REPUBLIC BANCORP INC /KY/
Form 10-Q
November 08, 2012

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

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, 2012

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.

þ 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).

þ 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 þ 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 þ 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, 2012, was 18,674,767 and 2,271,346, respectively.

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PART I – FINANCIAL INFORMATION

Item 1. Financial Statements.
CONSOLIDATED BALANCE SHEETS (in thousands) (unaudited)

| | September 30, 2012 | December 31, 2011 |
|---|---|---|
| ASSETS | | |
| | | |
| Cash and cash equivalents | $ 96,187 | $ 362,971 |
| Securities available for sale | 533,236 | 645,948 |
| Securities to be held to maturity (fair value of $48,448 in 2012 and $28,342 in 2011) | 48,026 | 28,074 |
| Mortgage loans held for sale | 3,385 | 4,392 |
| Loans, net of allowance for loan losses of $24,100 and $24,063 (2012 and 2011) | 2,618,257 | 2,261,232 |
| Federal Home Loan Bank stock, at cost | 28,784 | 25,980 |
| Premises and equipment, net | 32,984 | 34,681 |
| Goodwill | 10,168 | 10,168 |
| Other real estate owned | 25,148 | 10,956 |
| Other assets and accrued interest receivable | 39,601 | 35,589 |
| | | |
| TOTAL ASSETS | $ 3,435,776 | $ 3,419,991 |
| | | |
| LIABILITIES | | |
| | | |
| Deposits | | |
| Non interest-bearing | $ 514,893 | $ 408,483 |
| Interest-bearing | 1,540,717 | 1,325,495 |
| Total deposits | 2,055,610 | 1,733,978 |
| | | |
| Securities sold under agreements to repurchase and other short-term borrowings | 169,839 | 230,231 |
| Federal Home Loan Bank advances | 553,487 | 934,630 |
| Subordinated note | 41,240 | 41,240 |
| Other liabilities and accrued interest payable | 57,844 | 27,545 |
| | | |
| Total liabilities | 2,878,020 | 2,967,624 |
| | | |
| STOCKHOLDERS' EQUITY | | |
| | | |
| Preferred stock, no par value | - | - |
| Class A Common Stock and Class B Common Stock, no par value | 4,945 | 4,947 |
| Additional paid in capital | 132,797 | 131,482 |
| Retained earnings | 414,133 | 311,799 |
| Accumulated other comprehensive income | 5,881 | 4,139 |
| | | |
| Total stockholders' equity | 557,756 | 452,367 |
| | | |
| TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY | $ 3,435,776 | $ 3,419,991 |

See accompanying footnotes to consolidated financial statements.

CONSOLIDATED STATEMENTS OF INCOME
(UNAUDITED)
(in thousands, except per share data)1

| | Three Months Ended September 30, 2012 | Three Months Ended September 30, 2011 | Nine Months Ended September 30, 2012 | Nine Months Ended September 30, 2011 |
|---|---|---|---|---|
| INTEREST INCOME: | | | | |
| Loans, including fees | $31,292 | $30,225 | $137,118 | $148,229 |
| Taxable investment securities | 2,483 | 3,864 | 8,654 | 11,549 |
| Federal Home Loan Bank stock and other | 353 | 337 | 1,757 | 1,730 |
| Total interest income | 34,128 | 34,426 | 147,529 | 161,508 |
| INTEREST EXPENSE: | | | | |
| Deposits | 1,197 | 2,057 | 3,949 | 7,267 |
| Securities sold under agreements to repurchase and other short-term borrowings | 110 | 111 | 340 | 535 |
| Federal Home Loan Bank advances | 3,619 | 4,467 | 11,245 | 13,857 |
| Subordinated note | 630 | 628 | 1,891 | 1,886 |
| Total interest expense | 5,556 | 7,263 | 17,425 | 23,545 |
| NET INTEREST INCOME | 28,572 | 27,163 | 130,104 | 137,963 |
| Provision for loan losses | 2,083 | (140) | 13,719 | 17,503 |
| NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES | 26,489 | 27,303 | 116,385 | 120,460 |
| NON INTEREST INCOME: | | | | |
| Service charges on deposit accounts | 3,438 | 3,421 | 10,027 | 10,581 |
| Refund transfer fees | 231 | 425 | 78,127 | 88,071 |
| Mortgage banking income | 2,274 | 1,352 | 5,591 | 3,092 |
| Debit card interchange fee income | 1,390 | 1,415 | 4,387 | 4,392 |
| Bargain purchase gain - Tennessee Commerce Bank | (189) | - | 27,614 | - |
| Bargain purchase gain - First Commercial Bank | 27,112 | - | 27,112 | - |
| Gain on sale of banking center | - | 2,856 | - | 2,856 |
| Gain on sale of securities available for sale | - | 301 | 56 | 2,208 |
| Total impairment losses on investment securities | - | - | - | (279) |
| Gain recognized in other comprehensive income | - | - | - | - |
| Net impairment loss recognized in earnings | - | - | - | (279) |
| Other | 589 | 706 | 2,826 | 2,235 |
| Total non interest income | 34,845 | 10,476 | 155,740 | 113,156 |
| NON INTEREST EXPENSES: | | | | |
| Salaries and employee benefits | 14,921 | 13,145 | 46,205 | 43,634 |
| Occupancy and equipment, net | 5,718 | 5,138 | 16,936 | 16,436 |
| Communication and transportation | 1,045 | 1,081 | 4,667 | 4,468 |
| Marketing and development | 828 | 736 | 2,670 | 2,508 |
| FDIC insurance expense | 287 | 918 | 1,008 | 3,718 |
| Bank franchise tax expense | 729 | 713 | 3,363 | 2,992 |
| Data processing | 1,030 | 787 | 3,446 | 2,352 |
| Debit card interchange expense | 648 | 566 | 1,909 | 1,690 |
| Supplies | 270 | 409 | 1,748 | 1,617 |
| Other real estate owned expense | 1,328 | 608 | 2,488 | 1,467 |
| Charitable contributions | 232 | 178 | 3,110 | 5,710 |
| Legal expense | 388 | 784 | 1,283 | 3,123 |

| | | | | |
|---|---|---|---|---|
| FDIC civil money penalty | - | - | - | 2,000 |
| FHLB advance prepayment expense | - | - | 2,436 | - |
| Other | 2,338 | 1,375 | 7,097 | 6,067 |
| Total non interest expenses | 29,762 | 26,438 | 98,366 | 97,782 |
| INCOME BEFORE INCOME TAX EXPENSE | 31,572 | 11,341 | 173,759 | 135,834 |
| INCOME TAX EXPENSE | 10,904 | 3,471 | 61,041 | 47,889 |
| NET INCOME | $20,668 | $7,870 | $112,718 | $87,945 |
| | | | | |
| BASIC EARNINGS PER SHARE: | | | | |
| Class A Common Stock | $0.99 | $0.38 | $5.38 | $4.20 |
| Class B Common Stock | 0.97 | 0.36 | 5.34 | 4.16 |
| DILUTED EARNINGS PER SHARE: | | | | |
| Class A Common Stock | $0.98 | $0.38 | $5.36 | $4.19 |
| Class B Common Stock | 0.97 | 0.36 | 5.32 | 4.15 |

See accompanying footnotes to consolidated financial statements.

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (UNAUDITED)
(in thousands, except per share data)

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| | 2012 | 2011 | 2012 | 2011 |
| Net income | $ 20,668 | $ 7,870 | $ 112,718 | $ 87,945 |
| OTHER COMPREHENSIVE INCOME | | | | |
| Unrealized gain on securities available for sale | 649 | 3,588 | 2,324 | 5,474 |
| Change in unrealized losses on securities available for sale for which a portion of an other-than-temporary impairment has been recognized in earnings | 374 | 143 | 411 | (75) |
| Realized amount on securities sold | - | (300) | (55) | (2,208) |
| Reclassification adjustment for losses realized in income | - | - | - | (279) |
| Net unrealized gains | 1,023 | 3,431 | 2,680 | 2,912 |
| Tax effect | (358) | (1,201) | (938) | (1,019) |
| Net of tax amount | 665 | 2,230 | 1,742 | 1,893 |
| COMPREHENSIVE INCOME | $ 21,333 | $ 10,100 | $ 114,460 | $ 89,838 |

See accompanying footnotes to consolidated financial statements.

CONSOLIDATED STATEMENT OF STOCKHOLDERS’ EQUITY
(UNAUDITED)
NINE MONTHS ENDED
SEPTEMBER 30, 2012

| (in thousands, except per share data) | Common Stock 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, 2012 | 18,652 | 2,300 | $ 4,947 | $ 131,482 | $ 311,799 | $ 4,139 | $ 452,367 |
| Net income | - | - | - | - | 112,718 | - | 112,718 |
| Net change in accumulated other comprehensive income | - | - | - | - | - | 1,742 | 1,742 |
| Dividend declared Common Stock: | | | | | | | |
| Class A ($0.484 per share) | - | - | - | - | (9,033 ) | - | (9,033 ) |
| Class B ($0.440 per share) | - | - | - | - | (1,007 ) | - | (1,007 ) |
| Stock options exercised, net of shares redeemed | 8 | - | 2 | 213 | (68 ) | - | 147 |
| Repurchase of Class A Common Stock | (17 ) | - | (4 ) | (106 ) | (276 ) | - | (386 ) |
| Conversion of Class B Common Stock to Class A Common Stock | 29 | (29 ) | - | - | - | - | - |
| Notes receivable on Common Stock, net of cash payments | - | - | - | 413 | - | - | 413 |
| Deferred director compensation expense - Company Stock | 1 | - | - | 140 | - | - | 140 |
| Stock based compensation expense | - | - | - | 655 | - | - | 655 |
| Balance, September 30, 2012 | 18,673 | 2,271 | $ 4,945 | $ 132,797 | $ 414,133 | $ 5,881 | $ 557,756 |

See accompanying footnotes to consolidated financial statements.

CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)
NINE MONTHS ENDED SEPTEMBER 30, 2012 AND 2011 (in thousands)

| | 2012 | 2011 |
|---|---|---|
| OPERATING ACTIVITIES: | | |
| Net income | $ 112,718 | $ 87,945 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Depreciation, amortization and accretion, net | 7,348 | 2,393 |
| Provision for loan losses | 13,719 | 17,503 |
| Net gain on sale of mortgage loans held for sale | (6,541) | (2,976) |
| Origination of mortgage loans held for sale | (166,224) | (93,052) |
| Proceeds from sale of mortgage loans held for sale | 173,772 | 106,535 |
| Net realized impairment of mortgage servicing rights | 129 | 203 |
| Net realized gain on sales, calls and impairment of securities | (56) | (1,929) |
| Net gain on sale of other real estate owned | (381) | (424) |
| Writedowns of other real estate owned | 1,207 | 463 |
| Deferred director compensation expense - Company Stock | 140 | 130 |
| Stock based compensation expense | 655 | 213 |
| Bargain purchase gains on acquisitions | (54,726) | - |
| Gain on sale of banking center | - | (2,856) |
| Net change in other assets and liabilities: | | |
| Accrued interest receivable | (409) | (308) |
| Accrued interest payable | (228) | (566) |
| Other assets | 5,864 | 3,115 |
| Other liabilities | 16,347 | 17,660 |
| Net cash provided by operating activities | 103,334 | 134,049 |
| | | |
| INVESTING ACTIVITIES: | | |
| Net cash received in FDIC-assisted transactions | 921,161 | - |
| Purchases of securities available for sale | (61,716) | (694,640) |
| Purchases of securities to be held to maturity | (23,115) | (500) |
| Purchases of Federal Home Loan Bank stock | - | (1) |
| Proceeds from calls, maturities and paydowns of securities available for sale | 193,403 | 384,947 |
| Proceeds from calls, maturities and paydowns of securities to be held to maturity | 3,354 | 4,114 |
| Proceeds from sales of securities available for sale | 38,724 | 160,075 |
| Proceeds from sales of Federal Home Loan Bank stock | 62 | 60 |
| Proceeds from sales of other real estate owned | 21,688 | 10,622 |
| Purchase of commercial real estate loans | - | (32,650) |
| Net change in loans | (184,454) | (50,848) |
| Net purchases of premises and equipment | (2,499) | (1,845) |
| Sale of banking center | - | (15,410) |
| Net cash provided by/(used in) investing activities | 906,608 | (236,076) |
| | | |
| FINANCING ACTIVITIES: | | |
| Net change in deposits | (822,074) | (468,372) |
| Net change in securities sold under agreements to repurchase and other short-term borrowings | (60,392) | (91,160) |
| Payments of Federal Home Loan Bank advances | (589,208) | (55,146) |
| Proceeds from Federal Home Loan Bank advances | 205,000 | 15,000 |

| | | | | |
|---|---|---|---|---|
| Repurchase of Common Stock | | (386) | | (411) |
| Net proceeds from Common Stock options exercised | | 147 | | 438 |
| Cash dividends paid | | (9,813) | | (9,120) |
| Net cash used in financing activities | | (1,276,726) | | (608,771) |
| | | | | |
| NET CHANGE IN CASH AND CASH EQUIVALENTS | | (266,784) | | (710,798) |
| CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD | | 362,971 | | 786,371 |
| CASH AND CASH EQUIVALENTS AT END OF PERIOD | $ | 96,187 | $ | 75,573 |
| | | | | |
| SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION | | | | |
| Cash paid during the period for: | | | | |
| Interest | $ | 17,653 | $ | 24,118 |
| Income taxes | | 68,603 | | 34,706 |
| | | | | |
| SUPPLEMENTAL NONCASH DISCLOSURES | | | | |
| Transfers from loans to real estate acquired in settlement of loans | $ | 16,018 | $ | 9,873 |
| Loans provided for sales of other real estate owned | | 591 | | 1,963 |

See accompanying footnotes to consolidated financial statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – SEPTEMBER 30, 2012 AND 2011 (UNAUDITED) AND DECEMBER 31, 2011

## 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") and Republic Bank ("RB") (collectively referred together as the "Bank"), Republic Funding Company and Republic Invest Co. Republic Invest Co. includes its subsidiary, Republic Capital LLC. The consolidated financial statements also include the wholly-owned subsidiaries of RB&T: Republic Financial Services, LLC, TRS RAL Funding, LLC and Republic Insurance Agency, LLC. 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.

