REPUBLIC BANCORP INC /KY/
Form 10-Q
November 07, 2014
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# UNITED STATES

# SECURITIES AND EXCHANGE COMMISSION

**Washington, D.C. 20549**

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# FORM 10-Q

**x Quarterly report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**

**For the quarterly period ended September 30, 2014**

**or**

**o Transition report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**

**Commission File Number: 0-24649**

# REPUBLIC BANCORP, INC.

(Exact name of registrant as specified in its charter)

| | |
|---|---|
| **Kentucky** | **61-0862051** |
| (State of other jurisdiction of incorporation or organization) | (I.R.S. Employer Identification No.) |
| **601 West Market Street, Louisville, Kentucky** | **40202** |
| (Address of principal executive offices) | (Zip Code) |

**(502) 584-3600**

(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 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. x Yes o No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). x Yes o 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 o | Accelerated filer x |
| Non-accelerated filer o | Smaller reporting company o |

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

Indicate the number of shares outstanding of each of the issuer s classes of common stock, as of the latest practicable date:

The number of shares outstanding of the registrant s Class A Common Stock and Class B Common Stock, as of October 31, 2014, was 18,571,000 and 2,245,000, respectively.

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**PART I FINANCIAL INFORMATION**

**Item 1. Financial Statements.**

**CONSOLIDATED BALANCE SHEETS** *(in thousands) (unaudited)*

| | September 30, 2014 | December 31, 2013 |
|---|---|---|
| **ASSETS** | | |
| Cash and cash equivalents | $ 69,682 | $ 170,863 |
| Securities available for sale | 452,974 | 432,893 |
| Securities held to maturity (fair value of $47,541 in 2014 and $50,768 in 2013) | 47,247 | 50,644 |
| Mortgage loans held for sale, at fair value | 5,890 | 3,506 |
| Loans | 2,908,535 | 2,589,792 |
| Allowance for loan losses | (23,617) | (23,026) |
| Loans, net | 2,884,918 | 2,566,766 |
| Federal Home Loan Bank stock, at cost | 28,208 | 28,342 |
| Premises and equipment, net | 32,395 | 32,908 |
| Goodwill | 10,168 | 10,168 |
| Other real estate owned | 11,937 | 17,102 |
| Bank owned life insurance | 51,037 | 25,086 |
| Other assets and accrued interest receivable | 31,163 | 33,626 |
| **TOTAL ASSETS** | $ 3,625,619 | $ 3,371,904 |
| **LIABILITIES** | | |
| Deposits: | | |
| Non interest-bearing | $ 534,662 | $ 488,642 |
| Interest-bearing | 1,525,174 | 1,502,215 |
| Total deposits | 2,059,836 | 1,990,857 |
| Securities sold under agreements to repurchase and other short-term borrowings | 275,874 | 165,555 |
| Federal Home Loan Bank advances | 662,000 | 605,000 |
| Subordinated note | 41,240 | 41,240 |
| Other liabilities and accrued interest payable | 29,301 | 26,459 |
| **Total liabilities** | 3,068,251 | 2,829,111 |
| Commitments and contingent liabilities (Footnote 9) | | |
| **STOCKHOLDERS EQUITY** | | |
| Preferred stock, no par value | | |
| Class A Common Stock and Class B Common Stock, no par value | 4,897 | 4,894 |
| Additional paid in capital | 134,109 | 133,012 |
| Retained earnings | 413,501 | 401,766 |
| Accumulated other comprehensive income | 4,861 | 3,121 |

| | | | | |
|---|---|---|---|---|
| **Total stockholders equity** | | 557,368 | | 542,793 |
| **TOTAL LIABILITIES AND STOCKHOLDERS EQUITY** | $ | 3,625,619 | $ | 3,371,904 |

*See accompanying footnotes to consolidated financial statements.*

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**CONSOLIDATED STATEMENTS OF INCOME** (*UNAUDITED*)

(*in thousands, except per share data*)

| | Three Months Ended September 30, 2014 | Three Months Ended September 30, 2013 | Nine Months Ended September 30, 2014 | Nine Months Ended September 30, 2013 |
|---|---|---|---|---|
| **INTEREST INCOME:** | | | | |
| Loans, including fees | $ 30,916 | $ 31,619 | $ 91,188 | $ 95,268 |
| Taxable investment securities | 1,896 | 1,984 | 5,663 | 6,000 |
| Federal Home Loan Bank stock and other | 332 | 406 | 1,195 | 1,261 |
| Total interest income | 33,144 | 34,009 | 98,046 | 102,529 |
| | | | | |
| **INTEREST EXPENSE:** | | | | |
| Deposits | 930 | 1,043 | 2,845 | 3,073 |
| Securities sold under agreements to repurchase and other short-term borrowings | 28 | 11 | 72 | 53 |
| Federal Home Loan Bank advances | 3,116 | 3,788 | 9,947 | 11,081 |
| Subordinated note | 628 | 628 | 1,886 | 1,886 |
| Total interest expense | 4,702 | 5,470 | 14,750 | 16,093 |
| **NET INTEREST INCOME** | 28,442 | 28,539 | 83,296 | 86,436 |
| Provision for loan losses | 1,510 | 2,200 | 1,500 | 2,480 |
| **NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES** | 26,932 | 26,339 | 81,796 | 83,956 |
| | | | | |
| **NON-INTEREST INCOME:** | | | | |
| Service charges on deposit accounts | 3,568 | 3,676 | 10,426 | 10,384 |
| Net refund transfer fees | (133) | 152 | 16,091 | 13,849 |
| Mortgage banking income | 876 | 1,026 | 2,174 | 6,480 |
| Debit card interchange fee income | 1,551 | 1,519 | 5,224 | 4,986 |
| Bargain purchase gain - First Commercial Bank | | | | 1,324 |
| Net gain on sale of other real estate owned | 67 | 403 | 733 | 1,714 |
| Increase in cash surrender value of bank owned life insurance | 381 | | 951 | |
| Other | 834 | 723 | 2,388 | 1,961 |
| Total non-interest income | 7,144 | 7,499 | 37,987 | 40,698 |
| | | | | |
| **NON-INTEREST EXPENSES:** | | | | |
| Salaries and employee benefits | 12,164 | 12,226 | 40,612 | 43,426 |
| Occupancy and equipment, net | 5,544 | 5,462 | 16,874 | 16,354 |
| Communication and transportation | 905 | 990 | 2,787 | 3,011 |
| Marketing and development | 1,020 | 745 | 2,466 | 2,418 |
| FDIC insurance expense | 424 | 419 | 1,407 | 1,234 |
| Bank franchise tax expense | 731 | 707 | 3,901 | 3,279 |
| Data processing | 868 | 934 | 2,622 | 2,442 |
| Debit card interchange expense | 744 | 655 | 2,505 | 2,216 |
| Supplies | 205 | 228 | 705 | 800 |
| Other real estate owned expense | 950 | 497 | 2,580 | 2,331 |
| Legal expense | 367 | 1,343 | 867 | 3,111 |
| Other | 1,900 | 2,079 | 6,026 | 6,555 |
| Total non-interest expenses | 25,822 | 26,285 | 83,352 | 87,177 |
| | | | | |
| **INCOME BEFORE INCOME TAX EXPENSE** | 8,254 | 7,553 | 36,431 | 37,477 |
| **INCOME TAX EXPENSE** | 3,008 | 2,950 | 12,879 | 13,399 |
| **NET INCOME** | $ 5,246 | $ 4,603 | $ 23,552 | $ 24,078 |

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| **BASIC EARNINGS PER COMMON SHARE:** | | | | | | | | |
| Class A Common Stock | $ | 0.25 | $ | 0.22 | $ | 1.14 | $ | 1.16 |
| Class B Common Stock | $ | 0.24 | $ | 0.21 | $ | 1.09 | $ | 1.12 |
| | | | | | | | | |
| **DILUTED EARNINGS PER COMMON SHARE:** | | | | | | | | |
| Class A Common Stock | $ | 0.25 | $ | 0.22 | $ | 1.13 | $ | 1.16 |
| Class B Common Stock | $ | 0.24 | $ | 0.21 | $ | 1.08 | $ | 1.11 |
| | | | | | | | | |
| **DIVIDENDS DECLARED PER COMMON SHARE:** | | | | | | | | |
| Class A Common Stock | $ | 0.187 | $ | 0.176 | $ | 0.550 | $ | 0.517 |
| Class B Common Stock | $ | 0.170 | $ | 0.160 | $ | 0.500 | $ | 0.470 |

*See accompanying footnotes to consolidated financial statements.*

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**CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME** (*UNAUDITED)*

(*in thousands*)

| | Three Months Ended September 30, 2014 | Three Months Ended September 30, 2013 | Nine Months Ended September 30, 2014 | Nine Months Ended September 30, 2013 |
|---|---|---|---|---|
| Net income | $ 5,246 | $ 4,603 | $ 23,552 | $ 24,078 |
| **OTHER COMPREHENSIVE INCOME (LOSS):** | | | | |
| Change in fair value of derivatives used for cash flow hedges | 28 | | (676) | |
| Reclassification amount for derivative losses realized in income | 104 | | 303 | |
| Unrealized gain (loss) on securities available for sale | (10) | (198) | 2,618 | (3,163) |
| Change in unrealized gain on securities available for sale for which a portion of an other-than-temporary impairment has been recognized in earnings | 65 | (4) | 434 | 418 |
| Net unrealized gains (losses) | 187 | (202) | 2,679 | (2,745) |
| Tax effect | (66) | 71 | (939) | 962 |
| Total other comprehensive income (loss), net of tax | 121 | (131) | 1,740 | (1,783) |
| **COMPREHENSIVE INCOME** | $ 5,367 | $ 4,472 | $ 25,292 | $ 22,295 |

*See accompanying footnotes to consolidated financial statements.*

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**CONSOLIDATED STATEMENT OF STOCKHOLDERS EQUITY** *(UNAUDITED)*

**NINE MONTHS ENDED SEPTEMBER 30, 2014**

| (in thousands, except per share data) | Class A Shares Outstanding | Common Stock Class B Shares Outstanding | Amount | Additional Paid In Capital | Retained Earnings | Accumulated Other Comprehensive Income | Total Stockholders Equity |
|---|---|---|---|---|---|---|---|
| Balance, January 1, 2014 | 18,541 | 2,260 | $ 4,894 | $ 133,012 | $ 401,766 | $ 3,121 | $ 542,793 |
| Net income | | | | | 23,552 | | 23,552 |
| Net change in accumulated other comprehensive income | | | | | | 1,740 | 1,740 |
| Dividend declared Common Stock: | | | | | | | |
| Class A shares ($0.550 per share) | | | | | (10,201) | | (10,201) |
| Class B shares ($0.500 per share) | | | | | (1,126) | | (1,126) |
| Stock options exercised, net of shares redeemed | 26 | | 6 | 681 | (244) | | 443 |
| Repurchase of Class A Common Stock | (15) | | (3) | (95) | (249) | | (347) |
| Conversion of Class B Common Stock to Class A Common Stock | 15 | (15) | | | | | |
| Net change in notes receivable on Class A Common Stock | | | | | | | |
| Deferred director compensation expense - Class A Common Stock | 2 | | | 145 | | | 145 |
| Stock based compensation - restricted stock | (2) | | | 328 | 3 | | 331 |
| Stock based compensation expense - options | | | | 38 | | | 38 |
| Balance, September 30, 2014 | 18,567 | 2,245 | $ 4,897 | $ 134,109 | $ 413,501 | $ 4,861 | $ 557,368 |

*See accompanying footnotes to consolidated financial statements.*

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**CONSOLIDATED STATEMENTS OF CASH FLOWS** (*UNAUDITED*)

**NINE MONTHS ENDED SEPTEMBER 30, 2014 AND 2013** (*in thousands*)

| | 2014 | 2013 |
|---|---|---|
| **OPERATING ACTIVITIES:** | | |
| Net income | $ 23,552 | $ 24,078 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Depreciation of premises and equipment | 4,753 | 3,846 |
| Amortization (accretion) on investment securitites, net | 446 | 328 |
| Amortization (accretion) on loans, net | (5,618) | (7,880) |
| Amortization of mortgage servicing rights | 996 | 1,811 |
| Amortization of core deposit intangible asset | | 221 |
| Provision for loan losses | 1,500 | 2,480 |
| Net gain on sale of mortgage loans held for sale | (1,894) | (6,340) |
| Origination of mortgage loans held for sale | (54,046) | (263,411) |
| Proceeds from sale of mortgage loans held for sale | 53,556 | 270,562 |
| Net realized recovery of mortgage servicing rights | | (345) |
| Net gain on sale of other real estate owned | (733) | (1,714) |
| Writedowns of other real estate owned | 2,042 | 1,074 |
| Deferred director compensation expense - Company Stock | 145 | 152 |
| Stock based compensation expense | 366 | 401 |
| Bargain purchase gain on acquisition | | (1,324) |
| Increase in cash surrender value of bank owned life insurance | (951) | |
| Net change in other assets and liabilities: | | |
| Accrued interest receivable | (283) | 1,115 |
| Accrued interest payable | (310) | 32 |
| Other assets | 1,750 | 4,137 |
| Other liabilities | 1,500 | (7,447) |
| Net cash provided by operating activities | 26,771 | 21,776 |
| | | |
| **INVESTING ACTIVITIES:** | | |
| Purchases of securities available for sale | (119,427) | (175,275) |
| Purchases of securities to be held to maturity | | (15,000) |
| Proceeds from calls, maturities and paydowns of securities available for sale | 102,111 | 129,041 |
| Proceeds from calls, maturities and paydowns of securities to be held to maturity | 3,342 | 8,900 |
| Proceeds from sales of Federal Home Loan Bank stock | 134 | 35 |
| Proceeds from sales of other real estate owned | 8,991 | 19,642 |
| Net change in outstanding warehouse lines of credit | (123,008) | 93,766 |
| Purchase of loans, including premiums paid | (144,669) | |
| Net change in other loans | (51,492) | 1,718 |
| Purchase of bank owned life insurance | (25,000) | |
| Net purchases of premises and equipment | (4,240) | (3,275) |
| Net cash provided by (used in) investing activities | (353,258) | 59,552 |
| | | |
| **FINANCING ACTIVITIES:** | | |
| Net change in deposits | 68,979 | 36,857 |
| Net change in securities sold under agreements to repurchase and other short-term borrowings | 110,319 | (144,511) |
| Payments of Federal Home Loan Bank advances | (108,000) | (25,580) |
| Proceeds from Federal Home Loan Bank advances | 165,000 | 70,000 |
| Repurchase of Common Stock | (347) | (4,095) |
| Net proceeds from Common Stock options exercised | 443 | 295 |
| Cash dividends paid | (11,088) | (10,400) |

| | | | | |
|---|---|---|---|---|
| Net cash provided by (used in) financing activities | | 225,306 | | (77,434) |
| | | | | |
| **NET CHANGE IN CASH AND CASH EQUIVALENTS** | | (101,181) | | 3,894 |
| **CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD** | | 170,863 | | 137,691 |
| **CASH AND CASH EQUIVALENTS AT END OF PERIOD** | $ | 69,682 | $ | 141,585 |

*(continued)*

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**CONSOLIDATED STATEMENTS OF CASH FLOWS** (*UNAUDITED*)

**NINE MONTHS ENDED SEPTEMBER 30, 2014 AND 2013** (*in thousands*)

| | 2014 | 2013 |
|---|---|---|
| **SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:** | | |
| Cash paid during the period for: | | |
| Interest | $ 15,060 | $ 16,061 |
| Income taxes | 13,703 | 26,674 |
| | | |
| **SUPPLEMENTAL NONCASH DISCLOSURES:** | | |
| Transfers from loans to real estate acquired in settlement of loans | $ 6,466 | $ 8,690 |
| Loans provided for sales of other real estate owned | 1,331 | 644 |
| Change in fair value of derivatives used for cash flow hedges | (676) | |
| Change in fair value of available for sale securities | 3,052 | (2,745) |

*See accompanying footnotes to consolidated financial statements.*

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**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS SEPTEMBER 30, 2014 AND 2013 (UNAUDITED) AND DECEMBER 31, 2013**

## 1. BASIS OF PRESENTATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

**Basis of Presentation** The consolidated financial statements include the accounts of Republic Bancorp, Inc. (the Parent Company ) and its wholly-owned subsidiaries, Republic Bank & Trust Company ( RB&T or the Bank ) and Republic Insurance Services, Inc. (the Captive ). RB&T is a Kentucky-based, state chartered non-member financial institution. The Captive, which was formed during the third quarter of 2014, is a wholly-owned insurance subsidiary of the Company that provides property and casualty insurance coverage to the Company and the Bank. The Captive provides reinsurance to five other third party insurance captives for which insurance may not be currently available or economically feasible in today s insurance marketplace. Republic Bancorp Capital Trust ( RBCT ) is a Delaware statutory business trust that is a wholly-owned unconsolidated finance subsidiary of Republic Bancorp, Inc. All companies are collectively referred to as Republic or the Company. All significant intercompany balances and transactions are eliminated in consolidation.

During the second quarter of 2014, Republic Bank, the Company s wholly-owned, federally chartered savings institution, was legally merged into RB&T. The merged institution operates under the name Republic Bank & Trust Company. The merger did not materially impact the Company s consolidated financial statements.

The accompanying unaudited consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles ( GAAP ) for interim financial information and with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. Accordingly, the financial statements do not include all of the information and footnotes required by GAAP for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for fair presentation have been included. Operating results for the three and nine months ended September 30, 2014 are not necessarily indicative of the results that may be expected for the year ending December 31, 2014. For further information, refer to the consolidated financial statements and footnotes thereto included in Republic s Form 10-K for the year ended December 31, 2013.

As of September 30, 2014, the Company was divided into three distinct business operating segments: Traditional Banking, Mortgage Banking and Republic Processing Group ( RPG ). Tax Refund Solutions ( TRS ), Republic Payment Solutions ( RPS ) and Republic Credit Solutions ( RCS ) operate as divisions of the RPG segment. The TRS division comprises the substantial majority of revenues and expenses of RPG. The RPS and RCS divisions are considered immaterial for separate and independent segment reporting.

**Traditional Banking and Mortgage Banking (collectively Core Banking )**

As of September 30, 2014, in addition to an Internet delivery channel, Republic had 42 full-service banking centers with locations as follows:

- Kentucky 33

- Metropolitan Louisville 20
- Central Kentucky 8
- Elizabethtown 1
- Frankfort 1
- Georgetown 1
- Lexington 4
- Shelbyville 1
- Western Kentucky 2
- Owensboro 2
- Northern Kentucky 3
- Covington 1
- Florence 1
- Independence 1
- Southern Indiana 3
- Floyds Knobs 1
- Jeffersonville 1
- New Albany 1
- Metropolitan Tampa, Florida 3
- Metropolitan Cincinnati, Ohio 1
- Metropolitan Nashville, Tennessee 2

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Republic s headquarters are located in Louisville, which is the largest city in Kentucky based on population.

Core Banking results of operations are primarily dependent upon net interest income, which represents the difference between the interest income and fees on interest-earning assets and the interest expense on interest-bearing liabilities. Principal interest-earning Core Banking assets represent investment securities and commercial and consumer loans primarily secured by real estate and/or personal property. Interest-bearing liabilities primarily consist of interest-bearing deposit accounts, securities sold under agreements to repurchase, as well as short-term and long-term borrowing sources. FHLB advances have traditionally been a significant borrowing source for the Bank.

Other sources of Core Banking income include service charges on deposit accounts, debit and credit card interchange fee income, title insurance commissions, fees charged to customers for trust services and revenue generated from Mortgage Banking activities. Mortgage Banking activities represent both the origination and sale of loans in the secondary market and the servicing of loans for others, primarily the Federal Home Loan Mortgage Corporation ( Freddie Mac or FHLMC ).

Core Banking operating expenses consist primarily of salaries and employee benefits, occupancy and equipment expenses, communication and transportation costs, data processing, debit card interchange expenses, marketing and development expenses, FDIC insurance expense, and various general and administrative costs. Core Banking results of operations are significantly impacted by general economic and competitive conditions, particularly changes in market interest rates, government laws and policies and actions of regulatory agencies.

The Core Bank provides short-term, revolving credit facilities to mortgage bankers across the Nation through mortgage warehouse lines of credit. These credit facilities are secured by single family, first lien residential real estate loans. Outstanding balances on these credit facilities may be subject to significant fluctuations consistent with the overall market demand for mortgage loans.

The Core Bank began acquiring single family, first lien mortgage loans for investment through its Correspondent Lending division in May 2014. Correspondent Lending generally involves the Bank acquiring, primarily from its Mortgage Warehouse clients, closed loans that meet the Bank s specifications. Substantially all loans purchased through the Correspondent Lending channel are purchased at a premium. Premiums on loans held for investment acquired though the Correspondent Lending division are amortized into interest income on the level-yield method over the expected life of the loan. Loans acquired through the Correspondent Lending division generally reflect borrowers outside of the Bank s historical market footprint. As of September 30, 2014, a substantial majority of loans originated through the Company s Correspondent Lending division were secured by single family residences located in the state of California.

**Republic Processing Group**

All divisions of the RPG segment operate through the Bank. Nationally, RPG facilitates the receipt and payment of federal and state tax refunds under the TRS division, primarily through refund transfers ( RT s). RTs are products whereby a tax refund is issued to the taxpayer after the Bank has received the refund from the federal or state government. There is no credit risk or borrowing cost associated with these products, because they are only delivered to the taxpayer upon receipt of the tax refund directly from the governmental paying authority. Fees earned on RTs, net of rebates, are the primary source of revenue for the TRS division and the RPG segment, and are reported as non-interest income under the line item Net refund transfer fees.

The TRS division historically originated and obtained a significant source of revenue from Refund Anticipation Loans ( RAL s), but terminated this product effective April 30, 2012. RALs were short-term consumer loans offered to taxpayers that were secured by the customer s anticipated tax refund, which represented the sole source of repayment. While RALs were terminated in 2012, TRS has received and expects to continue receiving recoveries from previously charged-off RALs.

The RPS division is an issuing bank offering general purpose reloadable prepaid debit cards through third party program managers.

The RCS division is piloting short-term consumer credit products.

