	\$ 336	\$ 69,434
Allowance for loans individually evaluated for impairment	925	-	-		925
Allowance for loans collectively evaluated for impairment	\$ 33,512	\$ 28,436	\$ 6,225	\$ 336	\$ 68,509
Ending balance of loans	\$ 2,436,202	\$ 1,989,030	\$ 1,056,793		\$ 5,482,025
Ending balance of originated loans individually evaluated for impairment	15,025	4,248	2,722		21,995
Ending balance of acquired loans individually evaluated for impairment	9,873	-	-		9,873
Ending balance of acquired loans collectively evaluated for impairment	385,669	199,196	300,360		885,225
Ending balance of originated loans collectively evaluated for impairment	\$ 2,025,635	\$ 1,785,586	\$ 753,711		\$ 4,564,932
As of December 31, 2013					
Allowance for loan losses	\$ 35,090	\$ 27,694	\$ 6,520	\$ 130	\$ 69,434
Allowance for loans individually evaluated for impairment	715	-	-		715
Allowance for loans collectively evaluated for impairment	\$ 34,375	\$ 27,694	\$ 6,520	\$ 130	\$ 68,719