The accompanying unaudited consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles 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 U.S. generally accepted accounting principles ("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, 2012 are not necessarily indicative of the results that may be expected for the year ending December 31, 2012. 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, 2011.

As of September 30, 2012, the Company was divided into three distinct business operating segments: Traditional Banking, Mortgage Banking and Republic Processing Group ("RPG"). During 2012, the Company realigned the previously reported Tax Refund Solutions ("TRS") segment as a division of the newly formed RPG segment. Along with the TRS division, Republic Payment Solutions ("RPS") and Republic Credit Solutions ("RCS") also operate as divisions of the newly formed RPG segment.

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

Republic operates 44 banking centers, primarily in the retail banking industry, and conducts its operations predominately in metropolitan Louisville, Kentucky; central Kentucky; northern Kentucky; southern Indiana; metropolitan Tampa, Florida; metropolitan Cincinnati, Ohio; metropolitan Nashville, Tennessee, metropolitan Minneapolis, Minnesota and through an Internet banking delivery channel.

Effective January 27, 2012, RB&T acquired certain assets and assumed substantially all of the deposits and certain other liabilities of Tennessee Commerce Bank ("TCB"), headquartered in Franklin, Tennessee from the FDIC, as receiver for TCB. This acquisition of a failed bank represented a single banking center located in metropolitan Nashville and was also RB&T's initial entrance into the Tennessee market

Effective September 7, 2012 RB&T acquired substantially all of the assets and assumed substantially all of the liabilities of First Commercial Bank ("FCB"), headquartered in Bloomington, Minnesota from the FDIC, as receiver for FCB. This acquisition of a failed bank represented a single banking center located in metropolitan Minneapolis and was also RB&T's initial entrance into the Minnesota market. See additional discussion regarding the TCB and FCB acquisitions under Footnote 2 "Acquisitions of Failed Banks" of Part I Item 1 "Financial Statements."

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 real estate mortgage, commercial and consumer loans. 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.

Other sources of Core Banking income include service charges on deposit accounts, debit 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. Additionally, in June 2011, the Bank commenced business in its newly established warehouse lending division. Through this division, the Bank provides short-term, revolving credit facilities to mortgage bankers across the nation. These credit facilities are secured by single family residential real estate loans.

Core Banking operating expenses consist primarily of salaries and employee benefits, occupancy and equipment expenses, communication and transportation costs, marketing and development expenses, Federal Deposit Insurance Corporation ("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.

RPG

Nationally, through RB&T, RPG facilitates the receipt and payment of federal and state tax refund products under the TRS division. Nationally, through RB, the RPS division is preparing to become an issuing bank to offer general purpose reloadable prepaid debit, payroll, gift and incentive cards through third party program managers. Nationally, through RB&T, the RCS division is preparing to pilot short-term consumer credit products through multiple channels.

TRS division:

Republic, through its TRS division, is one of a limited number of financial institutions that facilitates the payment of federal and state tax refund products through third-party tax preparers located throughout the U.S., as well as tax-preparation software providers. The TRS division's three primary tax-related products have historically included: Refund Transfers ("RTs") (formerly referred to as Electronic Refund Checks/Electronic Refund Deposits or "ERCs/ERDs" or "ARs/ARDs") and Refund Anticipation Loans ("RALs"). Substantially all of the business generated by the TRS division occurs in the first quarter of the year. The TRS division traditionally operates at a loss during the second half of the year, during which time the division incurs costs preparing for the upcoming year's first quarter tax season.

As previously disclosed, effective December 8, 2011, RB&T entered into an agreement with the FDIC resolving its differences regarding the TRS division. RB&T's resolution with the FDIC was in the form of a Stipulation Agreement and a Consent Order (collectively, the "Agreement"). As part of the Agreement, RB&T and the FDIC settled all matters set out in the FDIC's Amended Notice of Charges dated May 3, 2011 and the lawsuit filed against the FDIC by RB&T. As required by this settlement, RB&T discontinued its offering of the RAL product effective April 30, 2012.

RTs are products whereby a tax refund is issued to the taxpayer after RB&T has received the refund from the federal or state government. There is no credit risk or borrowing cost for RB&T associated with these products because they are only delivered to the taxpayer upon receipt of the refund directly from the Internal Revenue Service ("IRS"). Fees earned on RTs are reported as non interest income under the line item "Refund Transfer fees."

RALs were short-term consumer loans offered to taxpayers that were secured by the customer's anticipated tax refund, which represented the source of repayment. The fees earned on RALs are reported as interest income under the line item "Loans, including fees."

For additional discussion regarding the Agreement, see the Company's Form 8-K filed with the SEC on December 9, 2011, including Exhibits 10.1 and 10.2.

Termination of Material TRS Contracts:

On August 27, 2012, RB&T received a termination notice to the Amended and Restated Marketing and Servicing Agreement, dated November 29, 2011, with Liberty Tax Service ("Liberty") related to RB&T's RT products, as well as RB&T's previously offered RAL product. Approximately 19% and 20% of the TRS division's gross revenue for the nine months ended as of September 30, 2012 and 2011 was derived from Liberty tax offices.

On September 18, 2012, RB&T received a termination notice to the Amended and Restated Program Agreement, dated August 3, 2011, with Jackson Hewitt Technology Services LLC ("JHTSL") related to RB&T's RT products, as well as RB&T's previously offered RAL product. Approximately 40% of the TRS division's gross revenue for the nine months ended as of September 30, 2012 and 2011 was derived from JHTSL's tax offices.

For additional discussion regarding TRS, a division of RPG, see the following sections:

- Part I Item 1 "Financial Statements:"
  - o Footnote 4 "Loans and Allowance for Loan Losses"
  - o Footnote 6 "Federal Home Loan Bank Advances"
  - o Footnote 11 "Segment Information"
  - o Management's Discussion and Analysis
- Part I Item 2 "Management's Discussion and Analysis of Financial Condition and Results of Operations"
  - o Business Segment Composition
    - RPG Segment
      - Discontinuance of the RAL Product and Future Competition
      - Termination of Material TRS Contracts
- Part II Item 1A "Risk Factors"

RPS division:

Nationally, through RB, the RPS division is preparing to become an issuing bank to offer general purpose reloadable prepaid debit, payroll, gift and incentive cards through third party program managers. If successful, this program is expected to:

- o Generate a low-cost deposit source;
- o Generate float revenue from the previously mentioned low cost deposit source;
- o Serve as a source of fee income; and
- o Generate debit card interchange revenue.

For the projected near-term, as the prepaid card program is being established, the operating results of the RPS division are expected to be immaterial to the Company's overall results of operations and will be reported as part of the RPG business operating segment. The RPS division will not be reported as a separate business operating segment until such time, if any, that it becomes material to the Company's overall results of operations.

The Company divides prepaid cards into two general categories: reloadable and non-reloadable cards.

Reloadable Cards: These types of cards are considered general purpose reloadable ("GPR") cards. These cards may take the form of payroll cards issued to an employee by an employer to receive the direct deposit of their payroll. GPR cards can also be issued to a consumer at a retail location or mailed to a consumer after completing an on-line application. GPR cards can be reloaded multiple times with a consumer's payroll, government benefit, a federal or state tax refund or through cash reload networks located at retail locations. Reloadable cards are generally open loop cards as described below.

Non-Reloadable Cards: These are generally one-time use cards that are only active until the funds initially loaded to the card are spent. These types of cards are considered gift or incentive cards. These cards may be open loop or closed loop, as described below. Normally these types of cards are used for the purchase of goods or services at retail locations and cannot be used to receive cash.

Prepaid cards may be open loop, closed loop or semi-closed loop. Open loop cards can be used to receive cash at ATM locations or purchase goods or services by PIN or signature at retail locations. These cards can be used virtually anywhere that Visa® or MasterCard® is accepted. Closed loop cards can only be used at a specific merchant. Semi-closed loop cards can be used at several merchants such as a shopping mall.

The prepaid card market is one of the fastest growing segments of the payments industry in the U.S. This market has experienced significant growth in recent years due to consumers and merchants embracing improved technology, greater convenience, more product choices and greater flexibility. Prepaid cards have also proven to be an attractive alternative to traditional bank accounts for certain segments of the population, particularly those without, or who could not qualify for, a checking or savings account.

The RPS division will work with various third parties to distribute prepaid cards to consumers throughout the U.S. The Company will also likely work with these third parties to develop additional financial services for consumers to increase the functionality of the program and prepaid card usage.

See additional discussion under Part II Item 1A "Risk Factors."

RCS division:

Nationally, through RB&T, the RCS division is preparing to pilot short-term consumer credit products through multiple channels. In general, the credit products are expected to be unsecured small dollar consumer loans with maturities of 30 days or more, and are dependent on various factors including the consumer's ability to repay. All RCS programs will be piloted for a period of time to ensure all aspects are meeting expectations before continuation.

RB&T management preliminarily expects to fund RCS during its pilot phase with a nominal amount of capital. At the conclusion of its pilot phase, RB&T management will determine whether or not to expand or modify the program based on the results of the pilot phase. As with most start-up ventures, management expects the pilot to operate at a loss in its initial stages. Given the speculative nature of the program, management cannot currently predict how much money the program may lose during the pilot phase, however, RB&T does not plan to put more than $5 million of capital at risk until such time the program may become profitable.

Summary of New Significant Accounting Policies Related to the Acquisitions of Failed Banks:

Loans purchased in the acquisitions of failed banks may be accounted for using the following accounting standards:

> FASB Accounting Standards Codification ("ASC") Topic 310-30, Loans and Debt Securities Acquired with Deteriorated Credit Quality, is used to value loans with post origination credit quality deterioration. For these loans, it is probable the acquirer will be unable to collect all contractually required payments from the borrower. Under ASC Topic 310-30, the expected cash flows that exceed the initial investment in the loan (fair value) represent the "accretable yield," which is recognized as interest income on a level-yield basis over the expected cash flow periods of the loans.

> ASC Topic 310-20, Non refundable Fees and Other Costs, is used to value loans that have not demonstrated post origination credit quality deterioration and the acquirer expects to collect all contractually required payments from the borrower. For these loans, the difference between the fair value of the loan at acquisition and the amortized cost of the loan would be amortized or accreted into income using the interest method. The Bank has historically applied this ASC to its deferred loan fees and costs associated with its traditional loan portfolio. In 2012, the Bank expanded the scope of this ASC to account for discounts on purchased loans.

Purchased Credit Impaired Loans (ASC Topic 310-30) – Management individually evaluates substantially all purchased credit impaired loans. This evaluation allows management to determine the estimated fair value of the purchased credit impaired loans and includes no carryover of any previously recorded allowance for loan losses. In determining the estimated fair value of purchased credit impaired loans, management considers a number of factors including, among other things, the remaining life of the acquired loans, estimated prepayments, estimated loss ratios, estimated value of the underlying collateral, estimated holding periods, and net present value of cash flows expected to be received. To the extent that any purchased credit impaired loan acquired in a FDIC-assisted acquisition is not specifically reviewed, management applies a loss estimate to that loan based on the average expected loss rates for the purchased credit impaired loans that were individually reviewed in that purchased loan portfolio. For the TCB and FCB acquisitions, RB&T elected to account for purchased credit impaired loans individually, as opposed to aggregating the loans into pools based on common risk characteristics such as loan type.

As provided for under GAAP, management has up to twelve months following the date of the acquisition to finalize the fair values of acquired assets and assumed liabilities. Material events that occur during the measurement period will be analyzed to determine if the new information reflected facts and circumstances that existed as of the acquisition date that if known, would have affected the measurement of fair value of the amounts recognized as of the acquisition date. The measurement period ends as soon as the Bank receives the information it was seeking about facts and circumstances that existed as of the acquisition date or learns more information is not obtainable. As previously mentioned, the measurement period is limited to one year from the acquisition date. Once management has finalized the fair values of acquired assets and assumed liabilities within this twelve month period, management considers such values to be the final "day-one fair values."

