CENTRAL PACIFIC FINANCIAL CORP
Form 10-Q
November 08, 2016

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

FORM 10-Q

(Mark One)

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

For the quarterly period ended September 30, 2016

or

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

For the transition period from to

Commission file number 001-31567

CENTRAL PACIFIC FINANCIAL CORP.
(Exact name of registrant as specified in its charter)

Hawaii	99-0212597
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

220 South King Street, Honolulu, Hawaii 96813
(Address of principal executive offices) (Zip Code)

(808) 544-0500
(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. Yes ý No o

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). Yes ý No o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of “accelerated filer and large accelerated filer” in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer x Accelerated filer o 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). Yes o No ý

The number of shares outstanding of registrant’s common stock, no par value, on November 4, 2016 was 30,830,598 shares.

CENTRAL PACIFIC FINANCIAL CORP. AND SUBSIDIARIES

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PART I.   FINANCIAL INFORMATION

Forward-Looking Statements

This document may contain forward-looking statements concerning projections of revenues, income/loss, earnings/loss per share, capital expenditures, dividends, capital structure, net interest margin or other financial items, concerning plans and objectives of management for future operations, concerning future economic performance, or concerning any of the assumptions underlying or relating to any of the foregoing. Forward-looking statements can be identified by the fact that they do not relate strictly to historical or current facts, and may include the words “believes,” “plans,” “intends,” “expects,” “anticipates,” “forecasts,” “hopes,” “should,” “estimates” or words of similar meaning. While we that our forward-looking statements and the assumptions underlying them are reasonably based, such statements and assumptions are by their nature subject to risks and uncertainties, and thus could later prove to be inaccurate or incorrect. Accordingly, actual results could materially differ from projections for a variety of reasons, to include, but not be limited to: adverse changes in the financial performance and/or condition of our borrowers and, as a result, increased loan delinquency rates, deterioration in asset quality, and losses in our loan portfolio; the impact of local, national, and international economies and events (including natural disasters such as wildfires, tsunamis, storms and earthquakes) on the Company’s business and operations and on tourism, the military, and other major industries operating within the Hawaii market and any other markets in which the Company does business; deterioration or malaise in domestic economic conditions, including any further destabilization in the financial industry and deterioration of the real estate market, as well as the impact of declining levels of consumer and business confidence in the state of the economy in general and in financial institutions in particular; changes in estimates of future reserve requirements based upon the periodic review thereof under relevant regulatory and accounting requirements; the impact of the Dodd-Frank Wall Street Reform and Consumer Protection Act, changes in capital standards, other regulatory reform, including but not limited to regulations promulgated by the Consumer Financial Protection Bureau, government-sponsored enterprise reform, and any related rules and regulations on our business operations and competitiveness; the costs and effects of legal and regulatory developments, including the resolution of legal proceedings or regulatory or other governmental inquiries and the results of regulatory examinations or reviews; ability to successfully implement our initiatives to lower our efficiency ratio; the effects of and changes in trade, monetary and fiscal policies and laws, including the interest rate policies of the Board of Governors of the Federal Reserve System; inflation, interest rate, securities market and monetary fluctuations; negative trends in our market capitalization and adverse changes in the price of the Company’s common stock; political instability; acts of war or terrorism; changes in consumer spending, borrowings and savings habits; failure to maintain effective internal control over financial reporting or disclosure controls and procedures; technological changes; changes in the competitive environment among financial holding companies and other financial service providers; the effect of changes in accounting policies and practices, as may be adopted by the regulatory agencies, as well as the Public Company Accounting Oversight Board, the Financial Accounting Standards Board and other accounting standard setters; our ability to attract and retain key personnel; changes in our organization, compensation and benefit plans; and our success at managing the risks involved in the foregoing items. For further information on factors that could cause actual results to materially differ from projections, please see the Company’s publicly available Securities and Exchange Commission filings, including the Company’s Form 10-K for the last fiscal year and, in particular, the discussion of “Risk Factors” set forth therein. The Company does not update any of its forward-looking statements except as required by law.

CENTRAL PACIFIC FINANCIAL CORP. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS (Unaudited)

(dollars in thousands)	September 30, 2016	December 31, 2015
Assets		
Cash and due from banks	$79,647	$71,797
Interest-bearing deposits in other banks	23,727	8,397
Investment securities:		
Available-for-sale, at fair value	1,262,224	1,272,255
Held-to-maturity, at amortized cost; fair value of: $230,529 at September 30, 2016 and $244,136 at December 31, 2015	226,573	247,917
Total investment securities	1,488,797	1,520,172
Loans held for sale	12,755	14,109
Loans and leases	3,439,654	3,211,532
Allowance for loan and lease losses	(59,384)	(63,314)
Net loans and leases	3,380,270	3,148,218
Premises and equipment, net	48,242	49,161
Accrued interest receivable	14,554	14,898
Investment in unconsolidated subsidiaries	7,011	6,157
Other real estate owned	791	1,962
Mortgage servicing rights	15,638	17,797
Core deposit premium	5,349	7,355
Bank-owned life insurance	155,233	153,967
Federal Home Loan Bank stock	12,173	8,606
Other assets	75,760	108,692
Total Assets	$5,319,947	$5,131,288
Liabilities		
Deposits:		
Noninterest-bearing demand	$1,194,557	$1,145,244
Interest-bearing demand	849,128	824,895
Savings and money market	1,379,484	1,399,093
Time	1,095,409	1,064,207
Total deposits	4,518,578	4,433,439
Short-term borrowings	150,000	69,000
Long-term debt	92,785	92,785
Other liabilities	39,092	41,425
Total Liabilities	4,800,455	4,636,649
Equity		
Preferred stock, no par value, authorized 1,000,000 shares; issued and outstanding: none at September 30, 2016 and December 31, 2015	—	—
Common stock, no par value, authorized 185,000,000 shares; issued and outstanding: 30,930,598 at September 30, 2016 and 31,361,452 at December 31, 2015	534,856	548,878

Surplus	84,207	82,847
Accumulated deficit	(116,225)	(137,314)
Accumulated other comprehensive income	16,628	203
Total Shareholders' Equity	519,466	494,614
Non-controlling interest	26	25
Total Equity	519,492	494,639
Total Liabilities and Equity	$5,319,947	$5,131,288

See accompanying notes to consolidated financial statements.

