ENTERPRISE FINANCIAL SERVICES CORP
Form 10-Q
May 01, 2019

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 March 31, 2019.

[ ] 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 001-15373

ENTERPRISE FINANCIAL SERVICES CORP

Incorporated in the State of Delaware
I.R.S. Employer Identification # 43-1706259
Address: 150 North Meramec
Clayton, MO 63105
Telephone: (314) 725-5500

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months, 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 every Interactive Data File required to be submitted 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 such files). Yes [X] No [ ]

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

Large accelerated filer [X]	Accelerated filer [ ]
Non-accelerated filer [ ]	Smaller reporting company [ ]
	Emerging growth company [ ]

If an emerging growth company, indicate by check mark if the registrant has elected to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to section 13(a) of the Exchange Act. [ ]

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

As of April 26, 2019, the Registrant had 26,880,408 shares of outstanding common stock, $0.01 par value per share.

This document is also available through our website at http://www.enterprisebank.com.

ENTERPRISE FINANCIAL SERVICES CORP AND SUBSIDIARIES
TABLE OF CONTENTS

PART 1 - ITEM 1 - FINANCIAL STATEMENTS
ENTERPRISE FINANCIAL SERVICES CORP AND SUBSIDIARIES
Condensed Consolidated Balance Sheets (Unaudited)

(in thousands, except share and per share data)	March 31, 2019	December 31, 2018
Assets		
Cash and due from banks	$85,578	$91,511
Federal funds sold	1,934	1,714
Interest-earning deposits (including $6,665 and $1,305 pledged as collateral, respectively)	133,970	103,327
Total cash and cash equivalents	221,482	196,552
Interest-earning deposits greater than 90 days	3,485	3,185
Securities available for sale	1,099,185	721,369
Securities held to maturity, at cost	64,368	65,679
Loans held for sale	654	392
Loans	5,017,077	4,350,001
Less: Allowance for loan losses	43,095	43,476
Loans, net	4,973,982	4,306,525
Other real estate	6,804	469
Other investments, at cost	34,860	26,654
Fixed assets, net	60,301	32,109
Operating lease right-of-use asset	14,858	—
Accrued interest receivable	26,276	16,069
State tax credits held for sale, at cost	37,215	37,587
Goodwill	207,632	117,345
Intangible assets, net	31,048	8,553
Other assets	150,607	113,174
Total assets	$6,932,757	$5,645,662
Liabilities and Shareholders' Equity		
Demand deposits	$1,186,508	$1,100,718
Interest-bearing transaction accounts	1,389,826	1,037,684
Money market accounts	1,580,291	1,565,729
Savings	575,740	199,425
Certificates of deposit:		
Brokered	180,788	198,981
Other	623,960	485,448
Total deposits	5,537,113	4,587,985
Subordinated debentures and notes (net of debt issuance cost of $972 and $1,005, respectively)	140,668	118,156
Federal Home Loan Bank advances	180,466	70,000
Other borrowings	172,171	221,450
Notes payable	40,000	2,000
Operating lease liability	15,462	—
Accrued interest payable	3,231	1,977
Other liabilities	45,811	40,290
Total liabilities	6,134,922	5,041,858
Shareholders' equity:		
	—	—

Preferred stock, $0.01 par value; 5,000,000 shares authorized; 0 shares issued and outstanding		
Common stock, $0.01 par value; 30,000,000 shares authorized; 28,004,905 and 23,938,994 shares issued, respectively	280	239
Treasury stock, at cost; 1,127,105 shares	(42,655)	(42,655)
Additional paid in capital	521,761	350,936
Retained earnings	316,959	304,566
Accumulated other comprehensive income (loss)	1,490	(9,282)
Total shareholders' equity	797,835	603,804
Total liabilities and shareholders' equity	$6,932,757	$5,645,662

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

1

ENTERPRISE FINANCIAL SERVICES CORP AND SUBSIDIARIES
Condensed Consolidated Statements of Operations (Unaudited)

	Three months ended March 31,	
(in thousands, except per share data)	2019	2018
Interest income:		
Interest and fees on loans	$61,025	$50,450
Interest on debt securities:		
Taxable	5,475	3,987
Nontaxable	447	282
Interest on interest-bearing deposits	447	240
Dividends on equity securities	223	205
Total interest income	67,617	55,164
Interest expense:		
Interest-bearing transaction accounts	1,790	806
Money market accounts	6,515	3,353
Savings accounts	183	125
Certificates of deposit	3,332	1,899
Subordinated debentures and notes	1,648	1,368
Federal Home Loan Bank advances	1,398	1,258
Notes payable and other borrowings	408	184
Total interest expense	15,274	8,993
Net interest income	52,343	46,171
Provision for loan losses	1,476	1,871
Net interest income after provision for loan losses	50,867	44,300
Noninterest income:		
Service charges on deposit accounts	2,935	2,851
Wealth management revenue	1,992	2,114
Card services revenue	1,790	1,516
Gain on sale of other real estate	66	—
Tax credit activity, net	158	252
Miscellaneous income	2,289	2,809
Total noninterest income	9,230	9,542
Noninterest expense:		
Employee compensation and benefits	19,352	16,491
Occupancy	2,637	2,406
Data processing	1,906	1,467
Professional fees	746	849
FDIC and other insurance	848	917
Loan legal and other real estate expense	482	299
Merger related expenses	7,270	—
Other	6,597	6,714
Total noninterest expense	39,838	29,143
Income before income tax expense	20,259	24,699
Income tax expense	4,103	3,778
Net income	$16,156	$20,921

Earnings per common share		
Basic	$0.68	$0.91
Diluted	0.67	0.90

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

ENTERPRISE FINANCIAL SERVICES CORP AND SUBSIDIARIES
Condensed Consolidated Statements of Comprehensive Income (Unaudited)