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**Recently Issued Accounting Standards Updates** ( **ASU** )

**ASU 2014-14 Receivables Troubled Debt Restructurings by Creditors** ***(Subtopic 310-40): Classification of Certain Government-Guaranteed Mortgage Loans upon Foreclosure.***

The amendments in this ASU require that a mortgage loan be derecognized and that a separate other receivable be recognized upon foreclosure if: a) the loan has a government guarantee that is not separable from the loan before foreclosure; b) at the time of foreclosure, the creditor has the intent to convey the real estate property to the guarantor and make a claim on the guarantee, and the creditor has the ability to recover under that claim; and c) at the time of foreclosure, any amount of the claim that is determined on the basis of the fair value of the real estate is fixed. The separate other receivable recognized upon foreclosure should be measured based on the amount of the loan balance (principal and interest) expected to be received from the guarantor. The amendments in this ASU are effective for the Company beginning January 1, 2015 and are not expected to have a material impact on the Company s financial statements.

**Reclassifications and recasts** Certain amounts presented in prior periods have been reclassified to conform to the current period presentation. These reclassifications had no impact on prior years net income.

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**2. INVESTMENT SECURITIES**

**Securities Available for Sale**

The gross amortized cost and fair value of securities available for sale and the related gross unrealized gains and losses recognized in accumulated other comprehensive income (loss) were as follows:

| September 30, 2014 (in thousands) | Gross Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses | Fair Value |
|---|---|---|---|---|
| U.S. Treasury securities and U.S. Government agencies | $ 149,709 | $ 257 | $ (75) | $ 149,891 |
| Private label mortgage backed security | 4,158 | 1,179 | | 5,337 |
| Mortgage backed securities - residential | 125,058 | 5,363 | (156) | 130,265 |
| Collateralized mortgage obligations | 150,355 | 1,167 | (844) | 150,678 |
| Freddie Mac preferred stock | | 669 | | 669 |
| Mutual fund | 1,000 | 10 | | 1,010 |
| Corporate bonds | 15,012 | 112 | | 15,124 |
| Total securities available for sale | $ 445,292 | $ 8,757 | $ (1,075) | $ 452,974 |

| December 31, 2013 (in thousands) | Gross Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses | Fair Value |
|---|---|---|---|---|
| U.S. Treasury securities and U.S. Government agencies | $ 97,157 | $ 409 | $ (101) | $ 97,465 |
| Private label mortgage backed security | 4,740 | 745 | | 5,485 |
| Mortgage backed securities - residential | 146,087 | 4,288 | (288) | 150,087 |
| Collateralized mortgage obligations | 164,264 | 1,228 | (1,546) | 163,946 |
| Mutual fund | 1,000 | | (5) | 995 |
| Corporate bonds | 15,015 | 50 | (150) | 14,915 |
| Total securities available for sale | $ 428,263 | $ 6,720 | $ (2,090) | $ 432,893 |

**Securities Held to Maturity**

The carrying value, gross unrecognized gains and losses, and fair value of securities held to maturity were as follows:

| September 30, 2014 (in thousands) | Carrying Value | Gross Unrecognized Gains | Gross Unrecognized Losses | Fair Value |
|---|---|---|---|---|
| U.S. Treasury securities and U.S. Government agencies | $ 2,257 | $ 7 | $ (8) | $ 2,256 |
| Mortgage backed securities - residential | 409 | 49 | | 458 |
| Collateralized mortgage obligations | 39,581 | 379 | (24) | 39,936 |
| Corporate bonds | 5,000 | | (109) | 4,891 |

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| Total securities held to maturity | $ | 47,247 | $ | 435 | $ | (141) | $ | 47,541 |

| December 31, 2013 (in thousands) | | Carrying Value | | Gross Unrecognized Gains | | Gross Unrecognized Losses | | Fair Value |
|---|---|---|---|---|---|---|---|---|
| U.S. Treasury securities and U.S. Government agencies | $ | 2,311 | $ | 7 | $ | (13) | $ | 2,305 |
| Mortgage backed securities - residential | | 420 | | 43 | | | | 463 |
| Collateralized mortgage obligations | | 42,913 | | 387 | | (184) | | 43,116 |
| Corporate bonds | | 5,000 | | | | (116) | | 4,884 |
| Total securities held to maturity | $ | 50,644 | $ | 437 | $ | (313) | $ | 50,768 |

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At September 30, 2014 and December 31, 2013, there were no holdings of securities of any one issuer, other than the U.S. Government and its agencies, in an amount greater than 10% of stockholders equity.

**Sales of Securities Available for Sale**

During the three and nine months ended September 30, 2014 and 2013, there were no sales or calls of securities available for sale or applicable income tax provisions for such transactions.

**Investment Securities by Contractual Maturity**

The amortized cost and fair value of the investment securities portfolio by contractual maturity at September 30, 2014 follows. Expected maturities may differ from contractual maturities if securities issuers have the right to call or prepay obligations with or without call or prepayment penalties. Securities not due at a single maturity date are detailed separately.

| | Securities available for sale | | Securities held to maturity | |
|---|---|---|---|---|
| **September 30, 2014 (in thousands)** | **Amortized Cost** | **Fair Value** | **Carrying Value** | **Fair Value** |
| Due in one year or less | $ 23,543 | $ 23,676 | $ 496 | $ 496 |
| Due from one year to five years | 131,178 | 131,283 | 1,761 | 1,760 |
| Due from five years to ten years | 10,000 | 10,056 | 5,000 | 4,891 |
| Due beyond ten years | | | | |
| Private label mortgage backed security | 4,158 | 5,337 | | |
| Mortgage backed securities - residential | 125,058 | 130,265 | 409 | 458 |
| Collateralized mortgage obligations | 150,355 | 150,678 | 39,581 | 39,936 |
| Freddie Mac preferred stock | | 669 | | |
| Mutual fund | 1,000 | 1,010 | | |
| Total securities | $ 445,292 | $ 452,974 | $ 47,247 | $ 47,541 |

**Freddie Mac Preferred Stock**

During 2008, the U.S. Treasury, the Federal Reserve Board, and the Federal Housing Finance Agency ( FHFA ) announced that the FHFA was placing Freddie Mac under conservatorship and giving management control to the FHFA. The Bank contemporaneously determined that its 40,000 shares of Freddie Mac preferred stock were fully impaired and recorded an Other Than Temporary Impairment ( OTTI ) charge of $2.1 million for the shares. The OTTI charge brought the carrying value of the stock to $0. During the second quarter of 2014, based on active trading volume of Freddie Mac preferred stock, the Company determined it appropriate to record an unrealized gain to other comprehensive income ( OCI ) related to its Freddie Mac preferred stock holdings. Based on the stock s market closing price as of September 30, 2014, the Company s unrealized gain for its Freddie Mac preferred stock totaled $669,000. In October 2014, the unrealized gain in the Company s Freddie Mac preferred stock fell to approximately $300,000 following a legal decision unfavorable to private investors in such stock.

**Corporate Bonds**

During 2013, the Bank purchased $20 million in floating rate corporate bonds with an initial weighted average yield of 1.36%. The bonds, which have a weighted average life of seven years, were rated investment grade by accredited rating agencies as of their respective purchase dates. The total fair value of the Bank s corporate bonds represented 4% of the Bank s investment portfolio as of both September 30, 2014 and December 31, 2013.

**Mortgage Backed Securities**

At September 30, 2014, with the exception of the $5.3 million private label mortgage backed security, all other mortgage backed securities held by the Bank were issued by U.S. government-sponsored entities and agencies, primarily Freddie Mac and the Federal National Mortgage Association ( Fannie Mae or FNMA ), institutions that the government has affirmed its commitment to support. At September 30, 2014 and December 31, 2013, there were gross unrealized/unrecognized losses of $1.0 million and $1.8 million related to available for sale mortgage backed securities. Because the decline in fair value of

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these mortgage backed securities is attributable to changes in interest rates and illiquidity, and not credit quality, and because the Bank does not have the intent to sell these mortgage backed securities, and it is likely that it will not be required to sell the securities before their anticipated recovery, management does not consider these securities to be other-than-temporarily impaired.

**Market Loss Analysis**

Securities with unrealized losses at September 30, 2014 and December 31, 2013, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position, are as follows:

| | Less than 12 months | | 12 months or more | | Total | |
|---|---|---|---|---|---|---|
| **September 30, 2014 (in thousands)** | **Fair Value** | **Unrealized Losses** | **Fair Value** | **Unrealized Losses** | **Fair Value** | **Unrealized Losses** |
| Securities available for sale: | | | | | | |
| U.S. Treasury securities and U.S. Government agencies | $ 57,722 | $ (75) | $ | $ | $ 57,722 | $ (75) |
| Mortgage backed securities - residential | 7,795 | (156) | | | 7,795 | (156) |
| Collateralized mortgage obligations | 54,539 | (660) | 6,837 | (184) | 61,376 | (844) |
| Total securities available for sale | $ 120,056 | $ (891) | $ 6,837 | $ (184) | $ 126,893 | $ (1,075) |

| | Less than 12 months | | 12 months or more | | Total | |
|---|---|---|---|---|---|---|
| | **Fair Value** | **Unrealized Losses** | **Fair Value** | **Unrealized Losses** | **Fair Value** | **Unrealized Losses** |
| Securities held to maturity: | | | | | | |
| U.S. Treasury securities and U.S. Government agencies | $ 519 | $ (8) | $ | $ | $ 519 | $ (8) |
| Collateralized mortgage obligations | 9,205 | (24) | | | 9,205 | (24) |
| Corporate bonds | 4,891 | (109) | | | 4,891 | (109) |
| Total securities held to maturity | $ 14,615 | $ (141) | $ | $ | $ 14,615 | $ (141) |

| | Less than 12 months | | 12 months or more | | Total | |
|---|---|---|---|---|---|---|
| **December 31, 2013 (in thousands)** | **Fair Value** | **Unrealized Losses** | **Fair Value** | **Unrealized Losses** | **Fair Value** | **Unrealized Losses** |
| Securities available for sale: | | | | | | |
| U.S. Treasury securities and U.S. Government agencies | $ 44,041 | $ (101) | $ | $ | $ 44,041 | $ (101) |
| Mortgage backed securities - residential | 19,494 | (288) | | | 19,494 | (288) |
| Collateralized mortgage obligations | 55,927 | (1,546) | | | 55,927 | (1,546) |
| Mutual fund | 995 | (5) | | | 995 | (5) |
| Corporate bonds | 9,850 | (150) | | | 9,850 | (150) |
| Total securities available for sale | $ 130,307 | $ (2,090) | $ | $ | $ 130,307 | $ (2,090) |

| | Less than 12 months | | 12 months or more | | Total | |
|---|---|---|---|---|---|---|
| | **Fair Value** | **Unrealized Losses** | **Fair Value** | **Unrealized Losses** | **Fair Value** | **Unrealized Losses** |
| Securities held to maturity: | | | | | | |

| | | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|
| U.S. Treasury securities and U.S. Government agencies | $ | 521 | $ | (13) | $ | | $ | | $ | 521 | $ | (13) |
| Collateralized mortgage obligations | | 18,686 | | (184) | | | | | | 18,686 | | (184) |
| Corporate bonds | | 4,884 | | (116) | | | | | | 4,884 | | (116) |
| | | | | | | | | | | | | |
| Total securities held to maturity | $ | 24,091 | $ | (313) | $ | | $ | | $ | 24,091 | $ | (313) |

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At September 30, 2014, the Bank s security portfolio consisted of 161 securities, 23 of which were in an unrealized loss position. At December 31, 2013, the Bank s security portfolio consisted of 162 securities, 27 of which were in an unrealized loss position.

**Other-than-temporary Impairment**

Unrealized losses for all investment securities are reviewed to determine whether the losses are other-than-temporary. Investment securities are evaluated for OTTI on at least a quarterly basis and more frequently when economic or market conditions warrant such an evaluation to determine whether a decline in value below amortized cost is other-than-temporary. In conducting this assessment, the Bank evaluates a number of factors including, but not limited to:

- The length of time and the extent to which fair value has been less than the amortized cost basis;
- The Bank s intent to hold until maturity or sell the debt security prior to maturity;
- An analysis of whether it is more likely than not that the Bank will be required to sell the debt security before its anticipated recovery;
- Adverse conditions specifically related to the security, an industry, or a geographic area;
- The historical and implied volatility of the fair value of the security;
- The payment structure of the security and the likelihood of the issuer being able to make payments;
- Failure of the issuer to make scheduled interest or principal payments;
- Any rating change by a rating agency; and
- Recoveries or additional decline in fair value subsequent to the balance sheet date.

The term other-than-temporary is not intended to indicate that the decline is permanent, but indicates that the prospects for a near-term recovery of value are not necessarily favorable, or that there is a general lack of evidence to support a realizable value equal to or greater than the carrying value of the investment. Once a decline in value is determined to be other-than-temporary, the value of the security is reduced and a corresponding charge to earnings is recognized for the anticipated credit losses.

The Bank owns one private label mortgage backed security with a total carrying value of $5.3 million at September 30, 2014. This security, with an average remaining life currently estimated at three years, is mostly backed by Alternative A first lien mortgage loans, but also has an insurance wrap or guarantee as an added layer of protection to the security holder. This asset is illiquid, and as such, the Bank determined it to be a Level 3 security in accordance with Accounting Standards Codification ( ASC ) Topic 820, *Fair Value Measurements and Disclosures.* Based on this determination, the Bank utilized an income valuation model ( present value model ) approach, in determining the fair value of the security. This approach is beneficial for positions that are not traded in active markets or are subject to transfer restrictions, and/or where valuations are adjusted to reflect illiquidity and/or non-transferability. Such adjustments are generally based on available market evidence. In the absence of such evidence, management s best estimate is used. Management s best estimate consists of both internal and external support for this investment.

*See additional discussion regarding the Bank s private label mortgage backed security under Footnote 6 Fair Value in this section of the filing.*

**Pledged Investment Securities**

Investment securities pledged to secure public deposits, securities sold under agreements to repurchase and securities held for other purposes, as required or permitted by law are as follows:

| **(in thousands)** | **September 30, 2014** | **December 31, 2013** |
|---|---|---|
| Carrying amount | $ 328,463 | $ 224,693 |
| Fair value | 328,763 | 224,989 |

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**3. LOANS AND ALLOWANCE FOR LOAN LOSSES**

The Bank s financing receivables consist primarily of loans and a minimal amount of lease financing receivables (together referred to as loans ). Loans that management has the intent and ability to hold for the foreseeable future or until maturity or payoff are reported at the principal balance outstanding, inclusive of purchase premiums or discounts, deferred loan fees and costs and the allowance for loan losses. Interest income is accrued on the unpaid principal balance. Loan origination fees, net of certain direct origination costs, are deferred and recognized in interest income using the level-yield method.

Lease financing receivables, all of which are direct financing leases, are reported at their principal balance outstanding net of any unearned income, deferred fees and costs and applicable allowance for losses. Leasing income is recognized on a basis that achieves a constant periodic rate of return on the outstanding lease financing balances over the lease terms.

The composition of loans follows:

| **(in thousands)** | **September 30, 2014** | **December 31, 2013** |
|---|---|---|
| Residential real estate: | | |
| Owner occupied | $ 1,127,595 | $ 1,097,795 |
| Owner occupied - correspondent* | 139,252 | |
| Non owner occupied | 98,365 | 110,809 |
| Commercial real estate | 771,765 | 773,173 |
| Commercial real estate - purchased whole loans* | 34,714 | 34,186 |
| Construction & land development | 44,462 | 44,351 |
| Commercial & industrial | 149,943 | 127,763 |
| Lease financing receivables | 819 | |
| Warehouse lines of credit | 272,584 | 149,576 |
| Home equity | 241,189 | 226,782 |
| Consumer: | | |
| RPG loans | 3,460 | 1,827 |
| Credit cards | 9,230 | 9,030 |
| Overdrafts | 966 | 944 |
| Purchased whole loans* | 4,664 | |
| Other consumer | 9,527 | 13,556 |
| Total loans** | 2,908,535 | 2,589,792 |
| Allowance for loan losses | (23,617) | (23,026) |
| Total loans, net | $ 2,884,918 | $ 2,566,766 |

** - Identifies loans outside of the Bank s historical market footprint.*

*** - Total loans are presented inclusive of premiums, discounts and net loan origination fees and costs. See table directly below for expanded detail.*

The table below reconciles the contractually receivable and carrying amounts of loans at September 30, 2014 and December 31, 2013:

| (in thousands) | September 30, 2014 | December 31, 2013 |
|---|---|---|
| Contractually receivable | $ 2,922,238 | $ 2,614,632 |
| Unearned income | (95) | |
| Unamortized premiums(1) | 3,032 | 260 |
| Unaccreted discounts(2) | (18,089) | (26,624) |
| Net unamortized deferred origination fees and costs | 1,449 | 1,524 |
| Carrying value of loans | $ 2,908,535 | $ 2,589,792 |

*(1) - Premiums predominately relate to loans acquired through the Bank s Correspondent Lending division.*

*(2) - Discounts predominately relate to loans acquired in the Bank s 2012 FDIC-assisted transactions.*

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**Loan Purchases**

In May 2014, the Bank began acquiring single family, first lien mortgage loans for investment within its loan portfolio through its Correspondent Lending division. Correspondent Lending generally involves the Bank acquiring, primarily from its Mortgage Warehouse clients, closed loans that meet the Bank s specifications. Substantially all loans purchased through the Correspondent Lending channel are purchased at a premium. Premiums on loans held for investment acquired though the Correspondent Lending division are amortized into interest income on a level-yield method over the expected life of the loan. Loans acquired through the Correspondent Lending division generally reflect borrowers outside of the Bank s historical market footprint, with a substantial majority of loans originated through the division as of September 30, 2014, secured by single residences located in the state of California.

In addition to secured mortgage loans acquired through its Correspondent Lending division, the Bank also began acquiring unsecured consumer installment loans for investment from a third-party originator in April 2014. Such consumer loans are purchased at par and are selected by the Bank based on certain underwriting characteristics.

The table below reflects the purchased activity of single family, first lien mortgage loans and unsecured consumer loans, by class, during the three and nine months ended September 30, 2014. No purchases of these type loans were made during 2013.

| **(in thousands)** | **Three Months Ended September 30, 2014** | **Nine Months Ended September 30, 2014** |
|---|---|---|
| Residential real estate: | | |
| Owner occupied - correspondent | $ 128,374 | $ 139,632 |
| Consumer: | | |
| Purchased whole loans | 2,524 | 5,037 |
| Total purchased loans | $ 130,898 | $ 144,669 |

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**Purchased Credit Impaired ( PCI ) Loans**

The contractual amount of PCI loans acquired during the Bank s 2012 FDIC-assisted transactions and accounted for under ASC 310-30, *Loans and Debt Securities Acquired with Deteriorated Credit Quality,* decreased from $58 million as of December 31, 2013 to $36 million as of September 30, 2014. The carrying value of these loans was $41 million as of December 31, 2013 compared to $25 million as of September 30, 2014.

The table below reconciles the contractually required and carrying amounts of PCI loans at September 30, 2014 and December 31, 2013:

| (in thousands) | September 30, 2014 | December 31, 2013 |
|---|---|---|
| Contractually-required principal | $ 35,760 | $ 57,992 |
| Non-accretable amount | (8,610) | (13,582) |
| Accretable amount | (2,418) | (3,457) |
| Carrying value of loans | $ 24,732 | $ 40,953 |

The following table presents a rollforward of the accretable amount on PCI loans for the three and nine months ended September 30, 2014 and 2013:

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| (in thousands) | 2014 | 2013 | 2014 | 2013 |
| Balance, beginning of period | $ (2,487) | $ (1,381) | $ (3,457) | $ (3,231) |
| Transfers between non-accretable and accretable | (609) | (3,725) | (2,949) | (5,421) |
| Net accretion into interest income on loans, including loan fees | 678 | 1,916 | 3,988 | 5,179 |
| Other changes | | | | 283 |
| Balance, end of period | $ (2,418) | $ (3,190) | $ (2,418) | $ (3,190) |

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**Credit Quality Indicators**

Based on the Bank s internal analyses performed as of September 30, 2014 and December 31, 2013, the following tables reflect loans by risk category, as such categories are defined in the Company s Annual Report on Form 10-K for the year ended December 31, 2013:

| September 30, 2014 (in thousands) | Pass | Special Mention * | Substandard * | Doubtful / Loss | Purchased Credit Impaired Loans - Group 1 | Purchased Credit Impaired Loans - Substandard | Total Rated Loans** |
|---|---|---|---|---|---|---|---|
| Residential real estate: | | | | | | | |
| Owner occupied | $ | $ 27,485 | $ 12,845 | $ | $ 1,612 | $ | $ 41,942 |
| Owner occupied - correspondent | | | | | | | |
| Non owner occupied | | 1,173 | 2,329 | | 3,988 | | 7,490 |
| Commercial real estate | 729,403 | 9,549 | 15,794 | | 16,978 | 41 | 771,765 |
| Commercial real estate - purchased whole loans | 34,714 | | | | | | 34,714 |
| Construction & land development | 41,248 | 122 | 2,462 | | 630 | | 44,462 |
| Commercial & industrial | 146,183 | 493 | 1,803 | | 1,253 | 211 | 149,943 |
| Lease financing receivables | 819 | | | | | | 819 |
| Warehouse lines of credit | 272,584 | | | | | | 272,584 |
| Home equity | | | 2,230 | | | | 2,230 |
| Consumer: | | | | | | | |
| RPG loans | | | | | | | |
| Credit cards | | | | | | | |
| Overdrafts | | | | | | | |
| Purchased whole loans | | | | | | | |
| Other consumer | | 14 | 48 | | 19 | | 81 |
| Total | $ 1,224,951 | $ 38,836 | $ 37,511 | $ | $ 24,480 | $ 252 | $ 1,326,030 |

** - At September 30, 2014, Special Mention and Substandard loans included $1 million and $5 million, respectively, which were removed from PCI accounting in accordance with ASC 310-30-35-13 due to a post-acquisition troubled debt restructuring.*

*** - The above table excludes all non-classified residential real estate and consumer loans at the respective period ends. The table also excludes most non-classified small commercial & industrial and commercial real estate relationships totaling $100,000 or less. These loans are not rated by the Company since they are accruing interest and are not past due 80-days-or-more.*