CENTRAL PACIFIC FINANCIAL CORP. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF INCOME (Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
(dollars in thousands, except per share data)	2016	2015	2016	2015
Interest income:				
Interest and fees on loans and leases	$33,384	$ 30,148	$98,055	$ 88,322
Interest and dividends on investment securities:				
Taxable interest	7,296	8,260	23,645	24,687
Tax-exempt interest	995	1,008	2,986	3,016
Dividends	10	9	30	26
Interest on deposits in other banks	17	6	45	28
Dividends on Federal Home Loan Bank stock	63	11	123	40
Total interest income	41,765	39,442	124,884	116,119
Interest expense:				
Interest on deposits:				
Demand	126	104	360	298
Savings and money market	254	230	786	678
Time	1,044	568	2,899	1,665
Interest on short-term borrowings	160	73	387	195
Interest on long-term debt	755	662	2,206	1,949
Total interest expense	2,339	1,637	6,638	4,785
Net interest income	39,426	37,805	118,246	111,334
Provision (credit) for loan and lease losses	(743)	(3,647)	(2,872)	(13,713)
Net interest income after credit for loan and lease losses	40,169	41,452	121,118	125,047
Other operating income:				
Service charges on deposit accounts	1,954	1,947	5,826	5,830
Loan servicing fees	1,357	1,407	4,081	4,257
Other service charges and fees	2,821	2,803	8,616	8,689
Income from fiduciary activities	880	854	2,577	2,518
Equity in earnings of unconsolidated subsidiaries	182	165	456	490
Fees on foreign exchange	129	126	403	352
Investment securities gains (losses)	—	—	—	(1,866)
Income from bank-owned life insurance	555	434	2,412	1,569
Loan placement fees	140	202	319	574
Net gain on sales of residential mortgage loans	2,212	1,551	5,523	4,775
Net gain on sales of foreclosed assets	57	252	606	379
Other	688	88	2,013	1,576
Total other operating income	10,975	9,829	32,832	29,143
Other operating expense:				
Salaries and employee benefits	17,459	17,193	52,246	49,534
Net occupancy	3,588	3,547	10,459	10,451
Equipment	852	775	2,432	2,617
Amortization of other intangible assets	1,690	1,683	6,291	5,347
Communication expense	948	895	2,826	2,661
Legal and professional services	1,699	1,808	5,035	5,669
Computer software expense	2,217	2,286	7,143	6,764
Advertising expense	772	502	1,839	1,586
Foreclosed asset expense	72	3	136	332

Other	3,989	3,483	11,969	13,690
Total other operating expense	33,286	32,175	100,376	98,651
Income before income taxes	17,858	19,106	53,574	55,539
Income tax expense	6,392	6,900	18,790	20,603
Net income	$11,466	$ 12,206	$34,784	$ 34,936
Per common share data:				
Basic earnings per common share	$0.37	$ 0.39	$1.12	$ 1.07
Diluted earnings per common share	$0.37	$ 0.38	$1.11	$ 1.06
Cash dividends declared	$0.16	$ 0.12	$0.44	$ 0.36
Shares used in computation:				
Basic shares	30,943,756	31,330,964	31,088,729	32,548,479
Diluted shares	31,142,128	31,749,880	31,277,402	32,932,347

See accompanying notes to consolidated financial statements.

CENTRAL PACIFIC FINANCIAL CORP. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
(dollars in thousands)	2016	2015	2016	2015
Net income	$11,466	$12,206	$34,784	$34,936
Other comprehensive income (loss), net of tax:				
Net change in unrealized gain (loss) on investment securities	(2,042)	7,563	15,677	3,102
Minimum pension liability adjustment	249	259	748	775
Total other comprehensive income (loss), net of tax	(1,793)	7,822	16,425	3,877
Comprehensive income	$9,673	$20,028	$51,209	$38,813

See accompanying notes to consolidated financial statements.

CENTRAL PACIFIC FINANCIAL CORP. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY (Unaudited)

	Common Shares Outstanding	Preferred Stock	Common Stock	Surplus	Accumulated Deficit	Accumulated Other Comprehensive Income	Non-Controlling Interest	Total
	(Dollars in thousands, except per share data)							
Balance at December 31, 2015	31,361,452	$ —	$548,878	$82,847	$(137,314)	$ 203	$ 25	$494,639
Net income	—	—	—	—	34,784	—	—	34,784
Other comprehensive income	—	—	—	—	—	16,425	—	16,425
Cash dividends ($0.44 per share)	—	—	—	—	(13,695)	—	—	(13,695)
22,800 net shares of common stock sold by directors' deferred compensation plan	—	—	(537)	—	—	—	—	(537)
636,922 shares of common stock repurchased and other related costs	(636,922)	—	(14,084)	—	—	—	—	(14,084)
Share-based compensation	206,068	—	599	1,360	—	—	—	1,959
Non-controlling interest	—	—	—	—	—	—	1	1
Balance at September 30, 2016	30,930,598	$ —	$534,856	$84,207	$(116,225)	$ 16,628	$ 26	$519,492
Balance at December 31, 2014	35,233,674	$ —	$642,205	$79,716	$(157,039)	$ 3,159	$ —	$568,041
Net income	—	—	—	—	34,936	—	—	34,936
Other comprehensive income	—	—	—	—	—	3,877	—	3,877
Cash dividends ($0.36 per share)	—	—	—	—	(11,718)	—	—	(11,718)
8,159 net shares of common stock sold by directors' deferred compensation plan	—	—	(154)	—	—	—	—	(154)
4,122,881 shares of common stock repurchased and other related costs	(4,122,881)	—	(93,533)	—	—	—	—	(93,533)
Share-based compensation	219,851	—	—	1,812	—	—	—	1,812
Non-controlling interest	—	—	—	—	—	—	—	—
Balance at September 30, 2015	31,330,644	$ —	$548,518	$81,528	$(133,821)	$ 7,036	$ —	$503,261

See accompanying notes to consolidated financial statements.