	Three months ended March 31,	
(in thousands)	2019	2018
Net income	$16,156	$20,921
Other comprehensive income (loss), net of tax:		
Unrealized gains (losses) on investment securities arising during the period, net of income tax expense (benefit) for three months of $3,774 and $(2,265), respectively	11,504	(6,904)
Less: Reclassification adjustment for realized gains (losses) on sale of securities available for sale included in net income, net of income tax expense (benefit) for three months of ($72) and $2, respectively	220	(7)
Unrealized loss on cash flow hedges arising during the period, net of income tax benefit of $312	(952)	—
Total other comprehensive income (loss)	10,772	(6,911)
Total comprehensive income	$26,928	$14,010

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

ENTERPRISE FINANCIAL SERVICES CORP AND SUBSIDIARIES
Condensed Consolidated Statements of Shareholders' Equity (Unaudited)

(in thousands, except per share data)	Common Stock	Treasury Stock	Additional paid in capital	Retained earnings	Accumulated other comprehensive income (loss)	Total shareholders' equity
Balance at December 31, 2018	$ 239	$(42,655)	$350,936	$304,566	$ (9,282)	$603,804
Net income	—	—	—	16,156	—	16,156
Other comprehensive income	—	—	—	—	10,772	10,772
Total comprehensive income	—	—	—	16,156	10,772	26,928
Cash dividends paid on common shares, $0.14 per share	—	—	—	(3,763)	—	(3,763)
Issuance under equity compensation plans, 75,089 shares, net	1	—	(1,941)	—	—	(1,940)
Share-based compensation	—	—	921	—	—	921
Shares issued in connection with acquisition of Trinity Capital Corporation, 3,990,822 shares	40	—	171,845	—	—	171,885
Balance at March 31, 2019	$ 280	$(42,655)	$521,761	$316,959	$ 1,490	$797,835

(in thousands, except per share data)	Common Stock	Treasury Stock	Additional paid in capital	Retained earnings	Accumulated other comprehensive income (loss)	Total shareholders' equity
Balance at December 31, 2017	$ 238	$(23,268)	$350,061	$225,360	$ (3,818)	$548,573
Net income	—	—	—	20,921	—	20,921
Other comprehensive loss	—	—	—	—	(6,911)	(6,911)
Total comprehensive income (loss)	—	—	—	20,921	(6,911)	14,010
Cash dividends paid on common shares, $0.11 per share	—	—	—	(2,542)	—	(2,542)
Repurchase of common shares	—	(3,058)	—	—	—	(3,058)
Issuance under equity compensation plans, 86,598 shares, net	1	—	(2,687)	—	—	(2,686)
Share-based compensation	—	—	718	—	—	718
Reclassification adjustment for change in accounting policies	—	—	—	834	(834)	—
Balance at March 31, 2018	$ 239	$(26,326)	$348,092	$244,573	$ (11,563)	$555,015

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

ENTERPRISE FINANCIAL SERVICES CORP AND SUBSIDIARIES
Condensed Consolidated Statements of Cash Flows (Unaudited)

	Three months ended March 31,	
(in thousands, except share data)	2019	2018
Cash flows from operating activities:		
Net income	$ 16,156	$ 20,921
Adjustments to reconcile net income to net cash provided by operating activities		
Depreciation	1,162	849
Provision for loan losses	1,476	1,870
Deferred income taxes	2,727	2,290
Net amortization of debt securities	407	533
Amortization of intangible assets	838	656
Loss (gain) on sale of investment securities	292	(9)
Mortgage loans originated for sale	(4,087)	(12,389)
Proceeds from mortgage loans sold	3,825	13,917
Gain on sale of other real estate	(66)	—
Gain on state tax credits, net	(158)	(252)
Share-based compensation	921	718
Net accretion of loan discount	(596)	(467)
Changes in:		
Accrued interest receivable	(6,210)	(3,209)
Accrued interest payable	884	315
Other assets	(104)	(888)
Other liabilities	(1,755)	(2,640)
Net cash provided by operating activities	15,712	22,215
Cash flows from investing activities:		
Acquisition cash purchase price, net of cash and cash equivalents acquired	(23,376)	—
Net decrease (increase) in loans	13,855	(93,125)
Proceeds from the sale of securities, available for sale	259,420	1,451
Proceeds from the paydown or maturity of securities, available for sale	27,684	19,683

Proceeds from the paydown or maturity of securities, held to maturity	1,269	1,639
Proceeds from the redemption of other investments	11,744	13,514
Proceeds from the sale of state tax credits held for sale	2,381	1,356
Proceeds from the sale of other real estate	66	—
Payments for the purchase/origination of:		
Available for sale debt securities	(221,711)	(40,313)
Other investments	(14,977)	(17,864)
State tax credits held for sale	(1,852)	—
Fixed assets, net	(1,268)	(370)
Net cash provided by (used in) investing activities	53,235	(114,029)
Cash flows from financing activities:		
Net decrease in noninterest-bearing deposit accounts	(83,290)	(22,202)
Net (increase) decrease in interest-bearing deposit accounts	(48,770)	147,165
Proceeds from Federal Home Loan Bank advances	364,525	484,500
Repayments of Federal Home Loan Bank advances	(259,500)	(432,500)
Proceeds from notes payable	40,000	—
Repayments of notes payable	(2,000)	—
Net decrease in other borrowings	(49,279)	(87,085)
Cash dividends paid on common stock	(3,763)	(2,542)
Payments for the repurchase of common stock	—	(3,058)
Payments for the issuance of equity instruments, net	(1,940)	(2,686)
Net cash (used in) provided by financing activities	(44,017)	81,592
Net increase (decrease) in cash and cash equivalents	24,930	(10,222)
Cash and cash equivalents, beginning of period	196,552	153,323
Cash and cash equivalents, end of period	$ 221,482	$ 143,101

Supplemental disclosures of cash flow information:				
Cash paid during the period for:				
Interest	$	14,020	$	8,677
Income taxes	—		685	
Noncash transactions:				
Transfer to other real estate owned in settlement of loans	$	1,372	$	—
Common shares issued in connection with acquisition	171,885		—	

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

ENTERPRISE FINANCIAL SERVICES CORP AND SUBSIDIARIES
Notes to Condensed Consolidated Financial Statements (Unaudited)

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The significant accounting policies used by Enterprise Financial Services Corp (the "Company" or "Enterprise") in the preparation of the condensed consolidated financial statements are summarized below:

Business and Consolidation

Enterprise is a financial holding company that provides a full range of banking and wealth management services to individuals and corporate customers located in the Arizona, Kansas, Missouri, and New Mexico markets through its banking subsidiary, Enterprise Bank & Trust (the "Bank").

