FIRST COMMONWEALTH FINANCIAL CORP /PA/
Form 10-Q
August 09, 2016

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-Q

x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended June 30, 2016
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 001-11138
First Commonwealth Financial Corporation
(Exact name of registrant as specified in its charter)

Pennsylvania	25-1428528
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

601 Philadelphia Street, Indiana, PA	15701
(Address of principal executive offices)	(Zip Code)

724-349-7220
(Registrant’s telephone number, including area code)
N/A
(Former name, former address and former fiscal year, if changed since last report)
Indicate by a 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 x 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 x No ¨
Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of “large accelerated filer,” “accelerated filer” and “smaller reporting company” in Rule 12b-2 of the Exchange Act.
Large accelerated filer x Accelerated filer ¨ Smaller reporting company ¨ Non-accelerated filer ¨
(Do not check if a 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 x
The number of shares outstanding of issuer’s common stock, $1.00 par value, as of August 8, 2016, was 88,949,995.

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FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION (Unaudited)

	June 30, 2016	December 31, 2015
	(dollars in thousands, except share data)	
Assets		
Cash and due from banks	$68,163	$66,644
Interest-bearing bank deposits	30,457	2,808
Securities available for sale, at fair value	855,333	886,560
Securities held to maturity, at amortized cost (Fair value of $414,770 and $382,341 at June 30, 2016 and December 31, 2015, respectively)	405,976	384,324
Other investments	58,087	62,952
Loans held for sale	11,613	5,763
Loans:		
Portfolio loans	4,843,776	4,683,750
Allowance for credit losses	(59,821)	(50,812)
Net loans	4,783,955	4,632,938
Premises and equipment, net	63,921	63,454
Other real estate owned	8,604	9,398
Goodwill	164,500	164,500
Amortizing intangibles, net	981	1,231
Bank owned life insurance	184,684	182,601
Other assets	113,547	103,717
Total assets	$6,749,821	$6,566,890
Liabilities		
Deposits (all domestic):		
Noninterest-bearing	$1,136,629	$1,116,689
Interest-bearing	3,257,891	3,079,205
Total deposits	4,394,520	4,195,894
Short-term borrowings	1,464,687	1,510,825
Subordinated debentures	72,167	72,167
Other long-term debt	9,034	9,314
Total long-term debt	81,201	81,481
Other liabilities	67,627	59,144
Total liabilities	6,008,035	5,847,344
Shareholders’ Equity		
Preferred stock, $1 par value per share, 3,000,000 shares authorized, none issued	—	—
Common stock, $1 par value per share, 200,000,000 shares authorized; 105,563,455 shares issued at June 30, 2016 and December 31, 2015, and 88,949,995 and 88,961,268 shares outstanding at June 30, 2016 and December 31, 2015, respectively	105,563	105,563
Additional paid-in capital	366,181	365,981
Retained earnings	390,110	378,081
Accumulated other comprehensive income (loss), net	7,947	(2,386)

Treasury stock (16,613,460 and 16,602,187 shares at June 30, 2016 and December 31, 2015, respectively)	(128,015)	(127,693)
Total shareholders’ equity	741,786	719,546
Total liabilities and shareholders’ equity	$6,749,821	$6,566,890

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.
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ITEM 1. Financial Statements and Supplementary Data (Continued)
FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF INCOME (Unaudited)

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2016	2015	2016	2015
	(dollars in thousands, except share data)			
Interest Income				
Interest and fees on loans	$45,698	$ 42,650	$90,732	$ 85,251
Interest and dividends on investments:				
Taxable interest	7,028	6,735	14,174	13,552
Interest exempt from federal income taxes	371	210	732	385
Dividends	748	553	1,554	2,042
Interest on bank deposits	5	2	11	5
Total interest income	53,850	50,150	107,203	101,235
Interest Expense				
Interest on deposits	1,928	1,880	3,517	4,030
Interest on short-term borrowings	2,100	1,116	4,335	2,074
Interest on subordinated debentures	644	579	1,278	1,148
Interest on other long-term debt	87	205	175	441
Total interest expense	4,759	3,780	9,305	7,693
Net Interest Income	49,091	46,370	97,898	93,542
Provision for credit losses	10,372	3,038	16,898	4,197
Net Interest Income after Provision for Credit Losses	38,719	43,332	81,000	89,345
Noninterest Income				
Net securities gains	28	20	28	125
Trust income	1,320	1,476	2,575	2,897
Service charges on deposit accounts	3,845	3,872	7,553	7,190
Insurance and retail brokerage commissions	1,985	2,178	3,944	4,373
Income from bank owned life insurance	1,311	1,378	2,607	2,732
Gain on sale of mortgage loans	932	585	1,615	1,024
Gain on sale of other loans and assets	466	396	661	620
Card-related interchange income	3,784	3,729	7,341	7,147
Derivatives mark to market	(531)	593	(1,545)	363
Swap fee income	800	283	1,260	643
Other income	1,618	1,837	3,234	3,424
Total noninterest income	15,558	16,347	29,273	30,538
Noninterest Expense				
Salaries and employee benefits	19,888	22,001	41,565	43,893
Net occupancy expense	3,186	3,316	6,667	7,227
Furniture and equipment expense	2,882	2,630	5,749	5,310
Data processing expense	1,788	1,509	3,547	2,947
Pennsylvania shares tax expense	1,092	1,110	1,850	1,904
Intangible amortization	114	156	251	312
Collection and repossession expense	474	917	1,043	1,428
Other professional fees and services	913	945	1,704	1,875

FDIC insurance	1,062	1,025	2,100	2,084
Loss on sale or write-down of assets	345	1,635	441	1,897
Litigation and operational losses	635	323	879	1,323
Other operating expenses	5,031	5,067	9,758	10,288
Total noninterest expense	37,410	40,634	75,554	80,488
Income Before Income Taxes	16,867	19,045	34,719	39,395
Income tax provision	4,860	5,598	10,239	11,727
Net Income	$12,007	$ 13,447	$24,480	$ 27,668
Average Shares Outstanding	88,831,758	88,922,392	88,835,923	89,893,662
Average Shares Outstanding Assuming Dilution	88,838,614	88,939,003	88,840,683	89,903,550
Per Share Data:				
Basic Earnings per Share	$0.14	$ 0.15	$0.28	$ 0.31
Diluted Earnings per Share	$0.14	$ 0.15	$0.28	$ 0.31
Cash Dividends Declared per Common Share	$0.07	$ 0.07	$0.14	$ 0.14

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.
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ITEM 1. Financial Statements and Supplementary Data (Continued)
FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (Unaudited)

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2016	2015	2016	2015
	(dollars in thousands)			
Net Income	$12,007	$13,447	$24,480	$27,668
Other comprehensive income (loss), before tax (expense) benefit:				
Unrealized holding gains (losses) on securities arising during the period	3,802	(3,814)	13,872	6,166
Less: reclassification adjustment for gains on securities included in net income	(28)	(20)	(28)	(125)
Unrealized holding gains (losses) on derivatives arising during the period	359	(527)	2,094	668
Less: reclassification adjustment for gains on derivatives included in net income	(26)	(11)	(41)	(6)
Total other comprehensive income (loss), before tax (expense) benefit	4,107	(4,372)	15,897	6,703
Income tax (expense) benefit related to items of other comprehensive income (loss)	(1,438)	1,530	(5,564)	(2,344)
Total other comprehensive income (loss)	2,669	(2,842)	10,333	4,359
Comprehensive Income	$14,676	$10,605	$34,813	$32,027

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.

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ITEM 1. Financial Statements and Supplementary Data (Continued)
FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY (Unaudited)

	Shares Outstanding	Common Stock	Additional Paid-in-Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss), net	Treasury Stock	Total Shareholders' Equity
	(dollars in thousands, except share and per share data)						
Balance at December 31, 2015	88,961,268	$105,563	$365,981	$378,081	$ (2,386)	$(127,693)	$719,546
Net income				24,480			24,480
Other comprehensive income					10,333		10,333
Cash dividends declared ($0.14 per share)				(12,451)			(12,451)
Treasury stock acquired	(97,769)					(902)	(902)
Treasury stock reissued	23,148		39	—		177	216
Restricted stock	63,348	—	161	—		403	564
Balance at June 30, 2016	88,949,995	$105,563	$366,181	$390,110	$ 7,947	$(128,015)	$741,786

	Shares Outstanding	Common Stock	Additional Paid-in-Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss), net	Treasury Stock	Total Shareholders' Equity
	(dollars in thousands, except share and per share data)						
Balance at December 31, 2014	91,723,028	$105,563	$365,615	$353,027	$ (4,499)	$(103,561)	$716,145
Net income				27,668			27,668
Other comprehensive income					4,359		4,359
Cash dividends declared ($0.14 per share)				(12,635)			(12,635)
Treasury stock acquired	(2,918,066)					(25,383)	(25,383)
Treasury stock reissued	20,936		32	—		160	192
Restricted stock	134,370	—	286	—		574	860
Balance at June 30, 2015	88,960,268	$105,563	$365,933	$368,060	$ (140)	$(128,210)	$711,206

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.
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ITEM 1. Financial Statements and Supplementary Data (Continued)
FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited)

	For the Six Months Ended June 30, 2016	2015
Operating Activities	(dollars in thousands)	
Net income	$24,480	$27,668
Adjustment to reconcile net income to net cash provided by operating activities:		
Provision for credit losses	16,898	4,197
Deferred tax expense	1,909	7,102
Depreciation and amortization	3,481	3,802
Net gains on securities and other assets	(372)	(235)
Net amortization of premiums and discounts on securities	2,264	1,151
Income from increase in cash surrender value of bank owned life insurance	(2,607)	(2,732)
(Increase) decrease in interest receivable	(315)	74
Mortgage loans originated for sale	(56,139)	(39,941)
Proceeds from sale of mortgage loans	55,251	36,079
Decrease in interest payable	(84)	(200)
(Decrease) increase in income taxes payable	(2,534)	503
Other-net	(4,758)	(14,817)
Net cash provided by operating activities	37,474	22,651
Investing Activities		
Transactions with securities held to maturity:		
Proceeds from maturities and redemptions	18,601	1,115
Purchases	(40,161)	(131,145)
Transactions with securities available for sale:		
Proceeds from sales	55,744	—
Proceeds from maturities and redemptions	82,527	235,971
Purchases	(94,777)	(10,800)
Purchases of FHLB stock	(20,324)	(29,251)
Proceeds from the redemption of FHLB stock	25,189	20,449
Proceeds from bank owned life insurance	—	294
Proceeds from sale of loans	213	102
Proceeds from sale of other assets	3,621	2,282
Net increase in loans	(173,817)	(48,785)
Purchases of other assets	(204)	—
Purchases of premises and equipment	(4,201)	(2,521)
Net cash (used in) provided by investing activities	(147,589)	37,711
Financing Activities		
Net (decrease) increase in federal funds purchased	(4,000)	15,000
Net (decrease) increase in other short-term borrowings	(42,138)	111,041
Net increase (decrease) in deposits	198,838	(105,404)
Repayments of other long-term debt	(280)	(50,270)
Dividends paid	(12,451)	(12,635)

Proceeds from reissuance of treasury stock	216	192
Purchase of treasury stock	(902)	(25,383)
Net cash provided by (used in) financing activities	139,283	(67,459)
Net increase (decrease) in cash and cash equivalents	29,168	(7,097)
Cash and cash equivalents at January 1	69,452	74,538
Cash and cash equivalents at June 30	$98,620	$67,441

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.

ITEM 1. Financial Statements and Supplementary Data
FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES
NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
Note 1 Basis of Presentation
The accounting and reporting policies of First Commonwealth Financial Corporation and its subsidiaries (“First Commonwealth” or the “Company”) conform with generally accepted accounting principles in the United States of America (“GAAP”). The preparation of financial statements in conformity with GAAP requires management to make estimates, assumptions and judgments that affect the amounts reported in the financial statements and accompanying notes. Actual realized amounts could differ from those estimates. In the opinion of management, the unaudited interim condensed consolidated financial statements include all adjustments (consisting of only normal recurring adjustments) necessary for a fair presentation of First Commonwealth’s financial position, results of operations, comprehensive income, cash flows and changes in shareholders’ equity as of and for the periods presented.
The results of operations for the six months ended June 30, 2016 are not necessarily indicative of the results that may be expected for the full year of 2016. These interim financial statements should be read in conjunction with First Commonwealth’s 2015 Annual Report on Form 10-K.
For purposes of reporting cash flows, cash and cash equivalents include cash on hand, amounts due from banks, federal funds sold and interest-bearing bank deposits. Generally, federal funds are sold for one-day periods.
Note 2 Supplemental Comprehensive Income Disclosures
The following table identifies the related tax effects allocated to each component of other comprehensive income (“OCI”) in the Condensed Consolidated Statements of Comprehensive Income. Reclassification adjustments related to securities available for sale are included in the "Net securities gains" line and reclassification adjustments related to losses on derivatives are included in the "Other operating expenses" line in the Condensed Consolidated Statements of Income.