CENTRAL PACIFIC FINANCIAL CORP. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited)

	Nine Months Ended September 30,	
	2016	2015
	(Dollars in thousands)	
Cash flows from operating activities:		
Net income	$34,784	$34,936
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision (credit) for loan and lease losses	(2,872)	(13,713)
Depreciation and amortization	4,493	4,406
Write down of other real estate, net of gain on sale	(251)	26
Amortization of other intangible assets	6,291	5,347
Net amortization of investment securities	9,326	7,418
Share-based compensation	1,360	1,812
Net loss on investment securities	—	1,866
Net gain on sales of residential loans	(5,523)	(4,775)
Proceeds from sales of loans held for sale	315,348	304,351
Originations of loans held for sale	(308,471)	(299,679)
Equity in earnings of unconsolidated subsidiaries	(456)	(490)
Net increase in cash surrender value of bank-owned life insurance	(2,772)	(1,889)
Deferred income taxes	18,790	19,045
Net change in other assets and liabilities	(1,035)	3,235
Net cash provided by operating activities	69,012	61,896
Cash flows from investing activities:		
Proceeds from maturities of and calls on investment securities available for sale	140,258	125,688
Proceeds from sales of investment securities available for sale	—	117,496
Purchases of investment securities available for sale	(112,870)	(290,019)
Proceeds from maturities of and calls on investment securities held to maturity	22,335	19,950
Purchases of investment securities held to maturity	(1,644)	(37,043)
Net loan originations	(152,906)	(122,479)
Purchases of loan portfolios	(77,702)	(52,806)
Proceeds from sales of loans originated for investment	—	6,658
Proceeds from sale of other real estate	2,850	6,687
Proceeds from bank-owned life insurance	1,506	723
Purchases of premises and equipment	(3,574)	(3,014)
Net return of capital from unconsolidated subsidiaries	528	424
Contributions to unconsolidated subsidiaries	(5)	—
Net (purchases) proceeds from redemption of FHLB stock	(3,567)	31,884
Net cash used in investing activities	(184,791)	(195,851)
Cash flows from financing activities:		
Net increase in deposits	85,139	120,203
Net increase in short-term borrowings	81,000	117,000
Cash dividends paid on common stock	(13,695)	(11,718)
Repurchases of common stock and other related costs	(14,084)	(93,533)
Net proceeds from issuance of common stock and stock option exercises	599	—
Net cash provided by financing activities	138,959	131,952
Net increase (decrease) in cash and cash equivalents	23,180	(2,003)
Cash and cash equivalents at beginning of period	80,194	86,007

Cash and cash equivalents at end of period	$ 103,374	$ 84,004
Supplemental disclosure of cash flow information:		
Cash paid during the period for:		
Interest	$ 6,261	$ 4,841
Income taxes	—	1,280
Cash received during the period for:		
Income taxes	1,605	—
Supplemental disclosure of non-cash investing and financing activities:		
Net change in common stock held by directors' deferred compensation plan	537	154
Net reclassification of loans to other real estate	1,428	5,679
Net transfer of loans to loans held for sale	—	6,658

See accompanying notes to consolidated financial statements.

CENTRAL PACIFIC FINANCIAL CORP. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation

The accompanying unaudited consolidated financial statements of Central Pacific Financial Corp. and Subsidiaries (herein referred to as the “Company,” “we,” “us” or “our”) 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, certain information and footnote disclosures normally included in financial statements prepared in accordance with GAAP have been condensed or omitted pursuant to such rules and regulations.

These interim condensed consolidated financial statements and notes should be read in conjunction with the Company’s consolidated financial statements and notes thereto filed on Form 10-K for the fiscal year ended December 31, 2015. In the opinion of management, all adjustments necessary for a fair presentation have been made and include all normal recurring adjustments. Interim results of operations are not necessarily indicative of results to be expected for the year.

Principles of Consolidation

The consolidated financial statements include the accounts of the Company and its majority-owned subsidiaries. All significant intercompany accounts and transactions have been eliminated in consolidation.

In December 2015, we acquired a 50% ownership interest in a mortgage loan origination and brokerage company, One Hawaii HomeLoans, LLC. The bank concluded that the investment meets the consolidation requirements under Financial Accounting Standards Board (“FASB”) Accounting Standards Codification (“ASC”) 810, "Consolidation." The bank concluded that the entity meets the definition of a variable interest entity and that we are the primary beneficiary of the variable interest entity. Accordingly, the investment has been consolidated into our financial statements as of September 30, 2016.

We have 50% ownership interests in four other mortgage loan origination and brokerage companies which are accounted for using the equity method and are included in investment in unconsolidated subsidiaries: Pacific Access Mortgage, LLC, Gentry HomeLoans, LLC, Haseko HomeLoans, LLC and Island Pacific HomeLoans, LLC.

