REPUBLIC BANCORP INC /KY/
Form 10-Q
August 07, 2015
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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 June 30, 2015

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 twelve months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. x Yes o No

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

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

Large accelerated filer o	Accelerated filer x
Non-accelerated filer o	Smaller reporting company o

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

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

The number of shares outstanding of the registrant s Class A Common Stock and Class B Common Stock, as of July 31, 2015, was 18,603,369 and 2,245,492.

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PART I FINANCIAL INFORMATION

Item 1. Financial Statements.

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

	June 30, 2015	December 31, 2014
ASSETS		
Cash and cash equivalents	$ 92,766	$ 72,878
Securities available for sale	456,612	435,911
Securities held to maturity (fair value of $43,600 in 2015 and $45,807 in 2014)	43,070	45,437
Mortgage loans held for sale, at fair value	10,277	6,388
Other loans held for sale, at the lower of cost or fair value	1,542	
Loans	3,323,977	3,040,495
Allowance for loan and lease losses	(25,248)	(24,410)
Loans, net	3,298,729	3,016,085
Federal Home Loan Bank stock, at cost	28,208	28,208
Premises and equipment, net	31,092	32,987
Premises, held for sale	2,468	1,317
Goodwill	10,168	10,168
Other real estate owned	2,920	11,243
Bank owned life insurance	52,117	51,415
Other assets and accrued interest receivable	36,250	34,976
TOTAL ASSETS	$ 4,066,219	$ 3,747,013
LIABILITIES		
Deposits:		
Non interest-bearing	$ 598,572	$ 502,569
Interest-bearing	1,681,038	1,555,613
Total deposits	2,279,610	2,058,182
Securities sold under agreements to repurchase and other short-term borrowings	229,825	356,108
Federal Home Loan Bank advances	916,500	707,500
Subordinated note	41,240	41,240
Other liabilities and accrued interest payable	26,072	25,252
Total liabilities	3,493,247	3,188,282
Commitments and contingent liabilities (Footnote 9)		
STOCKHOLDERS EQUITY		
Preferred stock, no par value		
Class A Common Stock and Class B Common Stock, no par value	4,903	4,904
Additional paid in capital	135,246	134,889
Retained earnings	428,475	414,623

Accumulated other comprehensive income		4,348		4,315
Total stockholders equity		572,972		558,731
TOTAL LIABILITIES AND STOCKHOLDERS EQUITY	$	4,066,219	$	3,747,013

See accompanying footnotes to consolidated financial statements.

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CONSOLIDATED STATEMENTS OF INCOME (*UNAUDITED*)

(*in thousands, except per share data*)

	Three Months Ended June,		Six Months Ended June,	
	2015	**2014**	**2015**	**2014**
INTEREST INCOME:				
Loans, including fees	$ 33,616	$ 30,110	$ 65,207	$ 60,272
Taxable investment securities	1,779	1,908	3,552	3,767
Federal Home Loan Bank stock and other	327	387	724	863
Total interest income	35,722	32,405	69,483	64,902
INTEREST EXPENSE:				
Deposits	1,021	937	2,165	1,915
Securities sold under agreements to repurchase and other short-term borrowings	17	22	55	44
Federal Home Loan Bank advances	2,997	3,267	5,925	6,831
Subordinated note	629	629	1,258	1,258
Total interest expense	4,664	4,855	9,403	10,048
NET INTEREST INCOME	31,058	27,550	60,080	54,854
Provision for loan and lease losses	904	693	1,089	(10)
NET INTEREST INCOME AFTER PROVISION FOR LOAN AND LEASE LOSSES	30,154	26,857	58,991	54,864
NON INTEREST INCOME:				
Service charges on deposit accounts	3,247	3,563	6,286	6,858
Net refund transfer fees	1,907	1,836	17,242	16,224
Mortgage banking income	1,224	812	2,577	1,298
Interchange fee income	2,044	1,681	4,238	3,725
Gain on call of security available for sale	88		88	
Net loss on other real estate owned	(155)	(69)	(274)	(551)
Increase in cash surrender value of bank owned life insurance	353	379	702	570
Other	777	879	1,612	1,672
Total non interest income	9,485	9,081	32,471	29,796
NON INTEREST EXPENSES:				
Salaries and employee benefits	14,323	13,965	29,600	28,448
Occupancy and equipment, net	5,142	5,508	10,343	11,330
Communication and transportation	771	856	1,817	1,882
Marketing and development	977	803	1,562	1,331
FDIC insurance expense	474	414	1,148	983
Bank franchise tax expense	847	831	3,248	3,170
Data processing	1,092	874	2,058	1,671
Interchange related expense	931	847	1,938	1,844