	For the Six Months Ended June 30,					
	2016			2015		
	Pretax Amount	Tax (Expense) Benefit	Net of Tax Amount	Pretax Amount	Tax (Expense) Benefit	Net of Tax Amount
	(dollars in thousands)					
Unrealized gains on securities:						
Unrealized holding gains on securities arising during the period	$13,872	$(4,855)	$9,017	$6,166	$(2,156)	$4,010
Reclassification adjustment for gains on securities included in net income	(28)	10	(18)	(125)	44	(81)
Total unrealized gains on securities	13,844	(4,845)	8,999	6,041	(2,112)	3,929
Unrealized gains on derivatives:						
Unrealized holding gains on derivatives arising during the period	2,094	(733)	1,361	668	(234)	434
Reclassification adjustment for gains on derivatives included in net income	(41)	14	(27)	(6)	2	(4)
Total unrealized gains on derivatives	2,053	(719)	1,334	662	(232)	430
Total other comprehensive income	$15,897	$(5,564)	$10,333	$6,703	$(2,344)	$4,359

ITEM 1. Financial Statements and Supplementary Data
FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES
NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

	For the Three Months Ended June 30,					
	2016			2015		
	Pretax Amount	Tax (Expense) Benefit	Net of Tax Amount	Pretax Amount	Tax (Expense) Benefit	Net of Tax Amount
	(dollars in thousands)					
Unrealized gains (losses) on securities:						
Unrealized holding gains (losses) on securities arising during the period	$3,802	$(1,331)	$2,471	$(3,814)	$ 1,335	$(2,479)
Reclassification adjustment for gains on securities included in net income	(28)	10	(18)	(20)	7	(13)
Total unrealized gains (losses) on securities	3,774	(1,321)	2,453	(3,834)	1,342	(2,492)
Unrealized gains (losses) on derivatives:						
Unrealized holding gains (losses) on derivatives arising during the period	359	(126)	233	(527)	184	(343)
Reclassification adjustment for gains on derivatives included in net income	(26)	9	(17)	(11)	4	(7)
Total unrealized gains (losses) on derivatives	333	(117)	216	(538)	188	(350)
Total other comprehensive income (loss)	$4,107	$(1,438)	$2,669	$(4,372)	$ 1,530	$(2,842)

The following table details the change in components of OCI for the six months ended June 30:

	2016				2015			
	Securities Available for Sale	Post-Retirement Obligation	Derivatives	Accumulated Other Comprehensive Income	Securities Available for Sale	Post-Retirement Obligation	Derivatives	Accumulated Other Comprehensive Income
	(dollars in thousands)							
Balance at December 31	$(2,956)	$ 10	$ 560	$ (2,386)	$(4,875)	$ 76	$ 300	$ (4,499)
Other comprehensive income before reclassification adjustment	9,017	—	1,361	10,378	4,010	—	434	4,444
Amounts reclassified from accumulated other comprehensive (loss) income	(18)	—	(27)	(45)	(81)	—	(4)	(85)
Net other comprehensive income during the period	8,999	—	1,334	10,333	3,929	—	430	4,359
Balance at June 30	$6,043	$ 10	$ 1,894	$ 7,947	$(946)	$ 76	$ 730	$ (140)

Note 3 Supplemental Cash Flow Disclosures
The following table presents information related to cash paid during the period for interest, as well as detail on non-cash investing and financing activities for the six months ended June 30:

	2016	2015
	(dollars in thousands)	
Cash paid during the period for:		
Interest	$9,583	$7,893
Income taxes	10,500	4,000

Non-cash investing and financing activities:		
Loans transferred to other real estate owned and repossessed assets	2,632	2,315
Loans transferred from held to maturity to held for sale	3,573	3,071
Gross increase in market value adjustment to securities available for sale	13,845	6,036
Gross increase in market value adjustment to derivatives	2,053	662
Investments committed to purchase, not settled	1,946	1,817
Proceeds from death benefit on bank-owned life insurance not received	523	—

ITEM 1. Financial Statements and Supplementary Data
FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES
NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Note 4 Earnings per Share

The following table summarizes the composition of the weighted-average common shares (denominator) used in the basic and diluted earnings per share computations:

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2016	2015	2016	2015
Weighted average common shares issued	105,563,455	105,563,455	105,563,455	105,563,455
Average treasury stock shares	(16,620,341)	(16,445,760)	(16,621,717)	(15,480,232)
Average unearned nonvested shares	(111,356)	(195,303)	(105,815)	(189,561)
Weighted average common shares and common stock equivalents used to calculate basic earnings per share	88,831,758	88,922,392	88,835,923	89,893,662
Additional common stock equivalents (nonvested stock) used to calculate diluted earnings per share	6,856	16,611	4,760	9,888
Weighted average common shares and common stock equivalents used to calculate diluted earnings per share	88,838,614	88,939,003	88,840,683	89,903,550

The following table shows the number of shares and the price per share related to common stock equivalents that were not included in the computation of diluted earnings per share for the six months ended June 30 because to do so would have been antidilutive.

	2016			2015		
		Price Range			Price Range	
	Shares	From	To	Shares	From	To
Restricted Stock	81,887	7.57	9.84	146,933	5.26	9.26

Note 5 Commitments and Contingent Liabilities

Commitments and Letters of Credit

Standby letters of credit and commercial letters of credit are conditional commitments issued by First Commonwealth to guarantee the performance of a customer to a third party. The contract or notional amount of these instruments reflects the maximum amount of future payments that First Commonwealth could be required to pay under the guarantees if there were a total default by the guaranteed parties, without consideration of possible recoveries under recourse provisions or from collateral held or pledged. In addition, many of these commitments are expected to expire without being drawn upon; therefore, the total commitment amounts do not necessarily represent future cash requirements.

The following table identifies the notional amount of those instruments at:

	June 30, 2016	December 31, 2015
	(dollars in thousands)	
Financial instruments whose contract amounts represent credit risk:		
Commitments to extend credit	$1,616,286	$1,643,187
Financial standby letters of credit	19,256	17,843
Performance standby letters of credit	28,067	26,497
Commercial letters of credit	1,615	1,672

The notional amounts outstanding as of June 30, 2016 include amounts issued in 2016 of $13 thousand in financial standby letters of credit, $2.3 million in performance standby letters of credit and $0.2 million commercial letters of credit. A liability of $0.2 million has been recorded as of both June 30, 2016 and December 31, 2015 which represents the estimated fair value of letters of credit issued. The fair value of letters of credit is estimated based on the unrecognized portion of fees received at the time the commitment was issued.

ITEM 1. Financial Statements and Supplementary Data
FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES
NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Unused commitments and letters of credit provide exposure to future credit loss in the event of nonperformance by the borrower or guaranteed parties. Management's evaluation of the credit risk related to these commitments resulted in the recording of a liability of $3.5 million as of June 30, 2016 and $4.4 million as of December 31, 2015. This liability is reflected in "Other liabilities" in the Condensed Consolidated Statements of Financial Condition. The credit risk evaluation incorporated probability of default, loss given default and estimated utilization for the next twelve months for each loan category and the letters of credit.

Legal Proceedings

First Commonwealth and its subsidiaries are subject in the normal course of business to various pending and threatened legal proceedings in which claims for monetary damages are asserted. As of June 30, 2016, management, after consultation with legal counsel, does not anticipate that the aggregate ultimate liability arising out of litigation pending or threatened against First Commonwealth or its subsidiaries will be material to First Commonwealth's consolidated financial position. On at least a quarterly basis, First Commonwealth assesses its liabilities and contingencies in connection with such legal proceedings. For those matters where it is probable that First Commonwealth will incur losses and the amounts of the losses can be reasonably estimated, First Commonwealth records an expense and corresponding liability in its consolidated financial statements. To the extent the pending or threatened litigation could result in exposure in excess of that liability, the amount of such excess is not currently estimable. Although not considered probable, the range of reasonably possible losses for such matters in the aggregate, beyond the existing recorded liability (if any), is between $0 and $7 million. Although First Commonwealth does not believe that the outcome of pending litigation will be material to First Commonwealth's consolidated financial position, it cannot rule out the possibility that such outcomes will be material to the consolidated results of operations and cash flows for a particular reporting period in the future.

First Commonwealth Financial Corporation and First Commonwealth Bank were named defendants in an action commenced August 27, 2015 by eight named plaintiffs that is pending in the Court of Common Pleas of Jefferson County, Pennsylvania. The plaintiffs allege that the Bank repossessed motor vehicles, sold the vehicles and sought to collect deficiency balances in a manner that did not comply with the notice requirements of the Pennsylvania Uniform Commercial Code (UCC), charged inappropriate costs and fees, including storage costs for dates that a repossessed vehicle was not in storage, and wrongly filed forms with the Department of Motor Vehicles asserting that the Bank had complied with applicable laws relating to the repossession of the vehicles. The plaintiffs seek to pursue the action as a class action on behalf of the named plaintiffs and other similarly situated plaintiffs who had their automobiles repossessed and seek to recover damages under the UCC and the Pennsylvania Fair Credit Extension Uniformity Act. First Commonwealth and the Bank contest the plaintiffs' allegations and intend to oppose class certification. The Bank has also asserted counterclaims for breach of contract, set-off and recoupment against the plaintiffs, individually, and as representatives of the putative class. The Bank and counsel for the plaintiffs reached an agreement-in-principle to settle the litigation during the second quarter. The parties are negotiating the terms of a definitive settlement agreement which would be subject to court approval and other customary conditions. The estimated cost of the settlement to the Bank was recorded as a liability as of June 30, 2016. As set forth in the preceding paragraph, all current litigation matters, including this action, are believed to be within the range of reasonably possible losses set forth in the preceding paragraph.

ITEM 1. Financial Statements and Supplementary Data
FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES
NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Note 6 Investment Securities
Securities Available for Sale
Below is an analysis of the amortized cost and estimated fair values of securities available for sale at:

	June 30, 2016				December 31, 2015			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
	(dollars in thousands)							
Obligations of U.S. Government Agencies:								
Mortgage-Backed Securities – Residential	$16,730	$2,032	$—	$18,762	$20,034	$2,071	$(13)	$22,092
Obligations of U.S. Government-Sponsored Enterprises:								
Mortgage-Backed Securities – Residential	732,618	15,012	(234)	747,396	778,476	7,983	(8,882)	777,577
Mortgage-Backed Securities – Commercial	2	—	—	2	28	—	—	28
Other Government-Sponsored Enterprises	19,300	22	—	19,322	19,201	2	(85)	19,118
Obligations of States and Political Subdivisions	27,071	965	—	28,036	27,066	532	—	27,598
Corporate Securities	5,898	524	—	6,422	1,897	422	—	2,319
Pooled Trust Preferred Collateralized Debt Obligations	42,750	500	(9,527)	33,723	42,239	916	(7,497)	35,658
Total Debt Securities	844,369	19,055	(9,761)	853,663	888,941	11,926	(16,477)	884,390
Equities	1,670	—	—	1,670	2,170	—	—	2,170
Total Securities Available for Sale	$846,039	$19,055	$(9,761)	$855,333	$891,111	$11,926	$(16,477)	$886,560

Mortgage backed securities include mortgage backed obligations of U.S. Government agencies and obligations of U.S. Government-sponsored enterprises. These obligations have contractual maturities ranging from less than one year to approximately 30 years with lower anticipated lives to maturity due to prepayments. All mortgage backed securities contain a certain amount of risk related to the uncertainty of prepayments of the underlying mortgages. Interest rate changes have a direct impact upon prepayment speeds; therefore, First Commonwealth uses computer simulation models to test the average life and yield volatility of all mortgage backed securities under various interest rate scenarios to monitor the potential impact on earnings and interest rate risk positions.

Expected maturities will differ from contractual maturities because issuers may have the right to call or repay obligations with or without call or prepayment penalties. Other fixed income securities within the portfolio also contain prepayment risk.

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The amortized cost and estimated fair value of debt securities available for sale at June 30, 2016, by contractual maturity, are shown below.

	Amortized Cost	Estimated Fair Value
	(dollars in thousands)	
Due within 1 year	$2,601	$2,602
Due after 1 but within 5 years	20,696	20,780
Due after 5 but within 10 years	27,070	28,036
Due after 10 years	44,652	36,085
	95,019	87,503
Mortgage-Backed Securities (a)	749,350	766,160
Total Debt Securities	$844,369	$853,663

(a) Mortgage Backed Securities include an amortized cost of $16.7 million and a fair value of $18.8 million for Obligations of U.S. Government agencies issued by Ginnie Mae and an amortized cost of $732.6 million and a fair value of $747.4 million for Obligations of U.S. Government-sponsored enterprises issued by Fannie Mae and Freddie Mac.

Proceeds from sales, gross gains (losses) realized on sales, maturities and other-than-temporary impairment charges related to securities available for sale were as follows for the six months ended June 30:

	2016	2015
	(dollars in thousands)	
Proceeds from sales	$ 55,744	$ —
Gross gains (losses) realized:		
Sales Transactions:		
Gross gains	$ 304	$ —
Gross losses	(276)	—
	28	—
Maturities and impairment		
Gross gains	—	105
Gross losses	—	—
Other-than-temporary impairment	—	—
	—	105
Net gains and impairment	$ 28	$ 105

Securities available for sale with an estimated fair value of $475.9 million and $416.1 million were pledged as of June 30, 2016 and December 31, 2015, respectively, to secure public deposits and for other purposes required or permitted by law.

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Securities Held to Maturity

Below is an analysis of the amortized cost and fair values of debt securities held to maturity at:

	June 30, 2016				December 31, 2015			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
	(dollars in thousands)							
Obligations of U.S. Government Agencies:								
Mortgage-Backed Securities – Residential	$4,712	$ 146	$ —	$4,858	$4,775	$ —	$ (7)	$4,768
Mortgage-Backed Securities- Commercial	36,529	403	—	36,932	16,843	—	(247)	16,596
Obligations of U.S. Government-Sponsored Enterprises:								
Mortgage-Backed Securities – Residential	313,987	6,746	—	320,733	315,609	30	(1,824)	313,815
Mortgage-Backed Securities – Commercial	14,940	460	—	15,400	15,187	—	(178)	15,009
Obligations of States and Political Subdivisions	35,808	1,039	—	36,847	31,910	301	(58)	32,153
Total Securities Held to Maturity	$405,976	$ 8,794	$ —	$414,770	$384,324	$ 331	$ (2,314)	$382,341

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

	Amortized Cost	Estimated Fair Value
	(dollars in thousands)	
Due within 1 year	$—	$—
Due after 1 but within 5 years	1,231	1,265
Due after 5 but within 10 years	28,052	28,940
Due after 10 years	6,525	6,642
	35,808	36,847
Mortgage-Backed Securities (a)	370,168	377,923
Total Debt Securities	$405,976	$414,770

(a) Mortgage Backed Securities include an amortized cost of $41.2 million and a fair value of $41.8 million for Obligations of U.S. Government agencies issued by Ginnie Mae and an amortized cost of $328.9 million and a fair value of $336.1 million for Obligations of U.S. Government-sponsored enterprises issued by Fannie Mae and Freddie Mac.