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| December 31, 2013 (in thousands) | Pass | Special Mention * | Substandard * | Doubtful / Loss | Purchased Credit Impaired Loans - Group 1 | Purchased Credit Impaired Loans - Substandard | Total Rated Loans** |
|---|---|---|---|---|---|---|---|
| Residential real estate: | | | | | | | |
| Owner occupied | $ | $ 27,431 | $ 10,994 | $ | $ 2,810 | $ | $ 41,235 |
| Owner occupied - correspondent | | | | | | | |
| Non owner occupied | | 919 | 1,292 | | 7,936 | | 10,147 |
| Commercial real estate | 709,610 | 11,125 | 25,296 | | 27,142 | | 773,173 |
| Commercial real estate - Purchased whole loans | 34,186 | | | | | | 34,186 |
| Construction & land development | 40,591 | 128 | 2,386 | | 1,246 | | 44,351 |
| Commercial & industrial | 123,646 | 296 | 2,035 | | 1,564 | 222 | 127,763 |
| Lease financing receivables | | | | | | | |
| Warehouse lines of credit | 149,576 | | | | | | 149,576 |
| Home equity | | 250 | 2,014 | | | | 2,264 |
| Consumer: | | | | | | | |
| RPG loans | | | | | | | |
| Credit cards | | | | | | | |
| Overdrafts | | | | | | | |
| Purchased whole loans | | | | | | | |
| Other consumer | | 18 | 66 | | 33 | | 117 |
| Total | $ 1,057,609 | $ 40,167 | $ 44,083 | $ | $ 40,731 | $ 222 | $ 1,182,812 |

** - At December 31, 2013, Special Mention and Substandard loans included $1 million and $6 million, respectively, which were removed from PCI accounting in accordance with ASC 310-30-35-13 due to a post-acquisition troubled debt restructuring.*

*** - The above table excludes all non-classified residential real estate and consumer loans at the respective period ends. The table also excludes most non-classified small commercial & industrial and commercial real estate relationships totaling $100,000 or less. These loans are not rated by the Company since they are accruing interest and are not past due 80-days-or-more.*

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**Allowance for Loan Losses**

Activity in the allowance for loan losses ( Allowance ) follows:

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| **(in thousands)** | **2014** | **2013** | **2014** | **2013** |
| Allowance, beginning of period | $ 22,772 | $ 22,491 | $ 23,026 | $ 23,729 |
| Charge offs - Traditional Banking | (1,071) | (1,627) | (2,698) | (4,744) |
| Charge offs - RPG | (2) | | (2) | |
| Total charge offs | (1,073) | (1,627) | (2,700) | (4,744) |
| Recoveries - Traditional Banking | 376 | 371 | 1,233 | 1,231 |
| Recoveries - RPG | 32 | 57 | 558 | 796 |
| Total recoveries | 408 | 428 | 1,791 | 2,027 |
| Net (charge offs) recoveries - Traditional Banking | (695) | (1,256) | (1,465) | (3,513) |
| Net (charge offs) recoveries - RPG | 30 | 57 | 556 | 796 |
| Net (charge offs) recoveries | (665) | (1,199) | (909) | (2,717) |
| Provision for losses - Traditional Banking | 1,542 | 2,257 | 2,012 | 3,276 |
| Provision for losses - RPG | (32) | (57) | (512) | (796) |
| Total provision for losses | 1,510 | 2,200 | 1,500 | 2,480 |
| Allowance, end of period | $ 23,617 | $ 23,492 | $ 23,617 | $ 23,492 |

The Allowance calculation includes the following qualitative factors, which are considered in combination with the Bank s historical loss rates in determining the general loss reserve within the Allowance:

- Changes in nature, volume and seasoning of the portfolio;
- Changes in experience, ability and depth of lending management and other relevant staff;
- Changes in the quality of the Bank s credit review system;
- Changes in policies and procedures, including changes in underwriting standards and collection, charge-off, and recovery practices not considered elsewhere in estimating credit losses;
- Changes in the volume and severity of past due, non-accrual and classified loans;
- Changes in the value of underlying collateral for collateral-dependent loans;

- Changes in international, national, regional, and local economic and business conditions and developments that affect the collectibility of portfolios, including the condition of various market segments;

- The existence and effect of any concentrations of credit, and changes in the level of such concentrations; and

- The effect of other external factors such as competition and legal and regulatory requirements on the level of estimated credit losses in the institution s existing portfolio.

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The following tables present the activity in the Allowance by portfolio class for the three months ended September 30, 2014 and 2013:

| Three Months Ended September 30, 2014 (in thousands) | Residential Real Estate Owner Occupied | Residential Real Estate Owner Occupied - Correspondent | Residential Real Estate Non Owner Occupied | Commercial Real Estate | Commercial Real Estate - Purchased Whole Loans | Construction & Land Development | Commercial & Industrial | Lease Financing Receivables |
|---|---|---|---|---|---|---|---|---|
| Beginning balance | $ 8,055 | $ 60 | $ 839 | $ 7,696 | $ 34 | $ 1,090 | $ 1,152 | $ 3 |
| Provision for losses | (148) | 706 | 50 | 547 | | (4) | (81) | 5 |
| Charge offs | (161) | | (135) | (365) | | | | |
| Recoveries | 26 | | 17 | 9 | | | 37 | |
| Ending balance | $ 7,772 | $ 766 | $ 771 | $ 7,887 | $ 34 | $ 1,086 | $ 1,108 | $ 8 |

*(continued)*

| | Warehouse Lines of Credit | Home Equity | RPG Loans | Consumer Credit Cards | Consumer Overdrafts | Consumer Purchased Whole Loans | Consumer Other Consumer | Total |
|---|---|---|---|---|---|---|---|---|
| Beginning balance | $ 610 | $ 2,403 | $ 46 | $ 286 | $ 280 | $ | $ 218 | $ 22,772 |
| Provision for losses | 71 | 283 | (32) | 19 | 17 | 189 | (112) | 1,510 |
| Charge offs | | (146) | (2) | (23) | (136) | | (105) | (1,073) |
| Recoveries | | 88 | 32 | 10 | 91 | | 98 | 408 |
| Ending balance | $ 681 | $ 2,628 | $ 44 | $ 292 | $ 252 | $ 189 | $ 99 | $ 23,617 |

| Three Months Ended September 30, 2013 (in thousands) | Residential Real Estate Owner Occupied | Residential Real Estate Owner Occupied - Correspondent | Residential Real Estate Non Owner Occupied | Commercial Real Estate | Commercial Real Estate - Purchased Whole Loans | Construction & Land Development | Commercial & Industrial | Lease Financing Receivables |
|---|---|---|---|---|---|---|---|---|
| Beginning balance | $ 7,563 | $ | $ 642 | $ 8,763 | $ 34 | $ 1,587 | $ 710 | $ |
| Provision for losses | 1,198 | | 157 | 686 | | 16 | 232 | |
| Charge offs | (578) | | (67) | (307) | | (16) | (102) | |
| Recoveries | 20 | | 59 | 38 | | 7 | 19 | |
| Ending balance | $ 8,203 | $ | $ 791 | $ 9,180 | $ 34 | $ 1,594 | $ 859 | $ |

*(continued)*

| | Warehouse Lines of Credit | Home Equity | RPG Loans | Consumer Credit Cards | Consumer Overdrafts | Consumer Purchased Whole Loans | Consumer Other Consumer | Total |
|---|---|---|---|---|---|---|---|---|
| Beginning balance | $ 462 | $ 1,932 | $ | $ 344 | $ 249 | $ | $ 205 | $ 22,491 |
| Provision for losses | (143) | 104 | (57) | (18) | 26 | | (1) | 2,200 |
| Charge offs | | (218) | | (60) | (169) | | (110) | (1,627) |
| Recoveries | | 55 | 57 | 4 | 95 | | 74 | 428 |
| Ending balance | $ 319 | $ 1,873 | $ | $ 270 | $ 201 | $ | $ 168 | $ 23,492 |

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The following tables present the activity in the Allowance by portfolio class for the nine months ended September 30, 2014 and 2013:

| Nine Months Ended September 30, 2014 (in thousands) | Residential Real Estate Owner Occupied | Residential Real Estate Owner Occupied - Correspondent | Residential Real Estate Non Owner Occupied | Commercial Real Estate | Commercial Real Estate - Purchased Whole Loans | Construction & Land Development | Commercial & Industrial | Lease Financing Receivables |
|---|---|---|---|---|---|---|---|---|
| Beginning balance | $ 7,816 | $ | $ 1,023 | $ 8,309 | $ 34 | $ 1,296 | $ 1,089 | $ |
| Provision for losses | 430 | 766 | (121) | 163 | | (277) | (68) | 8 |
| Charge offs | (580) | | (157) | (739) | | (18) | (20) | |
| Recoveries | 106 | | 26 | 154 | | 85 | 107 | |
| Ending balance | $ 7,772 | $ 766 | $ 771 | $ 7,887 | $ 34 | $ 1,086 | $ 1,108 | $ 8 |

*(continued)*

| | Warehouse Lines of Credit | Home Equity | RPG Loans | Consumer Credit Cards | Consumer Overdrafts | Consumer Purchased Whole Loans | Consumer Other Consumer | Total |
|---|---|---|---|---|---|---|---|---|
| Beginning balance | $ 449 | $ 2,396 | $ | $ 289 | $ 199 | $ | $ 126 | $ 23,026 |
| Provision for losses | 232 | 518 | (512) | 41 | 177 | 189 | (46) | 1,500 |
| Charge offs | | (429) | (2) | (65) | (429) | | (261) | (2,700) |
| Recoveries | | 143 | 558 | 27 | 305 | | 280 | 1,791 |
| Ending balance | $ 681 | $ 2,628 | $ 44 | $ 292 | $ 252 | $ 189 | $ 99 | $ 23,617 |

| Nine Months Ended September 30, 2013 (in thousands) | Residential Real Estate Owner Occupied | Residential Real Estate Owner Occupied - Correspondent | Residential Real Estate Non Owner Occupied | Commercial Real Estate | Commercial Real Estate - Purchased Whole Loans | Construction & Land Development | Commercial & Industrial | Lease Financing Receivables |
|---|---|---|---|---|---|---|---|---|
| Beginning balance | $ 7,006 | $ | $ 1,049 | $ 8,843 | $ 34 | $ 2,769 | $ 580 | $ |
| Provision for losses | 2,269 | | (106) | 1,192 | | (604) | 618 | |
| Charge offs | (1,291) | | (225) | (972) | | (616) | (412) | |
| Recoveries | 219 | | 73 | 117 | | 45 | 73 | |
| Ending balance | $ 8,203 | $ | $ 791 | $ 9,180 | $ 34 | $ 1,594 | $ 859 | $ |

*(continued)*

| | Warehouse Lines of Credit | Home Equity | RPG Loans | Consumer Credit Cards | Consumer Overdrafts | Consumer Purchased Whole Loans | Consumer Other Consumer | Total |
|---|---|---|---|---|---|---|---|---|
| Beginning balance | $ 541 | $ 2,348 | $ | $ 210 | $ 198 | $ | $ 151 | $ 23,729 |
| Provision for losses | (222) | (248) | (796) | 166 | 153 | | 58 | 2,480 |
| Charge offs | | (354) | | (120) | (474) | | (280) | (4,744) |
| Recoveries | | 127 | 796 | 14 | 324 | | 239 | 2,027 |
| Ending balance | $ 319 | $ 1,873 | $ | $ 270 | $ 201 | $ | $ 168 | $ 23,492 |

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**Non-performing Loans and Other Assets**

Detail of non-performing loans and other assets follows:

| (dollars in thousands) | September 30, 2014 | December 31, 2013 |
|---|---|---|
| Loans on non-accrual status(1) | $ 21,447 | $ 19,104 |
| Loans past due 90-days-or-more and still on accrual(2) | | 1,974 |
| | | |
| Total non-performing loans | 21,447 | 21,078 |
| Other real estate owned | 11,937 | 17,102 |
| Total non-performing assets | $ 33,384 | $ 38,180 |
| **Credit Quality Ratios** | | |
| Non-performing loans to total loans | 0.74% | 0.81% |
| Non-performing assets to total loans (including OREO) | 1.14% | 1.46% |
| Non-performing assets to total assets | 0.92% | 1.13% |

(1) *Loans on non-accrual status include impaired loans, which are discussed subsequently in Footnote 3 in this section of the filing.*

(2) *All loans past due 90-days-or-more and still accruing were PCI loans accounted for under ASC 310-30.*

The following table presents the recorded investment in non-accrual loans and loans past due 90-days-or-more and still on accrual by class:

| | Non-Accrual | | Past Due 90-Days-or-More and Still Accruing Interest* | |
|---|---|---|---|---|
| (in thousands) | September 30, 2014 | December 31, 2013 | September 30, 2014 | December 31, 2013 |
| Residential real estate: | | | | |
| Owner occupied | $ 9,457 | $ 8,538 | $ | $ 673 |
| Owner occupied - correspondent | | | | |
| Non owner occupied | 1,632 | 1,279 | | |
| Commercial real estate | 6,739 | 7,643 | | |
| Commercial real estate - purchased whole loans | | | | |
| Construction & land development | 1,990 | 97 | | 70 |
| Commercial & industrial | | 327 | | 1,231 |
| Lease financing receivables | | | | |
| Warehouse lines of credit | | | | |
| Home equity | 1,545 | 1,128 | | |
| Consumer: | | | | |
| RPG loans | | | | |
| Credit cards | | | | |
| Overdrafts | | | | |

| | | | | |
|---|---|---|---|---|
| Purchased whole loans | | | | |
| Other consumer | 84 | 92 | | |
| Total | $ 21,447 | $ 19,104 | $ | $ 1,974 |

* - *For all periods presented, loans past due 90-days-or-more and still on accrual consist entirely of PCI loans.*

Non-accrual loans and loans past due 90-days-or-more and still on accrual include both smaller balance homogeneous loans that are collectively evaluated for impairment and individually classified impaired loans. Non-accrual loans are typically returned to accrual status when all the principal and interest amounts contractually due are brought current and held current for six consecutive months and future contractual payments are reasonably assured. Troubled debt restructurings ( TDR s) on non-accrual status are reviewed for return to accrual status on an individual basis, with additional consideration given to performance under the modified terms.

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**Delinquent Loans**

The following tables present the aging of the recorded investment in loans by class:

| September 30, 2014 (dollars in thousands) | 30 - 59 Days Delinquent | 60 - 89 Days Delinquent | 90 or More Days Delinquent* | Total Delinquent | Total Not Delinquent | Total |
|---|---|---|---|---|---|---|
| Residential real estate: | | | | | | |
| Owner occupied | $ 1,440 | $ 1,474 | $ 2,983 | $ 5,897 | $ 1,121,698 | $ 1,127,595 |
| Owner occupied - correspondent | | | | | 139,252 | 139,252 |
| Non owner occupied | 87 | 464 | 133 | 684 | 97,681 | 98,365 |
| Commercial real estate | | | 2,433 | 2,433 | 769,332 | 771,765 |
| Commercial real estate - purchased whole loans | | | | | 34,714 | 34,714 |
| Construction & land development | | | 1,990 | 1,990 | 42,472 | 44,462 |
| Commercial & industrial | | | | | 149,943 | 149,943 |
| Lease financing receivables | | | | | 819 | 819 |
| Warehouse lines of credit | | | | | 272,584 | 272,584 |
| Home equity | 194 | 149 | 420 | 763 | 240,426 | 241,189 |
| Consumer: | | | | | | |
| RPG loans | 105 | 24 | | 129 | 3,331 | 3,460 |
| Credit cards | 45 | 13 | 3 | 61 | 9,169 | 9,230 |
| Overdrafts | 150 | 1 | | 151 | 815 | 966 |
| Purchased whole loans | | | | | 4,664 | 4,664 |
| Other consumer | 106 | 12 | | 118 | 9,409 | 9,527 |
| Total | $ 2,127 | $ 2,137 | $ 7,962 | $ 12,226 | $ 2,896,309 | $ 2,908,535 |
| Delinquency ratio** | 0.07% | 0.07% | 0.27% | 0.42% | | |

| December 31, 2013 (dollars in thousands) | 30 - 59 Days Delinquent | 60 - 89 Days Delinquent | 90 or More Days Delinquent* | Total Delinquent | Total Not Delinquent | Total |
|---|---|---|---|---|---|---|
| Residential real estate: | | | | | | |
| Owner occupied | $ 1,956 | $ 733 | $ 3,668 | $ 6,357 | $ 1,091,438 | $ 1,097,795 |
| Owner occupied - correspondent | | | | | | |
| Non owner occupied | 195 | 967 | 131 | 1,293 | 109,516 | 110,809 |
| Commercial real estate | 874 | 384 | 3,940 | 5,198 | 767,975 | 773,173 |
| Commercial real estate - purchased whole loans | | | | | 34,186 | 34,186 |
| Construction & land development | 332 | | 167 | 499 | 43,852 | 44,351 |
| Commercial & industrial | | | 1,415 | 1,415 | 126,348 | 127,763 |
| Lease financing receivables | | | | | | |
| Warehouse lines of credit | | | | | 149,576 | 149,576 |
| Home equity | 665 | 48 | 397 | 1,110 | 225,672 | 226,782 |
| Consumer: | | | | | | |
| RPG loans | | | | | 1,827 | 1,827 |
| Credit cards | 87 | 6 | 5 | 98 | 8,932 | 9,030 |
| Overdrafts | 159 | | | 159 | 785 | 944 |

| | | | | | | |
|---|---|---|---|---|---|---|
| Purchased whole loans | | | | | | |
| Other consumer | 67 | 27 | | 94 | 13,462 | 13,556 |
| Total | $ 4,335 | $ 2,165 | $ 9,723 | $ 16,223 | $ 2,573,569 | $ 2,589,792 |
| Delinquency ratio** | 0.17% | 0.08% | 0.38% | 0.63% | | |

** - Except for PCI loans, all loans 90-days-or-more past due as of September 30, 2014 and December 31, 2013 were on non-accrual status.*

*** - Delinquency ratio equals total delinquent loans by delinquency class divided by total loans.*

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**Impaired Loans**

The Bank defines impaired loans as follows:

- All loans internally rated as Substandard, Doubtful or Loss;
- All loans internally rated in a PCI category with cash flows that have deteriorated from management s initial estimate;
- All loans on non-accrual status and non-PCI loans past due 90 days-or-more still on accrual;
- All retail and commercial TDRs; and
- Any other situation where the full collection of the total amount due for a loan is improbable or otherwise meets the definition of impaired.

*See the section titled Credit Quality Indicators in this section of the filing for additional discussion regarding the Bank s loan classification structure.*

Information regarding the Bank s impaired loans follows:

| **(in thousands)** | **September 30, 2014** | **December 31, 2013** |
|---|---|---|
| Loans with no allocated Allowance | $ 32,748 | $ 36,721 |
| Loans with allocated Allowance | 57,565 | 71,273 |
| Total impaired loans | $ 90,313 | $ 107,994 |
| Amount of the Allowance allocated | $ 5,651 | $ 6,674 |

Approximately $14 million and $24 million of impaired loans at September 30, 2014 and December 31, 2013 were PCI loans. Approximately $5 million and $6 million of impaired loans at September 30, 2014 and December 31, 2013 were formerly PCI loans which became classified as impaired through a troubled debt restructuring.

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The following tables present the balance in the Allowance and the recorded investment in loans by portfolio class based on impairment method as of September 30, 2014 and December 31, 2013:

| | Residential Real Estate | | | | Commercial Real Estate - | | | |
|---|---|---|---|---|---|---|---|---|
| **September 30, 2014 (in thousands)** | **Owner Occupied** | **Owner Occupied - Correspondent** | **Non Owner Occupied** | **Commercial Real Estate** | **Purchased Whole Loans** | **Construction & Land Development** | **Commercial & Industrial** | **Lease Financing Receivables** |
| Allowance: | | | | | | | | |
| Ending Allowance balance: | | | | | | | | |
| Individually evaluated for impairment, excluding PCI loans | $ 3,298 | $ | $ 113 | $ 788 | $ | $ 190 | $ | $ |
| Collectively evaluated for impairment | 4,436 | 766 | 595 | 6,574 | 34 | 896 | 813 | 8 |
| PCI loans with post acquisition impairment | 38 | | 63 | 525 | | | 295 | |
| PCI loans without post acquisition impairment | | | | | | | | |
| Total ending Allowance: | $ 7,772 | $ 766 | $ 771 | $ 7,887 | $ 34 | $ 1,086 | $ 1,108 | $ 8 |
| Loans: | | | | | | | | |
| Impaired loans individually evaluated, excluding PCI loans | $ 40,274 | $ | $ 3,138 | $ 24,370 | $ | $ 2,656 | $ 3,884 | $ |
| Loans collectively evaluated for impairment | 1,085,709 | 139,252 | 91,239 | 730,376 | 34,714 | 41,176 | 144,595 | 819 |
| PCI loans with post acquisition impairment | 897 | | 3,162 | 8,265 | | | 1,365 | |
| PCI loans without post acquisition impairment | 715 | | 826 | 8,754 | | 630 | 99 | |
| | $ 1,127,595 | $ 139,252 | $ 98,365 | $ 771,765 | $ 34,714 | $ 44,462 | $ 149,943 | $ 819 |

*(continued)*

| | | | | | Consumer | | | |
|---|---|---|---|---|---|---|---|---|
| | **Warehouse Lines of Credit** | **Home Equity** | **RPG Loans** | **Credit Cards** | **Overdrafts** | **Purchased Whole Loans** | **Other Consumer** | **Total** |
| Allowance: | | | | | | | | |
| Ending Allowance balance: | | | | | | | | |
| Individually evaluated for impairment, excluding PCI loans | $ | $ 291 | $ | $ | $ | $ | $ 49 | $ 4,729 |
| Collectively evaluated for impairment | 681 | 2,337 | 44 | 292 | 252 | 189 | 49 | 17,966 |
| PCI loans with post acquisition impairment | | | | | | | 1 | 922 |
| PCI loans without post acquisition impairment | | | | | | | | |
| Total ending Allowance: | $ 681 | $ 2,628 | $ 44 | $ 292 | $ 252 | $ 189 | $ 99 | $ 23,617 |
| Loans: | | | | | | | | |
| Impaired loans individually evaluated, excluding PCI loans | $ | $ 2,230 | $ | $ | $ | $ | $ 62 | $ 76,614 |
| Loans collectively evaluated for impairment | 272,584 | 238,959 | 3,460 | 9,230 | 966 | 4,664 | 9,446 | 2,807,189 |
| PCI loans with post acquisition impairment | | | | | | | 10 | 13,699 |
| | | | | | | | 9 | 11,033 |

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| PCI loans without post acquisition impairment | | | | | | | | |
| | | | | | | | | |
| Total ending loan balance | $ 272,584 | $ 241,189 | $ 3,460 | $ 9,230 | $ 966 | $ 4,664 | $ 9,527 | $ 2,908,535 |