Supplies	219	60	580	500
Other real estate owned expense	120	308	339	698
Legal and professional fees	528	438	2,143	949
Other	1,741	1,380	3,463	3,677
Total non interest expenses	27,165	26,284	58,239	56,483
INCOME BEFORE INCOME TAX EXPENSE	12,474	9,654	33,223	28,177
INCOME TAX EXPENSE	4,154	3,332	11,115	9,871
NET INCOME	$ 8,320	$ 6,322	$ 22,108	$ 18,306
BASIC EARNINGS PER SHARE:				
Class A Common Stock	$ 0.40	$ 0.31	$ 1.07	$ 0.88
Class B Common Stock	$ 0.37	$ 0.29	$ 0.97	$ 0.85
DILUTED EARNINGS PER SHARE:				
Class A Common Stock	$ 0.40	$ 0.30	$ 1.07	$ 0.88
Class B Common Stock	$ 0.36	$ 0.29	$ 0.97	$ 0.85
DIVIDENDS DECLARED PER COMMON SHARE:				
Class A Common Stock	$ 0.198	$ 0.187	$ 0.385	$ 0.363
Class B Common Stock	$ 0.180	$ 0.170	$ 0.350	$ 0.330

See accompanying footnotes to consolidated financial statements.

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CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME *(UNAUDITED)*

(*in thousands*)

	Three Months Ended June, 2015	Three Months Ended June, 2014	Six Months Ended June, 2015	Six Months Ended June, 2014
Net income	$ 8,320	$ 6,322	$ 22,108	$ 18,306
OTHER COMPREHENSIVE INCOME				
Change in fair value of derivatives used for cash flow hedges	175	(364)	(221)	(704)
Reclassification adjustment for derivative losses recognized in income	103	99	204	199
Change in unrealized gain (loss) on securities available for sale	(1,056)	2,626	182	2,628
Reclassification adjustment for gain on security available for sale recognized in earnings	(88)		(88)	
Change in unrealized gain on security available for sale for which a portion of an other-than-temporary impairment has been recognized in earnings	(4)	315	(26)	369
Net unrealized gains (losses)	(870)	2,676	51	2,492
Tax effect	304	(937)	(18)	(873)
Total other comprehensive income (loss), net of tax	(566)	1,739	33	1,619
COMPREHENSIVE INCOME	$ 7,754	$ 8,061	$ 22,141	$ 19,925

See accompanying footnotes to consolidated financial statements.

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CONSOLIDATED STATEMENT OF STOCKHOLDERS EQUITY (*UNAUDITED*)

SIX MONTHS ENDED JUNE 30, 2015

(in thousands)	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, 2015	18,603	2,245	$ 4,904	$ 134,889	$ 414,623	$ 4,315	$ 558,731
Net income					22,108		22,108
Net change in accumulated other comprehensive income						33	33
Dividend declared Common Stock:							
Class A Shares					(7,167)		(7,167)
Class B Shares					(786)		(786)
Stock options exercised, net of shares redeemed	8		2	182	(65)		119
Repurchase of Class A Common Stock	(14)		(3)	(86)	(238)		(327)
Net change in notes receivable on Class A Common Stock				(51)			(51)
Deferred director compensation expense - Class A Common Stock	5			109			109
Stock based compensation - restricted stock				147			147
Stock based compensation expense - options				56			56
Balance, June 30, 2015	18,602	2,245	$ 4,903	$ 135,246	$ 428,475	$ 4,348	$ 572,972

See accompanying footnotes to consolidated financial statements.