Securities held to maturity with an amortized cost of $291.5 million and $45.7 million were pledged as of June 30, 2016 and December 31, 2015, respectively, to secure public deposits and for other purposes required or permitted by law.

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Note 7 Impairment of Investment Securities
Securities Available for Sale and Held to Maturity
As required by FASB ASC Topic 320, "Investments – Debt and Equity Securities," credit-related other-than-temporary impairment on debt securities is recognized in earnings, while non-credit related other-than-temporary impairment on debt securities not expected to be sold is recognized in OCI. During the six months ended June 30, 2016 and 2015, no other-than-temporary impairment charges were recognized.
First Commonwealth utilizes the specific identification method to determine the net gain or loss on debt securities and the average cost method to determine the net gain or loss on equity securities.
We review our investment portfolio on a quarterly basis for indications of impairment. This review includes analyzing the length of time and the extent to which the fair value has been lower than the cost, the financial condition and near-term prospects of the issuer, including any specific events which may influence the operations of the issuer and whether we are more likely than not to sell, or be required to sell, the security. We evaluate whether we are more likely than not to sell debt securities based upon our investment strategy for the particular type of security and our cash flow needs, liquidity position, capital adequacy, tax position and interest rate risk position. In addition, the risk of future other-than-temporary impairment may be influenced by additional bank failures, weakness in the U.S. economy, changes in real estate values and additional interest deferrals in our pooled trust preferred collateralized debt obligations. Our pooled trust preferred collateralized debt obligations are beneficial interests in securitized financial assets within the scope of FASB ASC Topic 325, "Investments – Other," and are therefore evaluated for other-than-temporary impairment using management's best estimate of future cash flows. If these estimated cash flows indicate that it is probable that an adverse change in cash flows has occurred, then other-than-temporary impairment would be recognized in accordance with FASB ASC Topic 320. There is a risk that First Commonwealth will record other-than-temporary impairment charges in the future. See Note 10, "Fair Values of Assets and Liabilities," for additional information.
The following table presents the gross unrealized losses and estimated fair values at June 30, 2016 for both available for sale and held to maturity securities by investment category and time frame for which securities have been in a continuous unrealized loss position:

	Less Than 12 Months		12 Months or More		Total	
	Estimated Fair Value	Gross Unrealized Losses	Estimated Fair Value	Gross Unrealized Losses	Estimated Fair Value	Gross Unrealized Losses
	(dollars in thousands)					
Obligations of U.S. Government-Sponsored Enterprises:						
Mortgage-Backed Securities – Residential	$15,227	$ (13)	$64,716	$ (221)	$79,943	$ (234)
Pooled Trust Preferred Collateralized Debt Obligations	—	—	28,276	(9,527)	28,276	(9,527)
Total Securities	$15,227	$ (13)	$92,992	$ (9,748)	$108,219	$ (9,761)

At June 30, 2016, fixed income securities issued by U.S. Government-sponsored enterprises comprised 2% of total unrealized losses due to changes in market interest rates. Pooled trust preferred collateralized debt obligations accounted for 98% of the unrealized losses primarily due to the illiquid market for this investment type. At June 30, 2016, there are 19 debt securities in an unrealized loss position.

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The following table presents the gross unrealized losses and estimated fair values at December 31, 2015 by investment category and time frame for which securities have been in a continuous unrealized loss position:

	Less Than 12 Months		12 Months or More		Total	
	Estimated Fair Value	Gross Unrealized Losses	Estimated Fair Value	Gross Unrealized Losses	Estimated Fair Value	Gross Unrealized Losses
	(dollars in thousands)					
Obligations of U.S. Government Agencies:						
Mortgage-Backed Securities – Residential	$6,798	$(20)	$—	$—	$6,798	$(20)
Mortgage-Backed Securities - Commercial	16,596	(247)	—	—	16,596	(247)
Obligations of U.S. Government-Sponsored Enterprises:						
Mortgage-Backed Securities – Residential	436,011	(3,293)	263,119	(7,413)	699,130	(10,706)
Mortgage-Backed Securities – Commercial	15,009	(178)	—	—	15,009	(178)
Other Government-Sponsored Enterprises	12,316	(85)	—	—	12,316	(85)
Obligation of States and Political Subdivisions	7,208	(58)	—	—	7,208	(58)
Pooled Trust Preferred Collateralized Debt Obligations	—	—	29,957	(7,497)	29,957	(7,497)
Total Securities	$493,938	$(3,881)	$293,076	$(14,910)	$787,014	$(18,791)

As of June 30, 2016, our corporate securities had an amortized cost and an estimated fair value of $5.9 million and $6.4 million, respectively. As of December 31, 2015, our corporate securities had an amortized cost and estimated fair value of $1.9 million and $2.3 million, respectively. Corporate securities are comprised of debt for large regional banks. There were no corporate securities in an unrealized loss position as of June 30, 2016 and December 31, 2015. When unrealized losses exist on these investments, management reviews each of the issuer's asset quality, earnings trends and capital position, to determine whether issues in an unrealized loss position were other-than-temporarily impaired. All interest payments on the corporate securities are being made as contractually required.

As of June 30, 2016, the book value of our pooled trust preferred collateralized debt obligations totaled $42.8 million with an estimated fair value of $33.7 million, which includes securities comprised of 274 banks and other financial institutions. All of our pooled securities are mezzanine tranches, three of which have no senior class remaining in the issue. The credit ratings on all of our issues are below investment grade. At the time of initial issue, the subordinated tranches ranged in size from approximately 7% to 35% of the total principal amount of the respective securities and no more than 5% of any pooled security consisted of a security issued by any one institution. As of June 30, 2016, after taking into account management's best estimates of future interest deferrals and defaults, three of our securities had no excess subordination in the tranches we own and six of our securities had excess subordination which ranged from 2% to 82% of the current performing collateral.

The following table provides information related to our pooled trust preferred collateralized debt obligations as of June 30, 2016:

Deal	Class	Book Value	Estimated Fair Value	Unrealized Gain (Loss)	Moody's/Fitch Ratings	Number of Banks	Deferrals and Defaults as a % of Current Collateral	Excess Subordination as a % of Current Performing Collateral
(dollars in thousands)								

Pre TSL IV	Mezzanine	$1,830	$1,301	$(529)	B1/BB	6	18.05 %	58.51 %
Pre TSL VII	Mezzanine	3,061	3,324	263	Ca/-	14	49.68	—
Pre TSL VIII	Mezzanine	2,042	1,691	(351)	C/C	28	53.00	—
Pre TSL IX	Mezzanine	2,394	1,797	(597)	B1/C	38	29.80	9.73
Pre TSL X	Mezzanine	1,675	1,817	142	Caa1/C	43	32.22	2.20
Pre TSL XII	Mezzanine	5,786	4,442	(1,344)	B3/C	66	22.03	—
Pre TSL XIII	Mezzanine	12,828	9,971	(2,857)	Ba3/C	56	11.34	47.86
Pre TSL XIV	Mezzanine	12,924	9,075	(3,849)	B1/CC	56	15.21	38.08
MMCap I	Mezzanine	210	305	95	Ca/C	8	58.11	81.96
Total		$42,750	$33,723	$(9,027)				

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Lack of liquidity in the market for trust preferred collateralized debt obligations, below investment grade credit ratings and market uncertainties related to the financial industry are factors contributing to the impairment on these securities. All of the Company's pooled trust preferred securities are included in the non-exclusive list issued by the regulatory agencies and therefore are not considered covered funds under the Volcker Rule.

On a quarterly basis we evaluate our debt securities for other-than-temporary impairment. During the three and six months ended June 30, 2016 and 2015, there were no credit-related other-than-temporary impairment charges recognized on our pooled trust preferred collateralized debt obligations. When evaluating these investments, we determine a credit-related portion and a non-credit related portion of other-than-temporary impairment. The credit-related portion is recognized in earnings and represents the difference between book value and the present value of future cash flows. The non-credit related portion is recognized in OCI and represents the difference between the fair value of the security and the amount of credit-related impairment. A discounted cash flow analysis provides the best estimate of credit-related other-than-temporary impairment for these securities.

Additional information related to the discounted cash flow analysis follows:

Our pooled trust preferred collateralized debt obligations are measured for other-than-temporary impairment within the scope of FASB ASC Topic 325 by determining whether it is probable that an adverse change in estimated cash flows has occurred. Determining whether there has been an adverse change in estimated cash flows from the cash flows previously projected involves comparing the present value of remaining cash flows previously projected against the present value of the cash flows estimated at June 30, 2016. We consider the discounted cash flow analysis to be our primary evidence when determining whether credit related other-than-temporary impairment exists.

Results of a discounted cash flow test are significantly affected by other variables, such as the estimate of future cash flows, credit worthiness of the underlying banks and determination of probability of default of the underlying collateral. The following provides additional information for each of these variables:

- Estimate of Future Cash Flows – Cash flows are constructed in an INTEX cash flow model which includes each deal’s structural features. Projected cash flows include prepayment assumptions, which are dependent on the issuer's asset size and coupon rate. For collateral issued by financial institutions over $15 billion in asset size with a coupon over 7%, a 100% prepayment rate is assumed. Financial institutions over $15 billion with a coupon of 7% or under are assigned a prepayment rate of 40% for two years and 2% thereafter. Financial institutions with assets between $2 billion and $15 billion with coupons over 7% are assigned a 5% prepayment rate. For financial institutions below $2 billion, if the coupon is over 10%, a prepayment rate of 5% is assumed and for all other issuers, there is no prepayment assumption incorporated into the cash flows. The modeled cash flows are then used to estimate if all the scheduled principal and interest payments of our investments will be returned.
- Credit Analysis – A quarterly credit evaluation is performed for each of the 274 banks comprising the collateral across the various pooled trust preferred securities. Our credit evaluation considers all evidence available to us and includes the nature of the issuer’s business, its years of operating history, corporate structure, loan composition, loan concentrations, deposit mix, asset growth rates, geographic footprint and local economic environment. Our analysis focuses on profitability, return on assets, shareholders’ equity, net interest margin, credit quality ratios, operating efficiency, capital adequacy and liquidity.
- Probability of Default – A probability of default is determined for each bank and is used to calculate the expected impact of future deferrals and defaults on our expected cash flows. Each bank in the collateral pool is assigned a probability of default for each year until maturity. Currently, any bank that is in default is assigned a 100% probability of default and a 0% projected recovery rate. All other banks in the pool are assigned a probability of default based on their unique credit characteristics and market indicators with a 10% projected recovery rate. For the majority of banks currently in deferral we assume the bank continues to defer and will eventually default and, therefore, a 100% probability of default is assigned. However, for some deferring collateral there is the possibility that they will become current on interest or principal payments at some point in the future and in those cases a probability that the deferral

will ultimately cure is assigned. The probability of default is updated quarterly. As of June 30, 2016, default probabilities for performing collateral ranged from 0.33% to 75%.

Our credit evaluation provides a basis for determining deferral and default probabilities for each underlying piece of collateral. Using the results of the credit evaluation, the next step of the process is to look at pricing of senior debt or credit default swaps for the issuer (or where such information is unavailable, for companies having similar credit profiles as the issuer). The pricing of these market indicators provides the information necessary to determine appropriate default probabilities for each bank.

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In addition to the above factors, our evaluation of impairment also includes a stress test analysis which provides an estimate of excess subordination for each tranche. We stress the cash flows of each pool by increasing current default assumptions to the level of defaults that results in an adverse change in estimated cash flows. This stressed breakpoint is then used to calculate excess subordination levels for each pooled trust preferred security. The results of the stress test allow management to identify those pools that are at a greater risk for a future break in cash flows so that we can monitor banks in those pools more closely for potential deterioration of credit quality.

Our cash flow analysis as of June 30, 2016, indicates that no credit-related other-than-temporary impairment has occurred on our pooled trust preferred securities during the six months ended June 30, 2016. Based upon the analysis performed by management, it is probable that three of our pooled trust preferred securities will experience principal and interest shortfalls and therefore appropriate other-than-temporary charges were recorded in prior periods. These securities are identified in the table on page 15 with 0% “Excess Subordination as a Percentage of Current Performing Collateral.” For the remaining securities listed in that table, our analysis as of June 30, 2016 indicates it is probable that we will collect all contractual principal and interest payments. For four of those securities, PreTSL IX, PreTSL XIII, PreTSL XIV and MMCap I, other-than-temporary impairment charges were recorded in prior periods; however, due to improvement in the expected cash flows of these securities, it is now probable that all contractual payments will be received.

During 2008, 2009 and 2010, other-than-temporary impairment charges were recognized on all of our pooled trust preferred securities, except for PreTSL IV. Our cash flow analysis as of June 30, 2016, for all of these impaired securities indicates that it is now probable we will collect principal and interest in excess of what was estimated at the time other-than-temporary impairment charges were recorded. This change can be attributed to improvement in the underlying collateral for these securities and has resulted in the present value of estimated future principal and interest payments exceeding the securities' current book value. The excess for each bond of the present value of future cash flows over our current book value ranges from 20% to 127% and will be recognized as an adjustment to yield over the remaining life of these securities. The excess subordination recognized as an adjustment to yield is reflected in the following table as increases in cash flows expected to be collected.

The following table provides a cumulative roll forward of credit losses recognized in earnings for debt securities held and not intended to be sold:

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2016	2015	2016	2015
	(dollars in thousands)			
Balance, beginning (a)	$24,590	$25,707	$24,851	$26,246
Credit losses on debt securities for which other-than-temporary impairment was not previously recognized	—	—	—	—
Additional credit losses on debt securities for which other-than-temporary impairment was previously recognized	—	—	—	—
Increases in cash flows expected to be collected, recognized over the remaining life of the security (b)	(280)	(341)	(541)	(662)
Reduction for debt securities called during the period	—	—	—	(218)
Balance, ending	$24,310	$25,366	$24,310	$25,366

(a) The beginning balance represents credit related losses included in other-than-temporary impairment charges recognized on debt securities in prior periods.
(b) Represents the increase in cash flows recognized in interest income during the period.