Operating results for the three months ended March 31, 2019 are not necessarily indicative of the results that may be expected for any other interim period or for the year ending December 31, 2019. For further information, refer to the consolidated financial statements and footnotes thereto included in the Company's Annual Report on Form 10-K for the year ended December 31, 2018, as filed with the Securities and Exchange Commission.

Basis of Financial Statement Presentation

The accompanying unaudited condensed consolidated financial statements of the Company and its subsidiaries have been prepared in accordance with the accounting principles generally accepted in the United States of America ("U.S. GAAP") for interim financial information and with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. The condensed consolidated financial statements include the accounts of the Company and its subsidiaries, all of which are wholly owned. All intercompany accounts and transactions have been eliminated.

In the opinion of management, the consolidated financial statements contain all adjustments (consisting of normal recurring accruals) considered necessary for the fair presentation of the statements of financial position, results of operations, and cash flow for the interim periods.

Recently Adopted Accounting Pronouncements

During the first quarter of 2019, the Company adopted Accounting Standards Update ("ASU") 2017-08, "Receivables - Nonrefundable Fees and Other Costs (Subtopic 310-20), Premium Amortization on Purchased Callable Debt Securities." ASU 2017-08 shortens the amortization period of certain callable debt securities held at a premium to the earliest call date. The adoption of this update did not have a material effect on the Company's consolidated financial statements.

The Company adopted ASU 2016-02 "Leases (Topic 842)" using the optional transition method effective on January 1, 2019. ASU 2016-02 requires organizations that lease assets to recognize the assets and liabilities for the rights and obligations created by leases. The Company recorded $15.5 million for right-to-use assets and $16.2 million for lease liabilities related to operating leases. The Company elected the practical expedients package which eliminates (1) the need to reassess whether any expired or existing contracts are or contain a lease, (2) the need to reassess the lease classification, and (3) the need to reassess initial direct costs for any existing leases. The Company also elected an accounting policy to not recognize assets and liabilities on leases 12 months or less, and an accounting policy for equipment and real estate leases to not separate nonlease components because the impact was immaterial.

Acquisitions

Acquisitions and business combinations are accounted for using the acquisition method of accounting. The assets and liabilities of the acquired entities have been recorded at their estimated fair values at the date of acquisition. Goodwill represents the excess of the purchase price over the fair value of net assets acquired, including the amount assigned to identifiable intangible assets.

The purchase price allocation process requires an estimation of the fair values of the assets acquired and the liabilities assumed. When a business combination agreement provides for an adjustment to the cost of the combination contingent on future events, the Company includes an estimate of the acquisition-date fair value as part of the cost of the combination. To determine the fair values, the Company relies on third party valuations, such as appraisals, or internal valuations based on discounted cash flow analyses or other valuation techniques. The results of operations of the acquired business are included in the Company's consolidated financial statements from the date of acquisition. Merger related costs are costs the Company incurs to effect a business combination. The Company presents merger related expenses as a separate component of Noninterest expenses on the Condensed Consolidated Statements of Operations. Merger related expenses include costs directly related to merger or acquisition activity and include legal and professional fees, system consolidation and conversion costs, gain or loss on sale of investment securities incurred through repositioning the acquired investment portfolio, and compensation costs such as severance and retention incentives for employees impacted by acquisition activity. The Company accounts for merger-related costs as expenses in the periods in which the costs are incurred and the services are received.

Revenue

The Company's revenues are primarily composed of interest income on financial instruments, including investment securities, which are excluded from the scope of the new guidance. Certain other noninterest income from loans, investment securities and derivative financial instruments is also excluded from this guidance. Service charges on deposit accounts, wealth management revenue, card services revenue, and gain on sale of other real estate are within the scope of the guidance; however, there were no accounting policy changes as the Company's policies were consistent with the new guidance. Other noninterest income sources of revenue are considered immaterial. Implementation of this guidance did not change current business practices or have any changes to the Company's consolidated financial statements.
Descriptions of our revenue-generating activities within the scope of this guidance, which are presented in our income statement as components of noninterest income are as follows:

- Service charges on deposit accounts - represents fees generated from a variety of deposit products and services provided to customers under a day-to-day contract. These fees are recognized on a daily or monthly basis.
- Wealth management revenue - represents monthly fees earned from directing, holding, and managing customers' assets. Revenue is recognized over regular intervals, either monthly or quarterly.
- Card services revenue - represents revenue earned from merchant, debit and credit cards as incurred and includes a contra revenue account for rebates.
- Gain on sale of other real estate - represents income recognized at delivery of control of a property at the time of a real estate closing.

Leases

We determine if an arrangement is a lease at inception. Operating leases are included in operating lease right-of-use ("ROU") assets on our consolidated balance sheet. ROU assets represent our right to use an underlying asset for the lease term and lease liabilities represent our obligation to make lease payments arising from the lease. Operating lease ROU assets and liabilities are recognized at commencement date based on the present value of lease payments over the lease term. We use our incremental borrowing rate based on the information available at commencement date in determining the present value of lease payments. The operating lease ROU asset also includes any lease payments made prior to commencement and excludes lease incentives. Our lease terms may include options to extend or terminate the lease when it is reasonably certain that we will exercise that option. Lease expense for lease payments is recognized on a straight-line basis over the lease term. We account for the lease and non-lease components as a single lease component.