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

	Six Months Ended June, 2015	2014
OPERATING ACTIVITIES:		
Net income	$ 22,108	$ 18,306
Adjustments to reconcile net income to net cash provided by operating activities:		
Amortization on investment securities, net	380	330
Accretion on loans, net	(1,649)	(4,494)
Depreciation of premises and equipment	3,251	2,724
Amortization of mortgage servicing rights	716	662
Provision for loan and lease losses	1,089	(10)
Net gain on sale of mortgage loans held for sale	(2,353)	(1,166)
Origination of mortgage loans held for sale	(96,008)	(33,284)
Proceeds from sale of mortgage loans held for sale	94,472	31,147
Origination of other loans held for sale	(24,410)	
Proceeds from sale of other loans held for sale	22,868	
Gain on call of security available for sale	(88)	
Net gain realized on sale of other real estate owned	(430)	(666)
Writedowns of other real estate owned	704	1,217
Deferred director compensation expense - Company Stock	109	91
Stock based compensation expense	203	268
Increase in cash surrender value of bank owned life insurance	(702)	(570)
Net change in other assets and liabilities:		
Accrued interest receivable	(131)	189
Accrued interest payable	(55)	(198)
Other assets	(1,859)	5,887
Other liabilities	581	(1,549)
Net cash provided by operating activities	18,796	18,884
INVESTING ACTIVITIES:		
Purchases of securities available for sale	(889,325)	(109,549)
Proceeds from maturities, calls and paydowns of securities available for sale	868,424	81,567
Proceeds from maturities and paydowns of securities held to maturity	2,342	2,269
Net change in outstanding warehouse lines of credit	(169,474)	(94,555)
Purchase of loans, including premiums paid	(63,163)	(14,695)
Net change in other loans	(48,458)	(25,008)
Proceeds from redemption of Federal Home Loan Bank stock		134
Proceeds from sales of other real estate owned	7,009	8,136
Net purchases of premises and equipment	(2,507)	(2,297)
Purchase of bank owned life insurance		(25,000)
Net cash used in investing activities	(295,152)	(178,998)
FINANCING ACTIVITIES:		
Net change in deposits	221,428	14,126
Net change in securities sold under agreements to repurchase and other short-term borrowings	(126,283)	31,884
Payments of Federal Home Loan Bank advances	(208,000)	(83,000)
Proceeds from Federal Home Loan Bank advances	417,000	118,000
Repurchase of Common Stock	(327)	(347)
Net proceeds from Common Stock options exercised	119	117
Cash dividends paid	(7,693)	(7,256)
Net cash provided by financing activities	296,244	73,524

NET CHANGE IN CASH AND CASH EQUIVALENTS		19,888		(86,590)
CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD		72,878		170,863
CASH AND CASH EQUIVALENTS AT END OF PERIOD	$	92,766	$	84,273
SUPPLEMENTAL DISCLOSURES OF CASHFLOW INFORMATION:				
Cash paid during the period for:				
Interest	$	9,458	$	10,246
Income taxes		6,130		7,304
SUPPLEMENTAL NONCASH DISCLOSURES:				
Transfers from loans to real estate acquired in settlement of loans	$	1,922	$	4,492
Loans provided for sales of other real estate owned		2,962		1,294

See accompanying footnotes to consolidated financial statements.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS JUNE 30, 2015 and 2014 (UNAUDITED) AND DECEMBER 31, 2014

1. BASIS OF PRESENTATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation The consolidated financial statements include the accounts of Republic Bancorp, Inc. (the Parent Company) and its wholly-owned subsidiaries, Republic Bank & Trust Company (RB&T or the Bank) and Republic Insurance Services, Inc. (the Captive). The Bank is a Kentucky-based, state chartered non-member financial institution. The Captive, which was formed during the third quarter of 2014, is a wholly-owned insurance subsidiary of the Company. The Captive provides property and casualty insurance coverage to the Company and the Bank as well as five other third-party insurance captives for which insurance may not be available or economically feasible. 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 (GAAP) for interim financial information and with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. Accordingly, the financial statements do not include all of the information and footnotes required by U.S. 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 six months ended June 30, 2015 are not necessarily indicative of the results that may be expected for the year ending December 31, 2015. 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, 2014.

As of June 30, 2015, the Company was divided into four distinct business operating segments: Traditional Banking, Warehouse Lending (Warehouse), Mortgage Banking and Republic Processing Group (RPG). Management considers the first three segments to collectively constitute Core Bank or Core Banking activities. The Warehouse segment was reported as a division of the Traditional Banking segment prior to the fourth quarter of 2014, but realized the quantitative and qualitative nature of a segment by the end of 2014. All prior periods have been reclassified to conform to the current presentation.

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Traditional Banking, Warehouse Lending and Mortgage Banking (collectively Core Banking)

The Traditional Bank provides traditional banking products primarily to customers in the Company s market footprint. As of June 30, 2015, in addition to Internet Banking and Correspondent Lending delivery channels, Republic had 40 full-service banking centers with locations as follows:

- Kentucky 32
- Metropolitan Louisville 19
- Central Kentucky 8
- Elizabethtown 1
- Frankfort 1
- Georgetown 1
- Lexington 4
- Shelbyville 1
- Western Kentucky 2
- Owensboro 2
- Northern Kentucky 3
- Covington 1
- Florence 1
- Independence 1
- Southern Indiana 3
- Floyds Knobs 1
- Jeffersonville 1
- New Albany 1
- Metropolitan Tampa, Florida 2

- Metropolitan Cincinnati, Ohio 1
- Metropolitan Nashville, Tennessee 2

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

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

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

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

The Core Bank began acquiring single family, first lien mortgage loans for investment through its Correspondent Lending channel in May 2014. Correspondent Lending generally involves the Bank acquiring, primarily from its Warehouse clients, closed loans that meet the Bank s specifications. Substantially all loans purchased through the Correspondent Lending channel are purchased at a premium.