In determining the day-one fair values of purchased credit impaired loans, management calculates a non-accretable difference (the credit component of the purchased loans) and an accretable difference (the yield component of the purchased loans). The non-accretable difference is the difference between the contractually required payments and the cash flows expected to be collected in accordance with management's determination of the day-one fair values. Subsequent decreases to the expected cash flows will generally result in a provision for loan and lease losses. Subsequent increases in cash flows will result in a reversal of the provision for loan and lease losses to the extent of prior charges and then an adjustment to accretable yield, which would have a positive impact on interest income. The accretable difference on purchased credit impaired loans is the difference between the expected cash flows and the net present value of expected cash flows. Such difference is accreted into earnings using the level yield method over the expected cash flow periods of the loans.

With regard to purchased credit-impaired loans which are accounted for under ASC Topic 310-30, management separately monitors this portfolio and on a quarterly basis and reviews the loans contained within this portfolio against the factors and assumptions used in determining the day-one fair values. In addition to its quarterly evaluation, a loan is typically reviewed when it is modified or extended, or when material information becomes available to the Bank that provides additional insight regarding the loan's performance, the status of the borrower, or the quality or value of the underlying collateral.

To the extent that a purchased credit impaired loan's performance deteriorates from management's expectation established in conjunction with the determination of the day-one fair values, such loan will be considered an impaired loan, and is considered in the determination of the required level of allowance for loan and lease losses. Any improvement in the expected performance of a purchased credit impaired loan would result in a reversal of the provision for loan and lease losses to the extent of prior charges and then an adjustment to accretable yield, which would have a positive impact on interest income.

Purchased Loans (ASC Topic 310-20) – Purchased loans accounted for under ASC Topic 310-20 are accounted for as would any other Bank-originated loan including presentation in any of the credit quality ratios, potentially becoming nonaccrual or impaired, as well as being risk rated under the Bank's standard practices and procedures. In addition, purchased loans accounted for under ASC Topic 310-20 are considered in the determination of the required allowance for loan and lease losses once day-one fair value have been finalized.

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. Additionally, as discussed above and in Footnote 2 "Acquisitions of Failed Banks," during the second and third quarters of 2012 the Bank posted adjustments to the TCB acquired assets in the determination of day-one fair values, which resulted in an immaterial overall adjustment to the bargain purchase gain.

## 2. ACQUISITIONS OF FAILED BANKS

### OVERVIEW

As Republic entered the 2012 calendar year, it implemented an acquisition strategy to selectively grow its franchise as a complement to its internal growth strategies.

During 2012, RB&T acquired two failed institutions in FDIC-assisted transactions. RB&T acquired Tennessee Commerce Bank ("TCB") during the first quarter of 2012 and First Commercial Bank ("FCB") during the third quarter of 2012. The Company did not raise capital to complete either of the above acquisitions.

RB&T determined that the acquisitions of these failed banks constituted "business acquisitions" as defined by ASC Topic 805, Business Combinations. Accordingly, the assets acquired and liabilities assumed are presented at their estimated fair values, as required. Fair values were determined based on the requirements of ASC Topic 820, Fair Value Measurements and Disclosures. In many cases, the determination of these fair values required management to make estimates about discount rates, future expected cash flows, market conditions and other future events that are highly subjective in nature and subject to change.

### TCB

On January 27, 2012, RB&T acquired specific assets and assumed substantially all of the deposits and specific other liabilities of TCB, headquartered in Franklin, Tennessee from the FDIC, as receiver for TCB, pursuant to the terms of a Purchase and Assumption Agreement — Whole Bank; All Deposits entered into among RB&T, the FDIC as receiver of TCB and the FDIC. On January 30, 2012, TCB's sole location re-opened as a division of RB&T.

RB&T acquired approximately $221 million in notional assets from the FDIC as receiver for TCB. In addition, RB&T also recorded a receivable from the FDIC for approximately $785 million, which represented the net difference between the assets acquired and the liabilities assumed adjusted for the discount RB&T received for the acquisition. The FDIC paid approximately $771 million of this receivable on January 30, 2012 with the remaining $14 million paid on February 15, 2012.

### FCB

On September 7, 2012, RB&T acquired specific assets and assumed substantially all of the liabilities of FCB, headquartered in Bloomington, Minnesota from the FDIC, as receiver for FCB, pursuant to the terms of a Purchase and Assumption Agreement — Whole Bank; All Deposits, entered into among RB&T, the FDIC as receiver of FCB and the FDIC. On September 10, 2012, FCB's sole location re-opened as a division of RB&T.

RB&T acquired approximately $215 million in notional assets from the FDIC as receiver for FCB. In addition, RB&T also recorded a receivable from the FDIC for approximately $64 million, which represented the net difference between the assets acquired and the liabilities assumed adjusted for the discount RB&T received for the acquisition. The FDIC paid substantially all of this receivable to RB&T on September 10, 2012.

ACQUISITION SUMMARY

A summary of the assets acquired and liabilities assumed in the TCB and FCB acquisitions, including recast adjustments, follows:

| Tennessee Commerce Bank | January 27, 2012 | | | |
|---|---|---|---|---|
| | As Previously Reported | | As Recasted | |
| (in thousands) | Contractual Amount | Fair Value Adjustments | Recast Adjustments | Fair Value |
| Assets acquired | | | | |
| Cash and cash equivalents | $61,943 | $ (89) | $(2) | $61,852 |
| Securities available for sale | 42,646 | - | - | 42,646 |
| Loans to be repurchased by the FDIC, net of discount | 19,800 | (2,797) | - | 17,003 |
| Loans | 79,112 | (22,666) | 830 | 57,276 |
| Federal Home Loan Bank stock, at cost | 2,491 | - | - | 2,491 |
| Other assets and accrued interest receivable | 945 | (60) | - | 885 |
| Other real estate owned | 14,189 | (3,359) | (1,113) | 9,717 |
| Core deposit intangible | - | 64 | - | 64 |
| Discount | (56,970) | 56,970 | - | - |
| FDIC settlement receivable | 784,545 | - | - | 784,545 |
| Total assets acquired | $948,701 | $ 28,063 | $(285) | $976,479 |
| Liabilities assumed | | | | |
| Deposits | | | | |
| Non interest-bearing | $19,754 | $ - | $- | $19,754 |
| Interest-bearing | 927,641 | 54 | - | 927,695 |
| Total deposits | 947,395 | 54 | - | 947,449 |
| Accrued income taxes payable | - | 9,988 | (100) | 9,888 |
| Other liabilities and accrued interest payable | 1,306 | 110 | - | 1,416 |
| Total liabilities assumed | $948,701 | $ 10,152 | $(100) | $958,753 |
| Equity | | | | |
| Bargain purchase gain, net of taxes | - | 17,911 | (185) | 17,726 |
| Other operating loss, net of taxes | - | - | - | - |
| Accumulated other comprehensive loss | - | - | - | - |
| Total liabilities assumed and equity | $948,701 | $ 28,063 | $(285) | $976,479 |

Information obtained subsequent to January 27, 2012 through the date of this filing was considered in forming TCB estimates of cash flows and collateral values as of the January 27, 2012 acquisition date.

| First Commercial Bank | September 7, 2012 | | |
|---|---|---|---|
| (in thousands) | Contractual Amount | Fair Value Adjustments | Fair Value |
| Assets acquired | | | |
| Cash and cash equivalents | $10,524 | $ - | $10,524 |
| Securities available for sale | 12,002 | - | 12,002 |
| Loans | 171,744 | (44,214) | 127,530 |
| Federal Home Loan Bank stock, at cost | 407 | - | 407 |
| Other assets and accrued interest receivable | 829 | (95) | 734 |
| Other real estate owned | 19,360 | (8,389) | 10,971 |
| Core deposit intangible | - | 559 | 559 |
| Discount | (79,412) | 79,412 | - |
| FDIC settlement receivable | 64,326 | - | 64,326 |
| Total assets acquired | $199,780 | $ 27,273 | $227,053 |
| Liabilities assumed | | | |
| Deposits | | | |
| Non interest-bearing | $7,197 | $ - | $7,197 |
| Interest-bearing | 189,057 | 3 | 189,060 |
| Total deposits | 196,254 | 3 | 196,257 |
| Federal Home Loan Bank advances | 3,002 | 63 | 3,065 |
| Accrued income taxes payable | - | 9,706 | 9,706 |
| Other liabilities and accrued interest payable | 524 | 95 | 619 |
| Total liabilities assumed | $199,780 | $ 9,867 | $209,647 |
| Equity | | | |
| Bargain purchase gain, net of taxes | - | 17,406 | 17,406 |
| Other operating loss, net of taxes | - | - | - |
| Accumulated other comprehensive loss | - | - | - |
| Total liabilities assumed and equity | $199,780 | $ 27,273 | $227,053 |

Information obtained subsequent to September 7, 2012 through the date of this filing was considered in forming FCB estimates of cash flows and collateral values as of the September 7, 2012 acquisition date.

A summary of the net assets acquired from the FDIC and the estimated fair value adjustments as of the respective acquisition dates follows:

| Tennessee Commerce Bank | January 27, 2012 | | | |
|---|---|---|---|---|
| (in thousands) | As Previously Reported | Second Quarter Recast Adjustments | Third Quarter Recast Adjustments | As Recasted |
| Assets acquired, at contractual amount | $ 221,126 | $ - | $ - | $ 221,126 |
| Liabilities assumed, at contractual amount | (948,701 ) | - | - | (948,701 ) |
| Net liabilities assumed per the P&A Agreement | (727,575 ) | - | - | (727,575 ) |
| Contractual Discount | (56,970 ) | - | - | (56,970 ) |
| Net receivable from the FDIC | $ (784,545 ) | $ - | $ - | $ (784,545 ) |
| Fair value adjustments: | | | | |
| Loans | $ (22,666 ) | $ 919 | $ (89 ) | $ (21,836 ) |
| Discount for loans to be repurchased by the FDIC | (2,797 ) | - | - | (2,797 ) |
| Other real estate owned | (3,359 ) | (1,000 ) | (113 ) | (4,472 ) |
| Other assets and accrued interest receivable | (60 ) | - | - | (60 ) |
| Core deposit intangible | 64 | - | - | 64 |
| Deposits | (54 ) | - | - | (54 ) |
| All other | (199 ) | (15 ) | 13 | (201 ) |
| Total fair value adjustments | (29,071 ) | (96 ) | (189 ) | (29,356 ) |
| Discount | 56,970 | - | - | 56,970 |
| Bargain purchase gain, pre-tax | $ 27,899 | $ (96 ) | $ (189 ) | $ 27,614 |

First Commercial Bank

| (in thousands) | September 7, 2012 |
|---|---|
| Assets acquired, at contractual amount | $ 214,866 |
| Liabilities assumed, at contractual amount | (199,780 ) |
| Net liabilities assumed per the P&A Agreement | 15,086 |
| Contractual Discount | (79,412 ) |
| Net receivable from the FDIC | $ (64,326 ) |
| Fair value adjustments: | |
| Loans | $ (44,214 ) |
| Other real estate owned | (8,389 ) |
| Other assets and accrued interest receivable | (95 ) |

| | | | |
|---|---|---|---|
| Core deposit intangible | | 559 | |
| Deposits | | (3 | ) |
| Federal Home Loan Bank advances | | (63 | ) |
| All other | | (95 | ) |
| Total fair value adjustments | | (52,300 | ) |
| | | | |
| Discount | | 79,412 | |
| Bargain purchase gain, pre-tax | $ | 27,112 | |

Tennessee Commerce Bank

During the first quarter of 2012, the Bank recorded an initial bargain purchase gain of $27.9 million as a result of the TCB acquisition. The bargain purchase gain was realized because the overall price paid by RB&T was substantially less than the fair value of the TCB assets acquired and liabilities assumed in the acquisition. Subsequent to the first quarter of 2012, the Bank posted adjustments to the acquired assets for its FDIC-assisted acquisition in the determination of day-one fair values and recorded a decrease to the bargain purchase gain of $285,000, as additional information relative to the acquisition date fair values became available.

On January 27, 2012, as part of the Purchase & Assumption Agreement, RB&T did not immediately acquire the TCB banking facility, including outstanding lease agreements and furniture, fixtures and equipment. During the third quarter of 2012, RB&T renegotiated a new lease with the landlord related to the sole banking facility and acquired all related data processing equipment and fixed assets totaling approximately $288,000.

First Commercial Bank

During the third quarter of 2012, the Bank recorded an initial bargain purchase gain of $27.1 million as a result of the FCB acquisition. The bargain purchase gain was realized because the overall price paid by RB&T was substantially less than the fair value of the FCB assets acquired and liabilities assumed in the acquisition.

On September 7, 2012, as part of the Purchase & Assumption Agreement, RB&T did not immediately acquire the FCB banking facility, including outstanding lease agreements and furniture, fixtures and equipment. RB&T will acquire all data processing equipment and fixed assets totaling approximately $350,000 during the fourth quarter of 2012, if RB&T chooses to maintain the current lease for FCB’s sole location.

FAIR VALUE METHODS ASSOCIATED WITH THE ACQUISITIONS OF FAILED BANKS

The following is a description of the methods used to determine the fair values of significant assets and liabilities at the respective acquisition dates as presented throughout:

Cash and Due from Banks and Interest-bearing Deposits in Banks –The carrying amount of these assets, adjusted for any cash items deemed uncollectible by management, was determined to be a reasonable estimate of fair value based on their short-term nature.

