PINNACLE FINANCIAL PARTNERS INC
Form 10-Q
November 09, 2015
UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

(mark one)
x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended September 30, 2015
or
o TRANSITION REPORT PURSUANT TO SECTION 13 OF 15(d)
OF THE SECURITIES AND EXCHANGE ACT OF 1934
For the transition period from ____ to ____
Commission File Number: 000-31225

, Inc.
(Exact name of registrant as specified in its charter)

Tennessee	62-1812853
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

150 Third Avenue South, Suite 900, Nashville, Tennessee	37201
(Address of principal executive offices)	(Zip Code)

(615) 744-3700
(Registrant's telephone number, including area code)
Not Applicable
(Former name, former address and former fiscal year, if changes since last report)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.
Yes No
Indicate by check mark whether the registrant has submitted electronically and posted on its corporate website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for shorter period that the registrant was required to submit and post such files).
Yes 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 definitions of "large accelerated filer", "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large Accelerated Filer	Accelerated Filer
Non-accelerated Filer (do not check if you are a smaller reporting company)	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

As of November 3, 2015 there were 40,850,715 shares of common stock, $1.00 par value per share, issued and outstanding.

Pinnacle Financial Partners, Inc.
Report on Form 10-Q
September 30, 2015

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FORWARD-LOOKING STATEMENTS

Certain of the statements in this quarterly report on Form 10-Q 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 words "expect," "anticipate," "goal," "objective," "intend," "plan," "believe," "should," "hope," "pursue," "seek," "estimate" and similar expressions are intended to identify such forward-looking statements, but other statements not based on historical information may also be considered forward-looking. All forward-looking statements are subject to risks, uncertainties and other factors that may cause the actual results, performance or achievements of Pinnacle Financial to differ materially from any results expressed or implied by such forward-looking statements. Such risks include, without limitation, (i) deterioration in the financial condition of borrowers resulting in significant increases in loan losses and provisions for those losses; (ii) continuation of the historically low short-term interest rate environment; (iii) the inability of Pinnacle Financial to maintain the historical growth of its loan portfolio; (iv) changes in loan underwriting, credit review or loss reserve policies associated with economic conditions, examination conclusions, or regulatory developments; (v) effectiveness of Pinnacle Financial's asset management activities in improving, resolving or liquidating lower-quality assets; (vi) increased competition with other financial institutions; (vii) greater than anticipated adverse conditions in the national or local economies including the Nashville-Davidson-Murfreesboro-Franklin MSA, the Knoxville MSA, the Chattanooga, TN-GA MSA and the Memphis, TN-MS-AR MSA, particularly in commercial and residential real estate markets; (viii) rapid fluctuations or unanticipated changes in interest rates on loans or deposits; (ix) the results of regulatory examinations; (x) the ability to retain large, uninsured deposits; (xi) the development of any new market other than the Nashville, Knoxville, Chattanooga or Memphis MSAs; (xii) a merger or acquisition; (xiii) risks of expansion into new geographic or product markets, like the recent expansion into the Chattanooga and Memphis MSAs; (xiv) any matter that would cause Pinnacle Financial to conclude that there was impairment of any asset, including intangible assets; (xv) reduced ability to attract additional financial advisors (or failure of such advisors to cause their clients to switch to Pinnacle Financial), to retain financial advisors (including those at CapitalMark Bank & Trust (CapitalMark) and Magna Bank (Magna)) or otherwise to attract new customers; (xvi) further deterioration in the valuation of other real estate owned and increased expenses associated therewith; (xvii) inability to comply with regulatory capital requirements, including those resulting from changes to capital calculation methodologies and required capital maintenance levels; (xviii) risks associated with litigation, including the applicability of insurance coverage; (xix) the risk that the cost savings and any revenue synergies from the recent mergers with CapitalMark and Magna may not be realized or take longer than anticipated to be realized; (xx) disruption from the CapitalMark and Magna mergers with customers, suppliers or employee relationships; (xxi) the risk of successful integration of CapitalMark's and Magna's business with ours; (xxii) the amount of the costs, fees, expenses, charges and changes to the fair value adjustments related to the CapitalMark and Magna mergers; (xxiii) reputational risk and the reaction of Pinnacle Financial's, CapitalMark's and Magna's customers to the recent CapitalMark and Magna mergers; (xxiv) the risk that the integration of CapitalMark's and Magna's operations with Pinnacle Financial's will be materially delayed or will be more costly or difficult than expected; (xxv) approval of the declaration of any dividend by Pinnacle Financial's board of directors; (xxvi) the vulnerability of our network and online banking portals to unauthorized access, computer viruses, phishing schemes, spam attacks, human error, natural disasters, power loss and other security breaches; (xxvii) the possibility of increased compliance costs as a result of increased regulatory oversight, including oversight of companies in which Pinnacle Financial has significant investments, the development of additional products and services for our corporate and consumer clients and potential asset growth above $10 billion; (xxviii) the risks associated with our being a minority investor in Bankers Healthcare Group, LLC, including the risk that the owners of a majority of the equity interests in Bankers Healthcare Group decide to sell the company; and (xxix) changes in state and federal legislation, regulations or policies applicable to banks and other financial service providers, including regulatory or legislative developments arising out of current unsettled conditions in the economy, including implementation of the Dodd-Frank Wall Street Reform and Consumer Protection Act. A more detailed description of these and other risks is contained herein and in Part II Item 1A. "Risk Factors" below. Many of such factors are beyond Pinnacle Financial's ability to control or predict, and readers are cautioned not to put undue reliance on such forward-looking statements. Pinnacle Financial disclaims any obligation to update or revise any forward-looking statements contained in this report, whether as a result of new information, future events or otherwise.