In the first six months of 2016 and 2015, no other-than-temporary impairment charges were recorded on equity securities. On a quarterly basis, management evaluates equity securities for other-than-temporary impairment by reviewing the severity and duration of decline in estimated fair value, research reports, analysts' recommendations, credit rating changes, news stories, annual reports, regulatory filings, impact of interest rate changes and other relevant information. As of June 30, 2016 and 2015, there were no equity securities in an unrealized loss position.

Other Investments

As a member of the Federal Home Loan Bank ("FHLB"), First Commonwealth is required to purchase and hold stock in the FHLB to satisfy membership and borrowing requirements. The level of stock required to be held is dependent on the amount of First Commonwealth's mortgage-related assets and outstanding borrowings with the FHLB. This stock is restricted in that it can only be sold to the FHLB or to another member institution, and all sales of FHLB stock must be at par. As a result of these restrictions, FHLB stock is unlike other investment securities insofar as there is no trading market for FHLB stock and the transfer price is determined by FHLB membership rules and not by market participants. As of June 30, 2016 and December 31, 2015, our FHLB stock totaled $58.1 million and $63.0 million, respectively, and is included in “Other investments” on the Condensed Consolidated Statements of Financial Condition.

FHLB stock is held as a long-term investment and its value is determined based on the ultimate recoverability of the par value. First Commonwealth evaluates impairment quarterly and has concluded that the par value of its investment in FHLB stock will be recovered. Accordingly, no impairment charge was recorded on these securities during the three and six months ended June 30, 2016.

Note 8 Loans and Allowance for Credit Losses

The following table provides outstanding balances related to each of our loan types:

	June 30, 2016	December 31, 2015
	(dollars in thousands)	
Commercial, financial, agricultural and other	$1,185,062	$1,150,906
Real estate construction	242,132	220,736
Residential real estate	1,199,005	1,224,465
Commercial real estate	1,648,222	1,479,000
Loans to individuals	569,355	608,643
Total loans	$4,843,776	$4,683,750

Credit Quality Information

As part of the on-going monitoring of credit quality within the loan portfolio, the following credit worthiness categories are used in grading our loans:

Pass	Acceptable levels of risk exist in the relationship. Includes all loans not classified as OAEM, substandard or doubtful.
Other Assets Especially Mentioned (OAEM)	Potential weaknesses that deserve management’s close attention. The potential weaknesses may result in deterioration of the repayment prospects or weaken the Company’s credit position at some future date. The credit risk may be relatively minor, yet constitute an undesirable risk in light of the circumstances surrounding the specific credit. No loss of principal or interest is expected.
Substandard	Well-defined weakness or a weakness that jeopardizes the repayment of the debt. A loan may be classified as substandard as a result of deterioration of the borrower’s financial condition and repayment capacity. Loans for which repayment plans have not been met or collateral equity margins do not protect the Company may also be classified as substandard.
Doubtful	Loans with the characteristics of substandard loans with the added characteristic that collection or liquidation in full, on the basis of presently existing facts and conditions, is highly improbable.

The use of creditworthiness categories to grade loans permits management’s use of migration analysis to estimate a portion of credit risk. The Company’s internal creditworthiness grading system provides a measurement of credit risk based primarily on an evaluation of the borrower’s cash flow and collateral. Movement between these rating categories provides a predictive measure of credit losses and therefore assists in determining the appropriate level for the loan loss reserves. Category ratings are reviewed each quarter, at which time management analyzes the results, as well as other external statistics and factors related to loan performance. Loans that migrate towards higher risk rating levels generally have an increased risk of default, whereas loans that migrate toward lower risk ratings generally will result in a lower risk factor being applied to those related loan balances.

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The following tables represent our credit risk profile by creditworthiness:

	June 30, 2016					
	Commercial, financial, agricultural and other	Real estate construction	Residential real estate	Commercial real estate	Loans to individuals	Total
	(dollars in thousands)					
Pass	$1,095,516	$ 241,840	$1,183,847	$1,625,206	$ 569,087	$4,715,496
Non-Pass						
OAEM	11,923	292	6,846	7,221	—	26,282
Substandard	77,623	—	8,312	15,795	268	101,998
Doubtful	—	—	—	—	—	—
Total Non-Pass	89,546	292	15,158	23,016	268	128,280
Total	$1,185,062	$ 242,132	$1,199,005	$1,648,222	$ 569,355	$4,843,776

	December 31, 2015					
	Commercial, financial, agricultural and other	Real estate construction	Residential real estate	Commercial real estate	Loans to individuals	Total
	(dollars in thousands)					
Pass	$1,074,858	$ 220,267	$1,209,606	$1,436,714	$ 608,342	$4,549,787
Non-Pass						
OAEM	11,825	442	5,244	30,012	—	47,523
Substandard	64,223	27	9,615	12,274	301	86,440
Doubtful	—	—	—	—	—	—
Total Non-Pass	76,048	469	14,859	42,286	301	133,963
Total	$1,150,906	$ 220,736	$1,224,465	$1,479,000	$ 608,643	$4,683,750

Portfolio Risks

The credit quality of our loan portfolio can potentially represent significant risk to our earnings, capital, regulatory agency relationships, investment community reputation and shareholder returns. First Commonwealth devotes a substantial amount of resources managing this risk primarily through our credit administration department that develops and administers policies and procedures for underwriting, maintaining, monitoring and collecting activities. Credit administration is independent of lending departments and oversight is provided by the credit committee of the First Commonwealth Board of Directors.

Criticized loans have been evaluated when determining the appropriateness of the allowance for credit losses, which we believe is adequate to absorb losses inherent to the portfolio as of June 30, 2016. However, changes in economic conditions, interest rates, borrower financial condition, delinquency trends or previously established fair values of collateral factors could significantly change those judgmental estimates.

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Age Analysis of Past Due Loans by Segment
The following tables delineate the aging analysis of the recorded investments in past due loans as of June 30, 2016 and December 31, 2015. Also included in these tables are loans that are 90 days or more past due and still accruing because they are well-secured and in the process of collection.

	June 30, 2016						
	30 - 59 days past due	60 - 89 days past due	90 days and greater and still accruing	Nonaccrual	Total past due and nonaccrual	Current	Total
	(dollars in thousands)						
Commercial, financial, agricultural and other	$2,344	$714	$ 283	$ 37,429	$ 40,770	$1,144,292	$1,185,062
Real estate construction	—	—	—	—	—	242,132	242,132
Residential real estate	4,544	1,542	243	6,448	12,777	1,186,228	1,199,005
Commercial real estate	1,166	—	1	3,931	5,098	1,643,124	1,648,222
Loans to individuals	2,072	700	857	268	3,897	565,458	569,355
Total	$10,126	$2,956	$ 1,384	$ 48,076	$ 62,542	$4,781,234	$4,843,776

	December 31, 2015						
	30 - 59 days past due	60 - 89 days past due	90 days and greater and still accruing	Nonaccrual	Total past due and nonaccrual	Current	Total
	(dollars in thousands)						
Commercial, financial, agricultural and other	$364	$49	$ 129	$ 23,653	$ 24,195	$1,126,711	$1,150,906
Real estate construction	280	—	—	28	308	220,428	220,736
Residential real estate	4,175	1,055	1,315	6,500	13,045	1,211,420	1,224,465
Commercial real estate	781	—	65	6,223	7,069	1,471,931	1,479,000
Loans to individuals	2,998	774	946	301	5,019	603,624	608,643
Total	$8,598	$1,878	$ 2,455	$ 36,705	$ 49,636	$4,634,114	$4,683,750

Nonaccrual Loans
The previous tables summarize nonaccrual loans by loan segment. The Company generally places loans on nonaccrual status when the full and timely collection of interest or principal becomes uncertain, when part of the principal balance has been charged off and no restructuring has occurred, or the loans reach a certain number of days past due. Generally, loans 90 days or more past due are placed on nonaccrual status, except for consumer loans, which are placed in nonaccrual status at 150 days past due.
When a loan is placed on nonaccrual, the accrued unpaid interest receivable is reversed against interest income and all future payments received are applied as a reduction to the loan principal. Generally, the loan is returned to accrual status when (a) all delinquent interest and principal becomes current under the terms of the loan agreement or (b) the loan is both well-secured and in the process of collection and collectability is no longer in doubt.
Impaired Loans

Management considers loans to be impaired when, based on current information and events, it is determined that the Company will not be able to collect all amounts due according to the loan contract, including scheduled interest payments. Determination of impairment is treated the same across all loan categories. When management identifies a loan as impaired, the impairment is measured based on the present value of expected future cash flows, discounted at the loan's effective interest rate, except when the sole source for repayment of the loan is the operation or liquidation of collateral. When the loan is collateral dependent, the appraised value less estimated cost to sell is utilized. If management determines the value of the impaired loan is less than the recorded investment in the loan, impairment is recognized through an allowance estimate or a charge-off to the allowance. Troubled debt restructured loans on accrual status are also considered to be impaired loans.

When the ultimate collectability of the total principal of an impaired loan is in doubt and the loan is on nonaccrual status, all payments are applied to principal under the cost recovery method. When the ultimate collectability of the total principal of an impaired loan is not in doubt and the loan is on nonaccrual status, contractual interest is credited to interest income when received under the cash basis method.

Significant nonaccrual loans as of June 30, 2016, include the following:

- $11.4 million relationship of commercial industrial loans to a steel and aluminum servicing company. These loans were originated in 2011 and were placed in nonaccrual status during the first quarter of 2016. A valuation of the collateral was completed during the second quarter of 2016.
- $10.5 million relationship of commercial industrial loans to a manufacturer of mine safety products. These loans were originated from 2014 to 2015 and were placed in nonaccrual status during the second quarter of 2016. All collateral valuations were completed in June 2016.
- $4.4 million relationship of commercial industrial loans to an oil and gas well services company. These loans were originated in 2014 and were placed in nonaccrual status during the fourth quarter of 2015. During the six months ended June 30, 2016, charge-offs of $2.0 million related to this relationship were recorded. All collateral valuations were completed in June 2016.
- $3.7 million relationship of commercial industrial loans to a local energy company involved in the drilling and production of natural gas wells. These loans were originated from 2008 to 2011 and were placed in nonaccrual status during the third quarter of 2013. Two of these loans were modified resulting in TDR classification: one loan totaling $1.3 million was modified in 2012, and the other loan totaling $2.4 million was modified in 2014. During the six months ended June 30, 2016, charge-offs of $1.1 million related to this relationship were recorded. A valuation of the collateral was updated during the first quarter of 2016.
- $3.5 million relationship of commercial industrial loans to a gear manufacturer. These loans were originated in 2013 and were placed in nonaccrual status during the third quarter of 2015. During the six months ended June 30, 2016, charge-offs of $0.2 million related to this relationship were recorded. A valuation of the collateral was completed during the second quarter of 2016.

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FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES
NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The following tables include the recorded investment and unpaid principal balance for impaired loans with the associated allowance amount, if applicable, as of June 30, 2016 and December 31, 2015. Also presented are the average recorded investment in impaired loans and the related amount of interest recognized while the loan was considered impaired. Average balances are calculated using month-end balances of the loans for the period reported and are included in the table below based on their period-end allowance position.

	June 30, 2016			December 31, 2015		
	Recorded investment	Unpaid principal balance	Related allowance	Recorded investment	Unpaid principal balance	Related allowance
	(dollars in thousands)					
With no related allowance recorded:						
Commercial, financial, agricultural and other	$16,078	$23,373		$11,344	$15,673	
Real estate construction	—	—		28	117	
Residential real estate	11,580	13,674		9,952	11,819	
Commercial real estate	6,390	8,043		7,562	9,449	
Loans to individuals	376	450		421	507	
Subtotal	34,424	45,540		29,307	37,565	
With an allowance recorded:						
Commercial, financial, agricultural and other	28,522	30,849	15,018	20,132	22,590	6,952
Real estate construction	—	—	—	—	—	—
Residential real estate	551	680	48	461	672	51
Commercial real estate	911	939	464	944	1,008	42
Loans to individuals	—	—	—	—	—	—
Subtotal	29,984	32,468	15,530	21,537	24,270	7,045
Total	$64,408	$78,008	$ 15,530	$50,844	$61,835	$ 7,045

	For the Six Months Ended June 30,			
	2016		2015	
	Average recorded investment	Interest Income Recognized	Average recorded investment	Interest Income Recognized
	(dollars in thousands)			
With no related allowance recorded:				
Commercial, financial, agricultural and other	$20,116	$ 249	$21,691	$ 120
Real estate construction	9	44	137	—
Residential real estate	11,232	137	11,025	86
Commercial real estate	7,136	67	8,760	43
Loans to individuals	442	3	312	2
Subtotal	38,935	500	41,925	251
With an allowance recorded:				
Commercial, financial, agricultural and other	17,939	91	5,337	72
Real estate construction	—	—	—	—
Residential real estate	347	—	319	—
Commercial real estate	861	11	194	3
Loans to individuals	—	—	—	—

Subtotal	19,147	102	5,850	75
Total	$58,082	$ 602	$47,775	$ 326

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	For the Three Months Ended June 30,			
	2016		2015	
	Average recorded investment	Interest Income Recognized	Average recorded investment	Interest Income Recognized
	(dollars in thousands)			
With no related allowance recorded:				
Commercial, financial, agricultural and other	$18,995	$ 95	$18,526	$ 65
Real estate construction	—	—	36	—
Residential real estate	11,462	90	11,302	45
Commercial real estate	6,887	29	8,682	24
Loans to individuals	405	2	316	1
Subtotal	37,749	216	38,862	135
With an allowance recorded:				
Commercial, financial, agricultural and other	22,788	65	5,237	42
Real estate construction	—	—	—	—
Residential real estate	476	—	329	—
Commercial real estate	921	6	193	1
Loans to individuals	—	—	—	—
Subtotal	24,185	71	5,759	43
Total	$61,934	$ 287	$44,621	$ 178

Unfunded commitments related to nonperforming loans were $2.2 million at June 30, 2016 and $0.1 million at December 31, 2015. After consideration of the requirements to draw and available collateral related to these commitments, a reserve of $24 thousand and $13 thousand was established for these off balance sheet exposures at June 30, 2016 and December 31, 2015, respectively.