Assumptions and judgments are used in applying ASC 842 and may include (1) the decision framework for identifying a lease, (2) the accounting policy election for equipment and real estate leases to not separate nonlease components, and (3) the discount rate for determining the initial present value of the lease payments which is based on information available at the commencement date for determining the lease term and assessing if optional periods are reasonably likely to be exercised. For the calculation at January 1, 2019, the discount rate was based on the remaining lease terms.

Derivative Instruments and Hedging Activities

FASB ASC 815, Derivatives and Hedging (“ASC 815”), provides the disclosure requirements for derivatives and hedging activities with the intent to provide users of financial statements with an enhanced understanding of: (a) how and why an entity uses derivative instruments, (b) how the entity accounts for derivative instruments and related hedged items, and (c) how derivative instruments and related hedged items affect an entity’s financial position, financial performance, and cash flows. Further, qualitative disclosures are required that explain the Company’s objectives and strategies for using derivatives, as well as quantitative disclosures about the fair value of and gains and losses on derivative instruments, and disclosures about credit-risk-related contingent features in derivative instruments.

As required by ASC 815, the Company records all derivatives on the balance sheet at fair value. The accounting for changes in the fair value of derivatives depends on the intended use of the derivative, whether the Company has elected to designate a derivative in a hedging relationship and apply hedge accounting and whether the hedging relationship has satisfied the criteria necessary to apply hedge accounting. Derivatives designated and qualifying as a hedge of the exposure to changes in the fair value of an asset, liability, or firm commitment attributable to a particular risk, such as interest rate risk, are considered fair value hedges. Derivatives designated and qualifying as a hedge of the exposure to variability in expected future cash flows, or other types of forecasted transactions, are considered cash flow hedges. Derivatives may also be designated as hedges of the foreign currency exposure of a net investment in a foreign operation. Hedge accounting generally provides for the matching of the timing of gain or loss recognition on the hedging instrument with the recognition of the changes in the fair value of the hedged asset or liability that are attributable to the hedged risk in a fair value hedge or the earnings effect of the hedged forecasted transactions in a cash flow hedge. The Company may enter into derivative contracts that are intended to economically hedge certain of its risk, even though hedge accounting does not apply, or the Company elects not to apply hedge accounting.

The Company does not offset derivative asset and liability positions. However, the Company's exposure to the credit risk of its derivative financial instruments is generally mitigated by master netting agreements with its counterparties.

The Alternative Reference Rates Committee ("ARRC") has proposed that the Secured Overnight Funding Rate ("SOFR") replace USD-LIBOR. ARRC has proposed that the transition to SOFR from USD-LIBOR will take place by the end of 2021. The Company has material contracts that are indexed to USD-LIBOR. Industry organizations are currently working on the transition plan. The Company is currently monitoring this activity and evaluating the risks involved.

NOTE 2 - ACQUISITION

Acquisition of Trinity Capital Corporation.
On March 8, 2019, the Company closed its acquisition of 100% of Trinity Capital Corporation (“Trinity”) and its wholly-owned subsidiary, Los Alamos National Bank (“LANB”). Trinity operated six full-service retail and commercial banking offices in Los Alamos, Santa Fe, and Albuquerque, New Mexico.

Trinity shareholders received cash consideration in an amount of $1.84 per share of Trinity common stock and 0.1972 shares of EFSC common stock per share of Trinity common stock with cash in lieu of fractional shares. Aggregate consideration at closing was 4.0 million shares of EFSC common stock and $37.3 million cash paid to Trinity shareholders. Based on EFSC’s closing stock price of $43.07 on March 7, 2019, the overall transaction had a value of $209.2 million. The Company also recognized $7.3 million and $1.3 million of merger related costs that were recorded in noninterest expense in the statement of operations for the three months ended March 31, 2019, and year ended December 31, 2018, respectively.

The acquisition of Trinity has been accounted for as a business combination using the acquisition method of accounting which requires assets acquired and liabilities assumed to be recognized at fair value as of the acquisition date. The estimates of fair value are preliminary and subject to refinement as the Company completes its evaluation of the acquired assets and liabilities. Goodwill of $90.3 million arising from the acquisition consists largely of the synergies and economies of scale expected from combining the operations of Trinity into Enterprise. The goodwill is assigned as part of the Company’s Banking reporting unit. None of the goodwill recognized is expected to be deductible for income tax purposes.

The following table presents the assets acquired and liabilities assumed of Trinity as of March 8, 2019. The following information is presented on a provisional basis based upon all information available to the Company at the present time and is subject to change, and such changes could be material. The Company continues to review the underlying assumptions and valuation techniques utilized to calculate the fair value of certain definite-lived intangibles, loans, goodwill and deferred income taxes. Additional adjustments may be recorded during the allocation period specified by ASC 805 as additional information becomes known.