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| December 31, 2013 (in thousands) | Residential Real Estate Owner Occupied | Residential Real Estate Owner Occupied - Correspondent | Residential Real Estate Non Owner Occupied | Commercial Real Estate | Commercial Real Estate - Purchased Whole Loans | Construction & Land Development | Commercial & Industrial | Lease Financing Receivables |
|---|---|---|---|---|---|---|---|---|
| Allowance: | | | | | | | | |
| Ending Allowance balance: | | | | | | | | |
| Individually evaluated for impairment, excluding PCI loans | $ 3,606 | $ | $ 61 | $ 1,232 | $ | $ 146 | $ 111 | $ |
| Collectively evaluated for impairment | 4,159 | | 672 | 6,474 | 34 | 1,140 | 661 | |
| PCI loans with post acquisition impairment | 51 | | 290 | 603 | | 10 | 317 | |
| PCI loans without post acquisition impairment | | | | | | | | |
| Total ending Allowance: | $ 7,816 | $ | $ 1,023 | $ 8,309 | $ 34 | $ 1,296 | $ 1,089 | $ |
| Loans: | | | | | | | | |
| Impaired loans individually evaluated, excluding PCI loans | $ 39,211 | $ | $ 2,061 | $ 33,519 | $ | $ 2,494 | $ 4,521 | $ |
| Loans collectively evaluated for impairment | 1,055,774 | | 100,812 | 712,512 | 34,186 | 40,611 | 121,456 | |
| PCI loans with post acquisition impairment | 1,455 | | 5,984 | 14,512 | | 267 | 1,609 | |
| PCI loans without post acquisition impairment | 1,355 | | 1,952 | 12,630 | | 979 | 177 | |
| Total ending loan balance | $ 1,097,795 | $ | $ 110,809 | $ 773,173 | $ 34,186 | $ 44,351 | $ 127,763 | $ |

*(continued)*

| | Warehouse Lines of Credit | Home Equity | RPG Loans | Consumer Credit Cards | Consumer Overdrafts | Consumer Purchased Whole Loans | Other Consumer | Total |
|---|---|---|---|---|---|---|---|---|
| Allowance: | | | | | | | | |
| Ending Allowance balance: | | | | | | | | |
| Individually evaluated for impairment, excluding PCI loans | $ | $ 203 | $ | $ | $ | $ | $ 43 | $ 5,402 |
| Collectively evaluated for impairment | 449 | 2,193 | 2 | 289 | 199 | | 80 | 16,352 |
| PCI loans with post acquisition impairment | | | | | | | 1 | 1,272 |
| PCI loans without post acquisition impairment | | | | | | | | |
| Total ending Allowance: | $ 449 | $ 2,396 | $ 2 | $ 289 | $ 199 | $ | $ 124 | $ 23,026 |
| Loans: | | | | | | | | |
| Impaired loans individually evaluated, excluding PCI loans | $ | $ 2,264 | $ | $ | $ | $ | $ 85 | $ 84,155 |
| Loans collectively evaluated for impairment | 149,576 | 224,518 | 1,827 | 9,030 | 944 | | 13,438 | 2,464,684 |
| PCI loans with post acquisition impairment | | | | | | | 12 | 23,839 |
| PCI loans without post acquisition impairment | | | | | | | 21 | 17,114 |
| Total ending loan balance | $ 149,576 | $ 226,782 | $ 1,827 | $ 9,030 | $ 944 | $ | $ 13,556 | $ 2,589,792 |

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The following tables present loans individually evaluated for impairment by class as of September 30, 2014 and December 31, 2013 and for the three and nine months ended September 30, 2014 and 2013. The difference between the Unpaid Principal Balance and Recorded Investment columns represents life-to-date partial write downs/charge offs taken on individual impaired credits.

| | As of September 30, 2014 | | | Three Months Ended September 30, 2014 | | | Nine Months Ended September 30, 2014 | | |
|---|---|---|---|---|---|---|---|---|---|
| **(in thousands)** | **Unpaid Principal Balance** | **Recorded Investment** | **Allowance Allocated** | **Average Recorded Investment** | **Interest Income Recognized** | **Cash Basis Interest Income Recognized** | **Average Recorded Investment** | **Interest Income Recognized** | **Cash Basis Interest Income Recognized** |
| **Impaired loans with no related allowance recorded:** | | | | | | | | | |
| Residential real estate: | | | | | | | | | |
| Owner occupied | $ 6,961 | $ 6,577 | $ | $ 6,717 | $ 66 | $ | $ 6,838 | $ 190 | $ |
| Owner occupied - correspondent | | | | | | | | | |
| Non owner occupied | 2,023 | 1,870 | | 1,731 | 11 | | 1,518 | 36 | |
| Commercial real estate | 17,767 | 16,516 | | 15,682 | 95 | | 17,985 | 434 | |
| Commercial real estate - purchased whole loans | | | | | | | | | |
| Construction & land development | 2,164 | 2,164 | | 2,123 | 3 | | 2,103 | 6 | |
| Commercial & industrial | 3,884 | 3,884 | | 4,019 | 31 | | 4,126 | 181 | |
| Lease financing receivables | | | | | | | | | |
| Warehouse lines of credit | | | | | | | | | |
| Home equity | 1,888 | 1,737 | | 1,802 | 11 | | 1,780 | 27 | |
| Consumer: | | | | | | | | | |
| RPG loans | | | | | | | | | |
| Credit cards | | | | | | | | | |
| Overdrafts | | | | | | | | | |
| Purchased whole loans | | | | | | | | | |
| Other consumer | | | | | | | 5 | | |
| | | | | | | | | | |
| **Impaired loans with an allowance recorded:** | | | | | | | | | |
| Residential real estate: | | | | | | | | | |
| Owner occupied | 35,090 | 34,594 | 3,336 | 34,919 | 246 | | 34,697 | 737 | |
| Owner occupied - correspondent | | | | | | | | | |
| Non owner occupied | 4,430 | 4,430 | 176 | 4,811 | 51 | | 5,700 | 149 | |
| Commercial real estate | 16,158 | 16,119 | 1,313 | 17,479 | 186 | | 20,338 | 499 | |
| Commercial real estate - purchased whole loans | | | | | | | | | |
| Construction & land development | 492 | 492 | 190 | 498 | 6 | | 546 | 17 | |
| Commercial & industrial | 1,365 | 1,365 | 295 | 1,374 | 18 | | 1,579 | 78 | |
| Lease financing receivables | | | | | | | | | |
| Warehouse lines of credit | | | | | | | | | |
| Home equity | 548 | 493 | 291 | 436 | | | 588 | | |
| Consumer: | | | | | | | | | |
| RPG loans | | | | | | | | | |
| Credit cards | | | | | | | | | |
| Overdrafts | | | | | | | | | |
| Purchased whole loans | | | | | | | | | |
| Other consumer | 72 | 72 | 50 | 69 | 1 | | 77 | 1 | |
| Total impaired loans | $ 92,842 | $ 90,313 | $ 5,651 | $ 91,660 | $ 725 | $ | $ 97,880 | $ 2,355 | $ |

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| | As of December 31, 2013 | | | Three Months Ended September 30, 2013 | | | Nine Months Ended September 30, 2013 | | |
|---|---|---|---|---|---|---|---|---|---|
| (in thousands) | Unpaid Principal Balance | Recorded Investment | Allowance Allocated | Average Recorded Investment | Interest Income Recognized | Cash Basis Interest Income Recognized | Average Recorded Investment | Interest Income Recognized | Cash Basis Interest Income Recognized |
| **Impaired loans with no related allowance recorded:** | | | | | | | | | |
| Residential real estate: | | | | | | | | | |
| Owner occupied | $ 7,136 | $ 6,569 | $ | $ 6,088 | $ 35 | $ | $ 9,876 | $ 89 | $ |
| Owner occupied - correspondent | | | | | | | | | |
| Non owner occupied | 1,498 | 1,256 | | 1,269 | | | 1,411 | 18 | |
| Commercial real estate | 21,886 | 20,953 | | 18,566 | 451 | | 18,382 | 809 | |
| Commercial real estate - purchased whole loans | | | | | | | | | |
| Construction & land development | 2,087 | 2,087 | | 1,930 | 73 | | 2,126 | 127 | |
| Commercial & industrial | 4,367 | 4,258 | | 3,460 | 204 | | 3,770 | 413 | |
| Lease financing receivables | | | | | | | | | |
| Warehouse lines of credit | | | | | | | | | |
| Home equity | 1,695 | 1,577 | | 1,724 | 34 | | 1,867 | 64 | |
| Consumer: | | | | | | | | | |
| RPG loans | | | | | | | | | |
| Credit cards | | | | | | | | | |
| Overdrafts | | | | | | | | | |
| Purchased whole loans | | | | | | | | | |
| Other consumer | 18 | 18 | | 37 | | | 221 | | |
| | | | | | | | | | |
| **Impaired loans with an allowance recorded:** | | | | | | | | | |
| Residential real estate: | | | | | | | | | |
| Owner occupied | 34,393 | 34,097 | 3,657 | 36,008 | 315 | | 33,841 | 876 | |
| Owner occupied - correspondent | | | | | | | | | |
| Non owner occupied | 6,789 | 6,789 | 351 | 5,688 | 166 | | 4,661 | 208 | |
| Commercial real estate | 27,080 | 27,078 | 1,835 | 26,508 | 549 | | 26,055 | 998 | |
| Commercial real estate - purchased whole loans | | | | | | | | | |
| Construction & land development | 674 | 674 | 156 | 2,000 | 30 | | 2,674 | 75 | |
| Commercial & industrial | 1,872 | 1,872 | 428 | 2,641 | 21 | | 2,702 | 27 | |
| Lease financing receivables | | | | | | | | | |
| Warehouse lines of credit | | | | | | | | | |
| Home equity | 688 | 687 | 203 | 1,026 | 21 | | 1,289 | 41 | |
| Consumer: | | | | | | | | | |
| RPG loans | | | | | | | | | |
| Credit cards | | | | | | | | | |
| Overdrafts | | | | | | | | | |
| Purchased whole loans | | | | | | | | | |
| Other consumer | 79 | 79 | 44 | 116 | 1 | | 92 | 3 | |
| Total impaired loans | $ 110,262 | $ 107,994 | $ 6,674 | $ 107,061 | $ 1,900 | $ | $ 108,967 | $ 3,748 | $ |

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**Troubled Debt Restructurings**

A TDR is the situation where, due to a borrower s financial difficulties, the Bank grants a concession to the borrower that the Bank would not otherwise have considered. In order to determine whether a borrower is experiencing financial difficulty, an evaluation is performed of the probability that the borrower will be in payment default on any of its debt in the foreseeable future without the modification. This evaluation is performed under the Bank s internal underwriting policy.

All TDRs are considered Impaired, including PCI loans subsequently restructured. The majority of the Bank s commercial related and construction TDRs involve a restructuring of financing terms such as a reduction in the payment amount to require only interest and escrow (if required) and/or extending the maturity date of the debt. The substantial majority of the Bank s residential real estate TDR concessions involve reducing the client s loan payment through a rate reduction for a set period of time based on the borrower s ability to service the modified loan payment. Retail loans may also be classified as TDRs due to legal modifications, such as bankruptcies.

Non-accrual loans modified as TDRs typically remain on non-accrual status and continue to be reported as non-performing loans for a minimum of six months. Accruing loans modified as TDRs are evaluated for non-accrual status based on a current evaluation of the borrower s financial condition and ability and willingness to service the modified debt. At September 30, 2014 and December 31, 2013, $15 million and $13 million of TDRs were on non-accrual status.

Detail of TDRs differentiated by loan class and accrual status follows:

| **September 30, 2014 (in thousands)** | **Troubled Debt Restructurings on Non-Accrual Status** | **Troubled Debt Restructurings on Accrual Status** | **Total Troubled Debt Restructurings** |
|---|---|---|---|
| Residential real estate | $ 6,836 | $ 32,984 | $ 39,820 |
| Commercial real estate | 6,258 | 15,665 | 21,923 |
| Construction & land development | 1,990 | 562 | 2,552 |
| Commercial & industrial | | 3,884 | 3,884 |
| Total troubled debt restructurings | $ 15,084 | $ 53,095 | $ 68,179 |

| **December 31, 2013 (in thousands)** | **Troubled Debt Restructurings on Non-Accrual Status** | **Troubled Debt Restructurings on Accrual Status** | **Total Troubled Debt Restructurings** |
|---|---|---|---|
| Residential real estate | $ 5,514 | $ 31,705 | $ 37,219 |
| Commercial real estate | 7,486 | 22,041 | 29,527 |
| Construction & land development | 97 | 2,608 | 2,705 |
| Commercial & industrial | 143 | 4,378 | 4,521 |
| Total troubled debt restructurings | $ 13,240 | $ 60,732 | $ 73,972 |

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The Bank considers a TDR to be performing to its modified terms if the loan is in accrual status and not past due 30 days or more as of the reporting date. A summary of TDRs outstanding by modification and performance under modified terms at September 30, 2014 and December 31, 2013 follows:

| **September 30, 2014 (in thousands)** | **Troubled Debt Restructurings Performing to Modified Terms** | **Troubled Debt Restructurings Not Performing to Modified Terms** | **Total Troubled Debt Restructurings** |
|---|---|---|---|
| Residential real estate loans (including home equity loans): | | | |
| Interest only payments | $ 683 | $ 395 | $ 1,078 |
| Rate reduction | 27,970 | 4,399 | 32,369 |
| Principal deferral | 1,066 | 385 | 1,451 |
| Legal modifications | 3,390 | 1,532 | 4,922 |
| Total residential TDRs | 33,109 | 6,711 | 39,820 |
| | | | |
| Commercial related and construction/land development loans: | | | |
| Interest only payments | 3,703 | 950 | 4,653 |
| Rate reduction | 9,900 | 2,881 | 12,781 |
| Principal deferral | 6,507 | 4,209 | 10,716 |
| Legal modifications | | 209 | 209 |
| Total commercial TDRs | 20,110 | 8,249 | 28,359 |
| Total troubled debt restructurings | $ 53,219 | $ 14,960 | $ 68,179 |

| **December 31, 2013 (in thousands)** | **Troubled Debt Restructurings Performing to Modified Terms** | **Troubled Debt Restructurings Not Performing to Modified Terms** | **Total Troubled Debt Restructurings** |
|---|---|---|---|
| Residential real estate loans (including home equity loans): | | | |
| Interest only payments | $ 430 | $ 671 | $ 1,101 |
| Rate reduction | 26,004 | 4,993 | 30,997 |
| Principal deferral | 1,840 | 632 | 2,472 |
| Legal modifications | 1,247 | 1,402 | 2,649 |
| Total residential TDRs | 29,521 | 7,698 | 37,219 |
| | | | |
| Commercial related and construction/land development loans: | | | |
| Interest only payments | 6,086 | 1,321 | 7,407 |
| Rate reduction | 13,958 | 663 | 14,621 |
| Principal deferral | 8,983 | 5,351 | 14,334 |
| Legal modifications | | 391 | 391 |
| Total commercial TDRs | 29,027 | 7,726 | 36,753 |
| Total troubled debt restructurings | $ 58,548 | $ 15,424 | $ 73,972 |

As of September 30, 2014 and December 31, 2013, 78% and 79% of the Bank s TDRs were performing according to their modified terms. The Bank had provided $4 million and $5 million of specific reserve allocations to customers whose debt terms have been modified in TDRs as of September 30, 2014 and December 31, 2013. Specific reserve allocations are generally assessed for commercial loans prior to loans being modified as a TDR, as most migrate from the Bank s internal watch list and have been specifically provided for or reserved for as part of the

Bank s normal loss provisioning methodology. The Bank had not committed to finance any additional material amounts to its existing TDR relationships at September 30, 2014.

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A summary of the categories of TDR loan modifications that occurred during the three months ended September 30, 2014 and 2013 follows:

| **Three Months Ended September 30, 2014 (in thousands)** | **Troubled Debt Restructurings Performing to Modified Terms** | **Troubled Debt Restructurings Not Performing to Modified Terms** | **Total Troubled Debt Restructurings** |
|---|---|---|---|
| Residential real estate loans (including home equity loans): | | | |
| Interest only payments | $ | $ 395 | $ 395 |
| Rate reduction | 358 | 127 | 485 |
| Principal deferral | 349 | | 349 |
| Legal modifications | 149 | 198 | 347 |
| Total residential TDRs | 856 | 720 | 1,576 |
| | | | |
| Commercial related and construction/land development loans: | | | |
| Interest only payments | 368 | 392 | 760 |
| Rate reduction | 2,374 | | 2,374 |
| Principal deferral | 1,172 | | 1,172 |
| Total commercial TDRs | 3,914 | 392 | 4,306 |
| Total troubled debt restructurings | $ 4,770 | $ 1,112 | $ 5,882 |

| **Three Months Ended September 30, 2013 (in thousands)** | **Troubled Debt Restructurings Performing to Modified Terms** | **Troubled Debt Restructurings Not Performing to Modified Terms** | **Total Troubled Debt Restructurings** |
|---|---|---|---|
| Residential real estate loans (including home equity loans): | | | |
| Rate reduction | $ 1,082 | $ | $ 1,082 |
| Principal deferral | | | |
| Legal modifications | 172 | 272 | 444 |
| Total residential TDRs | 1,254 | 272 | 1,526 |
| | | | |
| Commercial related and construction/land development loans: | | | |
| Interest only payments | 441 | 145 | 586 |
| Rate reduction | 3,407 | 189 | 3,596 |
| Principal deferral | 1,456 | | 1,456 |
| Legal modifications | | 167 | 167 |
| Total commercial TDRs | 5,304 | 501 | 5,805 |
| Total troubled debt restructurings | $ 6,558 | $ 773 | $ 7,331 |

As of September 30, 2014 and 2013, 81% and 89% of the Bank s TDRs that occurred during the third quarters of 2014 and 2013 were performing according to their modified terms. The Bank provided $268,000 and $294,000 in specific reserve allocations to customers whose loan terms were modified in TDRs during the third quarters of 2014 and 2013. As stated above, specific reserves for commercial loans are generally assessed prior to loans being modified as a TDR, as most of these loans migrate from the Bank s internal watch list and have been specifically reserved for as part of the Bank s normal reserving methodology.

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A summary of the categories of TDR loan modifications that occurred during the nine months ended September 30, 2014 and 2013 follows:

| **Nine Months Ended September 30, 2014 (in thousands)** | **Troubled Debt Restructurings Performing to Modified Terms** | **Troubled Debt Restructurings Not Performing to Modified Terms** | **Total Troubled Debt Restructurings** |
|---|---|---|---|
| Residential real estate loans (including home equity loans): | | | |
| Interest only payments | $ | $ 397 | $ 397 |
| Rate reduction | 2,053 | 1,451 | 3,504 |
| Principal deferral | 468 | 29 | 497 |
| Legal modifications | 2,146 | 796 | 2,942 |
| Total residential TDRs | 4,667 | 2,673 | 7,340 |
| | | | |
| Commercial related and construction/land development loans: | | | |
| Interest only payments | 672 | 392 | 1,064 |
| Rate reduction | 2,830 | 1,071 | 3,901 |
| Principal deferral | 1,420 | 1,744 | 3,164 |
| Total commercial TDRs | 4,922 | 3,207 | 8,129 |
| Total troubled debt restructurings | $ 9,589 | $ 5,880 | $ 15,469 |

| **Nine Months Ended Septemer 30, 2013 (in thousands)** | **Troubled Debt Restructurings Performing to Modified Terms** | **Troubled Debt Restructurings Not Performing to Modified Terms** | **Total Troubled Debt Restructurings** |
|---|---|---|---|
| Residential real estate loans (including home equity loans): | | | |
| Interest only payments | $ 165 | $ | $ 165 |
| Rate reduction | 2,703 | 689 | 3,392 |
| Principal deferral | 64 | 160 | 224 |
| Legal modifications | 1,405 | 826 | 2,231 |
| Total residential TDRs | 4,337 | 1,675 | 6,012 |
| | | | |
| Commercial related and construction/land development loans: | | | |
| Interest only payments | 719 | 145 | 864 |
| Rate reduction | 3,407 | 189 | 3,596 |
| Principal deferral | 1,765 | | 1,765 |
| Legal modifications | | 167 | 167 |
| Total commercial TDRs | 5,891 | 501 | 6,392 |
| Total troubled debt restructurings | $ 10,228 | $ 2,176 | $ 12,404 |

As of September 30, 2014 and 2013, 62% and 82% of the Bank s TDRs that occurred during the first nine months of 2014 and 2013 were performing according to their modified terms. The Bank provided $602,000 and $1 million in specific reserve allocations to customers whose loan terms were modified in TDRs during the first nine months of 2014 and 2013. As stated above, specific reserves are generally assessed prior to loans being modified as a TDR, as most of these loans migrate from the Bank s internal watch list and have been specifically reserved for as part of the Bank s normal reserving methodology.

There were no significant changes between the pre and post modification loan balances at September 30, 2014 and December 31, 2013.