2. RECENT ACCOUNTING PRONOUNCEMENTS

In June 2014, the FASB issued ASU 2014-12, “Accounting for Share-Based Payments When the Terms of an Award Provide That a Performance Target Could Be Achieved after the Requisite Service Period.” ASU 2014-12 requires that a performance target that affects vesting and that could be achieved after the requisite service period be treated as a performance condition. As of September 30, 2016, the Company did not have any share-based payment awards that included performance targets that could be achieved after the requisite service period. As such, the adoption of ASU 2014-12 on January 1, 2016 did not have a material impact on our consolidated financial statements.

In February 2015, the FASB issued ASU 2015-02, “Amendments to the Consolidation Analysis.” ASU 2015-02 changes the analysis that a reporting entity must perform to determine whether it should consolidate certain types of legal entities. Specifically, the amendments:1) modify the evaluation of whether limited partnerships and similar legal entities are variable interest entities (“VIEs”) or voting interest entities; 2) eliminate the presumption that a general partner should consolidate a limited partnership; 3) affect the consolidation analysis of reporting entities that are involved with VIEs, particularly those that have fee arrangements and related party relationships; 4) provide a scope exception from consolidation guidance for reporting entities with interests in legal entities that are required to comply with or operate in accordance with requirements that are similar to those in Rule 2a-7 of the Investment Company Act of 1940 for registered money market funds. All legal entities are subject to reevaluation under the revised consolidation model. The adoption of ASU 2015-02 on January 1, 2016 did not have a material impact on our consolidated financial statements.

In August 2016, the FASB issued ASU 2016-15, “Classification of Certain Cash Receipts and Cash Payments (Topic 230)." ASU 2016-15 provides guidance on eight statement of cash flow classification issues and is intended to reduce the current and future diversity in practice described in the amendments. Current GAAP is either unclear or does not include specific guidance on the eight statement of cash flow classification issues included in ASU 2016-15. ASU 2016-15 is effective for the Company's reporting period beginning January 1, 2018. Early adoption is permitted, provided that all of the amendments are adopted in the same period. The amendments in ASU 2016-15 should be applied using a retrospective transition method to each period presented. If it is impracticable to apply the amendments retrospectively for some of the issues, the amendments for those issues would be applied prospectively as of the earliest date practicable. As ASU 2016-15 only impacts classification within the statement of cash flows, we do not expect the adoption of this guidance to have a material impact on our consolidated financial statements.

3. INVESTMENT SECURITIES

A summary of held-to-maturity and available-for-sale investment securities are as follows:

(dollars in thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
September 30, 2016				
Held-to-Maturity:				
Mortgage-backed securities:				
Residential - U.S. Government-sponsored entities	$132,470	$ 890	$ (2)	$133,358
Commercial - U.S. Government-sponsored entities	94,103	3,068	—	97,171
Total	$226,573	$ 3,958	$ (2)	$230,529
Available-for-Sale:				
Debt securities:				
States and political subdivisions	$185,504	$ 6,300	$ (26)	$191,778
Corporate securities	107,011	2,609	(12)	109,608
Mortgage-backed securities:				
Residential - U.S. Government-sponsored entities	747,636	11,881	(314)	759,203
Residential - Non-government agencies	55,480	2,142	—	57,622
Commercial - Non-government agencies	135,296	7,933	—	143,229
Other	692	92	—	784
Total	$1,231,619	$ 30,957	$ (352)	$1,262,224

(dollars in thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
December 31, 2015				
Held-to-Maturity:				
Mortgage-backed securities:				
Residential - U.S. Government-sponsored entities	$152,315	$ 123	$ (2,915)	$149,523
Commercial - U.S. Government-sponsored entities	95,602	—	(989)	94,613
Total	$247,917	$ 123	$ (3,904)	$244,136
Available-for-Sale:				
Debt securities:				
States and political subdivisions	$187,552	$ 3,819	$ (898)	$190,473
Corporate securities	107,721	1,077	(227)	108,571
Mortgage-backed securities:				
Residential - U.S. Government-sponsored entities	771,657	5,885	(5,633)	771,909
Residential - Non-government agencies	64,286	733	(987)	64,032
Commercial - Non-government agencies	135,439	2,033	(1,118)	136,354

Other	848	68	—	916
Total	$1,267,503	$ 13,615	$ (8,863)	$1,272,255

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The amortized cost and estimated fair value of investment securities at September 30, 2016 by contractual maturity are shown below. Expected maturities will differ from contractual maturities because issuers may have the right to call or prepay obligations with or without call or prepayment penalties.

(dollars in thousands)	September 30, 2016 Amortized Cost	Estimated Fair Value
Held-to-Maturity:		
Mortgage-backed securities:		
Residential - U.S. Government-sponsored entities	$132,470	$ 133,358
Commercial - U.S. Government-sponsored entities	94,103	97,171
Total	$226,573	$ 230,529
Available-for-Sale:		
Due in one year or less	$13,648	$ 13,676
Due after one year through five years	124,029	127,061
Due after five years through ten years	73,338	75,987
Due after ten years	81,500	84,662
Mortgage-backed securities:		
Residential - U.S. Government-sponsored entities	747,636	759,203
Residential - Non-government agencies	55,480	57,622
Commercial - Non-government agencies	135,296	143,229
Other	692	784
Total	$1,231,619	$ 1,262,224

We did not sell any available-for-sale securities during the nine months ended September 30, 2016.

During the second quarter of 2015, we sold certain available-for-sale investment securities for gross proceeds of $117.5 million. Gross realized losses on the sale of the available-for-sale investment securities were $1.9 million. The specific identification method was used as the basis for determining the cost of all securities sold. We did not sell any available-for-sale securities during the first and third quarters of 2015.

Investment securities of $1.10 billion and $1.00 billion at September 30, 2016 and December 31, 2015, respectively, were pledged to secure public funds on deposit and other long-term debt and short-term borrowings.