(in thousands)	As Recorded by TCC	Adjustments		As Recorded by EFSC
Assets acquired:				
Cash and cash equivalents	$13,899	$ —		$13,899
Interest-earning deposits greater than 90 days	100	—		100
Securities	428,715	(414)	(a)	428,301
Loans, net	705,057	(21,493)	(b)	683,564
Other real estate	5,284	(321)	(c)	4,963
Other investments	6,673	—		6,673
Fixed assets, net	27,586	500	(d)	28,086
Accrued interest receivable	3,997	—		3,997
Intangible assets	—	23,333	(e)	23,333
Deferred tax assets	10,708	2	(f)	10,710
Other assets	35,045	(2,947)	(g)	32,098
Total assets acquired	$1,237,064	$ (1,340)		$1,235,724
Liabilities assumed:				
Deposits	$1,081,151	$ 36	(h)	$1,081,187
Subordinated debentures	26,806	(4,325)	(i)	22,481
Federal Home Loan Bank advances	6,800	171	(j)	6,971
Accrued interest payable	370	—		370
Other liabilities	5,842	—		5,842
Total liabilities assumed	$1,120,969	$ (4,118)		$1,116,851
Net assets acquired	$116,095	$ 2,778		$118,873
Consideration paid:				
Cash				$37,276
Common stock				171,884
Total consideration paid				$209,160
Goodwill				$90,287

(a) Fair value adjustments of the securities portfolio as of the acquisition date.
(b) Fair value adjustments based on the Company’s evaluation of the acquired loan portfolio, write-off of net deferred loan costs and elimination of the allowance for loan losses recorded by Trinity.
(c) Fair value adjustment based on the Company’s evaluation of the acquired OREO portfolio.
(d) Fair value adjustments based on the Company’s evaluation of the acquired premises and equipment.
(e) Recording of the core deposit intangible asset on the acquired core deposit accounts. Amount to be amortized using a sum of years digits method over a useful life of 10 years.
(f) Adjustment for deferred taxes at the acquisition date.

(g) Fair value adjustment of other assets at the acquisition date.
(h) Fair value adjustment to time deposits.
(i) Fair value adjustment to the trust preferred securities at the acquisition date.
(j) Fair value adjustment to the Federal Home Loan Bank borrowings.

The following table provides the unaudited pro forma information for the results of operations for the three months ended March 31, 2019 and 2018, as if the acquisition had occurred on January 1, 2018. The pro forma results combine the historical results of Trinity with the Company's Consolidated Statements of Income, adjusted for the impact of the application of the acquisition method of accounting including loan discount accretion, intangible assets amortization, and deposit and trust preferred securities premium accretion, net of taxes. The pro forma results have been prepared for comparative purposes only and are not necessarily indicative of the results that would have been obtained had the acquisition actually occurred on January 1, 2018. No assumptions have been applied to the pro forma results of operations regarding possible revenue enhancements, expense efficiencies or asset dispositions. Only the acquisition related expenses that have been incurred as of March 31, 2019 are included in net income in the table below.

	Pro Forma Three months ended March 31,	
(in thousands, except per share data)	2019	2018
Total revenues (net interest income plus noninterest income)	$71,983	$68,874
Net income	23,100	15,009
Diluted earnings per common share	0.82	0.55

NOTE 3 - EARNINGS PER SHARE

Basic earnings per common share data is calculated by dividing net income by the weighted average number of common shares outstanding during the period. Common shares outstanding include common stock and restricted stock awards where recipients have satisfied the vesting terms. Diluted earnings per common share gives effect to all dilutive potential common shares outstanding during the period using the treasury stock method.

The following table presents a summary of per common share data and amounts for the periods indicated.

	Three months ended March 31,	
(in thousands, except per share data)	2019	2018
Net income as reported	$16,156	$20,921
Weighted average common shares outstanding	23,927	23,115
Additional dilutive common stock equivalents	156	172
Weighted average diluted common shares outstanding	24,083	23,287
Basic earnings per common share:	$0.68	$0.91
Diluted earnings per common share:	0.67	0.90

For the three months ended March 31, 2019 and 2018, there were 122,270 and 0, respectively, common stock equivalents excluded from the earnings per share calculations because their effect would have been anti-dilutive.

NOTE 4 - INVESTMENTS

The following table presents the amortized cost, gross unrealized gains and losses and fair value of securities available for sale and held to maturity:

	March 31, 2019			
(in thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available for sale securities:				
Obligations of U.S. Government-sponsored enterprises	$54,128	$ —	$ (347)	$53,781
Obligations of states and political subdivisions	114,770	2,218	(3)	116,985
Agency mortgage-backed securities	895,899	6,461	(4,816)	897,544
U.S. Treasury bills	9,964	113	—	10,077
Corporate debt securities	20,768	30	—	20,798
Total securities available for sale	$1,095,529	$ 8,822	$ (5,166)	$1,099,185
Held to maturity securities:				
Obligations of states and political subdivisions	$12,490	$ 91	$ (20)	$12,561
Agency mortgage-backed securities	51,878	11	(303)	51,586
Total securities held to maturity	$64,368	$ 102	$ (323)	$64,147

	December 31, 2018			
(in thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available for sale securities:				
Obligations of U.S. Government-sponsored enterprises	$99,926	$ —	$(1,428)	$98,498
Obligations of states and political subdivisions	26,566	327	(83)	26,810
Agency mortgage-backed securities	596,825	1,160	(11,849)	586,136
U.S. Treasury Bills	$9,962	$ —	$(37)	$9,925
Total securities available for sale	$733,279	$ 1,487	$(13,397)	$721,369
Held to maturity securities:				
Obligations of states and political subdivisions	$12,506	$ 16	$(114)	$12,408
Agency mortgage-backed securities	53,173	—	(1,647)	51,526
Total securities held to maturity	$65,679	$ 16	$(1,761)	$63,934

At March 31, 2019, and December 31, 2018, there were no holdings of securities of any one issuer in an amount greater than 10% of shareholders' equity, other than U.S. Government agencies and sponsored enterprises. The agency mortgage-backed securities are all issued by U.S. Government agencies and sponsored enterprises. Securities having a fair value of $478.8 million and $433.7 million at March 31, 2019, and December 31, 2018, respectively, were pledged as collateral to secure deposits of public institutions and for other purposes as required by law or contract provisions.

The amortized cost and estimated fair value of debt securities at March 31, 2019, by contractual maturity, are shown below. Expected maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties. The weighted average life of the mortgage-backed securities is approximately 4 years.