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The following tables present loans by class modified as troubled debt restructurings within the previous twelve months of September 30, 2014 and 2013 and for which there was a payment default during the three months ended September 30, 2014 and 2013:

| **Three Months Ended September 30, 2014 (dollars in thousands)** | **Number of Loans** | | **Recorded Investment** |
|---|---|---|---|
| Residential real estate: | | | |
| Owner occupied | 1 | $ | 45 |
| Owner occupied - correspondent | | | |
| Non owner occupied | 6 | | 589 |
| Commercial real estate | 2 | | 467 |
| Commercial real estate - purchased whole loans | | | |
| Construction & land development | | | |
| Commercial & industrial | | | |
| Lease financing receivables | | | |
| Warehouse lines of credit | | | |
| Home equity | | | |
| Consumer: | | | |
| RPG loans | | | |
| Credit cards | | | |
| Overdrafts | | | |
| Purchased whole loans | | | |
| Other consumer | | | |
| Total | 9 | $ | 1,101 |

| **Three Months Ended September 30, 2013 (dollars in thousands)** | **Number of Loans** | | **Recorded Investment** |
|---|---|---|---|
| Residential real estate: | | | |
| Owner occupied | 14 | $ | 979 |
| Owner occupied - correspondent | | | |
| Non owner occupied | | | |
| Commercial real estate | 2 | | 357 |
| Commercial real estate - purchased whole loans | | | |
| Construction & land development | | | |
| Commercial & industrial | 1 | | 145 |
| Lease financing receivables | | | |
| Warehouse lines of credit | | | |
| Home equity | 1 | | 68 |
| Consumer: | | | |
| RPG loans | | | |
| Credit cards | | | |
| Overdrafts | | | |
| Purchased whole loans | | | |
| Other consumer | | | |
| Total | 18 | $ | 1,549 |

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The following tables present loans by class modified as troubled debt restructurings within the previous twelve months of September 30, 2014 and 2013 and for which there was a payment default during the nine months ended September 30, 2014 and 2013:

| **Nine Months Ended September 30, 2014 (dollars in thousands)** | **Number of Loans** | **Recorded Investment** |
|---|---|---|
| Residential real estate: | | |
| Owner occupied | 9 | $ 1,388 |
| Owner occupied - correspondent | | |
| Non owner occupied | 6 | 589 |
| Commercial real estate | 3 | 1,537 |
| Commercial real estate - purchased whole loans | | |
| Construction & land development | 1 | 1,500 |
| Commercial & industrial | | |
| Lease financing receivables | | |
| Warehouse lines of credit | | |
| Home equity | | |
| Consumer: | | |
| RPG loans | | |
| Credit cards | | |
| Overdrafts | | |
| Purchased whole loans | | |
| Other consumer | | |
| Total | 19 | $ 5,014 |

| **Nine Months Ended September 30, 2013 (dollars in thousands)** | **Number of Loans** | **Recorded Investment** |
|---|---|---|
| Residential real estate: | | |
| Owner occupied | 32 | $ 2,434 |
| Owner occupied - correspondent | | |
| Non owner occupied | | |
| Commercial real estate | 2 | 357 |
| Commercial real estate - purchased whole loans | | |
| Construction & land development | | |
| Commercial & industrial | 1 | 145 |
| Lease financing receivables | | |
| Warehouse lines of credit | | |
| Home equity | 2 | 74 |
| Consumer: | | |
| RPG loans | | |
| Credit cards | | |
| Overdrafts | | |
| Purchased whole loans | | |
| Other consumer | | |
| Total | 37 | $ 3,010 |

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## 4. DEPOSITS

Ending deposit balances at September 30, 2014 and December 31, 2013 were as follows:

| (in thousands) | September 30, 2014 | December 31, 2013 |
|---|---|---|
| Demand | $ 697,243 | $ 651,134 |
| Money market accounts | 469,142 | 479,569 |
| Brokered money market accounts | 33,517 | 35,533 |
| Savings | 87,838 | 78,020 |
| Individual retirement accounts* | 26,846 | 28,767 |
| Time deposits, $100,000 and over* | 75,918 | 67,255 |
| Other certificates of deposit* | 68,370 | 75,516 |
| Brokered certificates of deposit*(1) | 66,300 | 86,421 |
| Total interest-bearing deposits | 1,525,174 | 1,502,215 |
| Total non interest-bearing deposits | 534,662 | 488,642 |
| Total deposits | $ 2,059,836 | $ 1,990,857 |

*(*) Represents a time deposit.*

*(1) Includes brokered deposits less than, equal to and greater than $100,000.*

## 5. FEDERAL HOME LOAN BANK ( FHLB ) ADVANCES

At September 30, 2014 and December 31, 2013, FHLB advances were as follows:

| (in thousands) | September 30, 2014 | December 31, 2013 |
|---|---|---|
| Overnight advance with an interest rate of 0.08% due on October 1, 2014 | $ 130,000 | $ |
| Variable interest rate advance indexed to 3-Month LIBOR plus 0.14% due on December 19, 2014 | 10,000 | 10,000 |
| Fixed interest rate advances with a weighted average interest rate of 1.84% due through 2023 | 422,000 | 495,000 |
| Putable fixed interest rate advances with a weighted average interest rate of 4.39% due through 2017(1) | 100,000 | 100,000 |
| Total FHLB advances | $ 662,000 | $ 605,000 |

*(1) - Represents putable advances with the FHLB. These advances have original fixed rate periods ranging from one to five years with original maturities ranging from three to ten years if not put back to the Bank earlier by the FHLB. At the end of their respective fixed rate periods and on a quarterly basis thereafter, the FHLB has the right to require payoff of the advances by the Bank at no penalty. Based on market conditions at this time, the Bank does not believe that any of its putable advances are likely to be put back to the Bank in the short-term by the FHLB.*

Each FHLB advance is payable at its maturity date, with a prepayment penalty for fixed rate advances that are paid off earlier than maturity. FHLB advances are collateralized by a blanket pledge of eligible real estate loans. At September 30, 2014 and December 31, 2013, Republic had available collateral to borrow an additional $429 million and $282 million, respectively, from the FHLB. In addition to its borrowing line with the FHLB, Republic also had unsecured lines of credit totaling $166 million available through various other financial institutions as of September 30, 2014 and December 31, 2013.

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Aggregate future principal payments on FHLB advances and the weighted average cost of such advances, based on contractual maturity dates are detailed below:

| Year (dollars in thousands) | | Principal | Weighted Average Rate |
|---|---|---|---|
| 2014 | | 210,000 | 0.96% |
| 2015 | | 10,000 | 2.48% |
| 2016 | | 82,000 | 1.74% |
| 2017 | | 145,000 | 3.44% |
| 2018 | | 97,500 | 1.50% |
| 2019 | | 80,000 | 1.77% |
| Thereafter | | 37,500 | 1.93% |
| Total | $ | 662,000 | 1.86% |

The following table illustrates real estate loans pledged to collateralize advances and letters of credit with the FHLB:

| (in thousands) | | September 30, 2014 | | December 31, 2013 |
|---|---|---|---|---|
| First lien, single family residential real estate | $ | 1,253,537 | $ | 1,082,624 |
| Home equity lines of credit | | 100,783 | | 105,957 |
| Multi-family commercial real estate | | 9,373 | | 13,124 |

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**6. FAIR VALUE**

Fair value represents the exchange price that would be received for an asset or paid to transfer a liability (exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. There are three levels of inputs that may be used to measure fair values:

**Level 1:** Quoted prices (unadjusted) for 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 1 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 Bank used the following methods and significant assumptions to estimate the fair value of each type of financial instrument:

**Securities available for sale:** Quoted market prices in an active market are available for the Bank s mutual fund investment and fall within Level 1 of the fair value hierarchy.

Except for the Bank s mutual fund investment and its private label mortgage backed security, the fair value of securities available for sale is typically determined by matrix pricing, which is a mathematical technique used widely 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).

The Bank s private label mortgage backed security remains illiquid, and as such, the Bank classifies this security as a Level 3 security in accordance with ASC Topic 820, *Fair Value Measurements and Disclosures.* Based on this determination, the Bank utilized an income valuation model (present value model) approach in determining the fair value of this security.

*See in this section of the filing under Footnote 2 Investment Securities for additional discussion regarding the Bank s private label mortgage backed security.*

**Mortgage loans held for sale:** The fair value of mortgage loans held for sale is determined using quoted secondary market prices. Mortgage loans held for sale are classified as Level 2 in the fair value hierarchy.

**Derivative instruments**: Mortgage Banking derivatives used in the ordinary course of business primarily consist of mandatory forward sales contracts ( forward contracts ) and rate lock loan commitments. The fair value of the Bank s derivative instruments is primarily measured by obtaining pricing from broker-dealers recognized to be market participants. The pricing is derived from market observable inputs that can generally be verified and do not typically involve significant judgment by the Bank. Forward contracts and rate lock loan commitments are classified as Level 2 in the fair value hierarchy.

**Interest rate swap agreements used for interest rate risk management:** Interest rate swaps are recorded at fair value on a recurring basis. The Company utilizes interest rate swap agreements as part of the management of interest rate risk to modify the repricing characteristics of certain portions of the Company s interest-bearing liabilities. The Company values its interest rate swaps using Bloomberg Valuation Service s derivative pricing functions and therefore classifies such valuations as Level 2. Valuations of these interest rate swaps are also received from the relevant counterparty and validated against internal calculations. The Company has considered counterparty credit risk in the valuation of its interest rate swap assets and has considered its own credit risk in the valuation of its interest rate swap liabilities.

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**Impaired loans:** Collateral dependent impaired loans generally reflect partial charge-downs to their respective fair value, which is commonly based on recent real estate appraisals. These appraisals may utilize a single valuation approach or a combination of approaches including comparable sales and the income approach. Adjustments are routinely made in the appraisal process by the independent appraisers to adjust for differences between the comparable sales and income data available. Such adjustments are usually significant and typically result in a Level 3 classification of the inputs for determining fair value. Non-real estate collateral may be valued using an appraisal, net book value per the borrower s financial statements or aging reports, adjusted or discounted based on management s historical knowledge, changes in market conditions from the time of the valuation, and management s expertise and knowledge of the client and client s business, resulting in a Level 3 fair value classification. Collateral dependent loans are evaluated on a quarterly basis for additional impairment and adjusted accordingly.

**Other real estate owned:** Assets acquired through or instead of loan foreclosure are initially recorded at fair value less costs to sell when acquired, establishing a new cost basis. These assets are subsequently accounted for at lower of cost or fair value less estimated costs to sell. Fair value is commonly based on recent real estate appraisals. These appraisals may utilize a single valuation approach or a combination of approaches, including comparable sales and the income approach. Adjustments are routinely made in the appraisal process by the independent appraisers to adjust for differences between the comparable sales and income data available. Such adjustments may be significant and typically result in a Level 3 classification of the inputs for determining fair value.

Appraisals for both collateral-dependent impaired loans and other real estate owned are performed by certified general appraisers (for commercial properties) or certified residential appraisers (for residential properties) whose qualifications and licenses have been reviewed and verified by the Bank. Once the appraisal is received, a member of the Bank s Credit Administration Department reviews the assumptions and approaches utilized in the appraisal, as well as the overall resulting fair value in comparison with independent data sources, such as recent market data or industry-wide statistics. On an annual basis, the Bank compares the actual selling price of collateral that has been sold to the most recent appraised value to determine what additional adjustment, if any, should be made to the appraisal value to arrive at an estimated fair value.

**Mortgage servicing rights:** On a quarterly basis, mortgage servicing rights are evaluated for impairment based upon the fair value of the MSRs as compared to carrying amount. If the carrying amount of an individual grouping exceeds fair value, impairment is recorded and the respective individual tranche is carried at fair value. If the carrying amount of an individual grouping does not exceed fair value, impairment is reversed if previously recognized and the carrying value of the individual tranche is based on the amortization method. The valuation model utilizes assumptions that market participants would use in estimating future net servicing income and that can generally be validated against available market data (Level 2).

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Assets and liabilities measured at fair value on a **recurring basis** as of September 30, 2014 and December 31, 2013, including financial assets and liabilities for which the Bank has elected the fair value option, are summarized below:

| | Fair Value Measurements at September 30, 2014 Using: | | | |
|---|---|---|---|---|
| **(in thousands)** | **Quoted Prices in Active Markets for Identical Assets (Level 1)** | **Significant Other Observable Inputs (Level 2)** | **Significant Unobservable Inputs (Level 3)** | **Total Fair Value** |
| **Financial assets:** | | | | |
| Securities available for sale: | | | | |
| U.S. Treasury securities and U.S. Government agencies | $ | $ 149,891 | $ | $ 149,891 |
| Private label mortgage backed security | | | 5,337 | 5,337 |
| Mortgage backed securities - residential | | 130,265 | | 130,265 |
| Collateralized mortgage obligations | | 150,678 | | 150,678 |
| Freddie Mac preferred stock | | 669 | | 669 |
| Mutual fund | 1,010 | | | 1,010 |
| Corporate bonds | | 15,124 | | 15,124 |
| Total securities available for sale | $ 1,010 | $ 446,627 | $ 5,337 | $ 452,974 |
| | | | | |
| Mortgage loans held for sale | $ | $ 5,890 | $ | $ 5,890 |
| Rate lock commitments | | 335 | | 335 |
| **Financial liabilities:** | | | | |
| Mandatory forward contracts | | 18 | | 18 |
| Interest rate swap agreements | | 203 | | 203 |

| | Fair Value Measurements at December 31, 2013 Using: | | | |
|---|---|---|---|---|
| **(in thousands)** | **Quoted Prices in Active Markets for Identical Assets (Level 1)** | **Significant Other Observable Inputs (Level 2)** | **Significant Unobservable Inputs (Level 3)** | **Total Fair Value** |
| **Financial assets:** | | | | |
| Securities available for sale: | | | | |
| U.S. Treasury securities and U.S. Government agencies | $ | $ 97,465 | $ | $ 97,465 |
| Private label mortgage backed security | | | 5,485 | 5,485 |
| Mortgage backed securities - residential | | 150,087 | | 150,087 |
| Collateralized mortgage obligations | | 163,946 | | 163,946 |
| Mutual fund | 995 | | | 995 |
| Corporate bonds | | 14,915 | | 14,915 |
| Total securities available for sale | $ 995 | $ 426,413 | $ 5,485 | $ 432,893 |
| | | | | |
| Mortgage loans held for sale | $ | $ 3,506 | $ | $ 3,506 |
| Rate lock commitments | | 77 | | 77 |
| Mandatory forward contracts | | 12 | | 12 |
| Interest rate swap agreements | | 170 | | 170 |

All transfers between levels are generally recognized at the end of each quarter. There were no transfers into or out of Level 1, 2 or 3 assets during the three and nine months ended September 30, 2014 and 2013.

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**Private Label Mortgage Backed Security**

The table below presents a reconciliation of the Bank s private label mortgage backed security. This represents the sole asset that was measured at fair value on a recurring basis using significant unobservable inputs (Level 3) for the periods ended September 30, 2014 and 2013:

| (in thousands) | Three Months Ended September 30, 2014 | Three Months Ended September 30, 2013 | Nine Months Ended September 30, 2014 | Nine Months Ended September 30, 2013 |
|---|---|---|---|---|
| Balance, beginning of period | $ 5,461 | $ 5,641 | $ 5,485 | $ 5,687 |
| Total gains or losses included in earnings: | | | | |
| Net change in unrealized gain | 65 | (4) | 434 | 418 |
| Recovery of actual losses previously recorded | 35 | 37 | 101 | 37 |
| Principal paydowns | (224) | (217) | (683) | (685) |
| Balance, end of period | $ 5,337 | $ 5,457 | $ 5,337 | $ 5,457 |

The fair value of the Bank s single private label mortgage backed security is supported by analysis prepared by an independent third party. The third party s approach to determining fair value involved several steps: 1) detailed collateral analysis of the underlying mortgages, including consideration of geographic location, original loan-to-value and the weighted average Fair Isaac Corporation ( FICO ) score of the borrowers; 2) collateral performance projections for each pool of mortgages underlying the security (probability of default, severity of default, and prepayment probabilities) and 3) discounted cash flow modeling.

The significant unobservable inputs in the fair value measurement of the Bank s single private label mortgage backed security are prepayment rates, probability of default and loss severity in the event of default. Significant fluctuations in any of those inputs in isolation would result in a significantly lower/higher fair value measurement.

The following table presents quantitative information about recurring Level 3 fair value measurements at September 30, 2014 and December 31, 2013:

| September 30, 2014 (dollars in thousands) | Fair Value | Valuation Technique | Unobservable Inputs | Range |
|---|---|---|---|---|
| Private label mortgage backed security | $ 5,337 | Discounted cash flow | (1) Constant prepayment rate | 0.0% - 6.5% |
| | | | (2) Probability of default | 3.0% - 6.0% |
| | | | (2) Loss severity | 60% - 75% |

| December 31, 2013 (dollars in thousands) | Fair Value | Valuation Technique | Unobservable Inputs | Range |
|---|---|---|---|---|
| Private label mortgage backed security | $ 5,485 | Discounted cash flow | (1) Constant prepayment rate | 2.5% - 6.5% |
| | | | (2) Probability of default | 3.0% - 7.0% |

| | | |
|---|---|---|
| | (2) Loss severity | 55% - 75% |

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**Mortgage Loans Held for Sale**

The Bank has elected the fair value option for mortgage loans held for sale. These loans are intended for sale and the Bank believes that the fair value is the best indicator of the ultimate resolution of these loans. Interest income is recorded based on the contractual terms of the loan and in accordance with Bank policy for such instruments. None of these loans were past due 90-days-or-more nor on nonaccrual as of September 30, 2014 and December 31, 2013.

As of September 30, 2014 and December 31, 2013, the aggregate fair value, contractual balance (including accrued interest), and gain or loss was as follows:

| (in thousands) | September 30, 2014 | December 31, 2013 |
|---|---|---|
| Aggregate fair value | $ 5,890 | $ 3,506 |
| Contractual balance | 5,743 | 3,417 |
| Gain | 147 | 89 |

The total amount of gains and losses from changes in fair value included in earnings for the three and nine months ended September 30, 2014 and 2013 for mortgage loans held for sale are presented in the following table:

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| (in thousands) | 2014 | 2013 | 2014 | 2013 |
| Interest income | $ 38 | $ 130 | $ 133 | $ 388 |
| Change in fair value | (65) | (218) | 59 | (331) |
| Total included in earnings | $ (27) | $ (88) | $ 192 | $ 57 |

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Assets measured at fair value on a **non-recurring basis** as of September 30, 2014 and December 31, 2013 are summarized below:

| | Fair Value Measurements at September 30, 2014 Using: | | | |
|---|---|---|---|---|
| **(in thousands)** | **Quoted Prices in Active Markets for Identical Assets (Level 1)** | **Significant Other Observable Inputs (Level 2)** | **Significant Unobservable Inputs (Level 3)** | **Total Fair Value** |
| Impaired loans: | | | | |
| Residential real estate: | | | | |
| Owner occupied | $ | $ | $ 1,224 | $ 1,224 |
| Non owner occupied | | | 706 | 706 |
| Commercial real estate | | | 6,692 | 6,692 |
| Home equity | | | 1,157 | 1,157 |
| Total impaired loans* | $ | $ | $ 9,779 | $ 9,779 |
| | | | | |
| Other real estate owned: | | | | |
| Residential real estate | $ | $ | $ 980 | $ 980 |
| Commercial real estate | | | 1,385 | 1,385 |
| Construction & land development | | | 5,240 | 5,240 |
| Total other real estate owned | $ | $ | $ 7,605 | $ 7,605 |

| | Fair Value Measurements at December 31, 2013 Using: | | | |
|---|---|---|---|---|
| **(in thousands)** | **Quoted Prices in Active Markets for Identical Assets (Level 1)** | **Significant Other Observable Inputs (Level 2)** | **Significant Unobservable Inputs (Level 3)** | **Total Fair Value** |
| Impaired loans: | | | | |
| Residential real estate: | | | | |
| Owner occupied | $ | $ | $ 2,020 | $ 2,020 |
| Commercial real estate | | | 5,488 | 5,488 |
| Home equity | | | 1,030 | 1,030 |
| Total impaired loans* | $ | $ | $ 8,538 | $ 8,538 |
| | | | | |
| Other real estate owned: | | | | |
| Residential real estate | $ | $ | $ 1,716 | $ 1,716 |
| Commercial real estate | | | 507 | 507 |
| Construction & land development | | | 6,195 | 6,195 |
| Total other real estate owned | $ | $ | $ 8,418 | $ 8,418 |

** - The impaired loan balances in the preceding two tables exclude TDRs which are not collateral dependent. The difference between the carrying value and the fair value of impaired loans measured at fair value is reconciled in a subsequent table of this Footnote 6 and represents estimated selling costs to liquidate the underlying collateral on such debt.*

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The following tables present quantitative information about Level 3 fair value measurements for financial instruments measured at fair value on a **non-recurring basis** at September 30, 2014 and December 31, 2013:

| **September 30, 2014 (dollars in thousands)** | | **Fair Value** | **Valuation Technique** | **Unobservable Inputs** | **Range (Weighted Average)** |
|---|---|---|---|---|---|
| Impaired loans - residential real estate owner occupied | $ | 1,224 | Sales comparison approach | Adjustments determined for differences between comparable sales | 0% - 33% (9%) |
| Impaired loans - residential real estate non owner occupied | $ | 706 | Sales comparison approach | Adjustments determined for differences between comparable sales | 0% - 33% (15%) |
| Impaired loans - commercial real estate | $ | 4,952 | Sales comparison approach | Adjustments determined for differences between comparable sales | 0% - 9% (6%) |
| | $ | 1,740 | Income approach | Adjustments for differences between net operating income expectations | 3% (3%) |
| Impaired loans - home equity | $ | 1,157 | Sales comparison approach | Adjustments determined for differences between comparable sales | 0% - 35% (12%) |
| Other real estate owned - residential real estate | $ | 980 | Sales comparison approach | Adjustments determined for differences between comparable sales | 10% - 16% (16%) |
| Other real estate owned - commercial real estate | $ | 236 | Sales comparison approach | Adjustments determined for differences between comparable sales | 20% (20%) |
| | $ | 1,149 | Income approach | Adjustments for differences between net operating income expectations | 37% (37%) |
| Other real estate owned - construction & land development | $ | 2,488 | Sales comparison approach | Adjustments determined for differences between comparable sales | 13% - 70% (31%) |
| | $ | 2,752 | Income approach | Adjustments for differences between net operating income expectations | 13% - 30% (23%) |

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| December 31, 2013 (dollars in thousands) | Fair Value | | Valuation Technique | Unobservable Inputs | Range (Weighted Average) |
|---|---|---|---|---|---|
| Impaired loans - residential real estate | $ | 2,020 | Sales comparison approach | Adjustments determined for differences between comparable sales | 2% - 22% (7%) |
| Impaired loans - commercial real estate | $ | 5,488 | Sales comparison approach | Adjustments determined for differences between comparable sales | 0% - 30% (19%) |
| Impaired loans - home equity | $ | 1,030 | Sales comparison approach | Adjustments determined for differences between comparable sales | 0% - 10% (2%) |
| Other real estate owned - residential real estate | $ | 1,716 | Sales comparison approach | Adjustments determined for differences between comparable sales | 10% - 53% (30%) |
| Other real estate owned - commercial real estate | $ | 507 | Sales comparison approach | Adjustments determined for differences between comparable sales | 23% - 33% (29%) |
| Other real estate owned - construction & land development | $ | 2,236 | Sales comparison approach | Adjustments determined for differences between comparable sales | 17% - 58% (43%) |
| | $ | 3,959 | Income approach | Adjustments for differences between net operating income expectations | 21% (21%) |

The following section details impairment charges recognized during the period:

**Impaired Loans**

Collateral dependent impaired loans are generally measured for impairment using the fair market value for reasonable disposition of the underlying collateral. The Bank s practice is to obtain new or updated appraisals on the loans subject to the initial impairment review and then to evaluate the need for an update to this value on an as necessary or possibly annual basis thereafter (depending on the market conditions impacting the value of the collateral). The Bank may discount the appraisal amount as necessary for selling costs and past due real estate taxes. If a new or updated appraisal is not available at the time of a loan s impairment review, the Bank may apply a discount to the existing value of an old appraisal to reflect the property s current estimated value if it is believed to have deteriorated in either: (i) the physical or economic aspects of the subject property or (ii) material changes in market conditions. The impairment review generally results in a partial charge-off of the loan if fair value less selling costs are below the loan s carrying value. Impaired loans that are collateral dependent are classified within Level 3 of the fair value hierarchy when impairment is determined using the fair value method.