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

Republic Processing Group

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

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

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

The Republic Credit Solutions (RCS) division offers short-term consumer credit products.

Accounting Standards Update (ASU) 2015-3 Interest Imputation of Interest *(Topic 835-30):* *Simplifying the Presentation of Debt Issuance Costs*

To simplify presentation of debt issuance costs, the amendments in this ASU require that debt issuance costs related to a recognized debt liability be presented on the balance sheet as a direct deduction from the carrying amount of that debt liability, consistent with debt discounts. The recognition and measurement guidance for debt issuance costs are not affected by the amendments in this ASU. The amendments in this ASU are effective for financial statements issued for fiscal years beginning after December 15, 2015, and interim periods within those fiscal years. This ASU is not expected to have a material impact on the Company s financial statements.

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2. INVESTMENT SECURITIES

Securities Available for Sale

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

June 30, 2015 (in thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
U.S. Treasury securities and U.S. Government agencies	$ 198,071	$ 905	$ (125)	$ 198,851
Private label mortgage backed security	4,037	1,194		5,231
Mortgage backed securities - residential	103,378	4,631	(129)	107,880
Collateralized mortgage obligations	127,922	1,065	(727)	128,260
Freddie Mac preferred stock		231		231
Mutual fund	1,000	15		1,015
Corporate bonds	15,010	134		15,144
Total securities available for sale	$ 449,418	$ 8,175	$ (981)	$ 456,612

December 31, 2014 (in thousands)	Gross Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
U.S. Treasury securities and U.S. Government agencies	$ 146,625	$ 312	$ (15)	$ 146,922
Private label mortgage backed security	4,030	1,220		5,250
Mortgage backed securities - residential	118,836	5,511	(91)	124,256
Collateralized mortgage obligations	143,283	1,034	(1,146)	143,171
Freddie Mac preferred stock		231		231
Mutual fund	1,000	18		1,018
Corporate bonds	15,011	52		15,063
Total securities available for sale	$ 428,785	$ 8,378	$ (1,252)	$ 435,911

Securities Held to Maturity

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

June 30, 2015 (in thousands)	Carrying Value	Gross Unrecognized Gains	Gross Unrecognized Losses	Fair Value
	$ 1,536	$ 5	$ (2)	$ 1,539

U.S. Treasury securities and U.S. Government agencies								
Mortgage backed securities - residential		144		18				162
Collateralized mortgage obligations		36,390		554				36,944
Corporate bonds		5,000				(45)		4,955
Total securities held to maturity	$	43,070	$	577	$	(47)	$	43,600

December 31, 2014 (in thousands)		**Carrying Value**		**Gross Unrecognized Gains**		**Gross Unrecognized Losses**		**Fair Value**
U.S. Treasury securities and U.S. Government agencies	$	1,747	$	1	$	(7)	$	1,741
Mortgage backed securities - residential		147		20				167
Collateralized mortgage obligations		38,543		423		(4)		38,962
Corporate bonds		5,000				(63)		4,937
Total securities held to maturity	$	45,437	$	444	$	(74)	$	45,807

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At June 30, 2015 and December 31, 2014, there were no holdings of securities of any one issuer, other than the U.S. Government and its agencies, in an amount greater than 10% of stockholders equity.

Sales of Securities Available for Sale

During the three and six months ended June 30, 2015, the Bank recognized a gain of $88,000 on the call of one available for sale security.

During the three and six months ended June 30, 2014, there were no sales or calls of securities available for sale.

Investment Securities by Contractual Maturity

The amortized cost and fair value of the investment securities portfolio by contractual maturity at June 30, 2015 follows. Expected maturities may differ from contractual maturities if borrowers have the right to call or prepay obligations with or without call or prepayment penalties. Securities not due at a single maturity date are detailed separately.

