CENTRAL PACIFIC FINANCIAL CORP
Form 10-Q
November 04, 2014

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

FORM 10-Q

(Mark One)

T QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended September 30, 2014

or

£ 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 (State or other jurisdiction of incorporation or organization)	99-0212597 (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 T No £

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

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 £ Accelerated filer T Non-accelerated filer £ Smaller reporting company £

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

The number of shares outstanding of registrant’s common stock, no par value, on October 30, 2014 was 35,903,230 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, 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 believe 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: an increase in inventory or adverse conditions in the Hawaii and California real estate markets and deterioration in the construction industry; 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 skilled employees; 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)

	September 30, 2014	December 31, 2013
	(Dollars in thousands)	
Assets		
Cash and due from banks	$ 76,047	$ 45,092
Interest-bearing deposits in other banks	14,074	4,256
Investment securities:		
Available for sale, at fair value	1,184,564	1,407,999
Held to maturity, at amortized cost (fair value of $235,929 at September 30, 2014 and $238,705 at December 31, 2013)	242,141	252,047
Total investment securities	1,426,705	1,660,046
Loans held for sale	5,352	12,370
Loans and leases	2,874,755	2,630,601
Allowance for loan and lease losses	(82,838)	(83,820)
Net loans and leases	2,791,917	2,546,781
Premises and equipment, net	49,092	49,039
Accrued interest receivable	12,722	14,072
Investment in unconsolidated subsidiaries	7,548	9,127
Other real estate	3,596	5,163
Other intangible assets	30,498	32,783
Bank-owned life insurance	151,524	149,604
Federal Home Loan Bank stock	44,457	46,193
Other assets	136,737	166,672
Total assets	$ 4,750,269	$ 4,741,198
Liabilities and Equity		
Deposits:		
Noninterest-bearing demand	$ 996,033	$ 891,017
Interest-bearing demand	802,336	728,619
Savings and money market	1,229,576	1,207,016
Time	1,020,151	1,109,521
Total deposits	4,048,096	3,936,173
Short-term borrowings	-	8,015
Long-term debt	92,785	92,799
Other liabilities	40,346	44,037
Total liabilities	4,181,227	4,081,024
Equity:		
Preferred stock, no par value, authorized 1,100,000 shares, issued and outstanding		

none at September 30, 2014 and December 31, 2013, respectively		-		-
Common stock, no par value, authorized 185,000,000 shares, issued and outstanding 35,903,230 and 42,107,633 shares at September 30, 2014 and December 31, 2013, respectively		655,219		784,547
Surplus		77,598		75,498
Accumulated deficit		(166,740)		(184,087)
Accumulated other comprehensive income (loss)		2,965		(15,845)
Total shareholders' equity		569,042		660,113
Non-controlling interest		-		61
Total equity		569,042		660,174
Total liabilities and equity	$	4,750,269	$	4,741,198

See accompanying notes to consolidated financial statements.

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

	Three Months Ended September 30, 2014	Three Months Ended September 30, 2013	Nine Months Ended September 30, 2014	Nine Months Ended September 30, 2013
	(Amounts in thousands, except per share data)			
Interest income:				
Interest and fees on loans and leases	$ 28,364	$ 26,414	$ 83,287	$ 77,362
Interest and dividends on investment securities:				
Taxable interest	7,744	8,114	25,716	22,518
Tax-exempt interest	1,002	992	2,996	3,059
Dividends	8	5	10	16
Interest on deposits in other banks	9	21	24	178
Dividends on Federal Home Loan Bank stock	12	12	35	12
Total interest income	37,139	35,558	112,068	103,145
Interest expense:				
Interest on deposits:				
Demand	96	91	277	259
Savings and money market	225	227	672	663
Time	629	671	1,880	2,150
Interest on short-term borrowings	10	3	82	3
Interest on long-term debt	647	795	1,923	2,457
Total interest expense	1,607	1,787	4,834	5,532
Net interest income	35,532	33,771	107,234	97,613
Provision (credit) for loan and lease losses	(1,722)	(3,189)	(1,043)	(9,977)
Net interest income after provision for loan and lease losses	37,254	36,960	108,277	107,590
Other operating income:				
Service charges on deposit accounts	2,070	1,776	6,052	4,950
Loan servicing fees	1,446	1,509	4,338	4,578
Other service charges and fees	2,886	3,422	8,912	9,326
Income from fiduciary activities	797	724	2,687	2,107
Equity in earnings of unconsolidated subsidiaries	11	513	422	733
Fees on foreign exchange	118	149	351	348