Provided below is a summary of the 21 and 155 investment securities which were in an unrealized loss position at September 30, 2016 and December 31, 2015, respectively, segregated by continuous length of impairment.

(dollars in thousands)	Less Than 12 Months Fair Value	Unrealized Losses	12 Months or Longer Fair Value	Unrealized Losses	Total Fair Value	Unrealized Losses
September 30, 2016						
Debt securities:						
States and political subdivisions	$ 3,425	$ (26)	$ —	$ —	$3,425	$ (26)
Corporate securities	5,497	(12)	—	—	5,497	(12)
Mortgage-backed securities:						
	101,566	(263)	4,181	(53)	105,747	(316)

Residential - U.S. Government-sponsored entities						
Total temporarily impaired securities	$ 110,488	$ (301)	$ 4,181	$ (53)	$114,669	$ (354)

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(dollars in thousands)	Less Than 12 Months Fair Value	Less Than 12 Months Unrealized Losses	12 Months or Longer Fair Value	12 Months or Longer Unrealized Losses	Total Fair Value	Total Unrealized Losses
December 31, 2015						
Debt securities:						
States and political subdivisions	$ 30,481	$ (532)	$ 12,576	$ (366)	$ 43,057	$ (898)
Corporate securities	32,977	(227)	—	—	32,977	(227)
Mortgage-backed securities:						
Residential - U.S. Government-sponsored entities	507,525	(6,241)	88,271	(2,307)	595,796	(8,548)
Residential - Non-government agencies	37,975	(987)	—	—	37,975	(987)
Commercial - U.S. Government-sponsored entities	94,613	(989)	—	—	94,613	(989)
Commercial - Non-government agencies	62,555	(961)	4,644	(157)	67,199	(1,118)
Total temporarily impaired securities	$ 766,126	$ (9,937)	$ 105,491	$ (2,830)	$ 871,617	$ (12,767)

Other-Than-Temporary Impairment ("OTTI")

Unrealized losses for all investment securities are reviewed to determine whether the losses are deemed "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, we evaluate 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;
- 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 debt 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 declines 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 anticipated credit losses.

Because we have no intent to sell securities in an unrealized loss position and it is not more likely than not that we will be required to sell such securities before recovery of its amortized cost basis, we do not consider our investments to be other-than-temporarily impaired.

4. LOANS AND LEASES

Loans and leases, excluding loans held for sale, consisted of the following:

(dollars in thousands)	September 30, 2016	December 31, 2015
Commercial, financial and agricultural	$507,573	$520,457
Real estate:		
Construction	108,457	85,196
Residential mortgage	1,157,914	1,131,882
Home equity	351,258	301,980
Commercial mortgage	863,680	761,566
Consumer:		
Automobiles	217,526	190,202
Other consumer	230,789	217,822
Leases	756	1,028
Gross loans and leases	3,437,953	3,210,133
Net deferred costs	1,701	1,399
Total loans and leases, net of deferred costs	$3,439,654	$3,211,532

During the nine months ended September 30, 2016, we transferred the collateral in two portfolio loans with a carrying value totaling $1.3 million to other real estate owned. We did not transfer any loans to the held-for-sale category during the nine months ended September 30, 2016. In addition, we did not sell any portfolio loans during the nine months ended September 30, 2016.

In March 2016, we purchased a direct auto loan portfolio totaling $23.2 million which included a $0.3 million premium over the $22.9 million outstanding balance. At the time of purchase, the auto loans had a weighted average remaining term of 56 months and a weighted average yield of 3.38%. During the first quarter of 2016, we also purchased unsecured consumer loans totaling $29.2 million, which represented the outstanding balance at the time of purchases. At the time of purchases, the unsecured consumer loans had a weighted average remaining term of 38 months and a weighted average interest rate of 7.55%.

In May 2016, we purchased a direct auto loan portfolio totaling $18.0 million which included a $0.5 million premium over the $17.5 million outstanding balance. At the time of purchase, the auto loans had a weighted average remaining term of 75 months and a weighted average yield of 3.75%. During the second quarter of 2016, we also purchased unsecured consumer loans totaling $7.3 million, which represented the outstanding balance at the time of purchases. At the time of purchases, the unsecured consumer loans had a weighted average remaining term of 37 months and a weighted average interest rate of 7.57%.

During the nine months ended September 30, 2015, we transferred the collateral in seven portfolio loans with a carrying value of $2.1 million to other real estate owned. In the second quarter of 2015, we transferred two portfolio loans to a single borrower with a carrying value of $6.6 million to the held-for-sale category and subsequently sold the two loans in the second quarter of 2015 at its carrying value.

In August 2015, we purchased a participation interest in auto loans totaling $24.7 million, which included a $0.8 million premium over the $23.9 million outstanding balance. At the time of purchase, the auto loans had a weighted average remaining term of 68 months and a weighted average yield of 4.28%. In June 2015, we purchased a participation interest in auto loans totaling $28.1 million, which included a $1.0 million premium over the $27.1 million outstanding balance. At the time of the purchase, the auto loans had a weighted average remaining term of 79 months and a weighted average interest rate of 4.56%.