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Impaired loans, which are measured for impairment using the fair value of the collateral for collateral dependent loans are as follows:

| (in thousands) | September 30, 2014 | | December 31, 2013 | |
|---|---|---|---|---|
| Carrying amount of loans measured at fair value | $ | 8,729 | $ | 7,629 |
| Estimated selling costs considered in carrying amount | | 1,050 | | 909 |
| Total fair value | $ | 9,779 | $ | 8,538 |

**Other Real Estate Owned**

Other real estate owned, which is carried at the lower of cost or fair value, is periodically assessed for impairment based on fair value at the reporting date. Fair value is determined from external appraisals using judgments and estimates of external professionals. Many of these inputs are not observable and, accordingly, these measurements are classified as Level 3. The fair value of the Bank s other real estate owned properties equaled or exceeded their carrying value on an individual basis at September 30, 2014 and December 31, 2013.

Details of other real estate owned carrying value and write downs follows:

| (in thousands) | September 30, 2014 | | December 31, 2013 | |
|---|---|---|---|---|
| Carrying value of other real estate owned | $ | 11,937 | $ | 17,102 |

| | Three Months Ended September 30, | | | | Nine Months Ended September 30, | | | |
|---|---|---|---|---|---|---|---|---|
| (in thousands) | 2014 | | 2013 | | 2014 | | 2013 | |
| Other real estate owned write-downs | $ | 1,217 | $ | 190 | $ | 2,042 | $ | 1,074 |

**Mortgage Servicing Rights**

MSRs are carried at lower of cost or fair value. No MSRs were carried at fair value at September 30, 2014 and December 31, 2013.

Adjustments to mortgage banking income recorded due to the valuation of MSRs for the three and nine months ended September 30, 2014 and 2013 follow:

| Three Months Ended September 30, | Nine Months Ended September 30, |
|---|---|

| (in thousands) | 2014 | 2013 | 2014 | 2013 |
|---|---|---|---|---|
| Credit to mortgage banking income due to impairment evaluation | $ | $ (33) | $ | $ (345) |

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The carrying amounts and estimated fair values of all financial instruments, at September 30, 2014 and December 31, 2013 follows:

| | | Fair Value Measurements at September 30, 2014: | | | |
|---|---|---|---|---|---|
| **(in thousands)** | **Carrying Value** | **Level 1** | **Level 2** | **Level 3** | **Total Fair Value** |
| Assets: | | | | | |
| Cash and cash equivalents | $ 69,682 | $ 69,682 | $ | $ | $ 69,682 |
| Securities available for sale | 452,974 | 1,010 | 446,627 | 5,337 | 452,974 |
| Securities to be held to maturity | 47,247 | | 47,541 | | 47,541 |
| Mortgage loans held for sale, at fair value | 5,890 | | 5,890 | | 5,890 |
| Loans, net | 2,884,918 | | | 2,922,976 | 2,922,976 |
| Federal Home Loan Bank stock | 28,208 | | | | N/A |
| Accrued interest receivable | 8,555 | | 8,555 | | 8,555 |
| | | | | | |
| Liabilities: | | | | | |
| Non interest-bearing deposits | 534,662 | | 534,662 | | 534,662 |
| Transaction deposits | 1,287,740 | | 1,287,740 | | 1,287,740 |
| Time deposits | 237,434 | | 237,886 | | 237,886 |
| Securities sold under agreements to repurchase and other short-term borrowings | 275,874 | | 275,874 | | 275,874 |
| Federal Home Loan Bank advances | 662,000 | | 673,135 | | 673,135 |
| Subordinated note | 41,240 | | 39,618 | | 39,618 |
| Accrued interest payable | 1,149 | | 1,149 | | 1,149 |

| | | Fair Value Measurements at December 31, 2013: | | | |
|---|---|---|---|---|---|
| **(in thousands)** | **Carrying Value** | **Level 1** | **Level 2** | **Level 3** | **Total Fair Value** |
| Assets: | | | | | |
| Cash and cash equivalents | $ 170,863 | $ 170,863 | $ | $ | $ 170,863 |
| Securities available for sale | 432,893 | 995 | 426,413 | 5,485 | 432,893 |
| Securities to be held to maturity | 50,644 | | 50,768 | | 50,768 |
| Mortgage loans held for sale, at fair value | 3,506 | | 3,506 | | 3,506 |
| Loans, net | 2,566,766 | | | 2,585,476 | 2,585,476 |
| Federal Home Loan Bank stock | 28,342 | | | | N/A |
| Accrued interest receivable | 8,272 | | 8,272 | | 8,272 |
| | | | | | |
| Liabilities: | | | | | |
| Non interest-bearing deposits | 488,642 | | 488,642 | | 488,642 |
| Transaction deposits | 1,244,256 | | 1,244,256 | | 1,244,256 |
| Time deposits | 257,959 | | 259,345 | | 259,345 |
| Securities sold under agreements to repurchase and other short-term borrowings | 165,555 | | 165,555 | | 165,555 |
| Federal Home Loan Bank advances | 605,000 | | 618,064 | | 618,064 |
| Subordinated note | 41,240 | | 38,020 | | 38,020 |

| | | | |
|---|---|---|---|
| Accrued interest payable | 1,459 | 1,459 | 1,459 |

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Fair value estimates are based on existing on and off-balance sheet financial instruments without attempting to estimate the value of anticipated future business and the value of assets and liabilities that are not considered financial instruments. In addition, the tax ramifications related to the realization of the unrealized gains and losses can have a significant effect on fair value estimates and have not been considered in any of the Bank s estimates.

The assumptions used in the estimation of the fair value of the Company s financial instruments are explained below. Where quoted market prices are not available, fair values are based on estimates using discounted cash flow and other valuation techniques. Discounted cash flows can be significantly affected by the assumptions used, including the discount rate and estimates of future cash flows. The following fair value estimates cannot be substantiated by comparison to independent markets and should not be considered representative of the liquidation value of the Company s financial instruments, but rather a good-faith estimate of the fair value of financial instruments held by the Company.

In addition to those previously disclosed, the following methods and assumptions were used by the Company in estimating the fair value of its financial instruments:

*Cash and cash equivalents* The carrying amounts of cash and short-term instruments approximate fair values and are classified as Level 1.

*Loans, net of Allowance* The fair value of loans is calculated using discounted cash flows by loan type resulting in a Level 3 classification. The discount rate used to determine the present value of the loan portfolio is an estimated market rate that reflects the credit and interest rate risk inherent in the loan portfolio without considering widening credit spreads due to market illiquidity. The estimated maturity is based on the Bank s historical experience with repayments adjusted to estimate the effect of current market conditions. The Allowance is considered a reasonable discount for credit risk. The methods utilized to estimate the fair value of loans do not necessarily represent an exit price.

*Federal Home Loan Bank stock* It is not practical to determine the fair value of FHLB stock due to restrictions placed on its transferability.

*Accrued interest receivable/payable* The carrying amounts of accrued interest, due to their short-term nature, approximate fair value resulting in a Level 2 classification.

*Deposits* Fair values for certificates of deposit have been determined using discounted cash flows. The discount rate used is based on estimated market rates for deposits of similar remaining maturities and are classified as Level 2. The carrying amounts of all other deposits, due to their short-term nature, approximate their fair values and are also classified as Level 2.

*Securities sold under agreements to repurchase* The carrying amount for securities sold under agreements to repurchase generally maturing within ninety days approximates its fair value resulting in a Level 2 classification.

*Federal Home Loan Bank advances* The fair value of the FHLB advances is obtained from the FHLB and is calculated by discounting contractual cash flows using an estimated interest rate based on the current rates available to the Company for debt of similar remaining maturities and collateral terms resulting in a Level 2 classification.

*Subordinated note* The fair value for subordinated debentures is calculated using discounted cash flows based upon current market spreads to London Interbank Borrowing Rate ( LIBOR ) for debt of similar remaining maturities and collateral terms resulting in a Level 2 classification.

The fair value estimates presented herein are based on pertinent information available to management as of the respective period ends. Although management is not aware of any factors that would dramatically affect the estimated fair value amounts, such amounts have not been comprehensively revalued for purposes of these financial statements since that date and, therefore, estimates of fair value may differ significantly from the amounts presented.

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## 7. MORTGAGE BANKING ACTIVITIES

Activity for mortgage loans held for sale was as follows:

| September 30, (in thousands) | 2014 | 2013 |
|---|---|---|
| Balance, January 1 | $ 3,506 | $ 10,614 |
| Origination of mortgage loans held for sale | 54,046 | 263,411 |
| Proceeds from the sale of mortgage loans held for sale | (53,556) | (270,562) |
| Net gain on sale of mortgage loans held for sale | 1,894 | 6,340 |
| Balance, September 30 | $ 5,890 | $ 9,803 |

The following table presents the components of Mortgage Banking income:

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| (in thousands) | 2014 | 2013 | 2014 | 2013 |
| Net gain realized on sale of mortgage loans held for sale | $ 689 | $ 1,633 | $ 1,607 | $ 7,310 |
| Net change in fair value recognized on loans held for sale | (65) | (218) | 59 | (331) |
| Net change in fair value recognized on rate lock commitments | 79 | (44) | 258 | (432) |
| Net change in fair value recognized on forward contracts | 25 | (439) | (30) | (207) |
| Net gain recognized | 728 | 932 | 1,894 | 6,340 |
| Loan servicing income | 482 | 514 | 1,276 | 1,606 |
| Amortization of mortgage servicing rights | (334) | (453) | (996) | (1,811) |
| Change in mortgage servicing rights valuation allowance | | 33 | | 345 |
| Net servicing income recognized | 148 | 94 | 280 | 140 |
| Total Mortgage Banking income | $ 876 | $ 1,026 | $ 2,174 | $ 6,480 |

Activity for capitalized mortgage servicing rights was as follows:

| September 30, (in thousands) | 2014 | 2013 |
|---|---|---|
| Balance, January 1 | $ 5,409 | $ 4,777 |
| Additions | 468 | 2,171 |
| Amortized to expense | (996) | (1,811) |

| | | | | |
|---|---|---|---|---|
| Change in valuation allowance | | | | 345 |
| | | | | |
| Balance, September 30 | $ | 4,881 | $ | 5,482 |

Activity for the valuation allowance for capitalized mortgage servicing rights was as follows:

| **September 30, (in thousands)** | | **2014** | | **2013** |
|---|---|---|---|---|
| Balance, January 1 | $ | | $ | (345) |
| Additions | | | | |
| Reductions credited to operations | | | | 345 |
| | | | | |
| Balance, September 30 | $ | | $ | |

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Other information relating to mortgage servicing rights follows:

| (dollars in thousands) | September 30, 2014 | | December 31, 2013 | |
|---|---|---|---|---|
| Fair value of mortgage servicing rights portfolio | $ | 7,064 | $ | 7,337 |
| Prepayment speed range | | 105% - 462% | | 105% - 550% |
| Discount rate | | 10% | | 10% |
| Weighted average default rate | | 1.50% | | 1.50% |
| Weighted average life in years | | 6.22 | | 6.17 |

Mortgage Banking derivatives used in the ordinary course of business primarily consist of mandatory forward sales contracts and rate lock loan commitments. Mandatory forward contracts represent future commitments to deliver loans at a specified price and date and are used to manage interest rate risk on loan commitments and mortgage loans held for sale. Rate lock loan commitments represent commitments to fund loans at a specific rate. These derivatives involve underlying items, such as interest rates, and are designed to transfer risk. Substantially all of these instruments expire within 90 days from the date of issuance. Notional amounts are amounts on which calculations and payments are based, but which do not represent credit exposure, as credit exposure is limited to the amounts required to be received or paid.

Mandatory forward contracts also contain an element of risk in that the counterparties may be unable to meet the terms of such agreements. In the event the counterparties fail to deliver commitments or are unable to fulfill their obligations, the Bank could potentially incur significant additional costs by replacing the positions at then current market rates. The Bank manages its risk of exposure by limiting counterparties to those banks and institutions deemed appropriate by management and the Board of Directors. The Bank does not expect any counterparty to default on their obligations and therefore, the Bank does not expect to incur any cost related to counterparty default.

The Bank is exposed to interest rate risk on loans held for sale and rate lock loan commitments. As market interest rates fluctuate, the fair value of mortgage loans held for sale and rate lock commitments will decline or increase. To offset this interest rate risk the Bank enters into derivatives, such as mandatory forward contracts to sell loans. The fair value of these mandatory forward contracts will fluctuate as market interest rates fluctuate, and the change in the value of these instruments is expected to largely, though not entirely, offset the change in fair value of loans held for sale and rate lock commitments. The objective of this activity is to minimize the exposure to losses on rate loan lock commitments and loans held for sale due to market interest rate fluctuations. The net effect of derivatives on earnings will depend on risk management activities and a variety of other factors, including: market interest rate volatility; the amount of rate lock commitments that close; the ability to fill the forward contracts before expiration; and the time period required to close and sell loans.

The following table includes the notional amounts and fair values of mortgage loans held for sale and mortgage banking derivatives as of the period ends presented:

| | September 30, 2014 | | | | December 31, 2013 | | | |
|---|---|---|---|---|---|---|---|---|
| (in thousands) | Notional Amount | | Fair Value | | Notional Amount | | Fair Value | |
| **Included in Mortgage loans held for sale:** | | | | | | | | |
| Mortgage loans held for sale | $ | 5,742 | $ | 5,890 | $ | 3,417 | $ | 3,506 |
| | | | | | | | | |
| **Included in other assets:** | | | | | | | | |

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| Rate lock loan commitments | $ | 14,954 | $ | 335 | $ | 4,393 | $ | 77 |
| Mandatory forward contracts | | | | | | 5,571 | | 12 |
| Total included in other assets | $ | 14,954 | $ | 335 | $ | 9,964 | $ | 89 |
| | | | | | | | | |
| **Included in other liabilities:** | | | | | | | | |
| Mandatory forward contracts | $ | 13,211 | $ | 18 | $ | | $ | |

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## 8. INTEREST RATE SWAPS

During the fourth quarter of 2013, the Bank entered into two interest rate swap agreements as part of its interest rate risk management strategy. The Bank designated the swaps as cash flow hedges intended to reduce the variability in cash flows attributable to either FHLB advances tied to the three-month LIBOR or the overall changes in cash flows on certain money market deposit accounts. The counterparty for both swaps met the Bank s credit standards and the Bank believes that the credit risk inherent in the swap contracts is not significant.

The swaps were determined to be fully effective during all periods presented; therefore, no amount of ineffectiveness was included in net income. The aggregate fair value of the swaps is recorded in other assets with changes in fair value recorded in OCI. The amount included in accumulated OCI would be reclassified to current earnings should the hedge no longer be considered effective. The Bank expects the hedges to remain fully effective during the remaining term of the swaps.

Summary information about swaps designated as cash flow hedges as of September 30, 2014 and December 31, 2013 follows:

| **(dollars in thousands)** | | **September 30, 2014** | | **December 31, 2013** |
|---|---|---|---|---|
| Notional amount | $ | 20,000 | $ | 20,000 |
| Weighted average pay rate | | 2.25% | | 2.25% |
| Weighted average receive rate | | 0.19% | | 0.21% |
| Weighted average remaining maturity in years | | 6 | | 7 |
| Unrealized gain (loss) | $ | (203) | $ | 170 |
| Fair value of security pledged as collateral | $ | 341 | $ | |

The following table reflects the total interest expense recorded on these swap transactions in the consolidated statements of income during the three and nine months ended September 30, 2014 and 2013:

| **(in thousands)** | | **Three Months Ended September 30, 2014** | | **2013** | | **Nine Months Ended September 30, 2014** | | **2013** |
|---|---|---|---|---|---|---|---|---|
| Interest expense on deposits related to money market swap transaction | $ | 50 | $ | | $ | 150 | $ | |
| Interest expense on FHLB advances related to FHLB swap transaction | | 54 | | | | 153 | | |
| Total interest expense on swap transactions | $ | 104 | $ | | $ | 303 | $ | |

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The following tables present the net gains (losses) recorded in accumulated OCI and the consolidated statements of income relating to the swaps for the three and nine months ended September 30, 2014:

| **Three Months Ended September 30, 2014 (in thousands)** | **Amount of Gain (Loss) Recognized in Other Comprehensive Income on Derivative (Effective Portion)** | **Amount of Gain (Loss) Reclassified from Accumulated Other Comprehensive Income on Derivative (Effective Portion)** | **Amount of Gain (Loss) Recognized in Income on Derivative (Ineffective Portion)** |
|---|---|---|---|
| Cash flow hedges - interest rate swaps | $ 28 | $ (104) | $ |

| **Nine Months Ended September 30, 2014 (in thousands)** | **Amount of Gain (Loss) Recognized in Other Comprehensive Income on Derivative (Effective Portion)** | **Amount of Gain (Loss) Reclassified from Accumulated Other Comprehensive Income on Derivative (Effective Portion)** | **Amount of Gain (Loss) Recognized in Income on Derivative (Ineffective Portion)** |
|---|---|---|---|
| Cash flow hedges - interest rate swaps | $ (676) | $ (303) | $ |

The following table reflects the cash flow hedges included in the consolidated balance sheet as of September 30, 2014 and December 31, 2013:

| | **September 30, 2014** | | **December 31, 2013** | |
|---|---|---|---|---|
| **(in thousands)** | **Notional Amount** | **Fair Value** | **Notional Amount** | **Fair Value** |
| **Fair value included in other assets:** | | | | |
| Cash flow hedges - interest rate swaps | $ | $ | $ 20,000 | $ 170 |
| **Fair value included in other liabilities:** | | | | |
| Cash flow hedges - interest rate swaps | $ 20,000 | $ 203 | $ | $ |

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## 9. OFF BALANCE SHEET RISKS, COMMITMENTS AND CONTINGENT LIABILITIES

The Bank, in the normal course of business, is party to financial instruments with off balance sheet risk. These financial instruments primarily include commitments to extend credit and standby letters of credit. The contract or notional amounts of these instruments reflect the potential future obligations of the Bank pursuant to those financial instruments. Creditworthiness for all instruments is evaluated on a case by case basis in accordance with the Bank s credit policies. Collateral from the customer may be required based on the Bank s credit evaluation of the customer and may include business assets of commercial customers, as well as personal property and real estate of individual customers or guarantors.

The Bank also extends binding commitments to customers and prospective customers. Such commitments assure a borrower of financing for a specified period of time at a specified rate. Additionally, the Bank makes binding purchase commitments to third party loan correspondent originators. These commitments assure that the Bank will purchase a loan from such correspondent originators at a specific price for a specific period of time. The risk to the Bank under such loan commitments is limited by the terms of the contracts. For example, the Bank may not be obligated to advance funds if the customer s financial condition deteriorates or if the customer fails to meet specific covenants.

An approved but unfunded loan commitment represents a potential credit risk and a liquidity risk, since the Bank s customer(s) may demand immediate cash that would require funding. In addition, unfunded loan commitments represent interest rate risk as market interest rates may rise above the rate committed to the Bank s customer. Since a portion of these loan commitments normally expire unused, the total amount of outstanding commitments at any point in time may not require future funding.

The table below presents the Bank s commitments, exclusive of Mortgage Banking loan commitments for each year ended:

| **(in thousands)** | | **September 30, 2014** | | **December 31, 2013** |
|---|---|---|---|---|
| Unused warehouse lines of credit | $ | 209,916 | $ | 208,424 |
| Unused home equity lines of credit | | 237,632 | | 230,361 |
| Unused loan commitments - other | | 183,357 | | 178,776 |
| Commitments to purchase loans | | 76,913 | | |
| Standby letters of credit | | 12,679 | | 2,308 |
| FHLB letters of credit | | 750 | | 3,200 |
| Total commitments | $ | 721,247 | $ | 623,069 |

Standby letters of credit are conditional commitments issued by the Bank to guarantee the performance of a customer to a third party. The terms and risk of loss involved in issuing standby letters of credit are similar to those involved in issuing loan commitments and extending credit. In addition to credit risk, the Bank also has liquidity risk associated with standby letters of credit because funding for these obligations could be required immediately. The Bank does not deem this risk to be material.

At September 30, 2014 and December 31, 2013, the Bank had letters of credit from the FHLB issued on behalf of a RB&T client. This letter of credit was used as a credit enhancement for client bond offerings and reduced RB&T s available borrowing line at the FHLB. The Bank uses a blanket pledge of eligible real estate loans to secure these letters of credit.

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**10. EARNINGS PER SHARE**

Class A and Class B shares participate equally in undistributed earnings. The difference in earnings per share between the two classes of common stock results solely from the 10% per share cash dividend premium paid on Class A Common Stock over that paid on Class B Common Stock.