Investment securities gains	-	-	240	-
Income from bank-owned life insurance	810	611	2,246	1,492
Loan placement fees	35	81	356	408
Net gain on sales of residential loans	1,685	1,476	4,151	8,492
Net gain on sales of foreclosed assets	218	276	962	8,528
Other	1,387	1,393	2,894	1,810
Total other operating income	11,463	11,930	33,611	42,772
Other operating expense:				
Salaries and employee benefits	16,552	19,167	50,536	55,944
Net occupancy	4,051	3,802	11,375	10,651
Equipment	953	952	2,694	2,788
Amortization of other intangible assets	1,328	1,637	3,886	5,994
Communication expense	925	907	2,693	2,727
Legal and professional services	1,786	2,155	5,826	6,410
Computer software expense	1,659	1,056	4,592	3,182
Advertising expense	673	601	2,037	2,141
Foreclosed asset expense	1,355	(12)	1,443	993
Other	5,964	6,247	14,982	13,435
Total other operating expense	35,246	36,512	100,064	104,265
Income before income taxes	13,471	12,378	41,824	46,097
Income tax expense (benefit)	5,241	2,174	14,636	(115,683)
Net income	$ 8,230	$ 10,204	$ 27,188	$ 161,780
Per common share data:				
Basic earnings per share	$ 0.23	$ 0.24	$ 0.72	$ 3.86
Diluted earnings per share	0.23	0.24	0.71	3.83
Cash dividends declared	0.10	0.08	0.26	0.08
Shares used in computation:				
Basic shares	35,863	42,028	37,943	41,934
Diluted shares	36,353	42,421	38,440	42,263

See accompanying notes to consolidated financial statements.

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

	Three Months Ended September 30, 2014	Three Months Ended September 30, 2013	Nine Months Ended September 30, 2014	Nine Months Ended September 30, 2013
	(Dollars in thousands)			
Net income	$ 8,230	$ 10,204	$ 27,188	$ 161,780
Other comprehensive income (loss), net of tax				
Net change in unrealized gain (loss) on investment securities	(1,665)	2,667	18,221	(25,256)
Net change in unrealized loss on derivatives	-	-	-	10,993
Defined benefit plans	212	375	589	1,375
Other comprehensive income (loss), net of tax	(1,453)	3,042	18,810	(12,888)
Comprehensive income	$ 6,777	$ 13,246	$ 45,998	$ 148,892

See accompanying notes to consolidated financial statements.

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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 (Loss)	Non-Controlling Interests	Total
	(Dollars in thousands, except per share data)							
Balance at December 31, 2013	42,107,633	$ -	$ 784,547	$ 75,498	$ (184,087)	$ (15,845)	$ 61	$ 660,174
Net income	-	-	-	-	27,188	-	-	27,188
Other comprehensive income	-	-	-	-	-	18,810	-	18,810
Cash dividends paid ($0.26 per share)	-	-	-	-	(9,841)	-	-	(9,841)
1,118 net shares of common stock sold by directors' deferred compensation plan	-	-	(11)	-	-	-	-	(11)
6,369,266 shares of common stock repurchased and other related costs	(6,369,266)	-	(129,391)	-	-	-	-	(129,391)
Share-based compensation	164,863	-	74	2,100	-	-	-	2,174
Non-controlling interests	-	-	-	-	-	-	(61)	(61)
Balance at September 30, 2014	35,903,230	$ -	$ 655,219	$ 77,598	$ (166,740)	$ 2,965	$ -	$ 569,042
Balance at December 31, 2012	42,088,976	$ -	$ 784,512	$ 70,567	$ (349,427)	$ (830)	$ 9,957	$ 514,779
Net income	-	-	-	-	161,780	-	-	161,780
Other comprehensive loss	-	-	-	-	-	(12,888)	-	(12,888)
Cash dividends paid ($0.08 per share)	-	-	-	-	(3,367)	-	-	(3,367)

1,782 net shares of common stock purchased by directors' deferred compensation plan	-	-	(39)	-	-	-	-	(39)
Share-based compensation	2,204	-	-	3,168	-	-	-	3,168
Non-controlling interests	-	-	-	-	-	-	(9,897)	(9,897)
Balance at September 30, 2013	42,091,180	$ -	$ 784,473	$ 73,735	$ (191,014)	$ (13,718)	$ 60	$ 653,536

See accompanying notes to consolidated financial statements.

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

	Nine Months Ended September 30, 2014	Nine Months Ended September 30, 2013
	(Dollars in thousands)	
Cash flows from operating activities:		
Net income	$ 27,188	$ 161,780
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision (credit) for loan and lease losses	(1,043)	(9,977)
Depreciation and amortization	4,372	4,528
Write down of other real estate, net of gain on sale	529	(7,989)
Amortization of other intangible assets	3,886	5,994
Net amortization of investment securities	6,111	10,766
Share-based compensation	2,100	3,168
Net gain on investment securities	(240)	-
Net gain on sales of residential loans	(4,151)	(8,492)
Proceeds from sales of loans held for sale	279,641	545,199
Originations of loans held for sale	(268,472)	(510,861)
Equity in earnings of unconsolidated subsidiaries	(422)	(733)
Increase in cash surrender value of bank-owned life insurance	(2,402)	(1,492)
Deferred income taxes	14,701	(115,683)
Premium paid on repurchases of preferred stock of subsidiaries	-	1,895
Net change in other assets and liabilities	702	(8,425)
Net cash provided by operating activities	62,500	69,678
Cash flows from investing activities:		
Proceeds from maturities of and calls on investment securities available for sale	104,784	387,409
Proceeds from sales of investment securities available for sale	162,470	-
	(18,993)	(501,502)