	Available for sale		Held to maturity	
(in thousands)	Amortized Cost	Estimated Fair Value	Amortized Cost	Estimated Fair Value
Due in one year or less	$1,876	$1,888	$—	$ —
Due after one year through five years	67,451	67,377	2,534	2,546
Due after five years through ten years	31,819	32,135	9,957	10,015
Due after ten years	98,484	100,241	—	—
Agency mortgage-backed securities	895,899	897,544	51,877	51,586
	$1,095,529	$1,099,185	$64,368	$ 64,147

The following table represents a summary of investment securities that had an unrealized loss:

	March 31, 2019					
	Less than 12 months		12 months or more		Total	
(in thousands)	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Obligations of U.S. Government-sponsored enterprises	$19,854	$ 95	$29,796	$ 252	$49,650	$ 347
Obligations of states and political subdivisions	680	10	2,949	13	3,629	23
Agency mortgage-backed securities	47,506	685	326,319	4,434	373,825	5,119
	$68,040	$ 790	$359,064	$ 4,699	$427,104	$ 5,489

	December 31, 2018					
	Less than 12 months		12 months or more		Total	
(in thousands)	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Obligations of U.S. Government-sponsored enterprises	$19,622	$ 322	$78,876	$ 1,106	$98,498	$ 1,428
Obligations of states and political subdivisions	3,102	15	14,156	182	17,258	197
Agency mortgage-backed securities	87,357	2,211	389,770	11,285	477,127	13,496
U.S. Treasury bills	—	—	9,925	37	9,925	37
	$110,081	$ 2,548	$492,727	$ 12,610	$602,808	$ 15,158

The unrealized losses at both March 31, 2019, and December 31, 2018, were primarily attributable to changes in market interest rates since the securities were purchased. Management systematically evaluates investment securities for other-than-temporary declines in fair value on a quarterly basis. This analysis requires management to consider various factors, which include among other considerations (1) the present value of the cash flows expected to be collected compared to the amortized cost of the security, (2) duration and magnitude of the decline in value, (3) the financial condition of the issuer or issuers, (4) structure of the security, and (5) the intent to sell the security or whether it is more likely than not the Company would be required to sell the security before its anticipated recovery in market value. At March 31, 2019, management performed its quarterly analysis of all securities with an unrealized loss and concluded no individual securities were other-than-temporarily impaired.

13

NOTE 5 - LOANS

The loan portfolio is comprised of loans originated by the Company and loans acquired in connection with the Company's acquisitions. These loans are accounted for using the guidance in the Accounting Standards Codification (ASC) section 310-30 and 310-20. Loans accounted for using ASC 310-30 are sometimes referred to as purchased credit impaired ("PCI") loans.

The table below shows the loan portfolio composition including carrying value categorized by loans accounted for at amortized cost, which includes our originated loans, and by loans accounted for as PCI.

(in thousands)	March 31, 2019	December 31, 2018
Loans accounted for at amortized cost	$4,894,574	$ 4,303,600
Loans accounted for as PCI	122,503	46,401
Total loans	$5,017,077	$ 4,350,001

At March 31, 2019, loans acquired in the Trinity acquisition included $602 million accounted for at amortized cost and $80 million accounted for as PCI. These loans were recorded at fair value with no allowance for loan losses.

The table below shows the composition of the allowance for loan losses:

(in thousands)	March 31, 2019	December 31, 2018
Allowance for loans accounted for at amortized cost	$41,945	$ 42,295
Allowance for loans accounted for as PCI	1,150	1,181
Total allowance for loan losses	$43,095	$ 43,476

The following tables refer to loans accounted for at amortized cost.

Below is a summary of loans by category at March 31, 2019 and December 31, 2018:

(in thousands)	March 31, 2019	December 31, 2018
Commercial and industrial	$2,209,437	$ 2,121,008
Real estate:		
Commercial - investor owned	1,144,868	843,728
Commercial - owner occupied	647,198	604,498
Construction and land development	358,884	330,097
Residential	416,731	298,944
Total real estate loans	2,567,681	2,077,267
Consumer and other	119,368	107,351
Loans, before unearned loan fees	4,896,486	4,305,626
Unearned loan fees, net	(1,912)	(2,026)
Loans, including unearned loan fees	$4,894,574	$ 4,303,600

A summary of the activity in the allowance for loan losses and the recorded investment in loans by class and category based on impairment methodology through March 31, 2019, and at December 31, 2018, is as follows:

(in thousands)	Commercial and industrial	CRE - investor owned	CRE - owner occupied	Construction and land development	Residential real estate	Consumer and other	Total
Allowance for loan losses:							
Balance at December 31, 2018	$ 29,039	$ 4,683	$ 4,239	$ 1,987	$ 1,616	$ 731	$ 42,295
Provision (provision reversal) for loan losses	1,445	769	(431)	(252)	(288)	233	1,476
Losses charged off	(1,853)	(120)	(36)	(45)	(67)	(129)	(2,250)
Recoveries	29	7	2	9	364	13	424
Balance at March 31, 2019	$ 28,660	$ 5,339	$ 3,774	$ 1,699	$ 1,625	$ 848	$ 41,945