	Securities Available for Sale		Securities Held to Maturity	
June 30, 2015 (in thousands)	**Amortized Cost**	**Fair Value**	**Carrying Value**	**Fair Value**
Due in one year or less	$ 10,020	$ 10,041	$ 1,016	$ 1,021
Due from one year to five years	193,061	193,854	5,520	5,473
Due from five years to ten years	10,000	10,100		
Due beyond ten years				
Private label mortgage backed security	4,037	5,231		
Mortgage backed securities - residential	103,378	107,880	144	162
Collateralized mortgage obligations	127,922	128,260	36,390	36,944
Freddie Mac preferred stock		231		
Mutual fund	1,000	1,015		
Total securities	$ 449,418	$ 456,612	$ 43,070	$ 43,600

Freddie Mac Preferred Stock

During 2008, the U.S. Treasury, the Federal Reserve Board, and the Federal Housing Finance Agency (FHFA) announced that the FHFA was placing Freddie Mac under conservatorship and giving management control to the FHFA. The Bank contemporaneously determined that its 40,000 shares of Freddie Mac preferred stock were fully impaired and recorded an other-than-temporarily impairment (OTTI) charge of $2.1 million in 2008. The OTTI charge brought the carrying value of the stock to $0. During the second quarter of 2014, based on active trading volume of Freddie Mac preferred stock, the Company determined it appropriate to record an unrealized gain to Other Comprehensive Income (OCI) related to its Freddie Mac preferred stock holdings. Based on the stock s market closing price as of June 30, 2015, the Company s unrealized gain for its Freddie Mac preferred stock totaled $231,000.

Mortgage Backed Securities and Collateralized Mortgage Obligations

At June 30, 2015, with the exception of the $5.2 million private label mortgage backed security, all other mortgage backed securities and collateralized mortgage obligations (CMOs) held by the Bank were issued by U.S. government-sponsored entities and agencies, primarily Freddie Mac and the Federal National Mortgage Association (Fannie Mae or FNMA), institutions that the government has affirmed its commitment to support. At June 30, 2015 and December 31, 2014, there were gross unrealized losses of $856,000 and $1.2 million related to available for sale mortgage backed securities and CMOs. Because the decline in fair value of these 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 OTTI.

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Market Loss Analysis

Securities with unrealized losses at June 30, 2015 and December 31, 2014, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position, are as follows:

	Less than 12 months		12 months or more		Total	
June 30, 2015 (in thousands)	**Fair Value**	**Unrealized Losses**	**Fair Value**	**Unrealized Losses**	**Fair Value**	**Unrealized Losses**
Securities available for sale:						
U.S. Treasury securities and U.S. Government agencies	$ 19,880	$ (120)	$ 995	$ (5)	$ 20,875	$ (125)
Mortgage backed securities - residential	6,602	(129)			6,602	(129)
Collateralized mortgage obligations	3,963	(142)	28,736	(585)	32,699	(727)
Total securities available for sale	$ 30,445	$ (391)	$ 29,731	$ (590)	$ 60,176	$ (981)

	Less than 12 months		12 months or more		Total	
	Fair Value	**Unrealized Losses**	**Fair Value**	**Unrealized Losses**	**Fair Value**	**Unrealized Losses**
Securities held to maturity:						
U.S. Treasury securities and U.S. Government agencies	$ 518	$ (2)	$	$	$ 518	$ (2)
Corporate bonds	4,955	(45)			4,955	(45)
Total securities held to maturity	$ 5,473	$ (47)	$	$	$ 5,473	$ (47)

	Less than 12 months		12 months or more		Total	
December 31, 2014 (in thousands)	**Fair Value**	**Unrealized Losses**	**Fair Value**	**Unrealized Losses**	**Fair Value**	**Unrealized Losses**
Securities available for sale:						
U.S. Treasury securities and U.S. Government agencies	$ 2,089	$ (15)	$	$	$ 2,089	$ (15)
Mortgage backed securities - residential	7,535	(91)			7,535	(91)
Collateralized mortgage obligations	46,058	(881)	12,534	(265)	58,592	(1,146)
Total securities available for sale	$ 55,682	$ (987)	$ 12,534	$ (265)	$ 68,216	$ (1,252)

	Less than 12 months		12 months or more		Total	
	Fair Value	**Unrealized Losses**	**Fair Value**	**Unrealized Losses**	**Fair Value**	**Unrealized Losses**
Securities held to maturity:						
U.S. Treasury securities and U.S. Government agencies	$ 517	$ (7)	$	$	$ 517	$ (7)
Collateralized mortgage obligations	9,045	(4)			9,045	(4)
Corporate bonds	4,936	(63)			4,936	(63)
Total securities held to maturity	$ 14,498	$ (74)	$	$	$ 14,498	$ (74)

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At June 30, 2015, the Bank s security portfolio consisted of 159 securities, 19 of which were in an unrealized loss position. At December 31, 2014, the Bank s security portfolio consisted of 157 securities, 17 of which were in an unrealized loss position.

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 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.