Purchases of investment securities available for sale				
Proceeds from maturities of and calls on investment securities held to maturity		12,046		9,980
Purchases of investment securities held to maturity		(2,443)		(4,595)
Net loan originations		(183,197)		(258,612)
Purchase of loan portfolio		(62,648)		(37,104)
Proceeds from sales of loans originated for investment		-		10,679
Proceeds from sale of other real estate		2,790		16,375
Proceeds from bank-owned life insurance		481		-
Purchases of premises and equipment		(4,425)		(3,920)
Distributions from unconsolidated subsidiaries		470		553
Contributions to unconsolidated subsidiaries		466		(9,050)
Proceeds from redemption of FHLB stock		1,736		1,302
Net cash provided by (used in) investing activities		13,537		(388,485)
Cash flows from financing activities:				
Net increase in deposits		111,923		225,492
Repayments of long-term debt		(14)		(13)
Net increase (decrease) in short-term borrowings		(8,015)		28,000
Cash dividends paid on common stock		(9,841)		(3,367)
Repurchases of common stock and other related costs		(129,391)		-
Repurchases of preferred stock of subsidiaries		-		(11,781)
Net proceeds from issuance of common stock and stock option exercises		74		-
Net cash provided by (used in) financing activities		(35,264)		238,331
Net increase (decrease) in cash and cash equivalents		40,773		(80,476)
Cash and cash equivalents at beginning of period		49,348		177,375
Cash and cash equivalents at end of period	$	90,121	$	96,899

Supplemental disclosure of cash flow information:				
Cash paid during the period for:				
Interest	$	4,796	$	17,436
Income taxes		-		5
Cash received during the period for:				
Income taxes		79		-
Supplemental disclosure of noncash investing and financing activities:				
Net change in common stock held by directors' deferred compensation plan	$	11	$	39
Net reclassification of loans to other real estate		1,752		3,461
Net transfer of investment securities available for sale to held to maturity		-		101,669

See accompanying notes to consolidated financial statements.

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

1. 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, 2013. 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.

Certain prior period amounts in the consolidated financial statements and the notes thereto have been reclassified to conform to the current period presentation. Such reclassifications had no effect on net income or shareholders' equity for any periods presented.

2. REGULATORY MATTERS

On October 9, 2012, the bank entered into a Memorandum of Understanding (the "Compliance MOU") with the Federal Deposit Insurance Corporation (the "FDIC") to improve the bank's compliance management system ("CMS"). Under the Compliance MOU, we are required to, among other things, (i) improve the Board of Directors' oversight of the bank's CMS; (ii) ensure the establishment and implementation of the bank's CMS is commensurate with the complexity of the bank's operations; (iii) perform a full review of all compliance policy and procedures, then revise and adopt policy and procedures to ensure compliance with all consumer protection regulations; (iv) enhance the bank's training program relating to consumer protection and fair lending regulations; (v) develop and implement an effective internal monitoring program to ensure compliance with all applicable laws and regulations; (vi) strengthen the compliance audit function to ensure that the compliance audits are appropriately and comprehensively scoped; (vii) develop and implement internal controls for the bank's third-party payment processing activity; (viii) strengthen the Board of Directors and senior management's oversight of third-party relationships and (ix) enhance the bank's overdraft payment program. The bank believes it has fully complied with all of the requirements of the Compliance MOU. In addition, the bank received an "Outstanding" rating in the FDIC's 2012 Community Reinvestment performance evaluation that measures how financial institutions support their communities in the areas of lending, investment and service.

We cannot assure you whether or when the Company and the bank will be in full compliance with the Compliance MOU or whether or when the Compliance MOU will be terminated. Even if terminated, we may still be subject to other agreements with regulators which restrict our activities or may impose higher capital ratios or other requirements on our business. The requirements and restrictions of the Compliance MOU are judicially enforceable and the Company or the bank's failure to comply with such requirements and restrictions may subject the Company and the bank to additional regulatory restrictions including: the imposition of additional regulatory requirements or orders; limitations on our activities; the imposition of civil monetary penalties; and further directives which affect our business, including, in the most severe circumstances, termination of the bank's deposit insurance or appointment of a conservator or receiver for the bank.

3. RECENT ACCOUNTING PRONOUNCEMENTS

In July 2013, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) 2013-11, "Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists." The provisions of ASU 2013-11 provide guidance for financial statement presentation of an unrecognized tax benefit when a net operating loss carryforward, a similar loss or a tax credit carryforward exists. The Company has reflected the adoption of this guidance prospectively on January 1, 2014, the effective date of ASU 2013-11. The adoption of this guidance did not have a material impact on our consolidated financial statements.

4. INVESTMENT SECURITIES

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

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
		(Dollars in thousands)		
At September 30, 2014:				
Held to Maturity:				
Mortgage-backed securities - U.S. Government sponsored entities	$ 242,141	$ 63	$ (6,275)	$ 235,929
Available for Sale:				
Debt securities:				
States and political subdivisions	$ 191,553	$ 1,844	$ (3,238)	$ 190,159
Corporate securities	84,331	1,427	(206)	85,552
Mortgage-backed securities:				
U.S. Government sponsored entities	737,504	8,780	(5,745)	740,539
Non-agency collateralized mortgage obligations	165,518	3,320	(1,377)	167,461
Other	743	110	-	853
Total	$ 1,179,649	$ 15,481	$ (10,566)	$ 1,184,564
At December 31, 2013:				
Held to Maturity:				
Mortgage-backed securities - U.S. Government sponsored entities	$ 252,047	$ -	$ (13,342)	$ 238,705
Available for Sale:				
Debt securities:				
States and political subdivisions	$ 191,158	$ 305	$ (12,106)	$ 179,357
Corporate securities	157,337	1,878	(1,120)	158,095
Mortgage-backed securities:				
U.S. Government sponsored entities	936,144	7,085	(15,603)	927,626
Non-agency collateralized mortgage obligations	147,902	81	(5,937)	142,046
Other	755	120	-	875
Total	$ 1,433,296	$ 9,469	$ (34,766)	$ 1,407,999

The amortized cost and estimated fair value of investment securities at September 30, 2014 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.