(in thousands)	Commercial and industrial	CRE - investor owned	CRE - owner occupied	Construction and land development	Residential real estate	Consumer and other	Total
Balance March 31, 2019							
Allowance for loan losses - Ending balance:							
Individually evaluated for impairment	$ 2,199	$ 596	$ 119	$ —	$ —	$ —	$ 2,914
Collectively evaluated for impairment	26,461	4,743	3,655	1,699	1,625	848	39,031
Total	$ 28,660	$ 5,339	$ 3,774	$ 1,699	$ 1,625	$ 848	$ 41,945
Loans - Ending balance:							
Individually evaluated for impairment	$ 7,205	$ 1,527	$ 2,296	$ —	$ 408	$ —	$ 11,436
Collectively evaluated for impairment	2,202,232	1,143,341	644,902	358,884	416,323	117,456	4,883,138
Total	$ 2,209,437	$ 1,144,868	$ 647,198	$ 358,884	$ 416,731	$ 117,456	$ 4,894,574
Balance December 31, 2018							
Allowance for loan losses - Ending balance:							
Individually evaluated for impairment	$ 4,266	$ —	$ 109	$ —	$ 52	$ 26	$ 4,453
Collectively evaluated for impairment	24,773	4,683	4,130	1,987	1,564	705	37,842
Total	$ 29,039	$ 4,683	$ 4,239	$ 1,987	$ 1,616	$ 731	$ 42,295
Loans - Ending balance:							
Individually evaluated for impairment	$ 12,950	$ 398	$ 2,135	$ —	$ 2,277	$ 311	$ 18,071
Collectively evaluated for impairment	2,108,058	843,330	602,363	330,097	296,667	105,014	4,285,529
Total	$ 2,121,008	$ 843,728	$ 604,498	$ 330,097	$ 298,944	$ 105,325	$ 4,303,600

A summary of nonperforming loans individually evaluated for impairment by category at March 31, 2019 and December 31, 2018, and the income recognized on impaired loans is as follows:

(in thousands)	March 31, 2019					
	Unpaid Contractual	Recorded Investment	Recorded Investment	Total Recorded	Related Allowance	Average Recorded

	Principal Balance	With No Allowance	With Allowance	Investment		Investment
Commercial and industrial	$9,515	$ 2,168	$ 5,037	$ 7,205	$ 2,199	$ 7,855
Real estate:						
Commercial - investor owned	1,555	271	1,256	1,527	596	1,527
Commercial - owner occupied	484	467	—	467	—	471
Construction and land development	—	—	—	—	—	—
Residential	409	408	—	408	—	408
Consumer and other	—	—	—	—	—	—
Total	$11,963	$ 3,314	$ 6,293	$ 9,607	$ 2,795	$ 10,261

(in thousands)	December 31, 2018 Unpaid Contractual Principal Balance	Recorded Investment With No Allowance	Recorded Investment With Allowance	Total Recorded Investment	Related Allowance	Average Recorded Investment
Commercial and industrial	$21,893	$ 3,294	$ 9,656	$ 12,950	$ 4,266	$ 13,827
Real estate:						
Commercial - investor owned	553	398	—	398	—	277
Commercial - owner occupied	847	472	336	808	109	691
Construction and land development	—	—	—	—	—	—
Residential	2,425	1,659	618	2,277	52	778
Consumer and other	329	—	312	312	26	—
Total	$26,047	$ 5,823	$ 10,922	$ 16,745	$ 4,453	$ 15,573

(in thousands)	Three months ended March 31, 2019	2018
Total interest income that would have been recognized under original terms	$436	$534
Total cash received and recognized as interest income on non-accrual loans	62	11
Total interest income recognized on accruing, impaired loans	3	11

The recorded investment in nonperforming loans by category at March 31, 2019 and December 31, 2018, is as follows:

(in thousands)	March 31, 2019 Non-accrual	Restructured, not on non-accrual	Total
Commercial and industrial	$7,094	$ 111	$7,205
Real estate:			
Commercial - investor owned	1,527	—	1,527
Commercial - owner occupied	467	—	467
Construction and land development	—	—	—
Residential	328	80	408
Consumer and other	—	—	—
Total	$9,416	$ 191	$9,607

(in thousands)	December 31, 2018 Non-accrual	Restructured, not on non-accrual	Total
Commercial and industrial	$12,805	$ 145	$12,950
Real estate:			
Commercial - investor owned	398	—	398
Commercial - owner occupied	808	—	808
Construction and land development	—	—	—
Residential	2,197	80	2,277
Consumer and other	312	—	312

Total	$16,520	$ 225	$16,745

There were no loans over 90 days past due and still accruing interest at March 31, 2019 and December 31, 2018.

There were no portfolio loans restructured during the three months ended March 31, 2019 and 2018.

As of March 31, 2019, the Company had $1.2 million in specific reserves allocated to $4.7 million of loans that have been restructured. During the three months ended March 31, 2019 and 2018, there were no troubled debt restructurings that subsequently defaulted.

The aging of the recorded investment in past due loans by portfolio class and category at March 31, 2019 and December 31, 2018, is shown below.

	March 31, 2019				
(in thousands)	30-89 Days Past Due	90 or More Days Past Due	Total Past Due	Current	Total
Commercial and industrial	$22,062	$5,816	$27,878	$2,181,559	$2,209,437
Real estate:					
Commercial - investor owned	—	1,527	1,527	1,143,341	1,144,868
Commercial - owner occupied	708	229	937	646,261	647,198
Construction and land development	98	—	98	358,786	358,884
Residential	4,945	328	5,273	411,458	416,731
Consumer and other	69	—	69	117,387	117,456
Total	$27,882	$7,900	$35,782	$4,858,792	$4,894,574

	December 31, 2018				
(in thousands)	30-89 Days Past Due	90 or More Days Past Due	Total Past Due	Current	Total
Commercial and industrial	$66	$10,257	$10,323	$2,110,685	$2,121,008
Real estate:					
Commercial - investor owned	529	127	656	843,072	843,728
Commercial - owner occupied	292	565	857	603,641	604,498
Construction and land development	6	—	6	330,091	330,097
Residential	709	897	1,606	297,338	298,944
Consumer and other	—	312	312	105,013	105,325
Total	$1,602	$12,158	$13,760	$4,289,840	$4,303,600

The Company categorizes loans into risk categories based on relevant information about the ability of borrowers to service their debt, such as current financial information, payment experience, credit documentation, and current economic factors among other factors. This analysis is performed on a quarterly basis. The Company uses the following definitions for risk ratings:

- Grades 1, 2, and 3 – Includes loans to borrowers with a continuous record of strong earnings, sound balance sheet condition and capitalization, ample liquidity with solid cash flow, and whose management team has experience and depth within their industry.
- Grade 4 – Includes loans to borrowers with positive trends in profitability, satisfactory capitalization and balance sheet condition, and sufficient liquidity and cash flow.