Troubled debt restructured loans are those loans whose terms have been renegotiated to provide a reduction or deferral of principal or interest as a result of the financial difficulties experienced by the borrower, who could not obtain comparable terms from alternate financing sources.
The following table provides detail as to the total troubled debt restructured loans and total commitments outstanding on troubled debt restructured loans:

	June 30, 2016	December 31, 2015
	(dollars in thousands)	
Troubled debt restructured loans		
Accrual status	$16,332	$ 14,139
Nonaccrual status	9,672	12,360
Total	$26,004	$ 26,499
Commitments		
Unused lines of credit	$577	$ 3,252

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The following tables provide detail, including specific reserves and reasons for modification, related to loans identified as troubled debt restructurings:

	For the Six Months Ended June 30, 2016						
		Type of Modification					
	Number of Contracts	Extend Maturity	Modify Rate	Modify Payments	Total Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment	Specific Reserve
	(dollars in thousands)						
Commercial, financial, agricultural and other	5	$92	$4,009	$ —	$ 4,101	$ 3,708	$ 40
Residential real estate	26	—	114	2,416	2,530	2,440	—
Commercial real estate	6	1,264	—	25	1,289	1,227	74
Loans to individuals	5	—	29	11	40	30	—
Total	42	$1,356	$4,152	$ 2,452	$ 7,960	$ 7,405	$ 114

	For the Six Months Ended June 30, 2015						
		Type of Modification					
	Number of Contracts	Extend Maturity	Modify Rate	Modify Payments	Total Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment	Specific Reserve
	(dollars in thousands)						
Commercial, financial, agricultural and other	3	$1,751	$ —	$ 109	$ 1,860	$ 1,812	$ 53
Residential real estate	16	—	296	503	799	723	7
Commercial real estate	1	—	—	463	463	428	—
Loans to individuals	6	—	61	18	79	66	—
Total	26	$1,751	$ 357	$ 1,093	$ 3,201	$ 3,029	$ 60

The troubled debt restructurings included in the above tables are also included in the impaired loan tables provided earlier in this note. Loans defined as modified due to a change in rate may include loans that were modified for a change in rate as well as a reamortization of the principal and an extension of the maturity. For the six months ended June 30, 2016 and 2015, $4.2 million and $0.4 million, respectively, of total rate modifications represent loans with modifications to the rate as well as payment as a result of reamortization. For both 2016 and 2015 the changes in loan balances between the pre-modification balance and the post-modification balance are due to customer payments.

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FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES
NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The following tables provide detail, including specific reserves and reasons for modification, related to loans identified as troubled debt restructurings:

	For the Three Months Ended June 30, 2016						
		Type of Modification					
	Number of Contracts	Extend Maturity	Modify Rate	Modify Payments	Total Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment	Specific Reserve
	(dollars in thousands)						
Commercial, financial, agricultural and other	4	$92	$ 240	$ —	$ 332	$ 217	$ 40
Residential real estate	17	—	—	1,435	1,435	1,428	—
Commercial real estate	4	1,198	—	—	1,198	1,173	74
Loans to individuals	2	—	11	6	17	15	—
Total	27	$1,290	$ 251	$ 1,441	$ 2,982	$ 2,833	$ 114

	For the Three Months Ended, June 30, 2015						
		Type of Modification					
	Number of Contracts	Extend Maturity	Modify Rate	Modify Payments	Total Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment	Specific Reserve
	(dollars in thousands)						
Commercial, financial, agricultural and other	2	$252	$ —	$ 109	$ 361	$ 317	$ 53
Residential real estate	11	—	45	485	530	525	7
Loans to individuals	5	—	61	—	61	56	—
Total	18	$252	$ 106	$ 594	$ 952	$ 898	$ 60

The troubled debt restructurings included in the above tables are also included in the impaired loan tables provided earlier in this note. Loans defined as modified due to a change in rate may include loans that were modified for a change in rate as well as a reamortization of the principal and an extension of the maturity. For the three months ended June 30, 2016 and 2015, $0.3 million and $0.1 million, respectively, of total rate modifications represent loans with modifications to the rate as well as payment as a result of reamortization. For both 2016 and 2015 the changes in loan balances between the pre-modification balance and the post-modification balance are due to customer payments.

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A troubled debt restructuring is considered to be in default when a restructured loan is 90 days or more past due. The following table provides information related to restructured loans that were considered to be in default during the six months ended June 30:

	2016		2015	
	Number of Contracts	Recorded Investment	Number of Contracts	Recorded Investment
	(dollars in thousands)			
Residential real estate	—	$ —	2	$ 56
Total	—	$ —	2	$ 56

The following table provides information related to restructured loans that were considered to be in default during the three months ended June 30:

	2016		2015	
	Number of Contracts	Recorded Investment	Number of Contracts	Recorded Investment
	(dollars in thousands)			
Residential real estate	—	$ —	2	$ 56
Total	—	$ —	2	$ 56

The following tables provide detail related to the allowance for credit losses:

	For the Six Months Ended June 30, 2016					
	Commercial, financial, agricultural and other	Real estate construction	Residential real estate	Commercial real estate	Loans to individuals	Total
	(dollars in thousands)					
Allowance for credit losses:						
Beginning Balance	$31,035	$ 887	$ 2,606	$ 11,924	$ 4,360	$50,812
Charge-offs	(6,145)	—	(602)	(408)	(2,491)	(9,646)
Recoveries	198	227	260	783	289	1,757
Provision (credit)	21,269	(634)	341	(6,437)	2,359	16,898
Ending Balance	$46,357	$ 480	$ 2,605	$ 5,862	$ 4,517	$59,821
Ending balance: individually evaluated for impairment	$15,018	$ —	$ 48	$ 464	$ —	$15,530
Ending balance: collectively evaluated for impairment	31,339	480	2,557	5,398	4,517	44,291
Loans:						
Ending balance	1,185,062	242,132	1,199,005	1,648,222	569,355	4,843,776
Ending balance: individually evaluated for impairment	43,817	—	5,966	6,017	—	55,800
Ending balance: collectively evaluated for impairment	1,141,245	242,132	1,193,039	1,642,205	569,355	4,787,976

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	For the Six Months Ended June 30, 2015					
	Commercial, financial, agricultural and other	Real estate construction	Residential real estate	Commercial real estate	Loans to individuals	Total
	(dollars in thousands)					
Allowance for credit losses:						
Beginning Balance	$29,627	$ 2,063	$ 3,664	$ 11,881	$ 4,816	$52,051
Charge-offs	(7,940)	—	(1,050)	(688)	(2,383)	(12,061)
Recoveries	358	84	239	153	323	1,157
Provision (credit)	1,710	(629)	70	881	2,165	4,197
Ending Balance	$23,755	$ 1,518	$ 2,923	$ 12,227	$ 4,921	$45,344
Ending balance: individually evaluated for impairment	$1,596	$ —	$ 35	$ 44	$ —	$1,675
Ending balance: collectively evaluated for impairment	22,159	1,518	2,888	12,183	4,921	43,669
Loans:						
Ending balance	1,098,019	125,010	1,204,499	1,416,841	646,485	4,490,854
Ending balance: individually evaluated for impairment	21,419	—	7,700	7,625	—	36,744
Ending balance: collectively evaluated for impairment	1,076,600	125,010	1,196,799	1,409,216	646,485	4,454,110

	For the Three Months Ended June 30, 2016					
	Commercial, financial, agricultural and other	Real estate construction	Residential real estate	Commercial real estate	Loans to individuals	Total
	(dollars in thousands)					
Allowance for credit losses:						
Beginning Balance	$41,721	$ 901	$ 2,628	$ 5,483	$ 4,489	$55,222
Charge-offs	(4,753)	—	(220)	(143)	(1,022)	(6,138)
Recoveries	64	4	142	27	128	365
Provision (credit)	9,325	(425)	55	495	922	10,372
Ending Balance	$46,357	$ 480	$ 2,605	$ 5,862	$ 4,517	$59,821

	For the Three Months Ended, June 30, 2015					
	Commercial, financial, agricultural and other	Real estate construction	Residential real estate	Commercial real estate	Loans to individuals	Total
	(dollars in thousands)					
Allowance for credit losses:						
Beginning Balance	$24,406	$ 1,528	$ 3,387	$ 12,487	$ 4,889	$46,697
Charge-offs	(2,860)	—	(484)	(486)	(1,122)	(4,952)
Recoveries	158	84	143	15	161	561
Provision (credit)	2,051	(94)	(123)	211	993	3,038
Ending Balance	$23,755	$ 1,518	$ 2,923	$ 12,227	$ 4,921	$45,344

Note 9 Income Taxes

At June 30, 2016 and December 31, 2015, First Commonwealth had no material unrecognized tax benefits or accrued interest and penalties. If applicable, First Commonwealth will record interest and penalties as a component of noninterest expense. Federal and state tax years 2012 through 2014 are open for examination as of June 30, 2016.

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Note 10 Fair Values of Assets and Liabilities

FASB ASC Topic 820, "Fair Value Measurements and Disclosures," requires disclosures for non-financial assets and non-financial liabilities, except for items that are recognized or disclosed at fair value in the financial statements on a recurring basis (at least annually). All non-financial assets are included either as a separate line item on the Condensed Consolidated Statements of Financial Condition or in the "Other assets" category of the Condensed Consolidated Statements of Financial Condition. Currently, First Commonwealth does not have any non-financial liabilities to disclose.

FASB ASC Topic 825, "Financial Instruments", permits entities to irrevocably elect to measure select financial instruments and certain other items at fair value. The unrealized gains and losses are required to be included in earnings each reporting period for the items that fair value measurement is elected. First Commonwealth has elected not to measure any existing financial instruments at fair value under FASB ASC Topic 825; however, in the future we may elect to adopt this guidance for select financial instruments.

In accordance with FASB ASC Topic 820, First Commonwealth groups financial assets and financial liabilities measured at fair value in three levels based on the principal markets in which the assets and liabilities are transacted and the observability of the data points used to determine fair value. These levels are:

- Level 1 – Valuations for assets and liabilities traded in active exchange markets, such as the New York Stock Exchange ("NYSE"). Valuations are obtained from readily available pricing sources for market transactions involving identical assets or liabilities. Level 1 securities include equity holdings comprised of publicly traded bank stocks which were priced using quoted market prices.
- Level 2 – Valuations for assets and liabilities traded in less active dealer or broker markets. Valuations are obtained for identical or comparable assets or liabilities from alternative pricing sources with reasonable levels of price transparency. Level 2 includes Obligations of U.S. Government securities issued by Agencies and Sponsored Enterprises, Obligations of States and Political Subdivisions, corporate securities, FHLB stock, loans held for sale, interest rate derivatives (including interest rate caps, interest rate swaps and risk participation agreements), certain other real estate owned and certain impaired loans.

Level 2 investment securities are valued by a recognized third party pricing service using observable inputs. The model used by the pricing service varies by asset class and incorporates available market, trade and bid information as well as cash flow information when applicable. Because many fixed-income investment securities do not trade on a daily basis, the model uses available information such as benchmark yield curves, benchmarking of like investment securities, sector groupings and matrix pricing. The model will also use processes such as an option adjusted spread to assess the impact of interest rates and to develop prepayment estimates. Market inputs normally used in the pricing model include benchmark yields, reported trades, broker/dealer quotes, issuer spreads, two-sided markets, benchmark securities, bids, offers and reference data including market research publications.

Management validates the market values provided by the third party service by having another recognized pricing service price 100% of the securities on an annual basis and a random sample of securities each quarter, monthly monitoring of variances from prior period pricing and, on a monthly basis, evaluating pricing changes compared to expectations based on changes in the financial markets.

Other investments recorded in the Condensed Consolidated Statements of Financial Condition are comprised of FHLB stock whose estimated fair value is based on its par value. Additional information on FHLB stock is provided in Note 7, "Impairment of Investment Securities."

Loans held for sale include a commercial loan and residential mortgage loans originated for sale in the secondary mortgage market. The estimated fair value for these loans was determined on the basis of rates obtained in the respective secondary market.

Interest rate derivatives are reported at an estimated fair value utilizing Level 2 inputs and are included in other assets and other liabilities, and consist of interest rate swaps where there is no significant deterioration in the counterparties' (loan customers') credit risk since origination of the interest rate swap as well as interest rate caps and risk participation agreements. First Commonwealth values its interest rate swap and cap positions using a yield curve by taking market prices/rates for an appropriate set of instruments. The set of instruments currently used to determine the U.S. Dollar yield curve includes cash LIBOR rates from overnight to three months, Eurodollar futures contracts and swap rates from three years to thirty years. These yield curves determine the valuations of interest rate swaps. Interest rate derivatives are further described in Note 11, "Derivatives."

For purposes of potential valuation adjustments to our derivative positions, First Commonwealth evaluates the credit risk of its counterparties as well as our own credit risk. Accordingly, we have considered factors such as the likelihood of default, expected loss given default, net exposures and remaining contractual life, among other things, in determining if any fair value adjustments related to credit risk are required. We review our counterparty exposure quarterly, and when necessary, appropriate adjustments are made to reflect the exposure.

We also utilize this approach to estimate our own credit risk on derivative liability positions. In 2016, we have not realized any losses due to a counterparty's inability to pay any uncollateralized positions.

The estimated fair value for other real estate owned included in Level 2 is determined by either an independent market-based appraisal less estimated costs to sell or an executed sales agreement.

- Level 3 – Valuations for assets and liabilities that are derived from other valuation methodologies, including option pricing models, discounted cash flow models and similar techniques, and not based on market exchange, dealer or broker traded transactions. If the inputs used to provide the valuation are unobservable and/or there is very little, if any, market activity for the security or similar securities, the securities would be considered Level 3 securities. Level 3 valuations incorporate certain assumptions and projections in determining the fair value assigned to such assets or liabilities. The assets included in Level 3 are pooled trust preferred collateralized debt obligations, non-marketable equity investments, certain interest rate derivatives, certain other real estate owned and certain impaired loans.