	September 30, 2014	
	Amortized Cost	Estimated Fair Value
	(Dollars in thousands)	
Held to Maturity		
Mortage-backed securities	$ 242,141	$ 235,929

Available for Sale				
Due in one year or less	$	3,471	$	3,471
Due after one year through five years		53,494		54,842
Due after five years through ten years		99,948		99,847
Due after ten years		118,971		117,551
Mortage-backed securities		903,022		908,000
Other		743		853
Total	$	1,179,649	$	1,184,564

We sold certain available for sale investment securities during the second quarter of 2014 for gross proceeds of $162.5 million. Gross realized gains and losses on the sales of the available for sale investment securities were $0.9 million and $0.7 million, respectively. The specific identification method was used as the bases for determining the cost of all securities sold. We did not sell any available for sale securities during the first and third quarters of 2014 and the first nine months of 2013.

Investment securities of $894.1 million and $914.1 million at September 30, 2014 and December 31, 2013, respectively, were pledged to secure public funds on deposit and other long-term and short-term borrowings. None of these securities were pledged to a secured party that has the right to sell or repledge the collateral as of the same periods.

Provided below is a summary of the 218 and 321 investment securities which were in an unrealized loss position at September 30, 2014 and December 31, 2013, respectively.

	Less than 12 months		12 months or longer		Total	
Description of Securities	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
			(Dollars in thousands)			
At September 30, 2014:						
Debt securities:						
States and political subdivisions	$ 16,780	$ (192)	$ 85,566	$ (3,046)	$ 102,346	$ (3,238)
Corporate securities	12,732	(75)	8,354	(131)	21,086	(206)
Mortgage-backed securities:						
U.S. Government sponsored entities	100,487	(577)	461,952	(11,443)	562,439	(12,020)
Non-agency collateralized mortgage obligations	14,800	(52)	47,194	(1,325)	61,994	(1,377)
Total temporarily impaired securities	$ 144,799	$ (896)	$ 603,066	$ (15,945)	$ 747,865	$ (16,841)
At December 31, 2013:						
Debt securities:						
States and political subdivisions	$ 137,176	$ (8,985)	$ 32,747	$ (3,121)	$ 169,923	$ (12,106)
Corporate securities	75,368	(1,120)	-	-	75,368	(1,120)
Mortgage-backed securities:						
U.S. Government sponsored entities	909,585	(28,386)	4,848	(559)	914,433	(28,945)
Non-agency collateralized mortgage obligations	129,991	(5,937)	-	-	129,991	(5,937)
Total temporarily impaired securities	$ 1,252,120	$ (44,428)	$ 37,595	$ (3,680)	$ 1,289,715	$ (48,108)

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 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 anticipated credit losses.

The declines in market value were primarily attributable to changes in interest rates. 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 these investments to be other-than-temporarily impaired.

5. LOANS AND LEASES

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

	September 30, 2014	December 31, 2013
	(Dollars in thousands)	
Commercial, financial and agricultural	$ 441,697	$ 398,365
Real estate:		
Construction	109,617	75,927
Mortgage - residential	1,249,717	1,135,155
Mortgage - commercial	697,448	703,800
Consumer	371,693	311,670
Leases	3,691	6,241
	2,873,863	2,631,158
Net deferred costs (income)	892	(557)
Total loans and leases	$ 2,874,755	$ 2,630,601

During the nine months ended September 30, 2014, we foreclosed on four loans with a carrying value of $1.8 million. We did not transfer any portfolio loans to the held-for-sale category and no portfolio loans were sold during the nine months ended September 30, 2014. In May 2014, we purchased participation interests in auto loans totaling $11.2 million, which included a $0.3 million premium over the $10.9 million outstanding balance. At the time of purchase, the auto loans had a weighted average remaining term of 71 months. During the nine months ended September 30, 2014, we also purchased participation interests in student loans totaling $51.5 million, which represented the outstanding balance at the time of purchase. At the time of purchase, the student loans had a weighted average remaining term of 123 months.

During the nine months ended September 30, 2013, we foreclosed on nine loans with a carrying value of $3.5 million. We did not transfer any portfolio loans to the held-for-sale category and no portfolio loans were sold during the nine months ended September 30, 2013. In June 2013, we purchased an auto loan portfolio for $21.6 million, which included a $0.8 million premium over the $20.8 million outstanding balance. At the time of purchase, the auto loan portfolio had a weighted average remaining term of 76 months. During the nine months ended September 30, 2013, we also purchased participation interests in student loans totaling $15.5 million, which represented the outstanding balance at the time of purchase. At the time of purchases, the student loans had a weighted average remaining term of 122 months.