- Grade 5 – Includes loans to borrowers that may display fluctuating trends in sales, profitability, capitalization, liquidity, and cash flow.
- Grade 6 – Includes loans to borrowers where an adverse change or perceived weakness has occurred, but may be correctable in the near future. Alternatively, this rating category may also include circumstances where the

borrower is starting to reverse a negative trend or condition, or has recently been upgraded from a 7, 8, or 9 rating.

- Grade 7 – Watch credits are borrowers that have experienced financial setback of a nature that is not determined to be severe or influence 'ongoing concern' expectations. Although possible, no loss is anticipated, due to strong collateral and/or guarantor support.
- Grade 8 – Substandard credits include those borrowers characterized by significant losses and sustained downward trends in balance sheet condition, liquidity, and cash flow. Repayment reliance may have shifted to secondary sources. Collateral exposure may exist and additional reserves may be warranted.
- Grade 9 – Doubtful credits include borrowers that may show deteriorating trends that are unlikely to be corrected. Collateral values may appear insufficient for full recovery, therefore requiring a partial charge-off, or debt renegotiation with the borrower. The borrower may have declared bankruptcy or bankruptcy is likely in the near term. All doubtful rated credits will be on non-accrual.

The recorded investment by risk category of the loans by portfolio class and category at March 31, 2019, which is based upon the most recent analysis performed, and December 31, 2018, is as follows:

	March 31, 2019			
(in thousands)	Pass (1-6)	Watch (7)	Classified (8 & 9)	Total
Commercial and industrial	$1,991,293	$157,408	$60,736	$2,209,437
Real estate:				
Commercial - investor owned	1,124,030	17,088	3,750	1,144,868
Commercial - owner occupied	608,773	36,052	2,373	647,198
Construction and land development	354,835	3,984	65	358,884
Residential	409,032	1,996	5,703	416,731
Consumer and other	117,451	5	—	117,456
Total	$4,605,414	$216,533	$72,627	$4,894,574

	December 31, 2018			
(in thousands)	Pass (1-6)	Watch (7)	Classified (8 & 9)	Total
Commercial and industrial	$1,927,782	$146,033	$47,193	$2,121,008
Real estate:				
Commercial - investor owned	823,128	15,083	5,517	843,728
Commercial - owner occupied	563,003	31,834	9,661	604,498
Construction and land development	318,451	11,580	66	330,097
Residential	287,802	4,232	6,910	298,944
Consumer and other	105,007	6	312	105,325
Total	$4,025,173	$208,768	$69,659	$4,303,600

Below is a summary of PCI loans by category at March 31, 2019 which includes preliminary fair value adjustments related to the Trinity acquisition and December 31, 2018:

(in thousands)	March 31, 2019 Weighted-Average Risk Rating[1]	March 31, 2019 Recorded Investment PCI Loans	December 31, 2018 Weighted-Average Risk Rating[1]	December 31, 2018 Recorded Investment PCI Loans
Commercial and industrial	4.75	$ 17,613	6.09	$ 2,159
Real estate:				
Commercial - investor owned	6.68	42,948	7.19	23,939
Commercial - owner occupied	6.81	35,026	7.39	9,669
Construction and land development	6.16	10,481	6.03	4,548
Residential	6.20	16,171	6.40	6,082
Total real estate loans		122,239		46,397
Consumer and other	3.58	264	2.18	4
Total		$ 122,503		$ 46,401

[1]Risk ratings are based on the borrower’s contractual obligation, which is not reflective of the purchase discount.

The aging of the recorded investment in past due PCI loans by portfolio class and category at March 31, 2019 and December 31, 2018, is shown below:

(in thousands)	March 31, 2019 30-89 Days Past Due	90 or More Days Past Due	Total Past Due	Current	Total
Commercial and industrial	$945	$—	$945	$16,668	$17,613
Real estate:					
Commercial - investor owned	1,580	1,868	3,448	39,500	42,948
Commercial - owner occupied	751	6,358	7,109	27,917	35,026
Construction and land development	152	258	410	10,071	10,481
Residential	1,648	849	2,497	13,674	16,171
Consumer and other	—	—	—	264	264
Total	$5,076	$9,333	$14,409	$108,094	$122,503

(in thousands)	December 31, 2018 30-89 Days Past Due	90 or More Days Past Due	Total Past Due	Current	Total
Commercial and industrial	$—	$—	$—	$2,159	$2,159
Real estate:					
Commercial - investor owned	416	88	504	23,435	23,939
Commercial - owner occupied	591	6,279	6,870	2,799	9,669
Construction and land development	—	—	—	4,548	4,548
Residential	146	37	183	5,899	6,082

Consumer and other	—	—	—	4	4
Total	$1,153	$6,404	$7,557	$38,844	$46,401

The following table is a roll forward of PCI loans, net of the allowance for loan losses, for the three months ended March 31, 2019 and 2018.

(in thousands)	Contractual Cashflows	Non-accretable Difference	Accretable Yield	Carrying Amount
Balance December 31, 2018	$ 73,157	$ 15,299	$ 12,638	$45,220
Acquisitions	120,713	11,531	28,520	80,662
Principal reductions and interest payments	(10,033)	—	—	(10,033)
Accretion of loan discount	—	—	(1,603)	1,603
Changes in contractual and expected cash flows due to remeasurement	4,081	(6)	94	3,993
Reductions due to disposals	(120)	(28)		