Investment Securities – Investment securities were acquired at fair value from the FDIC. The fair values provided by the FDIC were reviewed and considered reasonable based on RB&T's understanding of the marketplace. Federal Home Loan Bank ("FHLB") stock was acquired at cost, as it is not practicable to determine its fair value given restrictions on its marketability.

With the TCB acquisition, RB&T acquired $43 million in securities at fair value. The majority of the securities acquired were subsequently sold during the first quarter of 2012 with RB&T realizing a net gain on the corresponding sales of approximately $56,000.

With the FCB acquisition, RB&T acquired $12 million in securities at fair value. The nature of these securities acquired were consistent with RB&T's existing investment portfolio and RB&T elected not to sell these securities.

Loans – Fair values for loans were based on a discounted cash flow methodology that considered factors including the type of loan and related collateral, classification status, fixed or variable interest rate, term of loan and whether or not the loan was amortizing, and a discount rate reflecting current market rates for new originations of comparable loans adjusted for the risk inherent in the cash flow estimates.

Certain loans that were deemed to be collateral dependent were valued based on the fair value of the underlying collateral. These estimates were based on the most recently available real estate appraisals with certain adjustments made based on the type of property, age of appraisal, current status of the property and other related factors to estimate the current value of the collateral.

With the TCB acquisition, RB&T purchased approximately $99 million in loans with a fair value of approximately $74 million. Subsequent to January 27, 2012, the FDIC repurchased approximately $20 million of TCB loans at a price of par less the original discount that RB&T received when it purchased the loans on January 27, 2012 of $3 million. Loans repurchased by the FDIC were valued at the contractual amount reduced by the applicable discount.

With the FCB acquisition, RB&T purchased approximately $172 million in loans with a fair value of approximately $127 million.

The composition of acquired loans as of the respective acquisition dates follows:

| Tennessee Commerce Bank | January 27, 2012 | | | |
|---|---|---|---|---|
| | As Previously Reported | | As Recasted | |
| (in thousands) | Contractual Amount | Fair Value Adjustments | Recast Adjustments | Fair Value |
| Residential real estate | $ 22,693 | $ (4,076) | $ 243 | $ 18,860 |
| Commercial real estate | 18,646 | (6,971) | 1,988 | 13,663 |
| Real estate construction | 14,877 | (2,681) | (1,972) | 10,224 |
| Commercial | 13,224 | (6,939) | 496 | 6,781 |
| Home equity | 6,220 | (606) | 24 | 5,638 |
| Consumer: | | | | |
| Credit cards | 608 | (22) | - | 586 |
| Overdrafts | 672 | (621) | - | 51 |
| Other consumer | 2,172 | (750) | 51 | 1,473 |
| Total loans | $ 79,112 | $ (22,666) | $ 830 | $ 57,276 |

| First Commercial Bank | September 7, 2012 | | |
|---|---|---|---|
| (in thousands) | Contractual Amount | Fair Value Adjustments | Fair Value |
| Residential real estate | $ 48,409 | $ (9,353) | $ 39,056 |
| Commercial real estate | 82,161 | (12,688) | 69,473 |
| Real estate construction | 14,918 | (6,182) | 8,736 |
| Commercial | 25,475 | (15,983) | 9,492 |
| Home equity | 404 | (3) | 401 |
| Consumer: | | | |
| Credit cards | - | - | - |
| Overdrafts | 6 | - | 6 |
| Other consumer | 371 | (5) | 366 |
| Total loans | $ 171,744 | $ (44,214) | $ 127,530 |

The following table presents the purchased loans that are included within the scope of ASC Topic 310-30:

| Tennessee Commerce Bank | January 27, 2012 | | |
|---|---|---|---|
| (in thousands) | As Previously Reported | Recast Adjustments | As Recasted |
| Contractually-required principal and interest payments | $52,278 | $ - | $52,278 |
| Non-accretable difference | (21,308) | 903 | (20,405) |
| Accretable yield | (425) | (58) | (483) |
| Fair value of loans | $30,545 | $ 845 | $31,390 |

First Commercial Bank Acquisition

| (in thousands) | September 7, 2012 |
| --- | --- |
| Contractually-required principal and interest payments | $ 116,940 |
| Non-accretable difference | (33,523 ) |
| Accretable yield | (2,827 ) |
| Fair value of loans | $ 80,590 |

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For the nine months ended September 30, 2012 the Bank did not "transfer" any amounts between non-accretable and accretable yield related to the TCB acquisition. Instead, any changes between the accretable and non-accretable components were deemed to be the result of facts and circumstances that existed the day of the acquisition and became known to the Bank after the fact. Thus any adjustments between the two categories since the date of acquisition were deemed to be recast adjustments to the bargain purchase gain.

Core Deposit Intangible – In its assumption of the deposit liabilities for the 2012 acquisitions, RB&T believed that the customer relationships associated with these deposits had intangible value, although this value was anticipated to be modest given the nature of the deposit accounts and the anticipated rapid account run-off since acquired. RB&T recorded a core deposit intangible asset of $64,000 and $559,000 related to the TCB and FCB acquisitions, respectively. The fair value of this intangible asset was estimated based on a discounted cash flow methodology that gave appropriate consideration to type of deposit, deposit retention, cost of the deposit base, and net maintenance cost attributable to customer deposits.

OREO – OREO is presented at fair value, which is the estimated value that management expects to receive when the property is sold, net of related costs to sell. These estimates were based on the most recently available real estate appraisals, with certain adjustments made based on the type of property, age of appraisal, current status of the property and other related factors to estimate the current value of the property.

RB&T acquired $14 million in OREO related to the TCB acquisition, which was reduced by a $3 million fair value adjustment as of January 27, 2012. Subsequent to the first quarter, RB&T posted a total recast adjustment of $1.1 million to OREO to mark several properties to market based on appraisals received.

RB&T acquired $19 million in OREO related to the FCB acquisition, which was reduced by a $8 million fair value adjustment as of September 7, 2012. Information obtained subsequent to September 7, 2012 through the date of this filing was considered in forming the estimates of the fair value of the TCB OREO acquired.

FHLB Advances – RB&T acquired $3 million in FHLB advances related to the FCB acquisition. The advances were marked to market as of the acquisition date based on their early termination penalties as of that date. RB&T paid off the advances in September 2012 at no additional loss beyond the fair value adjustment as of their date of acquisition.

Deposits – The fair values used for the demand and savings deposits that comprise the acquisition accounts acquired, by definition, equal the amount payable on demand at the acquisition date. The fair values for time deposits are estimated using a discounted cash flow calculation that applies interest rates currently being offered to the interest rates embedded on such time deposits.

RB&T assumed $947 million in deposits at estimated fair value in connection with the TCB acquisition. As permitted by the FDIC, within seven days of the acquisition date, RB&T had the option to disclose to TCB's deposit customers that it was repricing the acquired deposit portfolios. In addition, depositors had the option to withdraw funds without penalty. RB&T chose to re-price all of the acquired TCB interest-bearing deposits, including transaction, time and brokered deposits with an effective date of January 28, 2012. This re-pricing triggered time and brokered deposit run-off consistent with management's expectations. Through September 30, 2012, approximately 95% of the assumed TCB interest-bearing deposit account balances had exited RB&T, with no penalty on the applicable time and brokered deposits. At September 30, 2012, RB&T had $52 million of deposits remaining from the TCB acquisition.

RB&T assumed $196 million in deposits at estimated fair value in connection with the FCB acquisition. RB&T chose to re-price all of the acquired FCB time deposits with an effective date of October 1, 2012. This re-pricing triggered certificate of deposit run-off consistent with management's expectations. Through September 30, 2012, approximately 38% of the assumed interest-bearing deposit account balances had exited RB&T, with no penalty on the applicable time and brokered deposits. Information obtained subsequent to September 7, 2012 through the date of this filing, was considered in forming estimates of cash flows for the deposit liabilities assumed as of the acquisition date.

The composition of deposits assumed at fair value as of the respective 2012 acquisitions of failed banks follows:

| Tennessee Commerce Bank | January 27, 2012 | | | |
|---|---|---|---|---|
| (in thousands) | Contractual Amount | Fair Value Adjustments | Recast Adjustments | Fair Value |
| Demand | $3,190 | $ - | $ - | $3,190 |
| Money market accounts | 11,338 | - | - | 11,338 |
| Savings | 91,859 | - | - | 91,859 |
| Individual retirement accounts* | 15,486 | - | - | 15,486 |
| Time deposits, $100,000 and over* | 278,825 | - | - | 278,825 |
| Other certificates of deposit* | 108,003 | 14 | - | 108,017 |
| Brokered certificates of deposit* | 418,940 | 40 | - | 418,980 |
| Total interest-bearing deposits | 927,641 | 54 | - | 927,695 |
| Total non interest-bearing deposits | 19,754 | - | - | 19,754 |
| Total deposits | $947,395 | $ 54 | $ - | $947,449 |

| First Commercial Bank | September 7, 2012 | | | |
|---|---|---|---|---|
| (in thousands) | Contractual Amount | Fair Value Adjustments | Recast Adjustments | Fair Value |
| Demand | $4,003 | $ - | $ - | $4,003 |
| Money market accounts | 38,187 | - | - | 38,187 |
| Savings | - | - | - | - |
| Individual retirement accounts* | 16,780 | - | - | 16,780 |
| Time deposits, $100,000 and over* | 14,740 | - | - | 14,740 |
| Other certificates of deposit* | 62,033 | 3 | - | 62,036 |
| Brokered certificates of deposit* | 53,314 | - | - | 53,314 |
| Total interest-bearing deposits | 189,057 | 3 | - | 189,060 |
| Total non interest-bearing deposits | 7,197 | - | - | 7,197 |
| Total deposits | $196,254 | $ 3 | $ - | $196,257 |

* - denotes a time deposit

RESULTS OF OPERATIONS

With regard to the 2012 acquisitions of failed banks, disclosure of supplemental pro forma financial information and prior period comparisons is deemed neither practical nor meaningful given the troubled nature of the institutions prior to RB&T's acquisition. Results of operations for the TCB and FCB franchises included in the consolidated results follows:

Tennessee Commerce Bank

| (in thousands) | Three Months Ended September 30, 2012 | Nine Months Ended September 30, 2012 |
|---|---|---|
| Interest income: | | |
| Loans, including fees | $ 729 | $ 2,372 |
| Taxable investment securities | 253 | 696 |
| Total interest income | 982 | 3,068 |
| Interest expense: | | |
| Deposits | 9 | 56 |
| Total interest expense | 9 | 56 |
| Net interest income | 973 | 3,012 |
| Provision for loan losses | - | - |
| Net interest income after provision for loan losses | 973 | 3,012 |
| Non interest income: | | |
| Service charges on deposit accounts | 24 | 48 |
| Bargain purchase gain | (189) | 27,614 |
| Gain on sale of securities available for sale | - | 56 |
| Other | 74 | 700 |
| Total non interest income | (91) | 28,418 |
| Non interest income | | |
| Salaries and employee benefits | 488 | 2,497 |
| Occupancy and equipment, net | 188 | 774 |
| Communication and transportation | 29 | 189 |
| Marketing and development | (15) | 4 |
| FDIC insurance expense | 8 | 60 |
| Data processing | 78 | 685 |
| Supplies | 7 | 28 |
| Other real estate owned expense | 58 | 161 |
| Other | 183 | 963 |
| Total non interest expenses | 1,024 | 5,361 |
| Income before income tax expense | $ (142) | $ 26,069 |

Related to the TCB acquisition, RB&T incurred acquisition and integration costs of approximately $2.3 million through September 30, 2012. Included in the total integration costs was $671,000 for estimated short-term retention bonuses for certain former TCB employees and short-term incentive bonuses for existing RB&T employees related to the successful branch consolidation and core system conversion completed in July 2012. In addition, total integration costs included $622,000 for estimated professional and consulting fees, as well as $328,000 for a long-term incentive program for RB&T employees based upon a 2-year profitability target for the overall TCB operation.

On July 13, 2012, RB&T converted the TCB core operating platform into its own. Beginning in August, TCB achieved direct operating expenses more in-line with other banking center operating costs.

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First Commercial Bank

| (in thousands) | | Three and Nine Months Ended September 30, 2012 |
|---|---|---|
| Interest income: | | |
| Loans, including fees | $ | 474 |
| Taxable investment securities | | 4 |
| Total interest income | | 478 |
| Interest expense: | | |
| Deposits | | 141 |
| Total interest expense | | 141 |
| Net interest income | | 337 |
| Provision for loan losses | | - |
| Net interest income after provision for loan losses | | 337 |
| Non interest income: | | |
| Service charges on deposit accounts | | 7 |
| Bargain purchase gain | | 27,112 |
| Gain on sale of securities available for sale | | - |
| Other | | 1 |
| Total non interest income | | 27,120 |
| Non interest income | | |
| Salaries and employee benefits | | 613 |
| Occupancy and equipment, net | | 210 |
| Communication and transportation | | 15 |
| Marketing and development | | - |
| FDIC insurance expense | | 9 |
| Data processing | | 265 |
| Supplies | | 41 |
| Other real estate owned expense | | 165 |
| Other | | 644 |
| Total non interest expenses | | 1,962 |
| Income before income tax expense | $ | 25,495 |

Related to the FCB acquisition, RB&T accrued acquisition and integration costs of approximately $1.2 million through September 30, 2012. Included in the total integration costs was $402,000 for estimated short-term retention bonuses for certain former FCB employees and short-term incentive bonuses for existing RB&T employees related to a successful branch consolidation and core system conversion. In addition, total integration costs included $320,000 for estimated professional and consulting fees, as well as $88,000 for a long-term incentive program for RB&T employees based upon a 2-year profitability target for the overall FCB operation.