Our pooled trust preferred collateralized debt obligations are collateralized by the trust preferred securities of individual banks, thrifts and bank holding companies in the United States. There has been little or no active trading in these securities since 2009; therefore, it is more appropriate to determine estimated fair value using a discounted cash flow analysis. Detail on our process for determining the appropriate cash flows for this analysis is provided in Note 7, "Impairment of Investment Securities." The discount rate applied to the cash flows is determined by evaluating the current market yields for comparable corporate and structured credit products along with an evaluation of the risks associated with the cash flows of the comparable security. Due to the fact that there is no active market for the pooled trust preferred collateralized debt obligations, one key reference point is the market yield for the single issue trust preferred securities issued by banks and thrifts for which there is more activity than for the pooled securities. Adjustments are then made to reflect the credit and structural differences between these two security types.

Management validates the fair value of the pooled trust preferred collateralized debt obligations by monitoring the performance of the underlying collateral, discussing the discount rate, cash flow assumptions and general market trends with a specialized third party and confirming changes in the underlying collateral to the trustee reports. Management's monitoring of the underlying collateral includes deferrals of interest payments, payment defaults, cures of previously deferred interest payments, any regulatory filings or actions and general news related to the underlying collateral. Management also evaluates fair value changes compared to expectations based on changes in the interest rates used in determining the discount rate and general financial markets.

The estimated fair value of the non-marketable equity investments included in Level 3 is based on par value.

The estimated fair value of limited partnership investments included in Level 3 is based on par value.

For interest rate derivatives included in Level 3, the fair value incorporates credit risk by considering such factors as likelihood of default and expected loss given default based on the credit quality of the underlying counterparties (loan customers).

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In accordance with ASU 2011-4, the following table provides information related to quantitative inputs and assumptions used in Level 3 fair value measurements.

	Fair Value (dollars in thousands)		Valuation Technique	Unobservable Inputs	Range / (weighted average)
Pooled Trust Preferred Securities	$ 33,723		Discounted Cash Flow	Probability of default	0% - 100% (11.47%)
				Prepayment rates	0% - 73.03% (5.14%)
				Discount rates	5.50% - 12.50% (a)
Equities	1,670		Par Value	N/A	N/A
Impaired Loans	2,414	(b)	Reserve study	Discount rate	10.00%
				Gas per MCF	$1.63 - $3.38 (c)
				Oil per BBL/d	$40.97 - $56.16 (c)
	6,815	(b)	Discounted Cash Flow	Discount Rate	1.90% - 4.68%
Limited Partnership Investments	704		Par Value	N/A	N/A

(a) Incorporates spread over risk free rate related primarily to credit quality and illiquidity of securities.
(b) The remainder of impaired loans valued using Level 3 inputs are not included in this disclosure as the values of those loans are based on bankruptcy agreement documentation.
(c) Unobservable inputs are defined as follows: MCF - million cubic feet; BBL/d - barrels per day.

The significant unobservable inputs used in the fair value measurement of pooled trust preferred securities are the probability of default, discount rates and prepayment rates. Significant increases in the probability of default or discount rate used would result in a decrease in the estimated fair value of these securities, while decreases in these variables would result in higher fair value measurements. In general, a change in the assumption of probability of default is accompanied by a directionally similar change in the discount rate. In most cases, increases in the prepayment rate assumptions would result in a higher estimated fair value for these securities while decreases would provide for a lower value. The direction of this change is somewhat dependent on the structure of the investment and the amount of the investment tranches senior to our position.

The discount rate is the significant unobservable input used in the fair value measurement of impaired loans. Significant increases in this rate would result in a decrease in the estimated fair value of the loans, while a decrease in this rate would result in a higher fair value measurement. Other unobservable inputs in the fair value measurement of impaired loans relate to gas, oil and natural gas prices. Increases in these prices would result in an increase in the estimated fair value of the loans, while a decrease in these prices would result in a lower fair value measurement.

ITEM 1. Financial Statements and Supplementary Data
FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES
NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The tables below present the balances of assets and liabilities measured at fair value on a recurring basis:

	June 30, 2016			
	Level 1	Level 2	Level 3	Total
	(dollars in thousands)			
Obligations of U.S. Government Agencies:				
Mortgage-Backed Securities - Residential	$—	$18,762	$—	$18,762
Obligations of U.S. Government-Sponsored Enterprises:				
Mortgage-Backed Securities - Residential	—	747,396	—	747,396
Mortgage-Backed Securities - Commercial	—	2	—	2
Other Government-Sponsored Enterprises	—	19,322	—	19,322
Obligations of States and Political Subdivisions	—	28,036	—	28,036
Corporate Securities	—	6,422	—	6,422
Pooled Trust Preferred Collateralized Debt Obligations	—	—	33,723	33,723
Total Debt Securities	—	819,940	33,723	853,663
Equities	—	—	1,670	1,670
Total Securities Available for Sale	—	819,940	35,393	855,333
Other Investments	—	58,087	—	58,087
Loans held for sale	—	11,613	—	11,613
Other Assets(a)	—	22,382	704	23,086
Total Assets	$—	$912,022	$36,097	$948,119
Other Liabilities(a)	$—	$21,405	$—	$21,405
Total Liabilities	$—	$21,405	$—	$21,405

(a) Hedging and non-hedging interest rate derivatives

	December 31, 2015			
	Level 1	Level 2	Level 3	Total
	(dollars in thousands)			
Obligations of U.S. Government Agencies:				
Mortgage-Backed Securities - Residential	$—	$22,092	$—	$22,092
Obligations of U.S. Government-Sponsored Enterprises:				
Mortgage-Backed Securities - Residential	—	777,577	—	777,577
Mortgage-Backed Securities - Commercial	—	28	—	28
Other Government-Sponsored Enterprises	—	19,118	—	19,118
Obligations of States and Political Subdivisions	—	27,598	—	27,598
Corporate Securities	—	2,319	—	2,319
Pooled Trust Preferred Collateralized Debt Obligations	—	—	35,658	35,658
Total Debt Securities	—	848,732	35,658	884,390
Equities	—	—	2,170	2,170
Total Securities Available for Sale	—	848,732	37,828	886,560
Other Investments	—	62,952	—	62,952
Loans held for sale	—	5,763	—	5,763
Other Assets(a)	—	11,273	—	11,273
Total Assets	$—	$928,720	$37,828	$966,548
Other Liabilities(a)	$—	$10,829	$—	$10,829
Total Liabilities	$—	$10,829	$—	$10,829

(a) Hedging and non-hedging interest rate derivatives

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ITEM 1. Financial Statements and Supplementary Data
FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES
NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

For the six months ended June 30, changes in Level 3 assets and liabilities measured at fair value on a recurring basis are summarized as follows:

	2016 Pooled Trust Preferred Collateralized Debt Obligations	Equities	Other Assets	Total
	(dollars in thousands)			
Balance, beginning of period	$35,658	$2,170	$ —	$37,828
Total gains or losses				
Included in earnings	—	—	—	—
Included in other comprehensive income	(1,905)	—	—	(1,905)
Purchases, issuances, sales and settlements				
Purchases	—	36	168	204
Issuances	—	—	—	—
Sales	—	—	—	—
Settlements	(30)	—	—	(30)
Transfers from Level 3	—	(536)	—	(536)
Transfers into Level 3	—	—	536	536
Balance, end of period	$33,723	$1,670	$ 704	$36,097

	2015 Pooled Trust Preferred Collateralized Debt Obligations	Equities	Total
	(dollars in thousands)		
Balance, beginning of period	$28,999	$ 1,420	$30,419
Total gains or losses			
Included in earnings	105	—	105
Included in other comprehensive income	7,471	—	7,471
Purchases, issuances, sales and settlements			
Purchases	—	500	500
Issuances	—	—	—
Sales	—	—	—
Settlements	(1,054)	—	(1,054)
Transfers into Level 3	—	—	—
Balance, end of period	$35,521	$ 1,920	$37,441

During the six months ended June 30, 2016, $0.5 million in investments in limited partnerships were moved from other equity securities to other assets constituting the transfers into and out of Level 3. During the six months ended June 30, 2015, there were no transfers between fair value Levels 1, 2 or 3. There were no gains or losses included in earnings for the periods presented that are attributable to the change in realized gains (losses) relating to assets held at

June 30, 2016 and 2015.

ITEM 1. Financial Statements and Supplementary Data
FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES
NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

For the three months ended June 30, changes in Level 3 assets and liabilities measured at fair value on a recurring basis are summarized as follows:

	2016			
	Pooled Trust Preferred Collateralized Debt Obligations	Equities	Other Assets	Total
	(dollars in thousands)			
Balance, beginning of period	$33,273	$2,206	$ —	$35,479
Total gains or losses				
Included in earnings	—	—	—	—
Included in other comprehensive income	480	—	—	480
Purchases, issuances, sales and settlements				
Purchases	—	—	168	168
Issuances	—	—	—	—
Sales	—	—	—	—
Settlements	(30)	—	—	(30)
Transfers from Level 3	—	(536)	—	(536)
Transfers into Level 3	—	—	536	536
Balance, end of period	$33,723	$1,670	$ 704	$36,097

	2015		
	Pooled Trust Preferred Collateralized Debt Obligations	Equities	Total
	(dollars in thousands)		
Balance, beginning of period	$31,134	$ 1,920	33,054
Total gains or losses			
Included in earnings	—	—	—
Included in other comprehensive income	4,851	—	4,851
Purchases, issuances, sales and settlements			
Purchases	—	—	—
Issuances	—	—	—
Sales	—	—	—
Settlements	(464)	—	(464)
Transfers into Level 3	—	—	—
Balance, end of period	$35,521	$ 1,920	$37,441

During the three months ended June 30, 2016, $0.5 million in investments in limited partnerships were moved from other equity securities to other assets constituting the transfers into and out of Level 3. During the three months ended June 30, 2015, there were no transfers between fair value Levels 1, 2 or 3. There were no gains or losses included in earnings for the periods presented that are attributable to the change in realized gains (losses) relating to assets held at June 30, 2016 and 2015.

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ITEM 1. Financial Statements and Supplementary Data
FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES
NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The tables below present the balances of assets measured at fair value on a nonrecurring basis at:

	June 30, 2016			
	Level 1	Level 2	Level 3	Total
	(dollars in thousands)			
Impaired loans	$—	$30,774	$18,104	$48,878
Other real estate owned	—	10,036	—	10,036
Total Assets	$—	$40,810	$18,104	$58,914

	December 31, 2015			
	Level 1	Level 2	Level 3	Total
	(dollars in thousands)			
Impaired loans	$—	$30,979	$12,820	$43,799
Other real estate owned	—	10,039	8	10,047
Total Assets	$—	$41,018	$12,828	$53,846

The following losses were realized on the assets measured on a nonrecurring basis:

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2016	2015	2016	2015
	(dollars in thousands)			
Impaired loans	$(6,991)	$(382)	$(14,576)	$(843)
Other real estate owned	(245)	(1,126)	(258)	(1,154)
Total losses	$(7,236)	$(1,508)	$(14,834)	$(1,997)

Impaired loans over $100 thousand are individually reviewed to determine the amount of each loan considered to be at risk of non-collection. The fair value for impaired loans that are collateral based is determined by reviewing real property appraisals, equipment valuations, accounts receivable listings and other financial information. A discounted cash flow analysis is performed to determine fair value for impaired loans when an observable market price or a current appraisal is not available. For real estate secured loans, First Commonwealth's loan policy requires updated appraisals be obtained at least every twelve months on all impaired loans with balances of $250 thousand and over. For real estate secured loans with balances under $250 thousand, we rely on broker price opinions. For non-real estate secured assets, the Company normally relies on third party valuations specific to the collateral type.

The fair value for other real estate owned, determined by either an independent market-based appraisal less estimated costs to sell or an executed sales agreement, is classified as Level 2. The fair value for other real estate owned determined using an internal valuation is classified as Level 3. Other real estate owned has a current carrying value of $8.6 million as of June 30, 2016 and consists primarily of commercial real estate properties in Pennsylvania. We review whether events and circumstances subsequent to a transfer to other real estate owned have occurred that indicate the balance of those assets may not be recoverable. If events and circumstances indicate further impairment we will record a charge to the extent that the carrying value of the assets exceed their fair values, less estimated cost to sell, as determined by valuation techniques appropriate in the circumstances.

Certain other assets and liabilities, including goodwill and core deposit intangibles, are measured at fair value on a nonrecurring basis; that is, the instruments are not measured at fair value on an ongoing basis but are subject to fair value adjustments only in certain circumstances. Additional information related to goodwill is provided in Note 12, "Goodwill." There were no other assets or liabilities measured at fair value on a nonrecurring basis during the six months ended June 30, 2016.

FASB ASC 825-10, "Transition Related to FSP FAS 107-1" and APB 28-1, "Interim Disclosures about Fair Value of Financial Instruments," requires disclosure of the fair value of financial assets and financial liabilities, including those financial assets and financial liabilities that are not measured and reported at fair value on a recurring basis or nonrecurring basis. The methodologies for estimating the fair value of financial assets and financial liabilities that are measured at fair value on a recurring or nonrecurring basis are as discussed above. The methodologies for other financial assets and financial liabilities are discussed below.