A reconciliation of the combined Class A and Class B Common Stock numerators and denominators of the earnings per share and diluted earnings per share computations is presented below:

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| **(in thousands, except per share data)** | **2014** | **2013** | **2014** | **2013** |
| Net income | $ 5,246 | $ 4,603 | $ 23,552 | $ 24,078 |
| | | | | |
| Weighted average shares outstanding | 20,797 | 20,787 | 20,795 | 20,811 |
| Effect of dilutive securities | 94 | 140 | 96 | 94 |
| Average shares outstanding including dilutive securities | 20,891 | 20,927 | 20,891 | 20,905 |
| | | | | |
| Basic earnings per share: | | | | |
| Class A Common Share | $ 0.25 | $ 0.22 | $ 1.14 | $ 1.16 |
| Class B Common Share | $ 0.24 | $ 0.21 | $ 1.09 | $ 1.12 |
| | | | | |
| Diluted earnings per share: | | | | |
| Class A Common Share | $ 0.25 | $ 0.22 | $ 1.13 | $ 1.16 |
| Class B Common Share | $ 0.24 | $ 0.21 | $ 1.08 | $ 1.11 |

Stock options excluded from the detailed earnings per share calculation because their impact was antidilutive are as follows:

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| **(in thousands)** | **2014** | **2013** | **2014** | **2013** |
| Antidilutive stock options | 16 | 14 | 16 | 113 |
| Average antidilutive stock options | 16 | 10 | 15 | 110 |

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## 11. OTHER COMPREHENSIVE INCOME

OCI components and related tax effects were as follows:

| (in thousands) | Three Months Ended September 30, 2014 | Three Months Ended September 30, 2013 | Nine Months Ended September 30, 2014 | Nine Months Ended September 30, 2013 |
|---|---|---|---|---|
| **Available for Sale Securities:** | | | | |
| Unrealized gain (loss) on securities available for sale | $ (10) | $ (198) | $ 2,618 | $ (3,163) |
| Change in unrealized gain on securities available for sale for which a portion of an other-than-temporary impairment has been recognized in earnings | 65 | (4) | 434 | 418 |
| Net unrealized gains (losses) | 55 | (202) | 3,052 | (2,745) |
| Tax effect | (21) | 71 | (1,070) | 962 |
| Net of tax | 34 | (131) | 1,982 | (1,783) |
| | | | | |
| **Cash Flow Hedges:** | | | | |
| Change in fair value of derivatives used for cash flow hedges | 28 | | (676) | |
| Reclassification adjustment for losses realized in income | 104 | | 303 | |
| Net unrealized gains (losses) | 132 | | (373) | |
| Tax effect | (45) | | 131 | |
| Net of tax | 87 | | (242) | |
| | | | | |
| Total other comprehensive income, net of tax | $ 121 | $ (131) | $ 1,740 | $ (1,783) |

The following is a summary of the accumulated OCI balances, net of tax for the nine months ended September 30, 2014 and 2013:

| (in thousands) | Balance at December 31, 2013 | Change for Nine Months ending September 30, 2014 | Balance at September 30, 2014 |
|---|---|---|---|
| Unrealized gain on securities available for sale | $ 2,526 | $ 1,700 | $ 4,226 |
| Unrealized gain on security available for sale for which a portion of an other-than-temporary impairment has been recognized in earnings | 484 | 282 | 766 |
| Unrealized gain (loss) on cash flow hedge | 111 | (242) | (131) |
| Total unrealized gain | $ 3,121 | $ 1,740 | $ 4,861 |

| (in thousands) | Balance at December 31, 2012 | Change for Nine Months ending September 30, 2013 | Balance at September 30, 2013 |
|---|---|---|---|
| Unrealized gain (loss) on securities available for sale | $ 5,610 | $ (2,055) | $ 3,555 |
| Unrealized gain on security available for sale for which a portion of an other-than-temporary impairment has been recognized in earnings | 2 | 272 | 274 |

| | | | | | | |
|---|---|---|---|---|---|---|
| Total unrealized gain (loss) | $ | 5,612 | $ | (1,783) | $ | 3,829 |

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**12. SEGMENT INFORMATION**

Reportable segments are determined by the type of products and services offered and the level of information provided to the chief operating decision maker, who uses such information to review performance of various components of the business (such as banking centers and business units), which are then aggregated if operating performance, products/services, and customers are similar.

As of September 30, 2014, the Company was divided into three distinct business operating segments: Traditional Banking, Mortgage Banking and Republic Processing Group ( RPG ). Along with the Tax Refund Solutions ( TRS ) division, Republic Payment Solutions ( RPS ) and Republic Credit Solutions ( RCS ) operate as divisions of the RPG segment.

All divisions of the RPG segment operate through the Bank. The TRS division facilitates the receipt and payment of federal and state tax refund products. The RPS division is an issuing bank offering general purpose reloadable prepaid debit cards through third party program managers. The RCS division is piloting short-term consumer credit products.

Loans, investments and deposits provide the majority of the net revenue from Traditional Banking operations, while servicing fees and loan sales provide the majority of revenue from Mortgage Banking operations. Net refund transfer fees provide the majority of revenue for RPG. All Company operations are domestic.

The accounting policies used for Republic s reportable segments are the same as those described in the summary of significant accounting policies in the Company s 2013 Annual Report on Form 10-K. Segment performance is evaluated using operating income. Goodwill is not allocated. Income taxes are generally allocated based on income before income tax expense when specific segment allocations cannot be reasonably made. Transactions among reportable segments are made at carrying value.

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Segment information for the three months ended September 30, 2014 and 2013 follows:

| | Three Months Ended September 30, 2014 | | | |
|---|---|---|---|---|
| **(dollars in thousands)** | **Traditional Banking** | **Mortgage Banking** | **Republic Processing Group** | **Total Company** |
| Net interest income | $ 28,337 | $ 38 | $ 67 | $ 28,442 |
| Provision for loan losses | 1,542 | | (32) | 1,510 |
| Net refund transfer fees | | | (133) | (133) |
| Mortgage banking income | | 876 | | 876 |
| Other non-interest income | 6,073 | 41 | 287 | 6,401 |
| Total non-interest income | 6,073 | 917 | 154 | 7,144 |
| Total non-interest expenses | 22,982 | 754 | 2,086 | 25,822 |
| Income (loss) before income tax expense | 9,886 | 201 | (1,833) | 8,254 |
| Income tax expense (benefit) | 3,600 | 71 | (663) | 3,008 |
| Net income (loss) | $ 6,286 | $ 130 | $ (1,170) | $ 5,246 |
| Segment end of period assets | $ 3,598,186 | $ 11,150 | $ 16,283 | $ 3,625,619 |
| Net interest margin | 3.38% | NM | NM | 3.38% |

| | Three Months Ended September 30, 2013 | | | |
|---|---|---|---|---|
| **(dollars in thousands)** | **Traditional Banking** | **Mortgage Banking** | **Republic Processing Group** | **Total Company** |
| Net interest income | $ 28,390 | $ 130 | $ 19 | $ 28,539 |
| Provision for loan losses | 2,257 | | (57) | 2,200 |
| Net refund transfer fees | | | 152 | 152 |
| Mortgage banking income | | 1,026 | | 1,026 |
| Other non-interest income | 6,203 | 19 | 99 | 6,321 |
| Total non-interest income | 6,203 | 1,045 | 251 | 7,499 |
| Total non-interest expenses | 22,197 | 768 | 3,320 | 26,285 |
| Income (loss) before income tax expense | 10,139 | 407 | (2,993) | 7,553 |
| Income tax expense (benefit) | 3,856 | 142 | (1,048) | 2,950 |
| Net income (loss) | $ 6,283 | $ 265 | $ (1,945) | $ 4,603 |
| Segment end of period assets | $ 3,305,689 | $ 15,697 | $ 10,495 | $ 3,331,881 |
| Net interest margin | 3.54% | NM | NM | 3.54% |

*Segment assets are reported as of the respective period ends while income and margin data are reported for the respective periods.*

*NM Not Meaningful*

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Segment information for the nine months ended September 30, 2014 and 2013 follows:

| | Nine Months Ended September 30, 2014 | | | |
|---|---|---|---|---|
| **(dollars in thousands)** | **Traditional Banking** | **Mortgage Banking** | **Republic Processing Group** | **Total Company** |
| Net interest income | $ 82,891 | $ 133 | $ 272 | $ 83,296 |
| Provision for loan losses | 2,012 | | (512) | 1,500 |
| Net refund transfer fees | | | 16,091 | 16,091 |
| Mortgage banking income | | 2,174 | | 2,174 |
| Other non-interest income | 18,124 | 186 | 1,412 | 19,722 |
| Total non-interest income | 18,124 | 2,360 | 17,503 | 37,987 |
| Total non-interest expenses | 71,389 | 2,977 | 8,986 | 83,352 |
| Income (loss) before income tax expense | 27,614 | (484) | 9,301 | 36,431 |
| Income tax expense (benefit) | 9,594 | (169) | 3,454 | 12,879 |
| Net income (loss) | $ 18,020 | $ (315) | $ 5,847 | $ 23,552 |
| Segment end of period assets | $ 3,598,186 | $ 11,150 | $ 16,283 | $ 3,625,619 |
| Net interest margin | 3.34% | NM | NM | 3.32% |

| | Nine Months Ended September 30, 2013 | | | |
|---|---|---|---|---|
| **(dollars in thousands)** | **Traditional Banking** | **Mortgage Banking** | **Republic Processing Group** | **Total Company** |
| Net interest income | $ 85,957 | $ 388 | $ 91 | $ 86,436 |
| Provision for loan losses | 3,276 | | (796) | 2,480 |
| Net refund transfer fees | | | 13,849 | 13,849 |
| Mortgage banking income | | 6,480 | | 6,480 |
| Bargain purchase gain - FCB | 1,324 | | | 1,324 |
| Other non-interest income | 18,151 | 102 | 792 | 19,045 |
| Total non-interest income | 19,475 | 6,582 | 14,641 | 40,698 |
| Total non-interest expenses | 72,713 | 2,537 | 11,927 | 87,177 |
| Income before income tax expense | 29,443 | 4,433 | 3,601 | 37,477 |
| Income tax expense | 10,588 | 1,551 | 1,260 | 13,399 |
| Net income | $ 18,855 | $ 2,882 | $ 2,341 | $ 24,078 |
| Segment end of period assets | $ 3,305,689 | $ 15,697 | $ 10,495 | $ 3,331,881 |
| Net interest margin | 3.57% | NM | NM | 3.55% |

*Segment assets are reported as of the respective period ends while income and margin data are reported for the respective periods.*

*NM Not Meaningful*

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**Item 2. Management s Discussion and Analysis of Financial Condition and Results of Operations.**

Management s Discussion and Analysis of Financial Condition and Results of Operations of Republic Bancorp, Inc. ( Republic or the Company ) analyzes the major elements of Republic s consolidated balance sheets and statements of income. Republic, a bank holding company headquartered in Louisville, Kentucky, is the parent company of Republic Bank & Trust Company ( RB&T or the Bank ) and Republic Insurance Services, Inc. (the Captive ). RB&T is a Kentucky-based, state chartered non-member financial institution. The Captive, which was formed during the third quarter of 2014, is a wholly-owned insurance subsidiary of the Company that provides property and casualty insurance coverage to the Company and the Bank. The Captive provides insurance to five other third party insurance captives for which insurance may not be currently available or economically feasible in today s insurance marketplace. Republic Bancorp Capital Trust is a Delaware statutory business trust that is a 100%-owned unconsolidated finance subsidiary of Republic Bancorp, Inc. Management s Discussion and Analysis of Financial Condition and Results of Operations of Republic should be read in conjunction with Part I Item 1 *Financial Statements.*

During the second quarter of 2014, Republic Bank, the Company s wholly-owned, federally chartered savings institution, was legally merged into RB&T. The merged institution operates under the name Republic Bank & Trust Company. The merger did not materially impact the Company s consolidated financial statements.

As used in this filing, the terms Republic, the Company, we, our and us refer to Republic Bancorp, Inc., and, where the context requires, Republic Bancorp, Inc. and its subsidiaries; the term the Bank refers to the Company s subsidiary bank, RB&T; and the term the Captive refers to the Company s subsidiary insurance company, Republic Insurance Services, Inc.

Forward-looking statements involve known and unknown risks, uncertainties and other factors that may cause actual results, performance or achievements to be materially different from future results, performance or achievements expressed or implied by the forward-looking statements. Actual results may differ materially from those expressed or implied as a result of certain risks and uncertainties, including, but not limited to: changes in political and economic conditions; interest rate fluctuations; competitive product and pricing pressures; equity and fixed income market fluctuations; personal and corporate customers bankruptcies; inflation; recession; acquisitions and integrations of acquired businesses; technological changes; changes in law and regulations or the interpretation and enforcement thereof; changes in fiscal, monetary, regulatory and tax policies; monetary fluctuations; success in gaining regulatory approvals when required; information security breaches or cyber security attacks involving either the Company or one of the Company s third party service providers; as well as other risks and uncertainties reported from time to time in the Company s filings with the Securities and Exchange Commission ( SEC ) included under Part 1 Item 1A *Risk Factors* of the Company s 2013 Annual Report on Form 10-K.

Broadly speaking, forward-looking statements include:

- projections of revenue, income, expenses, losses, earnings per share, capital expenditures, dividends, capital structure or other financial items;
- descriptions of plans or objectives for future operations, products or services;
- forecasts of future economic performance; and
- descriptions of assumptions underlying or relating to any of the foregoing.

The Company may make forward-looking statements discussing management s expectations about various matters, including:

- loan delinquencies; non-performing, classified, or impaired loans; and troubled debt restructurings ( TDR s);
- further developments in the Bank s ongoing review of and efforts to resolve possible problem credit relationships, which could result in, among other things, additional provisions for loan losses;
- future credit quality, credit losses and the overall adequacy of the Allowance for Loan Losses ( Allowance );
- potential write-downs of other real estate owned ( OREO );
- future short-term and long-term interest rates and the respective impact on net interest income, net interest spread, net income, liquidity, capital and economic value of equity ( EVE );
- the future impact of Company strategies to mitigate interest rate risk;
- future long-term interest rates and their impact on the demand for Mortgage Banking products, warehouse lines of credit and correspondent lending;
- the future value of mortgage servicing rights ( MSR s);
- the future financial performance of the Tax Refund Solutions ( TRS ) division of the Republic Processing Group ( RPG ) segment;

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- future Refund Transfer ( RT ) volume for TRS;
- the future net revenue associated with RTs at TRS;
- the future financial performance of the Republic Payment Solutions ( RPS ) division of RPG;
- the future financial performance of the Republic Credit Solutions ( RCS ) division of RPG;
- the potential impairment of investment securities;
- the growth in the Bank s loan portfolio, in general;
- the growth in the Bank s Mortgage Warehouse and Correspondent Lending portfolios;
- the volatility of the Bank s Mortgage Warehouse portfolio outstanding balances;
- the Bank s ability to maintain and/or grow deposits;
- the concentrations and volatility of the Bank s securities sold under agreements to repurchase;
- the Company s ability to successfully implement strategic plans, including, but not limited to, those related to future business acquisitions, in general, and the Bank s two FDIC-assisted acquisitions from 2012;
- future accretion of discounts on loans acquired in the Bank s two FDIC-assisted acquisitions from 2012 and the effect of such accretion on the Bank s net interest income and net interest margin;
- future amortization of premiums on loans acquired through the Bank s Correspondent Lending division and the effect of such amortization on the Bank s net interest income and net interest margin;
- the extent to which regulations written and implemented by the Federal Bureau of Consumer Financial Protection ( CFPB ), and other federal, state and local governmental regulation of consumer lending and related financial products and services, may limit or prohibit the operation of the Company s business;
- financial services reform and other current, pending or future legislation or regulation that could have a negative effect on the Company s revenue and businesses, including but not limited to, Basel III capital reforms; the Dodd-Frank Act; and legislation and regulation relating to overdraft fees (and changes to the Bank s overdraft practices as a result thereof), debit card interchange fees, credit cards, and other bank services;
- the impact of new accounting pronouncements;
- legal and regulatory matters including results and consequences of regulatory guidance, litigation, administrative proceedings, rule-making, interpretations, actions and examinations;
- future capital expenditures; and
- the strength of the U.S. economy in general and the strength of the local economies in which the Company conducts operations.

Forward-looking statements discuss matters that are not historical facts. As forward-looking statements discuss future events or conditions, the statements often include words such as anticipate, believe, estimate, expect, intend, plan, project, target, can, could, may, similar expressions. Do not rely on forward-looking statements. Forward-looking statements detail management s expectations regarding the future and are not guarantees. Forward-looking statements are assumptions based on information known to management only as of the date the statements are made and management may not update them to reflect changes that occur subsequent to the date the statements are made.

*See additional discussion under Part I Item 1 Business and Part I Item 1A Risk Factors of the Company s 2013 Annual Report on Form 10-K.*

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**BUSINESS SEGMENT COMPOSITION**

As of September 30, 2014, the Company was divided into three distinct business operating segments: Traditional Banking, Mortgage Banking and Republic Processing Group ( RPG ). Along with the Tax Refund Solutions ( TRS ) division, Republic Payment Solutions ( RPS ) and Republic Credit Solutions ( RCS ) also operate as divisions of the RPG segment. The RPS and RCS divisions are considered immaterial for separate and independent segment reporting. Net income, total assets and net interest margin by segment for the three and nine months ended September 30, 2014 and 2013 are presented below:

| | Three Months Ended September 30, 2014 | | | |
|---|---|---|---|---|
| (in thousands) | Traditional Banking | Mortgage Banking | Republic Processing Group | Total Company |
| Net income | $ 6,286 | $ 130 | $ (1,170) | $ 5,246 |
| Segment assets | 3,598,186 | 11,150 | 16,283 | 3,625,619 |
| Net interest margin | 3.38% | NM | NM | 3.38% |

| | Three Months Ended September 30, 2013 | | | |
|---|---|---|---|---|
| (in thousands) | Traditional Banking | Mortgage Banking | Republic Processing Group | Total Company |
| Net income | $ 6,283 | $ 265 | $ (1,945) | $ 4,603 |
| Segment assets | 3,305,689 | 15,697 | 10,495 | 3,331,881 |
| Net interest margin | 3.54% | NM | NM | 3.54% |

| | Nine Months Ended September 30, 2014 | | | |
|---|---|---|---|---|
| (in thousands) | Traditional Banking | Mortgage Banking | Republic Processing Group | Total Company |
| Net income | $ 18,020 | $ (315) | $ 5,847 | $ 23,552 |
| Segment assets | 3,598,186 | 11,150 | 16,283 | 3,625,619 |
| Net interest margin | 3.34% | NM | NM | 3.32% |

| | Nine Months Ended September 30, 2013 | | | |
|---|---|---|---|---|
| (in thousands) | Traditional Banking | Mortgage Banking | Republic Processing Group | Total Company |
| Net income | $ 18,855 | $ 2,882 | $ 2,341 | $ 24,078 |
| Segment assets | 3,305,689 | 15,697 | 10,495 | 3,331,881 |
| Net interest margin | 3.57% | NM | NM | 3.55% |

*Segment assets are reported as of the respective period ends while income and margin data are reported for the respective periods.*

*NM Not Meaningful*

*For expanded segment financial data see Footnote 12 Segment Information of Part I Item 1 Financial Statements.*

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**(I) Traditional Banking segment**

As of September 30, 2014, in addition to an Internet delivery channel, Republic had 42 full-service banking centers with locations as follows:

- Kentucky 33
- Metropolitan Louisville 20
- Central Kentucky 8
- Elizabethtown 1
- Frankfort 1
- Georgetown 1
- Lexington 4
- Shelbyville 1
- Western Kentucky 2
- Owensboro 2
- Northern Kentucky 3
- Covington 1
- Florence 1
- Independence 1
- Southern Indiana 3
- Floyds Knobs 1
- Jeffersonville 1
- New Albany 1
- Metropolitan Tampa, Florida 3
- Metropolitan Cincinnati, Ohio 1

- Metropolitan Nashville, Tennessee 2

Republic s headquarters are located in Louisville, which is the largest city in Kentucky based on population.

The Bank principally markets its lending products and services through the following delivery channels:

**Retail Mortgage Lending** Primarily through its retail banking centers, the Bank originates single family, first lien residential real estate loans, home equity loans and home equity lines of credit. Such loans are generally collateralized by owner occupied property, predominately located in the Bank s primary market areas.

**Commercial Lending** The Bank s commercial real estate ( CRE ) loans are generally made to small-to-medium sized businesses in amounts up to 80% or 85% loan-to-value ( LTV ), depending on the market. LTV is based on the lesser of the appraised value or purchase price of the property.

A broad range of short-to-medium-term collateralized commercial and industrial ( C&I ) loans and leases are made available to businesses for working capital, business expansion (including acquisitions of real estate and improvements), and the purchase of equipment or machinery. These often represent term loans, lines of credit and equipment and receivables financing.

**Construction and Land Development Lending** The Bank originates residential construction real estate loans to finance the construction of single family dwellings. Construction loans may be made to consumers or to developers and builders to construct single family dwellings under contract.

The Bank also makes land development loans to real estate developers for the acquisition, development and construction of commercial projects.

**Consumer Lending** Traditional consumer loans made by the Bank include home improvement and home equity loans, as well as other secured and unsecured personal loans, in addition to credit cards. With the exception of home equity loans, which are actively marketed in conjunction with single family, first lien residential real estate loans, other traditional consumer loan products, while available, are not and have not been actively promoted in the Bank s markets.

**Internet Lending** The Bank accepts online loan applications through its website, www.republicbank.com. Loans originated through the Internet are primarily within the Bank s traditional markets of Kentucky and Indiana.

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**Warehouse Lines of Credit** The Bank provides short-term, revolving credit facilities to mortgage bankers across the Nation through mortgage warehouse lines of credit.

**Correspondent Lending** The Bank began acquiring single family, first lien mortgage loans for investment through its Correspondent Lending division in May 2014. Correspondent Lending generally involves the Bank acquiring, primarily from its Mortgage Warehouse clients, closed loans that meet the Bank s specifications. Substantially all loans purchased through the Correspondent Lending channel are purchased at a premium. Premiums on loans held for investment acquired though the Correspondent Lending division are amortized into interest income on the level-yield method over the expected life of the loan. Loans acquired through the Correspondent Lending division generally reflect borrowers outside of the Bank s historical market footprint. As of September 30, 2014, a substantial majority of loans originated through the Company s Correspondent Lending division were secured by single family residences located in the state of California.

**Private Banking** The Bank provides financial products and services to high net worth individuals through its Private Banking Department. The Bank s Private Banking officers have extensive banking experience and are trained to meet the unique financial needs of high net worth individuals.

**Treasury Management Services** The Bank provides various deposit products designed for commercial business customers located throughout its market areas. Lockbox processing, remote deposit capture, business on-line banking, account reconciliation and Automated Clearing House ( ACH ) processing are additional services offered to commercial businesses through the Bank s Treasury Management Department.

**Internet Banking** The Bank expands its market penetration and service delivery by offering customers Internet banking services and products through its website, www.republicbank.com.

**Other Banking Services** The Bank also provides trust, title insurance and other financial institution related products and services.

*See additional detail regarding the Traditional Banking segment under Footnote 12 Segment Information of Part I Item 1 Financial Statements.*

**(II) Mortgage Banking segment**

Mortgage Banking activities primarily include 15-, 20- and 30-year fixed-term single family, first lien residential real estate loans that are sold into the secondary market, primarily to the Federal Home Loan Mortgage Corporation ( FHLMC or Freddie Mac ). The Bank typically retains servicing on loans sold into the secondary market. Administration of loans with servicing retained by the Bank includes collecting principal and interest payments, escrowing funds for property taxes and insurance and remitting payments to secondary market investors. A fee is received by the Bank for performing these standard servicing functions.

*See additional detail regarding Mortgage Banking under Footnote 7 Mortgage Banking Activities and Footnote 12 Segment Information of Part I Item 1 Financial Statements.*

**(III) Republic Processing Group segment**

All divisions of the RPG segment operate through the Bank. Nationally, RPG facilitates the receipt and payment of federal and state tax refund products under the TRS division. The RPS division is an issuing bank offering general purpose reloadable prepaid debit cards through third party program managers. The RCS division is piloting short-term consumer credit products.

*See additional detail regarding RPG under Footnote 12 Segment Information of Part I Item 1 Financial Statements.*

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**OVERVIEW (Three Months Ended September 30, 2014 Compared to Three Months Ended September 30, 2013)**

Net income for the three months ended September 30, 2014 was $5.2 million, representing an increase of $643,000, or 14%, compared to the same period in 2013. Diluted earnings per Class A Common Share were $0.25 and $0.22 for the quarters ended September 30, 2014 and 2013.