3. 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, 2012 (in thousands) | Gross Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses | Fair Value |
|---|---|---|---|---|
| U.S. Treasury securities and | | | | |
| U.S. Government agencies | $91,910 | $771 | $- | $92,681 |
| Private label mortgage backed security | 5,818 | - | (866) | 4,952 |
| Mortgage backed securities - residential | 217,147 | 7,446 | - | 224,593 |
| Collateralized mortgage obligations | 209,312 | 1,758 | (60) | 211,010 |
| Total securities available for sale | $524,187 | $9,975 | $(926) | $533,236 |

| December 31, 2011 (in thousands) | Gross Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses | Fair Value |
|---|---|---|---|---|
| U.S. Treasury securities and | | | | |
| U.S. Government agencies | $152,085 | $814 | $(225) | $152,674 |
| Private label mortgage backed security | 5,818 | - | (1,276) | 4,542 |
| Mortgage backed securities - residential | 287,013 | 6,343 | (27) | 293,329 |
| Collateralized mortgage obligations | 194,663 | 1,281 | (541) | 195,403 |
| Total securities available for sale | $639,579 | $8,438 | $(2,069) | $645,948 |

Mortgage backed Securities

At September 30, 2012, the majority of the mortgage backed securities held by the Bank were issued by U.S. government-sponsored entities and agencies, primarily Federal Home Loan Mortgage Corporation (“Freddie Mac” or “FHLMC”) and Fannie Mae (“FNMA”), institutions that the government has affirmed its commitment to support. At September 30, 2012 and December 31, 2011, there were gross unrealized/unrecognized losses of $60,000 and $568,000 related to available for sale and held to maturity mortgage backed securities other than the private label mortgage backed security. Because the decline in fair value of 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.

The Bank’s mortgage backed securities portfolio includes one private label mortgage backed security with a fair value of $5.0 million that had gross unrealized losses of approximately $866,000 at September 30, 2012 and $1.3 million at December 31, 2011. As of September 30, 2012, the Bank believes there is no further credit loss component of OTTI related to the private label mortgage backed security in addition to that which has already been recorded. Additionally, the Bank does not have the intent to sell this security and it is likely that it will not be required to sell the security before its anticipated recovery.

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Securities to be held to maturity:

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

| September 30, 2012 (in thousands) | Carrying Value | Gross Unrecognized Gains | Gross Unrecognized Losses | Fair Value |
|---|---|---|---|---|
| U.S. Treasury securities and U.S. Government agencies | $4,417 | $ 13 | $ (7 ) | $4,423 |
| Mortgage backed securities - residential | 1,085 | 95 | - | 1,180 |
| Collateralized mortgage obligations | 42,524 | 321 | - | 42,845 |
| Total securities to be held to maturity | $48,026 | $ 429 | $ (7 ) | $48,448 |

| December 31, 2011 (in thousands) | Carrying Value | Gross Unrecognized Gains | Gross Unrecognized Losses | Fair Value |
|---|---|---|---|---|
| U.S. Treasury securities and U.S. Government agencies | $4,233 | $ 18 | $ (10 ) | $4,241 |
| Mortgage backed securities - residential | 1,376 | 101 | - | 1,477 |
| Collateralized mortgage obligations | 22,465 | 159 | - | 22,624 |
| Total securities to be held to maturity | $28,074 | $ 278 | $ (10 ) | $28,342 |

During the nine months ended September 30, 2012, the Bank recognized net securities gains in earnings for securities available for sale as follows:

The Bank sold six available for sale securities acquired in the TCB acquisition with an amortized cost of $35 million, resulting in a pre-tax gain of $53,000 during the first quarter of 2012.
The Bank realized $3,000 in pre-tax gains related to unamortized discount accretion on $10 million of callable U.S. Government agencies that were called during the first quarter of 2012 before their maturity.
There were no sales of securities available for sale during the second or third quarters of 2012.

During the nine months ended September 30, 2011, the Bank recognized net securities gains in earnings for securities available for sale as follows:

During the second quarter of 2011, the Bank sold available for sale mortgage backed securities with an amortized cost of $132 million, resulting in a pre-tax gain of $2.0 million.
During the third quarter of 2011, the Bank realized $188,000 in pre-tax gains related to unamortized discount accretion on $24 million of callable U.S. Government agencies that were called during the third quarter of 2011 before their maturity.

The tax provision related to the Bank's realized gains totaled $20,000 and $772,000 for the nine months ended September 30, 2012 and 2011, respectively.

See additional discussion regarding securities acquired in connection with the 2012 acquisitions of failed banks under Footnote 2 "Acquisitions of Failed Banks" of Part I Item 1 "Financial Statements."

The amortized cost and fair value of the investment securities portfolio by contractual maturity at September 30, 2012 follows. Expected maturities may differ from contractual maturities if borrowers have the right to call or prepay obligations whether or not there are associated call or prepayment penalties. Securities not due at a single maturity date are detailed separately.

| September 30, 2012 (in thousands) | Securities available for sale Amortized Cost | Securities available for sale Fair Value | Securities held to maturity Carrying Value | Securities held to maturity Fair Value |
|---|---|---|---|---|
| Due in one year or less | $ 1,009 | $ 1,009 | $ 2,211 | $ 2,213 |
| Due from one year to five years | 88,342 | 89,112 | 2,206 | 2,210 |
| Due from five years to ten years | 2,559 | 2,560 | - | - |
| Due beyond ten years | - | - | - | - |
| Private label mortgage backed security | 5,818 | 4,952 | - | - |
| Mortgage backed securities - residential | 217,147 | 224,593 | 1,085 | 1,180 |
| Collateralized mortgage obligations | 209,312 | 211,010 | 42,524 | 42,845 |
| Total securities | $ 524,187 | $ 533,236 | $ 48,026 | $ 48,448 |

At September 30, 2012 and December 31, 2011, 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.

Market Loss Analysis

Securities with unrealized losses at September 30, 2012 and December 31, 2011, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position, are as follows:

| September 30, 2012 (in thousands) | Less than 12 months Fair Value | Less than 12 months Unrealized Losses | 12 months or more Fair Value | 12 months or more Unrealized Losses | Total Fair Value | Total Unrealized Losses |
|---|---|---|---|---|---|---|
| U.S. Treasury securities and U.S. Government agencies | $ 500 | $ (7 ) | $ - | $ - | $ 500 | $ (7 ) |
| Private label mortgage backed security | - | - | 4,952 | (866 ) | 4,952 | (866 ) |
| Mortgage backed securities - residential, including Collateralized mortgage obligations | 16,336 | (60 ) | - | - | 16,336 | (60 ) |
| Total | $ 16,836 | $ (67 ) | $ 4,952 | $ (866 ) | $ 21,788 | $ (933 ) |

| December 31, 2011 (in thousands) | Less than 12 months Fair Value | Less than 12 months Unrealized Losses | 12 months or more Fair Value | 12 months or more Unrealized Losses | Total Fair Value | Total Unrealized Losses |
|---|---|---|---|---|---|---|

| | | | | | | |
|---|---|---|---|---|---|---|
| U.S. Treasury securities and U.S. Government agencies | $ 60,547 | $ (235 ) | $ - | $ - | $ 60,547 | $ (235 ) |
| Private label mortgage backed security | - | - | 4,542 | (1,276 ) | 4,542 | (1,276 ) |
| Mortgage backed securities - residential, including Collateralized mortgage obligations | 136,775 | (568 ) | - | - | 136,775 | (568 ) |
| Total | $ 197,322 | $ (803 ) | $ 4,542 | $ (1,276 ) | $ 201,864 | $ (2,079 ) |

At September 30, 2012, the Bank’s security portfolio consisted of 167 securities, six of which were in an unrealized loss position. The majority of the Bank’s unrealized loss dollars at September 30, 2012 were related to the Bank’s private label mortgage backed security, as discussed throughout this section of the filing.

Other-than-temporary impairment ("OTTI")

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 their 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 changes 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.

Nationally, residential real estate values have declined significantly since 2007. These declines in value, coupled with the reduced ability of certain homeowners to refinance or repay their residential real estate obligations, have led to elevated delinquencies and losses in residential real estate loans. Many of these loans have previously been securitized and sold to investors as private label mortgage backed securities. The Bank owns one private label mortgage backed security with a total carrying value of $5.8 million at September 30, 2012. This security is mostly backed by "Alternative A" first lien mortgage loans and is backed with an insurance "wrap" or guarantee with an average life currently estimated at five years. Due to current market conditions, this asset remains extremely illiquid, and as such, the Bank determined it to be a Level 3 security in accordance with FASB 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.

Further deterioration in economic conditions could cause the Bank to record additional impairment charges related to credit losses of up to $5.8 million, which is the current gross amortized cost of the Bank's one private label mortgage backed security.

See additional discussion regarding the Bank's private label mortgage backed security under Footnote 7 "Fair Value."

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, 2012 | December 31, 2011 |
|---|---|---|
| Carrying amount | $ 403,009 | $ 613,927 |
| Fair value | 411,720 | 620,922 |

4. LOANS AND ALLOWANCE FOR LOAN LOSSES

The composition of the loan portfolio follows:

| (in thousands) | | September 30, 2012 | | December 31, 2011 |
| --- | --- | --- | --- | --- |
| Residential real estate: | | | | |
| Owner occupied | $ | 1,144,544 | $ | 985,735 |
| Non owner occupied | | 80,142 | | 99,161 |
| Commercial real estate | | 716,516 | | 639,966 |
| Commercial real estate - purchased whole loans | | 33,374 | | 32,741 |
| Real estate construction | | 79,162 | | 67,406 |
| Commercial | | 146,400 | | 119,117 |
| Warehouse lines of credit | | 166,884 | | 41,496 |
| Home equity | | 251,072 | | 280,235 |
| Consumer: | | | | |
| Credit cards | | 8,570 | | 8,580 |
| Overdrafts | | 733 | | 950 |
| Other consumer | | 14,960 | | 9,908 |
| Total loans | | 2,642,357 | | 2,285,295 |
| Less: Allowance for loan losses | | 24,100 | | 24,063 |
| Total loans, net | $ | 2,618,257 | $ | 2,261,232 |

As discussed under Footnote 2 "Acquisitions of Failed Banks," the above loan balances at September 30, 2012, contained $160 million related to the 2012 TCB and FCB acquisitions.

The contractual amount of the loans purchased in the TCB acquisition decreased from $79 million as of the acquisition date to $45 million as of September 30, 2012. The carrying value of the loans purchased in the TCB acquisition was $57 million as of the acquisition date compared to $34 million as of September 30, 2012.

The contractual amount and carrying value of the loans purchased in the FCB acquisition were $162 million and $126 million, as of September 30, 2012.

The composition of TCB and FCB loans outstanding at September 30, 2012 follows:

| September 30, 2012 (in thousands) | | TCB | | FCB | | Total |
| --- | --- | --- | --- | --- | --- | --- |
| Residential real estate | $ | 13,215 | $ | 37,971 | $ | 51,186 |
| Commercial real estate | | 8,100 | | 69,440 | | 77,540 |
| Real estate construction | | 5,326 | | 8,732 | | 14,058 |
| Commercial | | 1,549 | | 9,238 | | 10,787 |
| Home equity | | 4,755 | | 381 | | 5,136 |
| Consumer: | | | | | | - |
| Credit cards | | 393 | | - | | 393 |
| Overdrafts | | 4 | | 8 | | 12 |
| Other consumer | | 859 | | 370 | | 1,229 |
| Total loans | $ | 34,201 | $ | 126,140 | $ | 160,341 |

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Credit Quality Indicators

Bank procedures for assessing and maintaining credit gradings differs slightly depending on whether a new or renewed loan is being underwritten, or whether an existing loan is being re-evaluated for potential credit quality concerns. The latter usually occurs upon receipt of updated financial information, or other pertinent data, that would potentially cause a change in the loan grade. Specific Bank procedures follow:

> For new and renewed commercial, commercial real estate and real estate construction, the Bank's Credit Administration Department ("CAD"), which acts independently of the loan officer, assigns the credit quality grade to the loan. Loan grades for new commercial, commercial real estate and real estate construction loans with an aggregate credit exposure of $1.5 million or greater are validated by the Senior Loan Committee ("SLC"). Loan grades for renewed commercial, commercial real estate and real estate construction loans with an aggregate credit exposure of $2 million or greater, are also validated by the SLC.
>
> The SLC is chaired by the Chief Operating Officer of Commercial Banking ("COO") and includes the Bank's Chief Commercial Credit Officer ("CCCO") and is attended by the Bank's Chief Risk Management Officer ("CRMO").
>
> Commercial loan officers are responsible for reviewing their loan portfolios and reporting any adverse material changes to the CCCO. When circumstances warrant a review and possible change in the credit quality grade, loan officers are required to notify the Bank's CAD.
>
> The COO meets monthly with commercial loan officers to discuss the status of past due loans and possible classified loans. These meetings are also designed to give loan officers an opportunity to identify an existing loan that should be downgraded.
>
> Monthly, members of senior management along with managers of Commercial Lending, CAD, Special Assets and Retail Collections attend a Special Asset Committee ("SAC") meeting. The SAC reviews all commercial and commercial real estate past due, classified, and impaired loans in excess of $100,000 and discusses the relative trends and current status of these assets. In addition, the SAC reviews all retail residential real estate loans exceeding $750,000 and all home equity loans exceeding $100,000 that are 80-days or more past due or that are on non-accrual status. SAC also reviews the actions taken by management regarding foreclosure mitigation, loan extensions, troubled debt restructures and collateral repossessions. Based on the information reviewed in this meeting, the SAC approves all specific loan loss allocations to be recognized by the Bank within its Allowance for Loan Loss analysis.
>
> All new and renewed warehouse lending loans are approved by the SLC and Executive Loan Committee. The CAD assigns the initial credit quality grade to warehouse lending loans. Monthly, members of senior management along with the SLC, review warehouse lending activity and monitor key performance indicators such as average days outstanding, average FICO, average LTV and other important factors.