ITEM 1. Financial Statements and Supplementary Data
FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES
NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Cash and due from banks and interest-bearing bank deposits: The carrying amounts for cash and due from banks and interest-bearing bank deposits approximate the estimated fair values of such assets.
Securities: Fair values for securities available for sale and held to maturity are based on quoted market prices, if available. If quoted market prices are not available, fair values are based on quoted market prices of comparable instruments. Pooled trust preferred collateralized debt obligations values are derived from other valuation methodologies, including option pricing models, discounted cash flow models and similar techniques, and not based on market exchange, dealer or broker traded transactions. These valuations incorporate certain assumptions and projections in determining the fair value assigned to each instrument. The carrying value of other investments, which includes FHLB stock, is considered a reasonable estimate of fair value.
Loans: The fair values of all loans are estimated by discounting the estimated future cash flows using interest rates currently offered for loans with similar terms to borrowers of similar credit quality adjusted for past due and nonperforming loans, which is not an exit price under FASB ASC Topic 820, “Fair Value Measurements and Disclosures.”
Loans Held for Sale: The estimated fair value of loans held for sale is based on market bids obtained from potential buyers.
Off-balance sheet instruments: Many of First Commonwealth’s off-balance sheet instruments, primarily loan commitments and standby letters of credit, are expected to expire without being drawn upon; therefore, the commitment amounts do not necessarily represent future cash requirements. FASB ASC Topic 460, “Guarantees” clarified that a guarantor is required to recognize, at the inception of a guarantee, a liability for the fair value of the obligation undertaken in issuing the guarantee. The carrying amount and fair value for standby letters of credit was $0.2 million and $0.2 million at June 30, 2016 and December 31, 2015, respectively. See Note 5, “Commitments and Contingent Liabilities,” for additional information.
Deposit liabilities: The estimated fair value of demand deposits, savings accounts and money market deposits is the amount payable on demand at the reporting date because of the customers’ ability to withdraw funds immediately. The carrying value of variable rate time deposit accounts and certificates of deposit approximate their fair values at the report date. Also, fair values of fixed rate time deposits for both periods are estimated by discounting the future cash flows using interest rates currently being offered and a schedule of aggregated expected maturities.
Short-term borrowings: The fair values of borrowings from the FHLB were estimated based on the estimated incremental borrowing rate for similar types of borrowings. The carrying amounts of other short-term borrowings such as federal funds purchased and securities sold under agreement to repurchase were used to approximate fair value due to the short-term nature of the borrowings.
Long-term debt and subordinated debt: The fair value of long-term debt and subordinated debt is estimated by discounting the future cash flows using First Commonwealth’s estimate of the current market rate for similar types of borrowing arrangements or an announced redemption price.

ITEM 1. Financial Statements and Supplementary Data
FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES
NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The following table presents carrying amounts and fair values of First Commonwealth's financial instruments:

	June 30, 2016				
		Fair Value Measurements Using:			
	Carrying Amount	Total	Level 1	Level 2	Level 3
	(dollars in thousands)				
Financial assets					
Cash and due from banks	$68,163	$68,163	$68,163	$ —	$ —
Interest-bearing deposits	30,457	30,457	30,457	—	—
Securities available for sale	855,333	855,333	—	819,940	35,393
Securities held to maturity	405,976	414,770	—	414,770	—
Other investments	58,087	58,087	—	58,087	—
Loans held for sale	11,613	11,613	—	11,613	—
Loans	4,843,776	4,857,127	—	30,774	4,826,353
Financial liabilities					
Deposits	4,394,520	4,395,297	—	4,395,297	—
Short-term borrowings	1,464,687	1,464,408	—	1,464,408	—
Subordinated debt	72,167	61,427	—	—	61,427
Long-term debt	9,034	10,077	—	10,077	—

	December 31, 2015				
		Fair Value Measurements Using:			
	Carrying Amount	Total	Level 1	Level 2	Level 3
	(dollars in thousands)				
Financial assets					
Cash and due from banks	$66,644	$66,644	$66,644	$ —	$ —
Interest-bearing deposits	2,808	2,808	2,808	—	—
Securities available for sale	886,560	886,560	—	848,732	37,828
Other investments	62,952	62,952	—	62,952	—
Loans held for sale	5,763	5,763	—	5,763	—
Loans	4,683,750	4,690,852	—	30,979	4,659,873
Financial liabilities					
Deposits	4,195,894	4,198,817	—	4,198,817	—
Short-term borrowings	1,510,825	1,510,718	—	1,510,718	—
Subordinated debt	72,167	62,794	—	—	62,794
Long-term debt	9,314	9,834	—	9,834	—

Note 11 Derivatives

Derivatives Not Designated as Hedging Instruments

First Commonwealth is a party to interest rate derivatives that are not designated as hedging instruments. These derivatives relate to interest rate swaps that First Commonwealth enters into with customers to allow customers to convert variable rate loans to a fixed rate. First Commonwealth pays interest to the customer at a floating rate on the notional amount and receives interest from the customer at a fixed rate for the same notional amount. At the same time the interest rate swap is entered into with the customer, an offsetting interest rate swap is entered into with another financial institution. First Commonwealth pays the other financial institution interest at the same fixed rate on the same notional amount as the swap entered into with the customer, and receives interest from the financial institution for the same floating rate on the same notional amount.

ITEM 1. Financial Statements and Supplementary Data
FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES
NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The changes in the fair value of the swaps offset each other, except for the credit risk of the counterparties, which is determined by taking into consideration the risk rating, probability of default and loss given default for all counterparties.

We have 22 risk participation agreements with financial institution counterparties for interest rate swaps related to loans in which we are a participant. The risk participation agreements provide credit protection to the financial institution should the borrower fail to perform on its interest rate derivative contract with the financial institution. We have seven risk participation agreements with financial institution counterparties for interest rate swaps related to loans in which we are the lead bank. The risk participation agreement provides credit protection to us should the borrower fail to perform on its interest rate derivative contract with us.

First Commonwealth is also party to interest rate caps that are not designated as hedging instruments. These derivatives relate to contracts that First Commonwealth enters into with loan customers that provide a maximum interest rate on their variable rate loan. At the same time the interest rate cap is entered into with the customer, First Commonwealth enters into an offsetting interest rate cap with another financial institution. The notional amount and maximum interest rate on both interest cap contracts are identical.

The fee received, less the estimate of the loss for the credit exposure, was recognized in earnings at the time of the transaction.

Derivatives Designated as Hedging Instruments

The Company has entered into four interest rate swap contracts that were designated as cash flow hedges. The interest rate swaps have a total notional amount of $200.0 million, $85.0 million with an original maturity of three years and $115.0 million with and original maturity of four years. The Company's risk management objective for these hedges is to reduce its exposure to variability in expected future cash flows related to interest payments on commercial loans benchmarked to the 1-month LIBOR rate. Therefore, the interest rate swaps convert the interest payments on the first $200.0 million of 1-month LIBOR based commercial loans into fixed rate payments.

The periodic net settlement of interest rate swaps is recorded as an adjustment to "Interest and fees on loans" in the Condensed Consolidated Statements of Income. For the three and six months ended June 30, 2016, there was a $0.9 million impact on interest income as a result of these interest rate swaps. Changes in the fair value of the effective portion of cash flow hedges are reported in OCI. When the cash flows associated with the hedged item are realized, the gain or loss included in OCI is recognized in "Interest and fees on loans," the same line item in the Condensed Consolidated Statements of Income as the income on the hedged items. The cash flow hedges were highly effective at June 30, 2016, and December 31, 2015, and changes in the fair value attributed to hedge ineffectiveness were not material.

The following table depicts the credit value adjustment recorded related to the notional amount of derivatives outstanding as well as the notional amount of risk participation agreements participated to other banks:

	June 30, 2016	December 31, 2015
	(dollars in thousands)	
Derivatives not Designated as Hedging Instruments		
Credit value adjustment	$(2,075)	$ (542)
Notional Amount:		
Interest rate derivatives	324,630	276,860
Interest rate caps	21,168	22,793
Risk participation agreements	164,850	126,612
Sold credit protection on risk participation agreements	(35,786)	(20,383)
Derivatives Designated as Hedging Instruments		
Fair value adjustment	(3,015)	922

Notional Amount - Interest rate derivatives	200,000	200,000

ITEM 1. Financial Statements and Supplementary Data
FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES
NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The table below presents the amount representing the change in the fair value of derivative assets and derivative liabilities attributable to credit risk included in "Other income" on the Condensed Consolidated Statements of Income:

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2016	2015	2016	2015
	(dollars in thousands)			
Non-hedging interest rate derivatives				
(Decrease) increase in other income	$(531)	$593	$(1,545)	$363
Hedging interest rate derivatives				
Increase in interest and fees on loans	424	557	854	938
Increase in other expense	26	12	41	21

The fair value of our derivatives is included in a table in Note 18, “Fair Values of Assets and Liabilities,” in the line items
“Other assets” and “Other liabilities.”

Note 12 Goodwill

FASB ASC Topic 350-20, “Intangibles – Goodwill and Other” requires an annual valuation of the fair value of a reporting unit that has goodwill and a comparison of the fair value to the book value of equity to determine whether the goodwill has been impaired. Goodwill is also required to be tested on an interim basis if an event or circumstance indicates that it is more likely than not that an impairment loss has been incurred. When triggering events or circumstances indicate that goodwill testing is required, an assessment of qualitative factors can be completed before performing the two step goodwill impairment test. ASU 2011-8 provides that if an assessment of qualitative factors determines it is more likely than not that the fair value of a reporting unit exceeds its carrying amount, then the two step goodwill impairment test is not required.

We consider First Commonwealth to be one reporting unit. The carrying amount of goodwill as of June 30, 2016 and December 31, 2015 was $164.5 million. No impairment charges on goodwill or other intangible assets were incurred in 2016 or 2015.

We test goodwill for impairment as of November 30th each year and again at any quarter-end if any material events occur during a quarter that may affect goodwill.

As of June 30, 2016, goodwill was not considered impaired; however, changing economic conditions that may adversely affect our performance, the fair value of our assets and liabilities, or our stock price could result in impairment, which could adversely affect earnings in future periods. Management will continue to monitor events that could impact this conclusion in the future.

Note 13 New Accounting Pronouncements

In August 2015, the FASB issued ASU No. 2015-14, “Revenue from Contracts with Customers (Topic 606).” In May 2014, the FASB issued ASU No. 2014-09, "Revenue from Contracts with Customers (Topic 606)," with an original effective date for annual reporting periods beginning after December 15, 2016. The core principle of ASU 2014-09 is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. ASU 2015-14 deferred the effective date of ASU 2014-09 to annual periods and interim periods within those annual periods beginning after December 15, 2017. We are currently evaluating the potential impact of ASU 2015-14 on our financial statements.

In January 2016, the FASB issued ASU No. 2016-01, "Financial Instruments - Overall (Subtopic 825-10)," which addresses certain aspects of recognition, measurement, presentation and disclosure of financial instruments. This ASU addresses: 1. requiring equity investments to be measured at fair value, recognizing the changes in fair value through net income; 2. simplifying the impairment assessment of equity investments without readily determinable fair values by requiring a qualitative assessment to identify impairment; 3. eliminating the requirement to disclose the fair value of financial instruments measured at amortized cost for entities that are not public entities; 4. eliminating the requirement for public entities to disclose the methods and significant assumptions used to estimate the fair value of financial instruments measured at amortized cost; 5. requiring public entities to use the exit price notion when measuring the fair value of financial instruments; 6. requiring and entity to present separately in other comprehensive income the portion of the total change in the fair value of a liability resulting from a change in instrument-specific credit risk when the entity has elected to measure the liability at fair value in accordance with the fair value option for financial instruments; 7. requiring separate presentation of financial assets and financial liabilities by measurement category and form of financial asset on the balance sheet or in the accompanying notes to the financial statements; and 8. clarifying that an entity should evaluate the need for a valuation allowance on a deferred tax asset related to available-for-sale securities in combination with the entity's other deferred tax assets. This ASU is effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2017 for public entities and for fiscal years beginning after December 15, 2018 for entities that are not public entities. The adoption of this ASU is not expected to have a material impact on First Commonwealth’s financial condition or results of operations.

In February 2016, the FASB issued ASU No. 2016-02, "Leases (Topic 842)," in order to increase transparency and comparability among organizations by recognizing lease assets and lease liabilities on the balance sheet and disclosing key information about leasing arrangements. Lessor accounting under the new guidance remains largely unchanged as it is substantially equivalent to existing guidance for sales-type leases, direct financing leases, and operating leases. Leveraged leases have been eliminated, although lessors can continue to account for existing leveraged leases using the current accounting guidance. Other limited changes were made to align lessor accounting with the lessee accounting model and the new revenue recognition standard. All entities will classify leases to determine how to recognize lease-related revenue and expense. Quantitative and qualitative disclosures will be required by lessees and lessors to meet the objective of enabling users of financial statements to assess the amount, timing, and uncertainty of cash flows arising from leases. The intention is to require enough information to supplement the amounts recorded in the financial statements so that users can understand more about the nature of an entity’s leasing activities. This ASU is effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2018. All entities are required to use a modified retrospective approach for leases that exist or are entered into after the beginning of the earliest comparative period in the financial statements. Entities have the option to use certain relief; full retrospective application is prohibited. Management has not yet evaluated the impact of the ASU on First Commonwealth's financial condition or results of operations and will be monitoring developments and additional guidance closely to determine the potential impact of the new standard.

In March 2016, FASB issued ASU No. 2016-05, "Derivatives and Hedging (Topic 815)," which clarifies that a change in the counterparty to a derivative instrument that has been designated as the hedging instrument under Topic 815 does not, in and of itself, require dedesignation of that hedging relationship provided that all other hedge accounting criteria continue to be met. This ASU is effective for public entities beginning after December 15, 2016, and interim periods within those fiscal years. The adoption of this ASU is not expected to have a material impact on First Commonwealth’s financial condition or results of operations.

In March 2016, FASB issued ASU No. 2016-09, “Compensation - Stock Compensation (Topic 718) - Improvements to Employee Share-Based Payment Accounting.” This update requires all income tax effects of awards to be recognized in the income statement when the awards vest or are settled. It also allows an employer to repurchase more of an employee’s shares than it can today for tax withholding purposes without triggering liability accounting and to make a policy election for forfeitures as they occur. The guidance is effective for public business entities for fiscal years beginning after December 15, 2016, and interim periods within those years. Early adoption is permitted. The adoption of this ASU is not expected to have a material impact on First Commonwealth’s financial condition or results of operations.

In June 2016, the FASB issued ASU No. 2016-13, “Financial Instruments – Credit Losses (Topic 326), Measurement of Credit Losses on Financial Instruments,” which amends the guidance for recognizing credit losses from an “incurred loss” methodology that delays recognition of credit losses until it is probable a loss has been incurred to an expected credit loss methodology. The guidance requires the use of the modified retrospective transition method by means of a cumulative-effect adjustment to equity as of the beginning of the period in which the guidance is adopted. The standard is effective for the Company as of January 1, 2020. Management is currently evaluating the impact of the amended guidance on First Commonwealth's financial condition or results of operations.