Within the Company s Traditional Banking segment, net income for the third quarter of 2014 was $6.3 million, approximately equivalent to the same period in 2013.

The Company s Mortgage Banking segment reflected net income of $130,000 for the third quarter of 2014 compared to $265,000 for the same period in 2013.

The TRS division of the RPG segment derives substantially all of its revenue during the first and second quarters of the year and historically operates at a net loss during the second half of the year, as the Company prepares for the upcoming tax season.

The RPG segment reflected a third quarter 2014 net loss of $1.2 million, an improvement of $775,000, or 40%, over a $1.9 million net loss for the same period in 2013.

Other general highlights by segment for the quarter ended September 30, 2014 consisted of the following:

**Traditional Banking segment**

- Net income increased $3,000, or less than 1%, for the third quarter of 2014 compared to the same period in 2013.

- Provision for loan losses ( Provision ) was $1.5 million for the quarter ended September 30, 2014 compared to $2.3 million for the same period in 2013.

- Net interest income was $28.3 million for the third quarter of 2014 compared to $28.4 million for the same period in 2013. The Traditional Banking segment net interest margin decreased 16 basis points for the quarter ended September 30, 2014 to 3.38%.

- Total non-interest income decreased $130,000, or 2%, for the third quarter of 2014 compared to the same period in 2013.

- Total non-interest expense increased $785,000, or 4%, during the third quarter of 2014 compared to the third quarter of 2013.

- Gross Traditional Bank loans, excluding outstanding Mortgage Warehouse lines, increased by $155 million, or 6%, during the third quarter of 2014 compared to a decline of $12 million, or less than 1% during the same period in 2013. Growth during the third quarter of 2014 was primarily driven by the Traditional Bank s Correspondent Lending division, which acquired $128 million of loans during the quarter.

- Outstanding Mortgage Warehouse lines of credit increased by $28 million, or 12%, during the third quarter of 2014 compared to a decline of $55 million, or 31% during the same period in 2013.

**Mortgage Banking segment**

- Within the Mortgage Banking segment, mortgage banking income decreased $150,000, or 15%, during the third quarter of 2014 compared to the same period in 2013.

- Overall, Republic s proceeds from the sale of secondary market loans totaled $22 million during the third quarter of 2014 compared to $71 million during the same period in 2013. Increases in long-term interest rates, which began to occur in May 2013, continued to negatively impact demand for mortgage refinances in particular, with this impact expected to continue through 2014.

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**Republic Processing Group segment**

- Net loss for RPG improved $775,000, or 40%, for the third quarter of 2014 compared to the same period in 2013.

- While RB&T permanently discontinued the offering of its Refund Anticipation Loan ( RAL ) product effective April 30, 2012, the Bank still records recoveries on RAL loans charged-off in prior periods. Additionally, RPG provides for losses on short-term consumer loans originated through the RCS division. RPG recorded a net credit to the Provision of $32,000 for the third quarter of 2014 compared to a $57,000 credit for the same period in 2013.

- Non-interest income was $154,000 for the third quarter of 2014 compared to $251,000 for the same period in 2013.

- Non-interest expenses were $2.1 million for the third quarter of 2014 compared to $3.3 million for the same period in 2013. The improved performance was primarily driven by the TRS division, which experienced a $902,000 decrease in legal fees for the quarter, as the Company incurred substantial legal expenses during the third quarter of 2013 related to contract disputes with its previously two largest product providers and the Bank s unsuccessful effort to acquire H&R Block Bank.

**RESULTS OF OPERATIONS (Three Months Ended September 30, 2014 Compared to Three Months Ended September 30, 2013)**

**Net Interest Income**

Banking operations are significantly dependent upon net interest income. Net interest income is the difference between interest income on interest-earning assets, such as loans and investment securities, and interest expense on liabilities used to fund those assets, such as interest-bearing deposits, securities sold under agreements to repurchase and Federal Home Loan Bank ( FHLB ) advances. Net interest income is impacted by both changes in the amount and composition of interest-earning assets and interest-bearing liabilities, as well as market interest rates.

Total Company net interest income decreased $97,000, or less than 1%, for the third quarter of 2014 compared to the same period in 2013. The total Company net interest margin decreased from 3.54% during the third quarter of 2013 to 3.38% for the third quarter of 2014. The minimal decrease in the Company s net interest income, as compared to the relatively large decrease in net interest margin, primarily reflects two main drivers: the first a continuing general decline in the Company s interest-earning asset yields without a similar offsetting decline in funding costs; the second a $219 million, or 9%, increase in the total Company s average loans over the past 12 months. The most significant components affecting the total Company s net interest income by business segment were as follows:

**Traditional Banking segment**

Net interest income within the Traditional Banking segment decreased $53,000, or less than 1%, for the quarter ended September 30, 2014 compared to the same period in 2013. The Traditional Banking net interest margin decreased 16 basis points from the same period in 2013 to 3.38%. The decrease in the Traditional Bank s net interest income and net interest margin during 2014 was primarily attributable to the following factors:

- Excluding the mortgage warehouse loan portfolio (discussed below), the Traditional Banking segment continued to experience downward repricing in its loans and investment portfolios during the third quarter of 2014. This downward repricing resulted from the ongoing paydowns and early payoffs of higher earning assets with new originations and purchases being made into lower yielding earning assets. As a result, the yield in both the loan and investment portfolios declined from the third quarter 2013 compared to the same period in 2014.

- Traditional Bank loans, excluding mortgage warehouse loans, experienced yield compression of 46 basis points from the third quarter of 2013 compared to the same period in 2014. Average loans outstanding, excluding mortgage warehouse loans, were $2.43 billion with a weighted average yield of 4.93% during the third quarter of 2013 compared to $2.55 billion with a weighted average yield of 4.47% during the same period 2014. The overall effect of these changes in rate and volume was a decline of $1.6 million in interest income.

- Traditional Bank taxable investment securities experienced yield compression of 11 basis points from the third quarter of 2013 compared to the same period in 2014. Average taxable investment securities outstanding were $531 million with a weighted average yield of 1.74% during the third quarter of 2013 compared to $539 million with a weighted average yield of 1.63% during the same period in 2014. The overall effect of these changes in rate and volume was a decrease of $105,000 in interest income.

- Average outstanding mortgage warehouse lines of credit increased $115 million from the third quarter of 2013 to the same period in 2014. Average mortgage warehouse loans outstanding were $243 million during the third quarter of 2014 with a weighted-average yield of 3.92%, compared to average loans outstanding of $128 million with a weighted-average yield of 4.46% for the same period in 2013. As a result of these changes in rate and volume, interest income on mortgage warehouse lines of credit increased $947,000 during the third quarter of 2014 compared to the same period in 2013. *See additional detail regarding Mortgage Warehouse lines of credit under the section titled Loan Portfolio in this section of the filing.*

- Average FHLB advances decreased $17 million from the third quarter of 2013 to the same period in 2014. Average FHLB advances were $576 million during the third quarter of 2014 with a weighted-average cost of 2.16%, compared to average advances of $593 million with a weighted-average cost of 2.56% for the same period in 2013. As a result of these changes in rate and volume, interest expense on FHLB advances decreased $672,000 during the third quarter of 2014 compared to the same period in 2013.

- Net interest income continued to benefit from discount accretion on loans acquired from the Bank s 2012 FDIC-assisted acquisitions, although to a lesser degree than it has in the past. Altogether, this discount accretion totaled $732,000 for the third quarter of 2014 compared to $2.0 million for the third quarter of 2013, contributing nine and 25 basis points, respectively, to the net interest margin for these periods. Management projects accretion of loan discounts related to the 2012 FDIC-assisted acquisitions to be approximately $500,000 for the fourth quarter of 2014. Similar to the first three quarters of 2014, the accretion estimate for the fourth quarter of 2014 could be positively impacted by positive workout arrangements in which the Bank receives loan payoffs for amounts greater than the loans respective carrying values.

The downward repricing of interest-earning assets is expected to continue to cause compression in Republic s net interest income and net interest margin in the near future. Because the Federal Funds Target Rate ( FFTR ), the index which many of the Bank s short-term deposit rates track, has remained at a target range between 0.00% and 0.25%, no future FFTR decreases from the Federal Open Market Committee of the Federal Reserve Bank ( FRB ) are possible, exacerbating the compression to the Bank s net interest income and net interest-bearing margin caused by its repricing loans and investments.

In addition to the margin compression challenges noted above, the Bank has employed certain strategies over the past 18 months to improve its net interest income. These strategies have expectedly had a negative impact on the Bank s interest rate risk position in a rising rate environment. Management s future strategies to improve its net interest income will likely continue to be impacted by the Bank s overall interest rate risk position at that time.

The Bank is unable to precisely determine its net interest income and net interest margin in the future because several factors remain unknown, including, but not limited to, the future demand for the Bank s financial products and its overall future liquidity needs, among many other factors.

*See additional detail regarding the Bank s interest rate risk position and interest rate risk mitigation strategies under the section titled Asset/Liability Management and Market Risk in this section of the filing.*

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Table 1 provides detailed total Company information as to average balances, interest income/expense and rates by major balance sheet category for the quarters ended September 30, 2014 and 2013.

**Table 1 Total Company Average Balance Sheets and Interest Rates for the Three Months Ended September 30, 2014 and 2013**

| | Three Months Ended September 30, 2014 | | | Three Months Ended September 30, 2013 | | |
|---|---|---|---|---|---|---|
| **(dollars in thousands)** | **Average Balance** | **Interest** | **Average Rate** | **Average Balance** | **Interest** | **Average Rate** |
| **ASSETS** | | | | | | |
| **Interest-earning assets:** | | | | | | |
| Taxable investment securities, including FHLB stock(1) | $ 539,020 | $ 2,202 | 1.63% | $ 530,759 | $ 2,307 | 1.74% |
| Federal funds sold and other interest-earning deposits | 29,713 | 26 | 0.35% | 113,042 | 83 | 0.29% |
| Loans and fees(2)(3) | 2,795,788 | 30,916 | 4.42% | 2,576,606 | 31,619 | 4.91% |
| Total interest-earning assets | 3,364,521 | 33,144 | 3.94% | 3,220,407 | 34,009 | 4.22% |
| Allowance for loan losses | (22,869) | | | (22,664) | | |
| **Non interest-earning assets:** | | | | | | |
| Non interest-earning cash and cash equivalents | 60,367 | | | 65,920 | | |
| Premises and equipment, net | 33,932 | | | 32,820 | | |
| Bank owned life insurance | 50,862 | | | | | |
| Other assets(1) | 43,200 | | | 43,113 | | |
| Total assets | $ 3,530,013 | | | $ 3,339,596 | | |
| **LIABILITIES AND STOCKHOLDERS EQUITY** | | | | | | |
| **Interest-bearing liabilities:** | | | | | | |
| Transaction accounts | $ 755,061 | $ 124 | 0.07% | $ 712,426 | $ 127 | 0.07% |
| Money market accounts | 472,242 | 189 | 0.16% | 497,332 | 149 | 0.12% |
| Time deposits | 167,531 | 253 | 0.60% | 180,422 | 345 | 0.76% |
| Brokered money market and brokered CD s | 102,968 | 364 | 1.41% | 123,150 | 422 | 1.37% |
| Total interest-bearing deposits | 1,497,802 | 930 | 0.25% | 1,513,330 | 1,043 | 0.28% |
| Securities sold under agreements to repurchase and other short-term borrowings | 317,053 | 28 | 0.04% | 139,293 | 11 | 0.03% |
| Federal Home Loan Bank advances | 575,761 | 3,116 | 2.16% | 592,735 | 3,788 | 2.56% |
| Subordinated note | 41,240 | 628 | 6.09% | 41,240 | 628 | 6.09% |
| Total interest-bearing liabilities | 2,431,856 | 4,702 | 0.77% | 2,286,598 | 5,470 | 0.96% |
| **Non interest-bearing liabilities and Stockholders equity** | | | | | | |

| | | | | | | |
|---|---|---|---|---|---|---|
| Non interest-bearing deposits | 521,360 | | | 488,386 | | |
| Other liabilities | 18,047 | | | 17,173 | | |
| Stockholders equity | 558,750 | | | 547,439 | | |
| Total liabilities and stockholders equity | $ 3,530,013 | | | $ 3,339,596 | | |
| Net interest income | | $ 28,442 | | | $ 28,539 | |
| Net interest spread | | | 3.17% | | | 3.26% |
| Net interest margin | | | 3.38% | | | 3.54% |

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*(1) For the purpose of this calculation, the fair market value adjustment on investment securities resulting from FASB ASC Topic 320, Investments Debt and Equity Securities, is included as a component of other assets.*

*(2) The amount of loan fee income included in total interest income was $1.8 million and $3.3 million for the three months ended September 30, 2014 and 2013.*

*(3) Average balances for loans include the principal balance of non-accrual loans and loans held for sale and are net of all premiums, discounts, fees and costs.*

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Table 2 illustrates the extent to which changes in interest rates and changes in the volume of total Company interest-earning assets and interest-bearing liabilities impacted Republic s interest income and interest expense during the periods indicated. Information is provided in each category with respect to (i) changes attributable to changes in volume (changes in volume multiplied by prior rate), (ii) changes attributable to changes in rate (changes in rate multiplied by prior volume) and (iii) net change. The changes attributable to the combined impact of volume and rate have been allocated proportionately to the changes due to volume and the changes due to rate.

**Table 2 Total Company Volume/Rate Variance Analysis for the Three Months Ended September 30, 2014 and 2013**

| | Three Months Ended September 30, 2014 Compared to Three Months Ended September 30, 2013 Increase / (Decrease) Due to | | |
|---|---|---|---|
| **(in thousands)** | **Total Net Change** | **Volume** | **Rate** |
| *Interest income:* | | | |
| Taxable investment securities, including FHLB stock | $ (105) | $ 36 | $ (141) |
| Federal funds sold and other interest-earning deposits | (57) | (71) | 14 |
| Loans and fees | (703) | 2,567 | (3,270) |
| Net change in interest income | (865) | 2,532 | (3,397) |
| *Interest expense:* | | | |
| Transaction accounts | (3) | 7 | (10) |
| Money market accounts | 40 | (8) | 48 |
| Time deposits | (93) | (24) | (69) |
| Brokered money market and brokered CDs | (58) | (71) | 13 |
| Securities sold under agreements to repurchase and other short-term borrowings | 18 | 16 | 2 |
| Federal Home Loan Bank advances | (672) | (106) | (566) |
| Subordinated note | | | |
| Net change in interest expense | (768) | (186) | (582) |
| Net change in net interest income | $ (97) | $ 2,718 | $ (2,815) |

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**Provision for Loan Losses (Three Months Ended September 30, 2014 Compared to Three Months Ended September 30, 2013)**

The Company recorded a $1.5 million Provision for the third quarter 2014, compared to $2.2 million for the same period in 2013. The significant components comprising the Company s Provision by business segment were as follows:

**Traditional Banking segment**

The Traditional Banking Provision during the third quarter of 2014 was $1.5 million, a $715,000 improvement from the $2.3 million Provision recorded during the third quarter of 2013. The improvement from the third quarter of 2013 to 2014 was primarily due to the following:

- The Traditional Bank posted a net decrease of $4,000 in Provision associated with loans rated Special Mention for the third quarter of 2014 compared to a net increase of $1.1 million for the same period in 2013. The increase during the third quarter of 2013 was primarily driven by an increase in reserves for retail troubled debt restructured loans. The change associated with the Bank s Special Mention credits, represented a positive swing in the Provision of approximately $1.1 million for the quarter.

- The Traditional Bank posted a net decrease of $69,000 to the Provision during the third quarter of 2014 associated with purchased credit impaired ( PCI ) loans compared to a net increase of $360,000 for same period in 2013. Increases in the Provision for PCI loans reflect probable shortfalls in cash flows below initial estimates for these loans. Credits to the Provision for PCI loans generally reflect reversals of provisions made in prior periods due to positive loan workouts. The change associated with the Bank s PCI credits, represented a positive swing in the Provision of approximately $429,000 for the quarter.

- The Traditional Bank posted a net increase of $343,000 in the Provision associated with loans rated Substandard for the third quarter of 2014 compared to a net increase of $837,000 for the same period in 2013. During the third quarter of 2014 and 2013, the Bank had no significant impairment charges for individually evaluated Substandard relationships. The change associated with the Bank s Substandard credits, represented a positive swing in the Provision of approximately $494,000 for the quarter.

- The Traditional Bank posted a net increase of $138,000 to the Provision during the third quarter of 2014 associated with small-dollar, retail nonaccrual loans compared to a net decrease of $16,000 to the Provision for the same period in 2013. Provisions for these loans during the periods were partially driven by an increase in the portfolio balance and partially by the Bank s updated migration analysis. The change associated with the Bank s small-dollar and retail nonaccrual credits, represented a negative swing in the Provision of approximately $154,000 for the quarter.

- The Traditional Bank posted a net increase of $1.1 million in allocations associated with Pass rated and non rated loans during the third quarter of 2014 compared to a net decrease of $58,000 for the same period in 2013. The change associated with the Bank s Pass rated and non rated loans represented a negative swing in the Provision of approximately $1.2 million for the quarter. The increase during the third quarter of 2014 was primarily driven by increases in residential real estate loans originated through the Bank s correspondent lending channel and higher usage rates on warehouse lines of credit during the period.

As a percentage of total loans, the Traditional Banking Allowance decreased to 0.81% at September 30, 2014 compared to 0.89% at December 31, 2013 and 0.92% at September 30, 2013. The Company believes, based on information presently available, that it has adequately provided for loan losses at September 30, 2014.

*See the sections titled Allowance for Loan Losses and Asset Quality in this section of the filing under Comparison of Financial Condition for additional discussion regarding the Provision and the Bank s credit quality.*

**Republic Processing Group segment**

As previously reported, the Company ceased offering the RAL product effective April 30, 2012. During the third quarters 2014 and 2013, RPG recorded net credits to the Provision of $32,000 and $57,000 due primarily to the collection of prior period RAL charge-offs.

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An analysis of changes in the Allowance and selected credit quality ratios follows:

**Table 3 Summary of Loan Loss Experience for the Three Months Ended September 30, 2014 and 2013**

| | Three Months Ended September 30, | |
|---|---|---|
| **(dollars in thousands)** | **2014** | **2013** |
| Allowance at beginning of period | $ 22,772 | $ 22,491 |
| Charge offs: | | |
| | | |
| Residential real estate: | | |
| Owner occupied | (161) | (578) |
| Owner occupied - correspondent | | |
| Non owner occupied | (135) | (67) |
| Commercial real estate | (365) | (307) |
| Commercial real estate - purchased whole loans | | |
| Construction & land development | | (16) |
| Commercial & industrial | | (102) |
| Lease financing receivables | | |
| Warehouse lines of credit | | |
| Home equity | (146) | (218) |
| Consumer: | | |
| RPG loans: | | |
| Refund Anticipation Loans | | |
| Other RPG loans | (2) | |
| Credit cards | (23) | (60) |
| Overdrafts | (136) | (169) |
| Purhcased whole loans | | |
| Other consumer | (105) | (110) |
| Total charge offs | (1,073) | (1,627) |
| | | |
| Recoveries: | | |
| | | |
| Residential real estate: | | |
| Owner occupied | 26 | 20 |
| Owner occupied - correspondent | | |
| Non owner occupied | 17 | 59 |
| Commercial real estate | 9 | 38 |
| Commercial real estate - purchased whole loans | | |
| Construction & land development | | 7 |
| Commercial & industrial | 37 | 19 |
| Lease financing receivables | | |
| Warehouse lines of credit | | |
| Home equity | 88 | 55 |
| Consumer: | | |
| RPG loans: | | |
| Refund Anticipation Loans | 32 | 57 |
| Other RPG loans | | |
| Credit cards | 10 | 4 |
| Overdrafts | 91 | 95 |
| Purhcased whole loans | | |
| Other consumer | 98 | 74 |

| | | | | |
|---|---|---|---|---|
| Total recoveries | | 408 | | 428 |
| | | | | |
| Net charge offs | | (665) | | (1,199) |
| | | | | |
| Provision - Traditional Banking | | 1,542 | | 2,257 |
| Provision - RPG Loans | | (32) | | (57) |
| Total Provision | | 1,510 | | 2,200 |
| | | | | |
| Allowance at end of period | $ | 23,617 | $ | 23,492 |

**Credit Quality Ratios:**

| | | |
|---|---|---|
| Allowance to total loans | 0.81% | 0.92% |
| Allowance to non-performing loans | 110% | 116% |
| Annualized net loan charge offs to average loans - Total Company | 0.10% | 0.19% |
| Annualized net loan charge offs to average loans - Traditional Banking | 0.10% | 0.19% |

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**Non-interest Income (Three Months Ended September 30, 2014 Compared to Three Months Ended September 30, 2013)**

Non-interest income decreased $355,000, or 5%, for the third quarter of 2014 compared to the same period in 2013. The most significant components comprising the total Company s change in non-interest income by business segment were as follows:

**Traditional Banking segment**

Traditional Banking segment non-interest income decreased $130,000, or 2%, for the third quarter of 2014 compared to the same period in 2013.

Net gains on the sale of OREO decreased $336,000, or 84%, from a net gain of $403,000 recorded during the third quarter of 2013 to $67,000 for the same period in 2014. Net gains on the sale of OREO during the third quarter of 2013 included a gain of $123,000 on a single property.

Net credit card interchange income decreased $172,000, as additional estimated credit card rebates were accrued in connection with a change in the Company s credit card rewards program.

Service charges on deposit accounts decreased from $3.7 million during the third quarter of 2013 to $3.6 million during the third quarter of 2014. The lack of growth in service charges on deposits reflects a generally flat to downward trend for the Bank over the past several years due primarily to on-going regulatory changes that have negatively impacted overdraft fee income. Management does not anticipate this trend to change in a substantial positive manner any time in the foreseeable future. The Bank earns a substantial majority of its fee income related to its overdraft service program from the per item fee it assesses its customers for each insufficient funds check or electronic debit presented for payment. The total per item fees, net of refunds, included in service charges on deposits for the quarter ended September 30, 2014 and 2013 were $2.0 million and $2.2 million. The total daily overdraft charges, net of refunds, included in interest income for the quarters ended September 30, 2014 and 2013 were $417,000 and $438,000.

Partially offsetting the decreases above, the Bank recorded $381,000 from an increase in the cash surrender value of its Bank Owned Life Insurance ( BOLI ) during the third quarter of 2014. The Bank first invested in BOLI during the fourt