The Bank owns one private label mortgage backed security with a total carrying value of $5.2 million at June 30, 2015. This security, with an average remaining life currently estimated at five years, is mostly backed by Alternative A first lien mortgage loans, but also has an insurance wrap or guarantee as an added layer of protection to the security holder. This asset is illiquid, and as such, the Bank determined it to be a Level 3 security in accordance with Accounting Standards Codification (ASC) Topic 820, *Fair Value Measurements and Disclosures.* Based on this determination, the Bank utilized an income valuation model (present value model) approach, in determining the fair value of the security. This approach is beneficial for positions that are not traded in active markets or are subject to transfer restrictions, and/or where valuations are adjusted to reflect illiquidity and/or non-transferability. Such adjustments are generally based on available market evidence. In the absence of such evidence, management s best estimate is used. Management s best estimate consists of both internal and external support for this investment.

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

Pledged Investment Securities

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

(in thousands)	June 30, 2015	December 31, 2014
Carrying amount	$ 328,844	$ 409,868
Fair value	329,417	410,307

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3. LOANS AND ALLOWANCE FOR LOAN AND LEASE LOSSES

The composition of the loan portfolio at June 30, 2015 and December 31, 2014 follows:

(in thousands)	June 30, 2015	December 31, 2014
Residential real estate:		
Owner occupied	$ 1,100,133	$ 1,118,341
Owner occupied - correspondent*	243,140	226,628
Non owner occupied	101,765	96,492
Commercial real estate	799,158	772,309
Commercial real estate - purchased whole loans*	35,277	34,898
Construction & land development	47,038	38,480
Commercial & industrial	202,456	157,339
Lease financing receivables	7,242	2,530
Warehouse lines of credit	488,905	319,431
Home equity	267,570	245,679
Consumer:		
RPG loans	6,467	4,095
Credit cards	10,942	9,573
Overdrafts	1,404	1,180
Purchased whole loans*	3,607	4,626
Other consumer	8,873	8,894
Total loans**	3,323,977	3,040,495
Allowance for loan and lease losses	(25,248)	(24,410)
Total loans, net	$ 3,298,729	$ 3,016,085

** - Identifies loans to borrowers located primarily outside of the Bank s historical market footprint.*

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

The table below reconciles the contractually receivable and carrying amounts of loans at June 30, 2015 and December 31, 2014:

(in thousands)	June 30, 2015	December 31, 2014
Contractually receivable	$ 3,329,849	$ 3,050,599
Unearned income(1)	(635)	(174)
Unamortized premiums(2)	4,191	4,490
Unaccreted discounts(3)	(10,859)	(15,675)
Net unamortized deferred origination fees and costs	1,431	1,255
Carrying value of loans	$ 3,323,977	$ 3,040,495

(1) Unearned income relates to lease financing receivables.

(2) - Premiums predominately relate to loans acquired through the Bank s Correspondent Lending channel.

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

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Loan Purchases

In May 2014, the Bank began acquiring single family, first lien mortgage loans for investment within its loan portfolio through its Correspondent Lending channel. Correspondent Lending generally involves the Bank acquiring, primarily from Warehouse clients, closed loans that meet the Bank s specifications. Substantially all loans purchased through the Correspondent Lending channel are purchased at a premium. Loans acquired through the Correspondent Lending channel generally reflect borrowers outside of the Bank s historical market footprint, with 83% of such loans as of June 30, 2015 secured by collateral in the state of California.

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

The table below reflects the purchased activity of single family, first lien mortgage loans and unsecured consumer loans, by class, during the three and six months ended June 30, 2015 and 2014.

	Three Months Ended June 30,		Six Months Ended June 30,	
(in thousands)	**2015**	**2014**	**2015**	**2014**
Residential real estate:				
Owner occupied - correspondent*	$ 43,632	$ 12,067	$ 62,802	$ 12,067
Consumer:				
Purchased whole loans*		2,628	361	2,628
Total purchased loans	$ 43,632	$ 14,695	$ 63,163	$ 14,695

** - Represents origination amount, inclusive of purchase premiums, where applicable.*

Purchased Credit Impaired (PCI) Loans

PCI loans acquired during the Bank s 2012 FDIC-assisted transactions are accounted for under ASC 310-30, *Loans and Debt Securities Acquired with Deteriorated Credit Quality.*

The table below reconciles the contractually required and carrying amounts of PCI loans at June 30, 2015 and December 31, 2014:

(in thousands)	**June 30, 2015**	**December 31, 2014**
Contractually-required principal	$ 20,080	$ 26,571

Non-accretable amount		(2,076)		(6,784)
Accretable amount		(4,323)		(2,297)
Carrying value of PCI loans	$	13,681	$	17,490

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The following table presents a rollforward of the accretable amount on PCI loans for the three and six months ended June 30, 2015 and 2014:

(in thousands)	Three Months Ended June 30, 2015	Three Months Ended June 30, 2014	Six Months Ended June 30, 2015	Six Months Ended June 30, 2014
Balance, beginning of period	$ (2,170)	$ (2,765)	$ (2,297)	$ (3,457)
Transfers between non-accretable and accretable	(3,378)	(1,029)	(3,354)	(2,340)
Net accretion into interest income on loans, including loan fees	1,225	1,307	1,328	3,310
Balance, end of period	$ (4,323)	$ (2,487)	$ (4,323)	$ (2,487)

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Credit Quality Indicators

Based on the Bank s internal analyses performed as of June 30, 2015 and December 31, 2014, the following tables reflect loans by risk category. Risk categories are defined in the Company s Annual Report on Form 10-K for the year ended December 31, 2014:

June 30, 2015 (in thousands)	Pass	Special Mention *	Substandard *	Doubtful / Loss	Purchased Credit Impaired Loans - Group 1	Purchased Credit Impaired Loans - Substandard	Total Rated Loans**
Residential real estate:							
Owner occupied	$	$ 24,473	$ 15,456	$	$ 927	$	$ 40,856
Owner occupied - correspondent							
Non owner occupied		1,544	1,983		1,203		4,730
Commercial real estate	770,583	7,455	10,842		10,278		799,158
Commercial real estate - purchased whole loans	35,277						35,277
Construction & land development	44,199	115	2,687		37		47,038
Commercial & industrial	198,956	2,063	201		1,236		202,456
Lease financing receivables	7,242						7,242
Warehouse lines of credit	488,905						488,905
Home equity			2,658				2,658
Consumer:							
RPG loans							
Credit cards							
Overdrafts							
Purchased whole loans							
Other consumer		9	84				93
Total	$ 1,545,162	$ 35,659	$ 33,911	$	$ 13,681	$	$ 1,628,413

** - At June 30, 2015, Special Mention and Substandard loans included $183,000 and $4 million, respectively, which were removed from PCI accounting in accordance with ASC 310-30-35-13 due to a post-acquisition troubled debt restructuring.*

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

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December 31, 2014 (in thousands)	Pass	Special Mention *	Substandard *	Doubtful / Loss	Purchased Credit Impaired Loans - Group 1	Purchased Credit Impaired Loans - Substandard	Total Rated Loans**
Residential real estate:							
Owner occupied	$	$ 26,828	$ 14,586	$	$ 1,205	$	$ 42,619
Owner occupied - correspondent							
Non owner occupied		844	2,886		1,709		5,439
Commercial real estate	736,012	7,838	15,636		12,823		772,309
Commercial real estate - purchased whole loans	34,898						34,898
Construction & land development	35,339	120	2,525		496		38,480
Commercial & industrial	153,362	625	2,108		1,244		157,339
Lease financing receivables	2,530						2,530
Warehouse lines of credit	319,431						319,431
Home equity			2,220				2,220
Consumer:							
RPG loans							
Credit cards							
Overdrafts							
Purchased whole loans							
Other consumer		13	38		13		64
Total	$ 1,281,572	$ 36,268	$ 39,999	$	$ 17,490	$	$ 1,375,329

** - At December 31, 2014, Special Mention and Substandard loans included $443,000 and $6 million, respectively, which were removed from PCI accounting in accordance with ASC 310-30-35-13 due to a post-acquisition troubled debt restructuring.*

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

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Allowance for Loan and Lease Losses

Activity in the allowance for loan and leases (Allowance) follows:

(in thousands)	Three Months Ended June 30, 2015	Three Months Ended June 30, 2014	Six Months Months Ended June 30, 2015	Six Months Months Ended June 30, 2014
Allowance, beginning of period	$ 24,631	$ 22,367	$ 24,410	$ 23,026
Charge offs - Core Banking	(685)	(715)	(1,177)	(1,627)
Charge offs - RPG	(21)		(26)	
Total charge offs	(706)	(715)	(1,203)	(1,627)
Recoveries - Core Banking	377	364	715	857
Recoveries - RPG	42	63	237	526
Total recoveries	419	427	952	1,383
Net (charge offs) recoveries - Core Banking	(308)	(351)	(462)	(770)
Net (charge offs) recoveries - RPG	21	63	211	526
Net (charge offs) recoveries	(287)	(288)	(251)	(244)
Provision for loan and lease losses (Provision) - Core Banking	717	710	1,092	470
Provision - RPG	187	(17)	(3)	(480)
Total Provision	904	693	1,089	(10)
Allowance, end of period	$ 25,248	$ 22,772	$ 25,248	$ 22,772