Note 14 Subsequent Event

On July 27, 2016, the Company announced that it had reached an agreement with FirstMerit Bank, NA to acquire 13 retail branches in Canton and Ashtabula, Ohio with approximately $735 million of deposits and $115 million of performing retail and business loans. This transaction is subject to regulatory approval and is expected to close in the fourth quarter of 2016.

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ITEM 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations
FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES
This discussion and the related financial data are presented to assist in the understanding and evaluation of the consolidated financial condition and the results of operations of First Commonwealth Financial Corporation including its subsidiaries (“First Commonwealth”) for the three and six months ended June 30, 2016 and 2015, and should be read in conjunction with the Condensed Consolidated Financial Statements and notes thereto included in this Form 10-Q.
Forward-Looking Statements
Certain statements contained in this report that are not historical facts may constitute “forward-looking statements” within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended (the “Exchange Act”), and are intended to be covered by the safe harbor provisions of the Private Securities Litigation Reform Act of 1995, notwithstanding that such statements are not specifically identified as such. In addition, certain statements may be contained in our future filings with the Securities and Exchange Commission, in press releases, and in oral and written statements made by us or with our approval that are not statements of historical fact and constitute “forward-looking statements” as well. These statements, which are based on certain assumptions and describe our future plans, strategies and expectations, can generally be identified by the use of words such as “may,” “will,” “should,” “could,” “would,” “plan,” “believe,” “expect,” “anticipate,” “intend,” “estimate” similar meaning. These forward-looking statements are subject to significant risks, assumptions and uncertainties, and could be affected by many factors, including, but not limited to: (1) local, regional, national and international economic conditions and the impact they may have on First Commonwealth and its customers; (2) volatility and disruption in national and international financial markets; (3) the effects of and changes in trade and monetary and fiscal policies and laws, including the interest rate policies of the Federal Reserve Board; (4) inflation, interest rate, commodity price, securities market and monetary fluctuations; (5) the effect of changes in laws and regulations (including laws and regulations concerning taxes, banking, securities and insurance) with which First Commonwealth or its customers must comply; (6) the soundness of other financial institutions; (7) political instability; (8) impairment of First Commonwealth’s goodwill or other intangible assets; (9) acts of God or of war or terrorism; (10) the timely development and acceptance of new products and services and perceived overall value of these products and services by users; (11) changes in consumer spending, borrowings and savings habits; (12) changes in the financial performance and/or condition of First Commonwealth’s borrowers; (13) technological changes; (14) acquisitions and integration of acquired businesses; (15) First Commonwealth’s ability to attract and retain qualified employees; (16) changes in the competitive environment in First Commonwealth’s markets and among banking organizations and other financial service providers; (17) the ability to increase market share and control expenses; (18) 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; (19) the reliability of First Commonwealth’s vendors, internal control systems or information systems; (20) the costs and effects of legal and regulatory developments, the resolution of legal proceedings or regulatory or other governmental inquiries, the results of regulatory examinations or reviews and the ability to obtain required regulatory approvals; and (21) other risks and uncertainties described in this report and in the other reports that we file with the Securities and Exchange Commission, including our most recent Annual Report on Form 10-K.
In light of these risks, uncertainties and assumptions, you should not place undue reliance on any forward-looking statements in this report. We undertake no obligation to publicly update or otherwise revise any forward-looking statements, whether as a result of new information, future events or otherwise.
Explanation of Use of Non-GAAP Financial Measure
In addition to the results of operations presented in accordance with generally accepted accounting principles (“GAAP”), First Commonwealth management uses, and this quarterly report contains or references, certain non-GAAP financial measures, such as net interest income on a fully taxable equivalent basis. We believe this non-GAAP financial measure provides information useful to investors in understanding our underlying operational performance and our business and performance trends as it facilitates comparison with the performance of others in the financial services

industry. Although we believe that this non-GAAP financial measure enhances investors' understanding of our business and performance, this non-GAAP financial measure should not be considered an alternative to GAAP.

We believe the presentation of net interest income on a fully taxable equivalent basis ensures comparability of net interest income arising from both taxable and tax-exempt sources and is consistent with industry practice. Interest income per the Condensed Consolidated Statements of Income is reconciled to net interest income adjusted to a fully taxable equivalent basis on pages 43 and 50 for the six and three months ended June 30, 2016 and 2015, respectively.

ITEM 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations (Continued)
FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES

Selected Financial Data

The following selected financial data should be read in conjunction with Management’s Discussion and Analysis of Financial Condition and Results of Operations, which follows, and with the Condensed Consolidated Financial Statements and related notes.

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
	2016	2015	2016	2015
	(dollars in thousands, except per share data)			
Net Income	$12,007	$13,447	$24,480	$27,668
Per Share Data:				
Basic Earnings per Share	$0.14	$0.15	$0.28	$0.31
Diluted Earnings per Share	0.14	0.15	0.28	0.31
Cash Dividends Declared per Common Share	0.07	0.07	0.14	0.14
Average Balance:				
Total assets	$6,707,132	$6,361,156	$6,662,363	$6,359,781
Total equity	739,513	712,110	734,933	715,195
End of Period Balance:				
Net loans			$4,795,568	$4,455,327
Total assets			6,749,821	6,316,728
Total deposits			4,394,520	4,210,107
Total equity			741,786	711,206
Key Ratios:				
Return on average assets	0.72 %	0.85 %	0.74 %	0.88 %
Return on average equity	6.53 %	7.57 %	6.70 %	7.80 %
Dividends payout ratio	50.00 %	46.67 %	50.00 %	45.16 %
Average equity to average assets ratio	11.03 %	11.19 %	11.03 %	11.25 %
Net interest margin	3.27 %	3.26 %	3.28 %	3.30 %
Net loans to deposits ratio			109.13 %	105.82 %

Results of Operations

Six Months Ended June 30, 2016 Compared to Six Months Ended June 30, 2015

Net Income

For the six months ended June 30, 2016, First Commonwealth had net income of $24.5 million, or $0.28 diluted earnings per share, compared to net income of $27.7 million, or $0.31 diluted earnings per share, in the six months ended June 30, 2015. The decrease in net income was primarily the result of an increase in the provision for loan losses, partially offset by an increase in net interest income and a decrease in other expenses.

For the six months ended June 30, 2016, the Company’s return on average equity was 6.70% and its return on average assets was 0.74%, compared to 7.80% and 0.88%, respectively, for the six months ended June 30, 2015.

Net Interest Income

Net interest income, on a fully taxable equivalent basis, was $99.8 million in the first six months of 2016, compared to $95.2 million for the same period in 2015. This increase was primarily due to growth in average interest earning assets of $303.0 million. Net interest income comprises a majority of our operating revenue (net interest income before provision expense plus noninterest income), at 77% and 75% for the six months ended June 30, 2016 and 2015, respectively.

The net interest margin, on a fully taxable equivalent basis, was 3.28% and 3.30% for the six months ended June 30, 2016 and June 30, 2015, respectively. The two basis point decline in the net interest margin is attributable to an increase in the overall cost of interest bearing liabilities.

The taxable equivalent yield on interest-earning assets was 3.59% for the six months ended June 30, 2016, an increase of two basis points compared to the 3.57% yield for the same period in 2015. Excluding the impact of a special FHLB dividend in the first quarter of 2015, the yield on interest-earning assets would have increased by four basis points. This increase is largely due to the investment portfolio yield, which, after excluding the impact of the $1.0 million special FHLB dividend, improved by 16 basis points when compared to the six months ended June 30, 2015. This increase can be attributed to the runoff or sale of lower yielding U.S. Agency securities which were replaced with higher yielding investment securities. Investment portfolio purchases during the six months ended June 30, 2016 have been primarily in mortgage-related assets with approximate durations of 48-60 months and municipal securities with durations of approximately five years. The mortgage-related investments have monthly principal payments that will provide for reinvestment opportunities if interest rates rise.

The cost of interest-bearing liabilities increased to 0.39% for the six months ended June 30, 2016, from 0.34% for the same period in 2015, primarily due to an increase in the cost of short-term borrowings. Offsetting that increase was an 11 basis point decline in the cost of time deposits, as higher cost time deposits ran off and were replaced with growth in noninterest-bearing demand deposits, interest bearing demand deposits and short-term borrowings.

For the six months ended June 30, 2016, changes in interest rates negatively impacted net interest income by $2.1 million when compared with the same period in 2015. The higher yield on interest-earning assets positively impacted net interest income by $0.2 million, while the increase in the cost of interest-bearing liabilities had a negative impact of $2.2 million. We have been able to partially mitigate the impact of low interest rates and the effect on net interest income through improving the mix of deposits and borrowed funds, growing the loan portfolio and increasing our investment yields by re-investing cash flow from runoff and from sales of lower-yielding investments.

While increases in the cost of interest-bearing liabilities compressed the net interest margin, increases in average interest-earning assets more than offset the effect on net interest income. Average earning assets for the six months ended June 30, 2016 increased $303.0 million, or 5%, compared to the same period in 2015. Average loans for the six months ended June 30, 2016 increased $300.6 million, or 7%, compared to the same period in 2015.

Changes in the volume of interest-earning assets and interest-bearing liabilities positively impacted net interest income by $6.7 million in the six months ended June 30, 2016, as compared to the same period in 2015. Higher levels of interest-earning assets resulted in an increase of $6.0 million in interest income, while changes in the volume of interest-bearing liabilities decreased interest expense by $0.6 million, primarily as the result of decreases in long-term debt and time deposits, including brokered deposits.

Net interest income also benefited from a $115.8 million increase in average net free funds at June 30, 2016 as compared to June 30, 2015. Average net free funds are the excess of noninterest-bearing demand deposits, other noninterest-bearing liabilities and shareholders' equity over noninterest-earning assets. The largest component of the increase in net free funds was an increase of $93.0 million, or 9.1%, in noninterest-bearing demand deposit average balances. Additionally, higher cost time deposits continue to mature and reprice into lower cost deposits or other funding alternatives. Average time deposits for the six months ended June 30, 2016 decreased by $155.0 million compared to the comparable period in 2015.

The following table reconciles interest income in the Condensed Consolidated Statements of Income to net interest income adjusted to a fully taxable equivalent basis for the six months ended June 30:

	2016	2015
	(dollars in thousands)	
Interest income per Condensed Consolidated Statements of Income	$107,203	$101,235
Adjustment to fully taxable equivalent basis	1,885	1,653
Interest income adjusted to fully taxable equivalent basis (non-GAAP)	109,088	102,888
Interest expense	9,305	7,693
Net interest income adjusted to fully taxable equivalent basis (non-GAAP)	$99,783	$95,195

ITEM 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (Continued)
FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES

The following is an analysis of the average balance sheets and net interest income on a fully taxable equivalent basis for the six months ended June 30:

	2016			2015		
	Average Balance	Income / Expense (a)	Yield or Rate	Average Balance	Income / Expense (a)	Yield or Rate
	(dollars in thousands)					
Assets						
Interest-earning assets:						
Interest-bearing deposits with banks	$5,096	$ 11	0.43 %	$4,385	$ 5	0.23 %
Tax-free investment securities	60,891	1,126	3.72	30,665	593	3.90
Taxable investment securities	1,260,138	15,728	2.51	1,288,712	15,594	2.44
Loans, net of unearned income (b)(c)	4,789,306	92,223	3.87	4,488,660	86,696	3.89
Total interest-earning assets	6,115,431	109,088	3.59	5,812,422	102,888	3.57
Noninterest-earning assets:						
Cash	67,728			66,028		
Allowance for credit losses	(54,701)			(50,870)		
Other assets	533,905			532,201		
Total noninterest-earning assets	546,932			547,359		
Total Assets	$6,662,363			$6,359,781		
Liabilities and Shareholders' Equity						
Interest-bearing liabilities:						
Interest-bearing demand deposits (d)	$728,404	$ 220	0.06 %	$652,583	$ 106	0.03 %
Savings deposits (d)	1,879,011	1,490	0.16	1,861,432	1,225	0.13
Time deposits	586,723	1,807	0.62	741,738	2,699	0.73
Short-term borrowings	1,475,233	4,335	0.59	1,172,957	2,074	0.36
Long-term debt	81,339	1,453	3.59	134,831	1,589	2.38
Total interest-bearing liabilities	4,750,710	9,305	0.39	4,563,541	7,693	0.34
Noninterest-bearing liabilities and shareholders' equity:						
Noninterest-bearing demand deposits (d)	1,117,159			1,024,197		
Other liabilities	59,561			56,848		
Shareholders' equity	734,933			715,195		
Total Noninterest-Bearing Funding Sources	1,911,653			1,796,240		
Total Liabilities and Shareholders' Equity	$6,662,363			$6,359,781		
Net Interest Income and Net Yield on Interest-Earning Assets		$ 99,783	3.28 %		$ 95,195	3.30 %

(a) Income on interest-earning assets has been computed on a fully taxable equivalent basis using the 35% federal income tax statutory rate.

(b) Loan balances include held for sale and nonaccrual loans. Income on nonaccrual loans is accounted for on the cash basis.

(c) Loan income includes loan fees earned.

(d) Average balances do not include reallocations from noninterest-bearing demand deposits and interest-bearing demand deposits into savings deposits, which were made for regulatory purposes.

ITEM 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (Continued)
FIRST COMMONWEALTH FINANCIAL CORPORATION AND SUBSIDIARIES

The following table shows the effect of changes in volumes and rates on interest income and interest expense for the six months ended June 30, 2016 compared with June 30, 2015:

	Analysis of Year-to-Year Changes in Net Interest Income		
	Total Change	Change Due To Volume	Change Due To Rate (a)
	(dollars in thousands)		
Interest-earning assets:			
Interest-bearing deposits with banks	$6	$ 1	$ 5
Tax-free investment securities	533	585	(52)
Taxable investment securities	134	(346)	480
Loans	5,527	5,800	(273)
Total interest income (b)	6,200	6,040	160
Interest-bearing liabilities:			
Interest-bearing demand deposits	114	11	103
Savings deposits	265	11	254
Time deposits	(892)	(561)	(331)
Short-term borrowings	2,261	540	