Impaired Loans

The following table presents by class, the balance in the allowance for loan and lease losses and the recorded investment in loans and leases based on the Company's impairment measurement method as of September 30, 2014 and December 31, 2013:

	Commercial, Financial & Agricultural	Construction	Real Estate Mortgage - Residential	Real Estate Mortgage - Commercial	Consumer	Leases	Total
	(Dollars in thousands)						
September 30, 2014							
Allowance for loan and lease losses:							
Ending balance attributable to loans:							
Individually evaluated for impairment	$ 2,778	$ -	$ -	$ -	$ -	$ -	$ 2,778
Collectively evaluated for impairment	9,086	14,897	19,269	24,527	8,269	12	76,060
	11,864	14,897	19,269	24,527	8,269	12	78,838
Unallocated							4,000
Total ending balance	$ 11,864	$ 14,897	$ 19,269	$ 24,527	$ 8,269	$ 12	$ 82,838
Loans and leases:							
Individually evaluated for impairment	$ 15,998	$ 5,017	$ 30,671	$ 23,727	$ -	$ -	$ 75,413
Collectively evaluated for impairment	425,699	104,600	1,219,046	673,721	371,693	3,691	2,798,450
	441,697	109,617	1,249,717	697,448	371,693	3,691	2,873,863
Net deferred costs (income)	634	(377)	2,091	(874)	(582)	-	892
Total ending balance	$ 442,331	$ 109,240	$ 1,251,808	$ 696,574	$ 371,111	$ 3,691	$ 2,874,755
December 31, 2013							
Allowance for loan and lease losses:							
Ending balance attributable to loans:							
Individually evaluated for impairment	$ 349	$ -	$ -	$ -	$ -	$ -	$ 349
Collectively evaluated for	12,847	2,774	25,272	29,947	6,576	55	77,471

impairment							
	13,196	2,774	25,272	29,947	6,576	55	77,820
Unallocated							6,000
Total ending balance	$ 13,196	$ 2,774	$ 25,272	$ 29,947	$ 6,576	$ 55	$ 83,820
Loans and leases:							
Individually evaluated for impairment	$ 3,939	$ 8,065	$ 36,779	$ 16,271	$ -	$ -	$ 65,054
Collectively evaluated for impairment	394,426	67,862	1,098,376	687,529	311,670	6,241	2,566,104
	398,365	75,927	1,135,155	703,800	311,670	6,241	2,631,158
Net deferred costs (income)	351	(311)	1,418	(1,033)	(982)	-	(557)
Total ending balance	$ 398,716	$ 75,616	$ 1,136,573	$ 702,767	$ 310,688	$ 6,241	$ 2,630,601

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The following table presents by class, impaired loans as of September 30, 2014 and December 31, 2013:

	Unpaid Principal Balance	Recorded Investment	Allowance Allocated
		(Dollars in thousands)	
September 30, 2014			
Impaired loans with no related allowance recorded:			
Commercial, financial & agricultural	$ 3,113	$ 3,113	$ -
Real estate:			
Construction	11,404	5,017	-
Mortgage - residential	33,909	30,671	-
Mortgage - commercial	30,850	23,727	-
Total impaired loans with no related allowance recorded	79,276	62,528	-
Impaired loans with an allowance recorded:			
Commercial, financial & agricultural	14,353	12,885	2,778
Total impaired loans with an allowance recorded	14,353	12,885	2,778
Total	$ 93,629	$ 75,413	$ 2,778
December 31, 2013			
Impaired loans with no related allowance recorded:			
Commercial, financial & agricultural	$ 1,069	$ 1,040	$ -
Real estate:			
Construction	14,451	8,065	-
Mortgage - residential	41,117	36,779	-
Mortgage - commercial	22,353	16,271	-
Total impaired loans with no related allowance recorded	78,990	62,155	-
Impaired loans with an allowance recorded:			
Commercial, financial & agricultural	4,367	2,899	349
Total impaired loans with an allowance recorded	4,367	2,899	349
Total	$ 83,357	$ 65,054	$ 349

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, 2014 and 2013:

	Three Months Ended September 30,				Nine Months Ended September 30,			
	2014		2013		2014		2013	
	Average Recorded Investment	Interest Income Recognized	Average Recorded Investment	Interest Income Recognized	Average Recorded Investment	Interest Income Recognized	Average Recorded Investment	Interest Income Recognized
				(Dollars in thousands)				
Commercial, financial & agricultural	$16,377	$ 6	$4,104	$ 6	$14,031	$ 17	$4,189	$ 18
Real estate:								
Construction	5,088	43	20,812	942	5,712	119	28,149	1,409

Mortgage - residential	31,460	85	36,151	15	33,762	522	38,840	343
Mortgage - commercial	19,195	137	19,513	350	17,147	252	22,355	532
Leases	-	-	-	-	-	-	43	-
Total	$72,120	$ 271	$80,580	$ 1,313	$70,652	$ 910	$93,576	$ 2,302

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 table presents by class, the aging of the recorded investment in past due loans and leases as of September 30, 2014 and December 31, 2013:

	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
				(Dollars in thousands)			
September 30, 2014							
Commercial, financial & agricultural	$ 633	$ 151	$ -	$ 15,625	$ 16,409	$ 425,922	$ 442,331
Real estate:							
Construction	-	-	-	324	324	108,916	109,240
Mortgage - residential	199	1,168	-	12,691	14,058	1,237,750	1,251,808
Mortgage - commercial	-	273	-	13,056	13,329	683,245	696,574
Consumer	1,115	494	62	-	1,671	369,440	371,111
Leases	-	-	-	-	-	3,691	3,691
Total	$ 1,947	$ 2,086	$ 62	$ 41,696	$ 45,791	$ 2,828,964	$ 2,874,755
December 31, 2013							
Commercial, financial & agricultural	$ 50	$ -	$ -	$ 3,533	$ 3,583	$ 395,133	$ 398,716
Real estate:							
Construction	-	120	-	4,015	4,135	71,481	75,616
Mortgage - residential	3,898	1,885	-	20,271	26,054	1,110,519	1,136,573
Mortgage - commercial	544	-	-	13,769	14,313	688,454	702,767
Consumer	577	92	-	-	669	310,019	310,688
Leases	-	-	15	-	15	6,226	6,241
Total	$ 5,069	$ 2,097	$ 15	$ 41,588	$ 48,769	$ 2,581,832	$ 2,630,601

Modifications

Troubled debt restructurings ("TDRs") included in nonperforming assets at September 30, 2014 consisted of 39 Hawaii residential mortgage loans with a combined principal balance of $7.6 million, a Hawaii commercial loan with a principal balance of $0.4 million, and a Hawaii construction and development loan with a principal balance of $0.2 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 $29.9 million of TDRs still accruing interest at September 30, 2014, none of which were more than 90 days delinquent. At December 31, 2013, there were $23.3 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. As a result, some loans 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 to our provision for loan and lease losses expense (the “Provision”) and the Allowance during the three and nine months ended September 30, 2014.

The following table presents by class, information related to loans modified in a TDR during the three and nine months ended September 30, 2014 and 2013.

	Number of Contracts	Recorded Investment (as of Period End)	Increase in the Allowance
		(Dollars in thousands)	
Three Months Ended September 30, 2014			
Real estate mortgage - residential	3	$ 220	$ -
Three Months Ended September 30, 2013			
Real estate:			
Mortgage - residential	1	$ 241	$ -
Mortgage - commercial	1	9,099	-
Total	2	$ 9,340	$ -
Nine Months Ended September 30, 2014			
Real estate mortgage - residential	12	$ 806	$ -
Nine Months Ended September 30, 2013			
Commercial, financial & agricultural	1	$ 564	$ -
Real estate:			
Construction	1	184	-
Mortgage - residential	4	1,860	-
Mortgage - commercial	1	9,099	-
Total	7	$ 11,707	$ -

The following table presents by class, loans modified as a TDR within the previous twelve months that subsequently defaulted during the nine months ended September 30, 2013. No loans were modified as a TDR within the previous twelve months that subsequently defaulted during the three and nine months ended September 30, 2014 and the three months ended September 30, 2013.

	Nine Months Ended September 30, 2013	
	Number of Contracts	Recorded Investment (as of Period End)
	(Dollars in thousands)	
Real estate mortgage - residential	1	$ 354

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 estimate 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, 2014 and December 31, 2013:

	Pass	Special Mention	Substandard	Subtotal	Net Deferred Costs (Income)	Total
			(Dollars in thousands)			
September 30, 2014						
Commercial, financial & agricultural	$ 412,141	$ 10,361	$ 19,195	$ 441,697	$ 634	$ 442,331
Real estate:						
Construction	105,739	-	3,878	109,617	(377)	109,240
Mortgage - residential	1,235,974	437	13,306	1,249,717	2,091	1,251,808
Mortgage - commercial	660,795	4,909	31,744	697,448	(874)	696,574
Consumer	371,381	-	312	371,693	(582)	371,111
Leases	3,691	-	-	3,691	-	3,691
Total	$ 2,789,721	$ 15,707	$ 68,435	$ 2,873,863	$ 892	$ 2,874,755
December 31, 2013						
Commercial, financial & agricultural	$ 371,285	$ 21,511	$ 5,569	$ 398,365	$ 351	$ 398,716
Real estate:						
Construction	67,435	4,477	4,015	75,927	(311)	75,616
Mortgage - residential	1,113,363	361	21,431	1,135,155	1,418	1,136,573
Mortgage - commercial	651,761	20,690	31,349	703,800	(1,033)	702,767
Consumer	311,670	-	-	311,670	(982)	310,688
Leases	6,241	-	-	6,241	-	6,241
Total	$ 2,521,755	$ 47,039	$ 62,364	$ 2,631,158	$ (557)	$ 2,630,601

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, 2014 and December 31, 2013, we did not have any loans that we considered to be subprime.