On at least an annual basis, the Bank's internal loan review department analyzes all aggregate lending relationships with outstanding balances greater than $1 million that are internally classified as "Special Mention/Watch," "Substandard," "Doubtful" or "Loss." In addition, for all "Pass" rated loans, the Bank analyzes, on at least an annual basis, al aggregate lending relationships with outstanding balances exceeding $4 million.

The Banks's credit quality indicators consist of an internal grading system used to assign grades to all loans except residential real estate, consumer loans and purchased credit impaired loans. The Bank categorizes loans into risk categories based on relevant information about the ability of borrowers to service their debt such as: current financial information, historical payment experience, public information, and current economic trends. The Bank also considers the fair value of the underlying collateral and the strength and willingness of the guarantor(s). The Bank analyzes loans individually and based on this analysis, establishes a credit risk rating. The Bank uses the following definitions for risk ratings:

Risk Grade 1 – Excellent (Pass): Loans fully secured by liquid collateral, such as certificates of deposit, reputable bank letters of credit, or other cash equivalents; loans fully secured by publicly traded marketable securities where there is no impediment to liquidation; or loans to any publicly held company with a current long-term debt rating of A or better.

Risk Grade 2 – Good (Pass): Loans to businesses that have strong financial statements containing an unqualified opinion from a Certified Public Accounting firm and at least three consecutive years of profits; loans supported by unaudited financial statements containing strong balance sheets, five consecutive years of profits, a five-year satisfactory relationship with the Bank, and key balance sheet and income statement trends that are either stable or positive; loans that are guaranteed or otherwise backed by the full faith and credit of the U.S. government or an agency thereof, such as the Small Business Administration; or loans to publicly held companies with current long-term debt ratings of Baa or better.

Risk Grade 3 – Satisfactory (Pass): Loans supported by financial statements (audited or unaudited) that indicate average or slightly below average risk and having some deficiency or vulnerability to changing economic conditions; loans with some weakness but offsetting features of other support are readily available; loans that are meeting the terms of repayment, but which may be susceptible to deterioration if adverse factors are encountered.

Risk Grade 4 – Satisfactory/Monitored (Pass): Loans in this category are considered to be of acceptable credit quality, but contain greater credit risk than Satisfactory loans due to weak balance sheets, marginal earnings or cash flow, or other uncertainties. These loans warrant a higher than average level of monitoring to ensure that weaknesses do not advance. The level of risk in a Satisfactory/Monitored loan is within acceptable underwriting guidelines so long as the loan is given the proper level of management supervision.

Risk Grade 5 – Special Mention/Watch: Loans that possess some credit deficiency or potential weakness that deserves close attention. Such loans pose an unwarranted financial risk that, if not corrected, could weaken the loan by adversely impacting the future repayment ability of the borrower. The key distinctions of a Special Mention/Watch classification are that (1) it is indicative of an unwarranted level of risk and (2) credit weaknesses are not defined impairments to the primary source of repayment and are consider potential.

Purchased Credit Impaired Loans Group 1 ("PCI-1"): To the extent that purchased credit impaired loans, accounted for under ASC Topic 310-30 are performing in accordance with management's performance expectations established in conjunction with the determination of the day-one fair values, such loans are not risk rated in the same categories as the Bank's originated loans and are not considered in the determination of the required allowance for loan and lease losses. These loans are classified in the "PCI-1" category within the Bank's classified loans, which is the equivalent of a "Watch" classification for the Bank's originated loans.

PCI-1 loans may include loans that qualify as Troubled Debt Restructurings ("TDRs"), and therefore impaired, under the applicable TDR accounting standards. These TDRs within the PCI-1 category, however, will not be downgraded to Purchased Credit Impaired Group 2 Loans and will not require an additional provision for loan losses if their restructured cash flows are within management's initial expectations when the loans were booked at fair value as of their date(s) of acquisition.

Any improvement in the expected performance of a PCI-1 loan would result in an adjustment to accretable yield, which would have a positive impact on interest income.

Purchased Credit Impaired Loans Group 2 ("PCI-2"): To the extent that purchased credit impaired loans, accounted for under ASC Topic 310-30 have deteriorated from management's expectation established in conjunction with the determination of the day-one fair values, such loans will be considered impaired, and are considered in the determination of the required level of allowance for loan and lease losses. These loans are classified in the "PCI-2" category within the Bank's classified loans, which is the equivalent of a "Substandard" classification for the Bank's originated loans.

Any decrease in the expected cash flows will generally result in a provision for loan and lease losses. Any improvement in the expected performance of a PCI-2 loan would result in a reversal of the provision for loan and lease losses to the extent of prior charges and then an adjustment to accretable yield, which would have a positive impact on interest income.

See additional discussion regarding purchased credit impaired loans under Footnote 2 "Acquisitions of Failed Banks" of Part I Item 1 "Financial Statements."

Risk Grade 6 – Substandard: One or more of the following characteristics may be exhibited in loans classified Substandard:

- Loans that possess a defined credit weakness. The likelihood that a loan will be paid from the primary source of repayment is uncertain. Financial deterioration is under way and very close attention is warranted to ensure that the loan is collected without loss.
- Loans are inadequately protected by the current net worth and paying capacity of the obligor.
- The primary source of repayment is gone, and the Bank is forced to rely on a secondary source of repayment, such as collateral liquidation or guarantees.
- Loans have a distinct possibility that the Bank will sustain some loss if deficiencies are not corrected.
- Unusual courses of action are needed to maintain a high probability of repayment.
- The borrower is not generating enough cash flow to repay loan principal, however, it continues to make interest payments.
- The Bank is forced into a subordinated or unsecured position due to flaws in documentation.
- Loans have been restructured so that payment schedules, terms and collateral represent concessions to the borrower when compared to the normal loan terms.
- The Bank is seriously contemplating foreclosure or legal action due to the apparent deterioration in the loan.
- There is significant deterioration in market conditions to which the borrower is highly vulnerable.

Risk Grade 7 – Doubtful: One or more of the following characteristics may be present in loans classified Doubtful:

- Loans have all of the weaknesses of those classified as Substandard. However, based on existing conditions, these weaknesses make full collection of principal highly improbable.
- The primary source of repayment is gone, and there is considerable doubt as to the quality of the secondary source of repayment.
- The possibility of loss is high but because of certain important pending factors which may strengthen the loan, loss classification is deferred until the exact status of repayment is known.

Risk Grade 8 – Loss: Loans are considered uncollectible and of such little value that continuing to carry them as assets is not feasible. Loans will be classified Loss when it is neither practical nor desirable to defer writing off or reserving all or a portion of a basically worthless asset, even though partial recovery may be possible at some time in the future. These loans will be either written off or a specific valuation allowance established.

For all residential real estate and consumer loans that do not meet the scope above, the Bank uses a grading system based on delinquency. Loans that are 80 days or more past due, on non-accrual, or are troubled debt restructurings are graded "Substandard." Occasionally a real estate loan below scope may be graded as "Special Mention/Watch" or "Substandard" if the loan is cross collateralized with a classified commercial or commercial real estate loan.

Related to purchased loans accounted for under ASC Topic 310-20, such loans would be accounted for as would any other Bank-originated loan including presentation in any of the credit quality ratios, potentially becoming nonaccrual or impaired, as well as being risk rated under the Bank's standard practices and procedures. In addition, purchased loans accounted for under ASC Topic 310-20 are considered in the determination of the required allowance for loan and lease losses.

Related to purchased credit-impaired loans accounted for under ASC Topic 310-30, management separately monitors this portfolio and on a quarterly basis reviews the loans contained within this portfolio against the factors and assumptions used in determining the day-one fair values. In addition to its quarterly evaluation, a loan is typically reviewed when it is modified or extended, or when material information becomes available to the Bank that provides additional insight regarding the loan's performance, the status of the borrower, or the quality or value of the underlying collateral.

For all risk rated loans, the Bank's risk category of loans by class of loans follows:

| September 30, 2012 (in thousands) | Pass | Special Mention / Watch | Substandard | Doubtful / Loss | Purchased Credit Impaired Loans Group 1 | Purchased Credit Impaired Loans Group 2 | Total Rated Loans* |
|---|---|---|---|---|---|---|---|
| Residential real estate: | | | | | | | |
| Owner occupied | $ - | $ 2,336 | $ 11,370 | $ - | $ 4,983 | $ - | $ 18,689 |
| Non owner occupied | - | 4,400 | 2,524 | - | 23,294 | - | 30,218 |
| Commercial real estate | 624,382 | 20,740 | 17,710 | - | 53,684 | - | 716,516 |
| Commercial real estate - Purchased whole loans | 33,374 | - | - | - | - | - | 33,374 |
| Real estate construction | 60,146 | 1,787 | 3,056 | - | 14,173 | - | 79,162 |
| Commercial | 138,356 | 2,215 | 589 | - | 5,240 | - | 146,400 |
| Warehouse lines of credit | 166,884 | - | - | - | - | - | 166,884 |
| Home equity | - | 136 | 2,223 | - | - | - | 2,359 |
| Consumer: | | | | | | | |
| Credit cards | - | - | - | - | - | - | - |
| Overdrafts | - | - | - | - | - | - | - |
| Other consumer | - | 355 | 58 | - | 202 | - | 615 |
| Total rated loans | $ 1,023,142 | $ 31,969 | $ 37,530 | $ - | $ 101,576 | $ - | $ 1,194,217 |

| December 31, 2011 (in thousands) | Pass | Special Mention / Watch | Substandard | Doubtful / Loss | Total Rated Loans* |
|---|---|---|---|---|---|
| Residential real estate: | | | | | |
| Owner occupied | $ - | $ 1,180 | $ 14,002 | $ - | $ 15,182 |
| Non owner occupied | - | 2,470 | 2,295 | - | 4,765 |
| Commercial real estate | 600,338 | 27,158 | 12,470 | - | 639,966 |
| Commercial real estate - Purchased whole loans | 32,741 | - | - | - | 32,741 |
| Real estate construction | 54,963 | 2,353 | 10,090 | - | 67,406 |
| Commercial | 116,450 | 2,294 | 373 | - | 119,117 |
| Warehouse lines of credit | 41,496 | - | - | - | 41,496 |
| Home equity | - | - | 3,856 | - | 3,856 |
| Consumer: | | | | | |
| Credit cards | - | - | - | - | - |

| | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| Overdrafts | | - | | - | | - | | - | | - |
| Other consumer | | - | | - | | 2 | | - | | 2 |
| Total rated loans | $ | 845,988 | $ | 35,455 | $ | 43,088 | $ | - | $ | 924,531 |

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

Allowance for Loan Losses

Activity in the allowance for loan losses follows:

| (in thousands) | Three Months Ended September 30, 2012 | Three Months Ended September 30, 2011 | Nine Months Ended September 30, 2012 | Nine Months Ended September 30, 2011 |
|---|---|---|---|---|
| Allowance for loan losses at beginning of period | $22,510 | $25,931 | $24,063 | $23,079 |
| Charge offs - Traditional Banking | (1,220) | (2,975) | (7,444) | (6,142) |
| Charge offs - Refund Anticipation Loans | - | (6) | (11,097) | (15,484) |
| Total charge offs | (1,220) | (2,981) | (18,541) | (21,626) |
| Recoveries - Traditional Banking | 267 | 442 | 976 | 1,554 |
| Recoveries - Refund Anticipation Loans | 460 | 693 | 3,883 | 3,435 |
| Total recoveries | 727 | 1,135 | 4,859 | 4,989 |
| Net loan charge offs - Traditional Banking | (953) | (2,533) | (6,468) | (4,588) |
| Net loan charge offs - Refund Anticipation Loans | 460 | 687 | (7,214) | (12,049) |
| Net loan charge offs | (493) | (1,846) | (13,682) | (16,637) |
| Provision for loan losses - Traditional Banking | 2,543 | 547 | 6,505 | 5,454 |
| Provision for loan losses - Refund Anticipation Loans | (460) | (687) | 7,214 | 12,049 |
| Total provision for loan losses | 2,083 | (140) | 13,719 | 17,503 |
| Allowance for loan losses at end of period | $24,100 | $23,945 | $24,100 | $23,945 |