Impaired Loans

The following tables present by class, the balance in the allowance for loan and lease losses (the "Allowance") and the recorded investment in loans and leases based on the Company’s impairment measurement method as of September 30, 2016 and December 31, 2015:

		Real Estate								
(dollars in thousands)	Comml, Fin & Ag	Constr	Resi Mortgage	Home Equity	Comml Mortgage	Consumer - Auto	Consumer - Other	Leases	Unallocated	Total
September 30, 2016										
Allowance for loan and lease losses attributable to loans:										
Individually evaluated for impairment	$5	$—	$—	$—	$—	$—	$—	$—	$—	$5
Collectively evaluated for impairment	4,547	2,386	13,914	4,012	26,370	2,937	3,213	—	—	57,379
Subtotal	4,552	2,386	13,914	4,012	26,370	2,937	3,213	—	—	57,384
Unallocated	—	—	—	—	—	—	—	—	2,000	2,000
Total ending balance	$4,552	$2,386	$13,914	$4,012	$26,370	$2,937	$3,213	$—	$2,000	$59,384
Loans and leases:										
Individually evaluated for impairment	$2,004	$3,046	$21,481	$573	$7,952	$—	$—	$—	$—	$35,056
Collectively evaluated for impairment	505,569	105,411	1,136,433	350,685	855,728	217,526	230,789	756	—	3,402,897
Subtotal	507,573	108,457	1,157,914	351,258	863,680	217,526	230,789	756	—	3,437,953
Net deferred costs (income)	411	(229)	2,827	(2)	(963)	—	(343)	—	—	1,701
Total loans and leases, net of deferred	$507,984	$108,228	$1,160,741	$351,256	$862,717	$217,526	$230,446	$756	$—	$3,439,654

costs
(income)

(dollars in thousands)	Comml, Fin & Ag	Real Estate Constr	Resi Mortgage	Home Equity	Comml Mortgage	Consumer - Auto	Consumer - Other	Leases	Unallocated	Total
December 31, 2015										
Allowance for loan and lease losses attributable to loans:										
Individually evaluated for impairment	$—	$—	$—	$—	$51	$—	$ —	$—	$ —	$51
Collectively evaluated for impairment	6,905	8,454	14,642	3,096	21,796	2,891	3,339	—	—	61,123
Subtotal	6,905	8,454	14,642	3,096	21,847	2,891	3,339	—	—	61,174
Unallocated	—	—	—	—	—	—	—	—	2,140	2,140
Total ending balance	$6,905	$8,454	$14,642	$3,096	$21,847	$2,891	3,339	$—	$ 2,140	$63,314
Loans and leases:										
Individually evaluated for impairment	$1,044	$4,126	$21,940	$776	$10,318	$—	$ —	$—	$ —	$38,204
Collectively evaluated for impairment	519,413	81,070	1,109,942	301,204	751,248	190,202	217,822	1,028	—	3,171,929
Subtotal	520,457	85,196	1,131,882	301,980	761,566	190,202	217,822	1,028	—	3,210,133
Net deferred costs (income)	629	(311)	2,443	—	(817)	—	(545)	—	—	1,399
Total loans and leases, net of deferred costs (income)	$521,086	$84,885	$1,134,325	$301,980	$760,749	$190,202	217,277	$1,028	$ —	$3,211,532

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The following tables present by class, information related to impaired loans as of September 30, 2016 and December 31, 2015:

(dollars in thousands)	Unpaid Principal Balance	Recorded Investment	Allowance Allocated
September 30, 2016			
Impaired loans with no related allowance recorded:			
Commercial, financial & agricultural	$943	$ 832	$ —
Real estate:			
Construction	9,310	3,046	—
Residential mortgage	23,260	21,481	—
Home equity	573	573	—
Commercial mortgage	8,810	7,952	—
Total impaired loans with no related allowance recorded	42,896	33,884	—
Impaired loans with an allowance recorded:			
Commercial, financial & agricultural	1,172	1,172	5
Total impaired loans with an allowance recorded	1,172	1,172	5
Total	$44,068	$ 35,056	$ 5

(dollars in thousands)	Unpaid Principal Balance	Recorded Investment	Allowance Allocated
December 31, 2015			
Impaired loans with no related allowance recorded:			
Commercial, financial & agricultural	$1,155	$ 1,044	$ —
Real estate:			
Construction	10,472	4,126	—
Residential mortgage	24,016	21,940	—
Home equity	776	776	—
Commercial mortgage	10,010	9,152	—
Total impaired loans with no related allowance recorded	46,429	37,038	—
Impaired loans with an allowance recorded:			
Commercial mortgage	1,166	1,166	51
Total impaired loans with an allowance recorded	1,166	1,166	51
Total	$47,595	$ 38,204	$ 51

The following table presents by class, the average recorded investment and interest income recognized on impaired loans for the three and nine months ended September 30, 2016 and 2015:

	Three Months Ended				Nine Months Ended			
	September 30, 2016		September 30, 2015		September 30, 2016		September 30, 2015	
(dollars in thousands)	Average Recorded Investment	Interest Income Recognized	Average Recorded Investment	Interest Income Recognized	Average Recorded Investment	Interest Income Recognized	Average Recorded Investment	Interest Income Recognized
Commercial, financial & agricultural	$2,047	$ —	$3,444	$ 4	$1,882	$ 10	$8,000	$ 14
Real estate:								
Construction	3,101	31	4,325	40	3,688	101	4,514	152
Residential mortgage	22,299	201	24,946	78	22,272	195	26,695	64
Home equity	659	5	520	9	630	18	550	17
Commercial mortgage	8,091	51	8,464	15	9,006	122	15,884	354
Total	$36,197	$ 288	$41,699	$ 146	$37,478	$ 446	$55,643	$ 601

Foreclosure Proceedings

The Company had $0.3 million of residential mortgage loans collateralized by residential real estate property that were in the process of foreclosure at September 30, 2016.