6. ALLOWANCE FOR LOAN AND LEASE LOSSES

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

	Commercial, Financial & Agricultural	Construction	Real estate Mortgage - Residential	Mortgage - Commercial	Consumer	Leases	Unallocated	Total
	(Dollars in thousands)							
Three Months Ended September 30, 2014								
Beginning balance	$ 12,255	$ 15,525	$ 19,198	$ 25,885	$ 6,723	$ 13	$ 4,000	$ 83,599
Provision (credit) for loan and lease losses	(760)	(1,728)	(173)	(1,372)	2,313	(2)	-	(1,722)
	11,495	13,797	19,025	24,513	9,036	11	4,000	81,877
Charge-offs	408	-	-	-	991	-	-	1,399
Recoveries	777	1,100	244	14	224	1	-	2,360
Net charge-offs (recoveries)	(369)	(1,100)	(244)	(14)	767	(1)	-	(961)
Ending balance	$ 11,864	$ 14,897	$ 19,269	$ 24,527	$ 8,269	$ 12	$ 4,000	$ 82,838
Three Months Ended September 30, 2013								
Beginning balance	$ 9,653	$ 6,460	$ 23,323	$ 37,751	$ 3,848	$ 70	$ 6,000	$ 87,105
Provision (credit) for loan and lease losses	3,385	(2,505)	1,236	(6,581)	1,292	(16)	-	(3,189)
	13,038	3,955	24,559	31,170	5,140	54	6,000	83,916
Charge-offs	360	3	63	-	466	-	-	892
Recoveries	259	569	91	1,137	146	2	-	2,204
Net charge-offs (recoveries)	101	(566)	(28)	(1,137)	320	(2)	-	(1,312)
Ending balance	$ 12,937	$ 4,521	$ 24,587	$ 32,307	$ 4,820	$ 56	$ 6,000	$ 85,228
Nine Months Ended September 30, 2014								
Beginning balance	$ 13,196	$ 2,774	$ 25,272	$ 29,947	$ 6,576	$ 55	$ 6,000	$ 83,820
Provision (credit) for loan and lease losses	(1,298)	10,279	(6,731)	(4,419)	3,167	(41)	(2,000)	(1,043)
	11,898	13,053	18,541	25,528	9,743	14	4,000	82,777

Charge-offs	1,963	-	139	1,041	2,242	8	-	5,393
Recoveries	1,929	1,844	867	40	768	6	-	5,454
Net charge-offs (recoveries)	34	(1,844)	(728)	1,001	1,474	2	-	(61)
Ending balance	$ 11,864	$ 14,897	$ 19,269	$ 24,527	$ 8,269	$ 12	$ 4,000	$ 82,838
Nine Months Ended September 30, 2013								
Beginning balance	$ 4,987	$ 4,510	$ 27,836	$ 50,574	$ 2,421	$ 85	$ 6,000	$ 96,413
Provision (credit) for loan and lease losses	9,230	(2,432)	(2,957)	(16,687)	2,903	(34)	-	(9,977)
	14,217	2,078	24,879	33,887	5,324	51	6,000	86,436
Charge-offs	2,201	358	857	3,674	1,023	-	-	8,113
Recoveries	921	2,801	565	2,094	519	5	-	6,905
Net charge-offs (recoveries)	1,280	(2,443)	292	1,580	504	(5)	-	1,208
Ending balance	$ 12,937	$ 4,521	$ 24,587	$ 32,307	$ 4,820	$ 56	$ 6,000	$ 85,228

In accordance with GAAP, loans held for sale and other real estate assets are not included in our assessment of the Allowance.

Our Provision was credits of $1.7 million and $1.0 million in the third quarter and first nine months of 2014, respectively, compared to credits of $3.2 million and $10.0 million in the third quarter and first nine months of 2013, respectively.

In determining the amount of our Allowance, we rely on an analysis of our loan portfolio, our experience and our evaluation of general economic conditions, as well as regulatory requirements and input. If our assumptions prove to be incorrect, our current Allowance may not be sufficient to cover future loan losses and we may experience significant increases to our Provision.

7. SECURITIZATIONS

In prior years, we securitized certain residential mortgage loans with a U.S. Government sponsored entity and continue to service the residential mortgage loans. The servicing assets were recorded at their respective fair values at the time of securitization.

All unsold mortgage-backed securities from prior securitizations were categorized as available for sale securities and were therefore recorded at their fair value of $3.8 million at September 30, 2014 and December 31, 2013. The fair values of these mortgage-backed securities were based on quoted prices of similar instruments in active markets. Unrealized gains of $0.2 million on unsold mortgage-backed securities were recorded in accumulated other comprehensive income ("AOCI") at September 30, 2014 and December 31, 2013.

8. OTHER INTANGIBLE ASSETS

Other intangible assets include a core deposit premium and mortgage servicing rights. The following table presents changes in other intangible assets for the nine months ended September 30, 2014:

	Core Deposit Premium	Mortgage Servicing Rights	Total
		(Dollars in thousands)	
Balance, beginning of period	$ 12,704	$ 20,079	$ 32,783
Additions	-	1,601	1,601
Amortization	(2,006)	(1,880)	(3,886)
Balance, end of period	$ 10,698	$ 19,800	$ 30,498

Income generated as the result of new mortgage servicing rights is reported as gains on sales of loans and totaled $0.7 million and $1.6 million for the three and nine months ended September 30, 2014, respectively, compared to $0.5 million and $2.1 million for the three and nine months ended September 30, 2013, respectively. Amortization of mortgage servicing rights was $0.7 million and $1.9 million for the three and nine months ended September 30, 2014, respectively, compared to $1.0 million and $4.0 million for the three and nine months ended September 30, 2013, respectively.