The Bank’s allowance calculation has historically included specific allowance allocations for qualitative factors such as:

- Concentrations of credit;
- Nature, volume and seasoning of particular loan portfolios;
- Experience, ability and depth of lending staff;
- Effects of any changes in risk selection and underwriting standards, and other changes in lending policies, procedures and practices;
- Trends that could impact collateral values;
- Expectations regarding business cycles;
- Credit quality trends (including trends in classified, past due and nonperforming loans);
- Competition, legal and regulatory requirements;
- General national and local economic and business conditions;
- Offering of new loan products; and
- Expansion into new markets

Prior to January 1, 2012, the Bank’s allowance for loan losses calculation was supported with qualitative factors, as described above, in addition to a nominal “unallocated” component that totaled $1.9 million as of December 31, 2011. The Bank believes that historically the “unallocated” allowance properly reflected estimated credit losses determined in accordance with GAAP. The unallocated allowance was primarily related to RB&T’s loan portfolio, which is highly concentrated in the Kentucky and Southern Indiana real estate markets. These markets have remained relatively stable during the current economic downturn, as compared to other parts of the U.S. With the Bank's recent expansion into the metropolitan Nashville, Tennessee and metropolitan Minneapolis, Minnesota markets, its plans to pursue future acquisitions into potentially new markets through FDIC-assisted transactions and its offering of new loan products, such as mortgage warehouse lines of credit, the Bank elected to revise its methodology to provide a more detailed calculation when estimating the impact of qualitative factors over the Bank's various loan categories.

In executing this methodology change, the Bank primarily focused on large groups of smaller-balance homogeneous loans that are collectively evaluated for impairment and are generally not included in the scope of ASC Topic 310-10-35 Accounting by Creditors for Impairment of a Loan. These portfolios are typically not graded and not subject to annual review. Such groups of loans include:

- Residential real estate
  - Owner Occupied
  - Non Owner Occupied
- Home equity
- Consumer:
  - Credit cards
  - Overdrafts
  - Other consumer

See the table below for the quantification of the unallocated allowance methodology change among the loan segments. This methodology change had no impact on the Bank's net provision for loan losses for the three and nine months ended September 30, 2012.

The following tables present the activity in the allowance for loan losses by portfolio class for the nine months ended September 30, 2012 and 2011:

| Nine Months Ended September 30, 2012 (in thousands) | Residential Real Estate Owner Occupied | Residential Real Estate Non Owner Occupied | Commercial Real Estate | Commercial Real Estate - Purchased Whole Loans | Real Estate Construction | Commercial | Warehouse Lines of Credit |
|---|---|---|---|---|---|---|---|
| Beginning balance | $ 5,212 | $ 1,142 | $ 7,724 | $ - | $ 3,042 | $ 1,025 | $ 104 |
| Allocation of previously unallocated allowance | 1,117 | 146 | 47 | - | - | - | - |
| Provision for loan losses | 2,617 | 255 | 1,513 | 40 | 1,604 | (293 ) | 313 |
| Loans charged off | (2,422 ) | (318 ) | (353 ) | - | (1,796 ) | (18 ) | - |
| Recoveries | 183 | 14 | 70 | - | 83 | 21 | - |
| Ending balance | $ 6,707 | $ 1,239 | $ 9,001 | $ 40 | $ 2,933 | $ 735 | $ 417 |

| (continued) | Home Equity | Refund Anticipation Loans | Credit Cards | Consumer Overdrafts | Consumer Other Consumer | Unallocated | Total |
|---|---|---|---|---|---|---|---|
| Beginning balance | $ 2,984 | $ - | $ 503 | $ 135 | $ 227 | $ 1,965 | $ 24,063 |
| Allocation of previously unallocated allowance | 536 | - | 47 | 17 | 55 | (1,965 ) | - |
| Provision for loan losses | 765 | 7,214 | (293 ) | (14 ) | (2 ) | - | 13,719 |
| Loans charged off | (1,947 ) | (11,097 ) | (87 ) | (318 ) | (185 ) | - | (18,541 ) |
| Recoveries | 73 | 3,883 | 33 | 332 | 167 | - | 4,859 |
| Ending balance | $ 2,411 | $ - | $ 203 | $ 152 | $ 262 | $ - | $ 24,100 |

| Nine Months Ended September 30, 2011 (in | Residential Real Estate Owner Occupied | Residential Real Estate Non Owner Occupied | Commercial Real Estate | Commercial Real Estate - Purchased Whole Loans | Real Estate Construction | Commercial | Warehouse Lines of Credit |
|---|---|---|---|---|---|---|---|

| thousands) | | | | | | | |
|---|---|---|---|---|---|---|---|
| Beginning balance | $ 3,775 | $ 1,507 | $ 7,214 | $ - | $ 2,612 | $ 1,347 | $ - |
| Provision for loan losses | 2,372 | 192 | 1,512 | - | 1,083 | (322) | 43 |
| Loans charged off | (1,699) | (512) | (1,081) | - | (823) | (100) | - |
| Recoveries | 186 | 4 | 284 | - | 231 | 125 | - |
| Ending balance | $ 4,634 | $ 1,191 | $ 7,929 | $ - | $ 3,103 | $ 1,050 | $ 43 |

| (continued) | Home Equity | Refund Anticipation Loans | Credit Cards | Consumer Overdrafts | Other Consumer | Unallocated | Total |
|---|---|---|---|---|---|---|---|
| Beginning balance | $ 3,581 | $ - | $ 492 | $ 125 | $ 461 | $ 1,965 | $ 23,079 |
| Provision for loan losses | 555 | 12,049 | 114 | 67 | (162) | - | 17,503 |
| Loans charged off | (1,043) | (15,484) | (172) | (486) | (226) | - | (21,626) |
| Recoveries | 100 | 3,435 | 24 | 395 | 205 | - | 4,989 |
| Ending balance | $ 3,193 | $ - | $ 458 | $ 101 | $ 278 | $ 1,965 | $ 23,945 |

Non-performing Loans and Non-performing Assets

Detail of non-performing loans and non-performing assets follows:

| (in thousands) | September 30, 2012 | | December 31, 2011 | |
|---|---|---|---|---|
| Loans on non-accrual status | $ 20,436 | | $ 23,306 | |
| Loans past due 90 days or more and still on accrual | 616 | | - | |
| Total non-performing loans | 21,052 | | 23,306 | |
| Other real estate owned | 25,148 | | 10,956 | |
| Total non-performing assets | $ 46,200 | | $ 34,262 | |
| Total Company Credit Quality Ratios: | | | | |
| Non-performing loans to total loans | 0.80 | % | 1.02 | % |
| Non-performing assets to total loans (including OREO) | 1.73 | % | 1.49 | % |
| Non-performing assets to total assets | 1.34 | % | 1.00 | % |
| Traditional Banking Credit Quality Ratios: | | | | |
| Non-performing loans to total loans | 0.80 | % | 1.02 | % |
| Non-performing assets to total loans (including OREO) | 1.73 | % | 1.49 | % |
| Non-performing assets to total assets | 1.34 | % | 1.10 | % |

The other real estate owned balance at September 30, 2012 includes $12 million related to the 2012 acquisitions of failed banks. See additional discussion regarding the TCB and FCB acquisitions under Footnote 2 “Acquisitions of Failed Banks” of Part I Item 1 “Financial Statements.”

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

| | Non-Accrual Loans | | Loans Past Due 90 Days or More and Still Accruing Interest | |
|---|---|---|---|---|
| in thousands) | September 30, 2012 | December 31, 2011 | September 30, 2012 | December 31, 2011 |
| Residential real estate: | | | | |
| Owner occupied | $ 11,636 | $ 12,183 | $ 158 | $ - |
| Non owner occupied | 1,582 | 1,565 | - | - |
| Commercial real estate | 2,808 | 3,032 | - | - |
| Commercial real estate - purchased whole loans | - | - | - | - |
| Real estate construction | 1,911 | 2,521 | 455 | - |
| Commercial | 505 | 373 | - | - |
| Warehouse lines of credit | - | - | - | - |
| Home equity | 1,880 | 3,603 | - | - |
| Consumer: | | | | |
| Credit cards | - | - | - | - |

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| Overdrafts | | - | | - | | - | | - |
| Other consumer | | 114 | | 29 | | 3 | | - |
| Total | $ | 20,436 | $ | 23,306 | $ | 616 | $ | - |

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 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 payments are reasonably assured. Non-accrual troubled debt restructurings (“TDRs”) are reviewed for return to accrual status on an individual basis, with additional consideration given to the modification terms.

Delinquent Loans

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

| September 30, 2012 (in thousands) | 30 - 59 Days Past Due | 60 - 89 Days Past Due | Greater than 90 Days Past Due * | Total Loans Past Due | Total Loans Not Past Due | Total Loans |
|---|---|---|---|---|---|---|
| Residential real estate: | | | | | | |
| Owner occupied | $2,488 | $968 | $7,034 | $10,490 | $1,134,054 | $1,144,544 |
| Non owner occupied | 842 | 5 | 602 | 1,449 | 78,693 | 80,142 |
| Commercial real estate | 446 | 606 | 737 | 1,789 | 714,727 | 716,516 |
| Commercial real estate - purchased whole loans | - | - | - | - | 33,374 | 33,374 |
| Real estate construction | - | - | 1,974 | 1,974 | 77,188 | 79,162 |
| Commercial | - | 191 | 67 | 258 | 146,142 | 146,400 |
| Warehouse lines of credit | - | - | - | - | 166,884 | 166,884 |
| Home equity | 814 | 89 | 676 | 1,579 | 249,493 | 251,072 |
| Consumer: | | | | | | |
| Credit cards | 50 | 10 | - | 60 | 8,510 | 8,570 |
| Overdrafts | 128 | 1 | - | 129 | 604 | 733 |
| Other consumer | 84 | 72 | 8 | 164 | 14,796 | 14,960 |
| Total | $4,852 | $1,942 | $11,098 | $17,892 | $2,624,465 | $2,642,357 |

The Bank had $160 million in loans outstanding related to the 2012 acquisitions of failed banks at September 30, 2012, with approximately $733,000 of the purchased loans (accounted for under both ASC Topic 310-20 and ASC Topic 310-30) past due 30 or more days. There were no past due loans related to the FCB acquisition at September 30, 2012, as the Bank was acquired on September 7, 2012. See additional discussion regarding the TCB and FCB acquisitions under Footnote 2 “Acquisitions of Failed Banks” of Part I Item 1 “Financial Statements.”

| December 31, 2011 (in thousands) | 30 - 59 Days Past Due | 60 - 89 Days Past Due | Greater than 90 Days Past Due * | Total Loans Past Due | Total Loans Not Past Due | Total Loans |
|---|---|---|---|---|---|---|
| Residential real estate: | | | | | | |
| Owner occupied | $4,275 | $1,850 | $7,083 | $13,208 | $972,527 | $985,735 |
| Non owner occupied | 51 | 71 | 969 | 1,091 | 98,070 | 99,161 |
| Commercial real estate | 2,094 | - | 3,032 | 5,126 | 634,840 | 639,966 |
| Commercial real estate - purchased whole loans | - | - | - | - | 32,741 | 32,741 |
| Real estate construction | - | - | 541 | 541 | 66,865 | 67,406 |
| Commercial | - | 16 | 89 | 105 | 119,012 | 119,117 |

| | | | | | | |
|---|---|---|---|---|---|---|
| Warehouse lines of credit | - | - | - | - | 41,496 | 41,496 |
| Home equity | 582 | 773 | 2,686 | 4,041 | 276,194 | 280,235 |
| Consumer: | | | | | | |
| Credit cards | 40 | 13 | - | 53 | 8,527 | 8,580 |
| Overdrafts | 129 | - | - | 129 | 821 | 950 |
| Other consumer | 60 | 79 | - | 139 | 9,769 | 9,908 |
| Total loans | $7,231 | $2,802 | $14,400 | $24,433 | $2,260,862 | $2,285,295 |

* - All loans that were 90 days or more past due as of September 30, 2012 and December 31, 2011 were on non-accrual status, except for purchased credit impaired loans accounted for under ASC Topic 310-30.

Impaired Loans

The Bank defines impaired loans as follows:

- All loans, excluding ASC Topic 310-30 purchased credit impaired loans, internally classified as “Substandard,” “Doubtful” or “Loss;”
- All loans, excluding ASC Topic 310-30 purchased credit impaired loans, internally classified as “Special Mention/Watch” on non-accrual status,
- All retail and commercial TDRs including ASC Topic 310-30 purchased credit impaired loans;
- ASC Topic 310-30 purchased credit impaired loans whereby current projected cash flows have deteriorated since acquisition, or cash flows cannot be reasonably estimated in terms of timing and amounts; and
- Any other situation where the collection of 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 document for additional discussion regarding the Bank’s loan classification structure.