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

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

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

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

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

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The following tables present the activity in the Allowance by portfolio class for the three months ended June 30, 2015 and 2014:

Three Months Ended June 30, 2015 (in thousands)	Residential Real Estate Owner Occupied	Residential Real Estate Owner Occupied- Correspondent	Non Owner Occupied	Commercial Real Estate	Commercial Real Estate - Purchased Whole Loans	Construction & Land Development	Commercial & Industrial	Lease Financing Receivables
Beginning balance	$ 8,629	$ 579	$ 920	$ 7,553	$ 35	$ 958	$ 1,157	$ 40
Provision	(313)	29	10	353		142	52	36
Charge offs	(178)		(29)	(147)			(27)	
Recoveries	64		3	81			9	
Ending balance	$ 8,202	$ 608	$ 904	$ 7,840	$ 35	$ 1,100	$ 1,191	$ 76

(continued)	Warehouse Lines of Credit	Home Equity	RPG Loans	Consumer Credit Cards	Consumer Overdrafts	Consumer Purchased Whole Loans	Other Consumer	Total
Beginning balance	$ 1,058	$ 2,708	$ 44	$ 362	$ 245	$ 184	$ 159	$ 24,631
Provision	164	56	187	40	57	83	8	904
Charge offs		(21)	(21)	(31)	(103)	(60)	(89)	(706)
Recoveries		22	42	28	87		83	419
Ending balance	$ 1,222	$ 2,765	$ 252	$ 399	$ 286	$ 207	$ 161	$ 25,248

Three Months Ended June 30, 2014 (in thousands)	Residential Real Estate Owner Occupied	Residential Real Estate Owner Occupied- Correspondent	Non Owner Occupied	Commercial Real Estate	Commercial Real Estate - Purchased Whole Loans	Construction & Land Development	Commercial & Industrial	Lease Financing Receivables
Beginning balance	$ 7,751	$	$ 984	$ 7,901	$ 34	$ 1,192	$ 1,080	$
Provision	460	60	(141)	(206)		(185)	70	3
Charge offs	(202)		(7)	(2)		(1)	(20)	
Recoveries	46		3	3		84	22	
Ending balance	$ 8,055	$ 60	$ 839	$ 7,696	$ 34	$ 1,090	$ 1,152	$ 3

(continued)	Warehouse Lines of Credit	Home Equity	RPG Loans	Consumer Credit Cards	Consumer Overdrafts	Consumer Purchased Whole Loans	Other Consumer	Total
Beginning balance	$ 477	$ 2,371	$	$ 276	$ 212	$	$ 89	$ 22,367
Provision	133	235	(17)	40	113		128	693
Charge offs		(217)		(37)	(142)		(87)	(715)
Recoveries		14	63	7	97		88	427
Ending balance	$ 610	$ 2,403	$ 46	$ 286	$ 280	$	$ 218	$ 22,772

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The following tables present the activity in the Allowance by portfolio class for the six months ended June 30, 2015 and 2014:

Six Months Ended June 30, 2015 (in thousands)	Residential Real Estate Owner Occupied	Residential Real Estate Owner Occupied- Correspondent	Residential Real Estate Non Owner Occupied	Commercial Real Estate	Commercial Real Estate - Purchased Whole Loans	Construction & Land Development	Commercial & Industrial	Lease Financing Receivables
Beginning balance	$ 8,565	$ 567	$ 837	$ 7,740	$ 34	$ 926	$ 1,167	$ 25
Provision	(173)	41	90	164	1	174	42	51
Charge offs	(314)		(29)	(154)			(56)	
Recoveries	124		6	90			38	
Ending balance	$ 8,202	$ 608	$ 904	$ 7,840	$ 35	$ 1,100	$ 1,191	$ 76

(continued)	Warehouse Lines of Credit	Home Equity	RPG Loans	Consumer Credit Cards	Consumer Overdrafts	Consumer Purchased Whole Loans	Consumer Other Consumer	Total
Beginning balance	$ 799	$ 2,730	$ 44	$ 285	$ 382	$ 185	$ 124	$ 24,410
Provision	423	48	(3)	144	(22)	94	15	1,089
Charge offs		(72)	(26)	(71)	(249)	(72)	(160)	(1,203)
Recoveries		59	237	41	175		182	952
Ending balance	$ 1,222	$ 2,765	$ 252	$ 399	$ 286	$ 207	$ 161	$ 25,248

Six Months Ended	Residential Real Estate Owner	Residential Real Estate Owner Occupied-	Non Owner	Commercial	Commercial Real Estate - Purchased	Construction &	Commercial &	Lease Financing