The following table presents the fair market value and key assumptions used in determining the fair market value of our mortgage servicing rights:

	Nine Months Ended September 30,	
	2014	2013
	(Dollars in thousands)	
Fair market value, beginning of period	$ 21,399	$ 22,356
Fair market value, end of period	20,471	20,763
Weighted average discount rate	9.5 %	8.0 %
Weighted average prepayment speed assumption	12.9	14.2

The gross carrying value and accumulated amortization related to our intangible assets are presented below:

	September 30, 2014			December 31, 2013		
	Gross Carrying Value	Accumulated Amortization	Net	Gross Carrying Value	Accumulated Amortization	Net
	(Dollars in thousands)					
Core deposit premium	$ 44,642	$ (33,944)	$ 10,698	$ 44,642	$ (31,938)	$ 12,704
Mortgage servicing rights	56,042	(36,242)	19,800	54,441	(34,362)	20,079
	$ 100,684	$ (70,186)	$ 30,498	$ 99,083	$ (66,300)	$ 32,783

Based on the core deposit premium and mortgage servicing rights held as of September 30, 2014, estimated amortization expense for the remainder of fiscal 2014, the next five succeeding fiscal years and all years thereafter are as follows:

	Estimated Amortization Expense		
	Core Deposit Premium	Mortgage Servicing Rights	Total
	(Dollars in thousands)		
2014 (remainder)	$ 669	$ 1,021	$ 1,690
2015	2,674	2,205	4,879
2016	2,674	1,691	4,365
2017	2,674	1,344	4,018
2018	2,007	1,067	3,074
2019	-	843	843
Thereafter	-	11,629	11,629
	$ 10,698	$ 19,800	$ 30,498

We perform an impairment assessment of our other intangible assets whenever events or changes in circumstance indicate that the carrying value of those assets may not be recoverable. Our impairment assessments involve, among other valuation methods, the estimation of future cash flows and other methods of determining fair value. Estimating future cash flows and determining fair values is subject to judgment and often involves the use of significant estimates and assumptions. The variability of the factors we use to perform our impairment tests depend on a number of conditions, including the uncertainty about future events and cash flows. All such factors are interdependent and, therefore, do not change in isolation. Accordingly, our accounting estimates may materially change from period to period due to changing market factors.

9. DERIVATIVES

We utilize various designated and undesignated derivative financial instruments to reduce our exposure to movements in interest rates including interest rate swaps, interest rate lock commitments and forward sale commitments. We measure all derivatives at fair value on our consolidated balance sheet. In each reporting period, we record the derivative instruments in other assets or other liabilities depending on whether the derivatives are in an asset or liability position. For derivative instruments that are designated as hedging instruments, we record the effective portion of the changes in the fair value of the derivative in AOCI, net of tax, until earnings are affected by the variability of cash flows of the hedged transaction. We immediately recognize the portion of the gain or loss in the fair value of the derivative that represents hedge ineffectiveness in current period earnings. For derivative instruments that are not designated as hedging instruments, changes in the fair value of the derivative are included in current period earnings.

Interest Rate Lock and Forward Sale Commitments

We enter into interest rate lock commitments on certain mortgage loans that are intended to be sold. To manage interest rate risk on interest rate lock commitments, we also enter into forward loan sale commitments. The interest rate locks and forward loan sale commitments are accounted for as undesignated derivatives and are recorded at their respective fair values in other assets or other liabilities, with changes in fair value recorded in current period earnings. These instruments serve to reduce our exposure to movements in interest rates. At September 30, 2014, we were a party to interest rate lock and forward sale commitments on $44.7 million and $21.4 million of mortgage loans, respectively.

The following table presents the location of all assets and liabilities associated with our derivative instruments within the consolidated balance sheet:

		Asset Derivatives		Liability Derivatives	
Derivatives Not Designated as Hedging Instruments	Balance Sheet Location	Fair Value at September 30, 2014	Fair Value at December 31, 2013	Fair Value at September 30, 2014	Fair Value at December 31, 2013
		(Dollars in thousands)			
Interest rate contracts	Other assets / other liabilities	$ 583	$ 425	$ 76	$ 146

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The following table presents the impact of derivative instruments and their location within the consolidated statements of income:

Derivatives in Cash Flow Hedging Relationship	Amount of Loss Reclassified from AOCI into Earnings (Effective Portion) (Dollars in thousands)
Three Months Ended September 30, 2014	
Interest rate contracts	$ -
Three Months Ended September 30, 2013	
Interest rate contracts	-
Nine Months Ended September 30, 2014	
Interest rate contracts	-
Nine Months Ended September 30, 2013	
Interest rate contracts	(394)

Amounts recognized in AOCI are net of income taxes. Amounts reclassified from AOCI into income are included in interest income in the consolidated statements of income. The ineffective portion has been recognized as other operating income in the consolidated statements of income.

Derivatives Not in Cash Flow Hedging Relationship	Location of Gain Recognized in Earnings on Derivatives	Amount of Gain Recognized in Earnings on Derivatives