Aging Analysis of Accruing and Non-Accruing Loans and Leases

For all loan types, the Company determines delinquency status by considering the number of days full payments required by the contractual terms of the loan are past due. The following tables present by class, the aging of the recorded investment in past due loans and leases as of September 30, 2016 and December 31, 2015:

(dollars in thousands)	Accruing Loans 30 - 59 Days Past Due	Accruing Loans 60 - 89 Days Past Due	Accruing Loans Greater Than 90 Days Past Due	Nonaccrual Loans	Total Past Due and Nonaccrual	Loans and Leases Not Past Due	Total
September 30, 2016							
Commercial, financial & agricultural	$ 486	$ 115	$ —	$ 2,005	$ 2,606	$505,378	$507,984
Real estate:							
Construction	—	—	—	—	—	108,228	108,228
Residential mortgage	—	578	200	5,424	6,202	1,154,539	1,160,741
Home equity	33	1,182	—	479	1,694	349,562	351,256
Commercial mortgage	972	—	—	2,967	3,939	858,778	862,717
Consumer:							
Automobiles	696	273	131	—	1,100	216,426	217,526
Other consumer	491	324	106	—	921	229,525	230,446
Leases	—	—	—	—	—	756	756
Total	$ 2,678	$ 2,472	$ 437	$ 10,875	$ 16,462	$3,423,192	$3,439,654

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(dollars in thousands)	Accruing Loans 30 - 59 Days Past Due	Accruing Loans 60 - 89 Days Past Due	Accruing Loans Greater Than 90 Days Past Due	Nonaccrual Loans	Total Past Due and Nonaccrual	Loans and Leases Not Past Due	Total
December 31, 2015							
Commercial, financial & agricultural	$ 276	$ 140	$ —	$ 1,044	$ 1,460	$519,626	$521,086
Real estate:							
Construction	—	—	—	—	—	84,885	84,885
Residential mortgage	3,134	325	—	5,464	8,923	1,125,402	1,134,325
Home equity	700	220	—	666	1,586	300,394	301,980
Commercial mortgage	54	—	—	7,094	7,148	753,601	760,749
Consumer:							
Automobiles	912	168	151	—	1,231	188,971	190,202
Other consumer	531	353	122	—	1,006	216,271	217,277
Leases	—	—	—	—	—	1,028	1,028
Total	$ 5,607	$ 1,206	$ 273	$ 14,268	$ 21,354	$3,190,178	$3,211,532

Modifications

Troubled debt restructurings (“TDRs”) included in nonperforming assets at September 30, 2016 totaled $3.8 million and consisted of 20 Hawaii residential mortgage loans with a combined principal balance of $3.0 million and three Hawaii commercial, financial and agricultural loans with a combined principal balance of $0.8 million.

Concessions made to the original contractual terms of these loans consisted primarily of the deferral of interest and/or principal payments due to deterioration in the borrowers’ financial condition. The principal balances on these TDRs had matured and/or were in default at the time of restructure and we have no commitments to lend additional funds to any of these borrowers. There were $17.8 million of TDRs still accruing interest at September 30, 2016, none of which were more than 90 days delinquent. At December 31, 2015, there were $20.3 million of TDRs still accruing interest, none of which were more than 90 days delinquent.

Some loans modified in a TDR may already be on nonaccrual status and partial charge-offs may have already been taken against the outstanding loan balance. Thus, these loans have already been identified as impaired and have already been evaluated under the Company’s allowance for loan and lease losses (the “Allowance”) methodology. Loans that were not on nonaccrual status when modified in a TDR may have the financial effect of increasing the specific allowance associated with the loan. The loans modified in a TDR did not have a material effect on our provision for loan and lease losses (the “Provision”) and the Allowance during the three and nine months ended September 30, 2016.

The following table presents by class, information related to loans modified in a TDR during the periods presented. No loans were modified in a TDR during the three months ended September 30, 2015.

(dollars in thousands)	Number of Contracts	Recorded Investment (as of Period End)	Increase in the Allowance
Three Months Ended September 30, 2016			
Real estate: Residential mortgage	3	289	—
Nine Months Ended September 30, 2016			

Real estate: Residential mortgage	3	289	—	
Nine Months Ended September 30, 2015				
Commercial, financial & agricultural	1	$ 512	$	—
Real estate: Commercial mortgage	1	957	—	
Total	2	$ 1,469	$	—

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No loans were modified as a TDR within the previous twelve months that subsequently defaulted during the three and nine months ended September 30, 2016 and 2015.

Credit Quality Indicators

The Company categorizes loans and leases into risk categories based on relevant information about the ability of borrowers to service their debt such as: current financial information, historical payment experience, credit documentation, public information, and current economic trends, among other factors. The Company analyzes loans and leases individually by classifying the loans and leases as to credit risk. This analysis includes non-homogeneous loans and leases, such as commercial and commercial real estate loans. This analysis is performed on a quarterly basis. The Company uses the following definitions for risk ratings:

Special Mention. Loans and leases classified as special mention, while still adequately protected by the borrower's capital adequacy and payment capability, exhibit distinct weakening trends and/or elevated levels of exposure to external conditions. If left unchecked or uncorrected, these potential weaknesses may result in deteriorated prospects of repayment. These exposures require management's close attention so as to avoid becoming undue or unwarranted credit exposures.

Substandard. Loans and leases classified as substandard are inadequately protected by the borrower's current financial condition and payment capability or of the collateral pledged, if any. Loans and leases so classified have a well-defined weakness or weaknesses that jeopardize the orderly repayment of debt. They are characterized by the distinct possibility that the bank will sustain some loss if the deficiencies are not corrected.

Doubtful. Loans and leases classified as doubtful have all the weaknesses inherent in those classified as substandard, with the added characteristic that the weaknesses make collection or orderly repayment in full, on the basis of current existing facts, conditions and values, highly questionable and improbable. Possibility of loss is extremely high, but because of certain important and reasonably specific factors that may work to the advantage and strengthening of the exposure, its classification as an estimated loss is deferred until its more exact status may be determined.

Loss. Loans and leases classified as loss are considered to be non-collectible and of such little value that their continuance as bankable assets is not warranted. This does not mean the loan has absolutely no recovery value, but rather it is neither practical nor desirable to defer writing off the loan, even though partial recovery may be obtained in the future. Losses are taken in the period in which they surface as uncollectible.