Information regarding the Bank’s impaired loans follows:

| (in thousands) | September 30, 2012 | December 31, 2011 |
|---|---|---|
| Loans with no allocated allowance for loan losses | $ 47,103 | $ 32,171 |
| Loans with allocated allowance for loan losses | 44,615 | 45,022 |
| Total impaired loans | $ 91,718 | $ 77,193 |
| | | |
| Amount of the allowance for loan losses allocated | $ 6,664 | $ 7,086 |

Approximately $14 million in impaired loans were added during the first nine months of 2012 in connection with the 2012 acquisitions of failed banks. Substantially all of these loans became classified as “impaired” through a modification of the original loan, which the Bank deemed to be a TDR. See additional discussion regarding the TCB and FCB acquisitions under Footnote 2 “Acquisitions of Failed Banks” of Part I Item 1 “Financial Statements.”

The following tables present the balance in the allowance for loan losses and the recorded investment in loans by portfolio class based on impairment method as of September 30, 2012 and December 31, 2011:

| September 30, 2012 (in thousands) | Residential Real Estate Owner Occupied | Residential Real Estate Non Owner Occupied | Commercial Real Estate | Commercial Real Estate - Purchased Whole Loans | Real Estate Construction | Commercial | Warehouse Lines of Credit |
|---|---|---|---|---|---|---|---|
| Allowance for loan losses: | | | | | | | |
| Ending allowance balance attributable to loans: | | | | | | | |
| Individually evaluated for impairment | $ 1,429 | $ 566 | $ 2,705 | $ - | $ 1,291 | $ 367 | $ - |
| Collectively evaluated for impairment | 5,278 | 673 | 6,296 | 40 | 1,642 | 368 | 417 |
| Acquired with deteriorated credit quality | - | - | - | - | - | - | - |
| Total ending allowance for loan losses | $ 6,707 | $ 1,239 | $ 9,001 | $ 40 | $ 2,933 | $ 735 | $ 417 |
| Loans: | | | | | | | |
| Impaired loans individually evaluated | $ 37,993 | $ 5,272 | $ 36,114 | $ - | $ 5,979 | $ 4,694 | $ - |
| Loans collectively evaluated for impairment | 1,106,551 | 74,870 | 680,402 | 33,374 | 73,183 | 141,706 | 166,884 |
| Loans acquired with deteriorated credit quality | - | - | - | - | - | - | - |
| Total ending loan balance | $ 1,144,544 | $ 80,142 | $ 716,516 | $ 33,374 | $ 79,162 | $ 146,400 | $ 166,884 |

| (continued) | Home Equity | Consumer Credit Cards | Consumer Overdrafts | Consumer Other Consumer | Total |
|---|---|---|---|---|---|

| | | | | | |
|---|---|---|---|---|---|
| Allowance for loan losses: | | | | | |
| Ending allowance balance attributable to loans: | | | | | |
| Individually evaluated for impairment | $ 306 | $ - | $ - | $ - | $ 6,664 |
| Collectively evaluated for impairment | 2,105 | 203 | 152 | 262 | 17,436 |
| Acquired with deteriorated credit quality | - | - | - | - | - |
| Total ending allowance for loan losses | $ 2,411 | $ 203 | $ 152 | $ 262 | $ 24,100 |
| Loans: | | | | | |
| Impaired loans individually evaluated | $ 1,300 | $ - | $ - | $ 366 | $ 91,718 |
| Loans collectively evaluated for impairment | 249,772 | 8,570 | 733 | 14,594 | 2,550,639 |
| Loans acquired with deteriorated credit quality | - | - | - | - | - |
| Total ending loan balance | $ 251,072 | $ 8,570 | $ 733 | $ 14,960 | $ 2,642,357 |

| December 31, 2011 (in thousands) | Residential Real Estate Owner Occupied | Residential Real Estate Non Owner Occupied | Commercial Real Estate | Commercial Real Estate - Purchased Whole Loans | Real Estate Construction | Commercial | Warehouse Lines of Credit |
|---|---|---|---|---|---|---|---|
| Allowance for loan losses: | | | | | | | |
| Ending allowance balance attributable to loans: | | | | | | | |
| Individually evaluated for impairment | $ 1,350 | $ 437 | $ 1,782 | $ - | $ 2,298 | $ 237 | $ - |
| Collectively evaluated for impairment | 3,862 | 705 | 5,942 | - | 744 | 788 | 104 |
| Total ending allowance for loan losses | $ 5,212 | $ 1,142 | $ 7,724 | $ - | $ 3,042 | $ 1,025 | $ 104 |
| Loans: | | | | | | | |
| Impaired loans individually evaluated | $ 25,803 | $ 2,777 | $ 28,046 | $ - | $ 12,968 | $ 4,492 | $ - |
| Loans collectively evaluated for impairment | 959,932 | 96,384 | 611,920 | 32,741 | 54,438 | 114,625 | 41,496 |
| Total ending loan balance | $ 985,735 | $ 99,161 | $ 639,966 | $ 32,741 | $ 67,406 | $ 119,117 | $ 41,496 |

| (continued) | Home Equity | Credit Cards | Consumer Overdrafts | Consumer Other Consumer | Unallocated | Total |
|---|---|---|---|---|---|---|
| Allowance for loan losses: | | | | | | |
| Ending allowance balance attributable to loans: | | | | | | |
| Individually evaluated for impairment | $ 982 | $ - | $ - | $ - | $ - | $ 7,086 |

| | | | | | | |
|---|---|---|---|---|---|---|
| Collectively evaluated for impairment | 2,002 | 503 | 135 | 227 | 1,965 | 16,977 |
| Total ending allowance for loan losses | $ 2,984 | $ 503 | $ 135 | $ 227 | $ 1,965 | $ 24,063 |
| Loans: | | | | | | |
| Impaired loans individually evaluated | $ 3,107 | $ - | $ - | $ - | $ - | $ 77,193 |
| Loans collectively evaluated for impairment | 277,128 | 8,580 | 950 | 9,908 | - | 2,208,102 |
| Total ending loan balance | $ 280,235 | $ 8,580 | $ 950 | $ 9,908 | $ - | $ 2,285,295 |

The following tables present loans individually evaluated for impairment by class of loans as of September 30, 2012 and December 31, 2011. 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.

| | | | | Three Months Ended September 30, 2012 | | Nine Months Ended September 30, 2012 | |
|---|---|---|---|---|---|---|---|
| September 30, 2012 (in thousands) | Unpaid Principal Balance | Recorded Investment | Allowance for Loan Losses Allocated | Average Recorded Investment | Interest Income Recognized | Average Recorded Investment | Interest Income Recognized |
| Impaired loans with no related allowance recorded: | | | | | | | |
| Residential real estate: | | | | | | | |
| Owner occupied | $ 30,879 | $ 30,879 | $ - | $ 28,249 | $ 177 | $ 25,378 | $ 397 |
| Non owner occupied | 2,557 | 2,557 | - | 2,097 | 138 | 1,539 | 138 |
| Commercial real estate | 9,257 | 9,257 | - | 10,416 | 404 | 8,924 | 456 |
| Commercial real estate - purchased whole loans | - | - | - | - | - | - | - |
| Real estate construction | 1,794 | 1,794 | - | 2,637 | 35 | 3,018 | 54 |
| Commercial | 2,082 | 2,082 | - | 2,096 | 28 | 2,127 | 68 |
| Warehouse lines of credit | - | - | - | - | - | - | - |
| Home equity | 168 | 168 | - | 782 | - | 648 | - |
| Consumer: | | | | | | | |
| Credit cards | - | - | - | - | - | - | - |
| Overdrafts | - | - | - | - | - | - | - |
| Other consumer | 366 | 366 | - | 214 | 13 | 123 | 13 |
| Impaired loans with an allowance recorded: | | | | | | | |
| Residential real estate: | | | | | | | |
| Owner occupied | 7,169 | 7,114 | 1,429 | 6,927 | 6 | 5,886 | 33 |
| Non owner occupied | 2,715 | 2,715 | 566 | 2,270 | 6 | 2,249 | 33 |
| Commercial real estate | 27,265 | 26,857 | 2,705 | 27,233 | 236 | 26,164 | 738 |
| Commercial real estate - purchased whole loans | - | - | - | - | - | - | - |
| Real estate construction | 5,304 | 4,185 | 1,291 | 5,165 | 36 | 6,108 | 108 |
| Commercial | 2,612 | 2,612 | 367 | 2,583 | 47 | 2,520 | 116 |
| Warehouse lines of credit | - | - | - | - | - | - | - |
| Home equity | 1,132 | 1,132 | 306 | 1,297 | 6 | 1,675 | 14 |
| Consumer: | | - | | | | | |
| Credit cards | - | - | - | - | - | - | - |

| | | | | | | | |
|---|---|---|---|---|---|---|---|
| Overdrafts | - | - | - | - | - | - | - |
| Other consumer | - | - | - | - | - | - | - |
| Total impaired loans | 93,300 | 91,718 | 6,664 | 91,966 | 1,132 | 86,359 | 2,168 |

| December 31, 2011 (in thousands) | Unpaid Principal Balance | Recorded Investment | Allowance for Loan Losses Allocated | Twelve Months Ended December 31, 2011 Average Recorded Investment | Interest Income Recognized |
|---|---|---|---|---|---|
| Impaired loans with no related allowance recorded: | | | | | |
| Residential real estate: | | | | | |
| Owner occupied | $21,033 | $21,033 | $- | $15,272 | $296 |
| Non owner occupied | 757 | 329 | - | 312 | - |
| Commercial real estate | 5,468 | 5,468 | - | 3,735 | 84 |
| Commercial real estate - purchased whole loans | - | - | - | - | - |
| Real estate construction | 2,824 | 2,625 | - | 1,589 | 72 |
| Commercial | 2,011 | 2,011 | - | 1,413 | 4 |
| Warehouse lines of credit | - | - | - | - | - |
| Home equity | 841 | 705 | - | 492 | 16 |
| Consumer: | | | | | |
| Credit cards | - | - | - | - | - |
| Overdrafts | - | - | - | - | - |
| Other consumer | - | - | - | - | - |
| Impaired loans with an allowance recorded: | | | | | |
| Residential real estate: | | | | | |
| Owner occupied | 4,864 | 4,770 | 1,350 | 3,137 | 22 |
| Non owner occupied | 2,451 | 2,448 | 437 | 1,983 | 52 |
| Commercial real estate | 23,052 | 22,578 | 1,782 | 17,916 | 723 |
| Commercial real estate - purchased whole loans | - | - | - | - | - |
| Real estate construction | 11,323 | 10,343 | 2,298 | 9,291 | 179 |
| Commercial | 2,481 | 2,481 | 237 | 3,137 | 16 |
| Warehouse lines of credit | - | - | - | - | - |
| Home equity | 2,402 | 2,402 | 982 | 1,434 | - |
| Consumer: | | | | | |
| Credit cards | - | - | - | - | - |
| Overdrafts | - | - | - | - | - |
| Other consumer | - | - | - | - | - |
| Total impaired loans | 79,507 | 77,193 | 7,086 | 59,711 | 1,464 |

Troubled Debt Restructurings

A TDR is the situation where the Bank grants a concession to the borrower that the Bank would not otherwise have considered due to a borrower's financial difficulties. 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" loans. The majority of the Bank's commercial related and construction TDRs involve a restructuring of loan 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 loan. The substantial majority of the Bank's residential real estate TDRs 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.

Management determines whether to classify a TDR as non-performing based on its accrual status prior to modification. Non-accrual loans modified as TDRs remain on non-accrual status and continue to be reported as non-performing loans. 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, 2012 and December 31, 2011, $10 million and $6 million of TDRs were classified as non-performing loans.

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

| September 30, 2012 (in thousands) | Troubled Debt Restructurings on Non-Accrual Status | Troubled Debt Restructurings on Accrual Status | Total Troubled Debt Restructurings |
|---|---|---|---|
| Residential real estate | $ 5,378 | $ 33,273 | $ 38,651 |
| Commercial real estate | 2,438 | 29,435 | 31,873 |
| Real estate construction | 1,974 | 3,060 | 5,034 |
| Commercial | 486 | 5,075 | 5,561 |
| Total troubled debt restructurings | $ 10,276 | $ 70,843 | $ 81,119 |

Approximately $12 million in TDRs were added during the first nine months of 2012 in connection with the acquisitions of failed banks. There were no TDRs related to the FCB acquisition at September 30, 2012. See additional discussion regarding the TCB and FCB acquisitions under Footnote 2 "Acquisitions of Failed Banks" of Part I Item 1 "Financial Statements."

| December 31, 2011 (in thousands) | Troubled Debt Restructurings on Non-Accrual Status | Troubled Debt Restructurings on Accrual Status | Total Troubled Debt Restructurings |
|---|---|---|---|
| Residential real estate | $ 2,573 | $ 24,557 | $ 27,130 |
| Commercial real estate | 1,294 | 22,246 | 23,540 |
| Real estate construction | | | |