Loans and leases not meeting the criteria above are considered to be pass-rated. The following table presents by class and credit indicator, the recorded investment in the Company's loans and leases as of September 30, 2016 and December 31, 2015:

(dollars in thousands)	Pass	Special Mention	Substandard	Loss	Subtotal	Net Deferred Costs (Income)	Total
September 30, 2016							
Commercial, financial & agricultural	$501,119	$3,765	$ 2,689	$—	$507,573	$411	$507,984
Real estate:							
Construction	98,740	9,670	47	—	108,457	(229)	108,228
Residential mortgage	1,152,179	111	5,624	—	1,157,914	2,827	1,160,741
Home equity	348,079	2,700	479	—	351,258	(2)	351,256
Commercial mortgage	827,005	20,569	16,106	—	863,680	(963)	862,717
Consumer:							
Automobiles	217,289	—	131	106	217,526	—	217,526
Other consumer	230,707	—	82	—	230,789	(343)	230,446
Leases	756	—	—	—	756	—	756
Total	$3,375,874	$36,815	$ 25,158	$106	$3,437,953	$1,701	$3,439,654
December 31, 2015							
Commercial, financial & agricultural	$514,971	$2,168	$ 3,318	$—	$520,457	$629	$521,086
Real estate:							
Construction	83,601	808	787	—	85,196	(311)	84,885
Residential mortgage	1,126,418	—	5,464	—	1,131,882	2,443	1,134,325
Home equity	301,314	—	666	—	301,980	—	301,980
Commercial mortgage	705,520	41,335	14,711	—	761,566	(817)	760,749
Consumer:							
Automobiles	190,051	—	151	—	190,202	—	190,202
Other consumer	217,727	95	—	—	217,822	(545)	217,277
Leases	1,028	—	—	—	1,028	—	1,028
Total	$3,140,630	$44,406	$ 25,097	$—	$3,210,133	$1,399	$3,211,532

In accordance with applicable Interagency Guidance issued by our primary bank regulators, we define subprime borrowers as typically having weakened credit histories that include payment delinquencies and possibly more severe problems such as charge-offs, judgments, and bankruptcies. They may also display reduced repayment capacity as measured by credit scores, debt-to-income ratios, or other criteria that may encompass borrowers with incomplete credit histories. Subprime loans are loans to borrowers displaying one or more of these characteristics at the time of origination or purchase. Such loans have a higher risk of default than loans to prime borrowers. At September 30, 2016 and December 31, 2015, we did not have any loans that we considered to be subprime.

5. ALLOWANCE FOR LOAN AND LEASE LOSSES

The following table presents by class, the activity in the Allowance for the periods indicated:

	Commercial, Financial & Agricultural	Real Estate Construction	Residential Mortgage	Home Equity	Commercial Mortgage	Consumer - Auto	Consumer - Other	Leases	Unallocated	Total
	(Dollars in thousands)									
Three Months Ended September 30, 2016										
Beginning balance	$4,442	$3,823	$14,192	$3,446	$27,448	$2,573	$2,840	$—	$2,000	$60,764
Provision (credit) for loan and lease losses	20	(1,528)	(451)	562	(1,206)	658	1,202	—	—	(743)
	4,462	2,295	13,741	4,008	26,242	3,231	4,042	—	2,000	60,021
Charge-offs	465	—	—	—	—	409	940	—	—	1,814
Recoveries	555	91	173	4	128	115	111	—	—	1,177
Net charge-offs (recoveries)	(90)	(91)	(173)	(4)	(128)	294	829	—	—	637
Ending balance	$4,552	$2,386	$13,914	$4,012	$26,370	$2,937	$3,213	$—	$2,000	$59,384
Three Months Ended September 30, 2015										
Beginning balance	$7,569	$10,670	$14,932	$2,914	$20,008	$3,410	$3,920	$1	$3,500	$66,924
Provision (credit) for loan and lease losses	(293)	(2,702)	(144)	121	(1,573)	424	548	(28)	—	(3,647)
	7,276	7,968	14,788	3,035	18,435	3,834	4,468	(27)	3,500	63,277
Charge-offs	170	—	—	46	—	299	575	—	—	1,090
Recoveries	504	283	191	5	3,130	209	108	27	—	4,457
Net charge-offs (recoveries)	(334)	(283)	(191)	41	(3,130)	90	467	(27)	—	(3,367)
Ending balance	$7,610	$8,251	$14,979	$2,994	$21,565	$3,744	$4,001	$—	$3,500	$66,644

	Commercial, Financial & Agricultural	Real Estate Construction	Residential Mortgage	Home Equity	Commercial Mortgage	Consumer - Auto	Consumer - Other	Leases	Unallocated	Total
	(Dollars in thousands)									
Nine Months Ended September 30, 2016										
Beginning balance	$6,905	$8,454	$14,642	$3,096	$21,847	$2,891	$3,339	$—	$2,140	$63,314
Provision (credit) for loan and lease losses	(2,888)	(6,177)	(1,119)	916	4,368	2,294	(126)	—	(140)	(2,872)
	4,017	2,277	13,523	4,012	26,215	5,185	3,213	—	2,000	60,442
Charge-offs	1,089	—	—	—	—	3,596	—	—	—	4,685
Recoveries	1,624	109	391	—	155	1,348	—	—	—	3,627
Net charge-offs (recoveries)	(535)	(109)	(391)	—	(155)	2,248	—	—	—	1,058
Ending balance	$4,552	$2,386	$13,914	$4,012	$26,370	$2,937	$3,213	$—	$2,000	$59,384

Nine Months Ended September 30, 2015								
Beginning balance	$8,954	$14,969	$15,031	$2,896	$20,869	$3,373	$3,941	$ 7