Item 1. Part I. Financial Information

PINNACLE FINANCIAL PARTNERS, INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
(Unaudited)

	September 30, 2015	December 31, 2014
ASSETS		
Cash and noninterest-bearing due from banks	$68,595,726	$48,741,692
Interest-bearing due from banks	245,289,355	134,176,054
Federal funds sold and other	13,153,196	4,989,764
Cash and cash equivalents	327,038,277	187,907,510
Securities available-for-sale, at fair value	972,295,754	732,054,785
Securities held-to-maturity (fair value of $31,850,119 and $38,788,870 at September 30, 2015 and December 31, 2014, respectively)	31,698,000	38,675,527
Mortgage loans held-for-sale	47,671,890	14,038,914
Loans held-for-sale	20,236,426	-
Loans	6,335,988,628	4,590,026,505
Less allowance for loan losses	(63,758,390)	(67,358,639)
Loans, net	6,272,230,238	4,522,667,866
Premises and equipment, net	81,527,013	71,576,016
Equity method investment	81,763,986	-
Accrued interest receivable	21,510,180	16,988,407
Goodwill	429,415,765	243,529,010
Core deposits and other intangible assets	11,640,802	2,893,072
Other real estate owned	4,772,567	11,186,414
Other assets	247,262,954	176,730,276
Total assets	$8,549,063,852	$6,018,247,797
LIABILITIES AND STOCKHOLDERS' EQUITY		
Deposits:		
Noninterest-bearing	$1,876,910,141	$1,321,053,083
Interest-bearing	1,293,247,497	1,005,450,690
Savings and money market accounts	2,691,218,826	2,024,957,383
Time	739,302,052	431,143,756
Total deposits	6,600,678,516	4,782,604,912
Securities sold under agreements to repurchase	68,077,412	93,994,730
Federal Home Loan Bank advances	545,329,689	195,476,384
Subordinated debt and other borrowings	142,476,000	96,158,292
Accrued interest payable	1,703,146	631,682
Other liabilities	56,573,535	46,688,416
Total liabilities	7,414,838,298	5,215,554,416
Stockholders' equity:		
Preferred stock, no par value, 10,000,000 shares authorized; no shares issued and outstanding	-	-
Common stock, par value $1.00; 90,000,000 shares authorized; 40,802,904 and 35,732,483 shares issued and outstanding		

at September 30, 2015 and December 31, 2014, respectively	40,802,904	35,732,483
Additional paid-in capital	835,279,986	561,431,449
Retained earnings	256,648,129	201,371,081
Accumulated other comprehensive loss, net of taxes	1,494,535	4,158,368
Total stockholders' equity	1,134,225,554	802,693,381
Total liabilities and stockholders' equity	$8,549,063,852	$6,018,247,797

See accompanying notes to consolidated financial statements (unaudited).

PINNACLE FINANCIAL PARTNERS, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF INCOME
(Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2015	2014	2015	2014
Interest income:				
Loans, including fees	$61,453,541	$47,510,761	$161,245,890	$136,296,125
Securities:				
Taxable	3,953,948	3,469,311	10,858,790	10,817,854
Tax-exempt	1,416,954	1,533,029	4,300,740	4,694,438
Federal funds sold and other	367,671	268,455	967,935	828,335
Total interest income	67,192,114	52,781,556	177,373,355	152,636,752
Interest expense:				
Deposits	3,587,048	2,435,426	8,610,266	7,512,428
Securities sold under agreements to repurchase	39,437	38,702	99,725	100,546
Federal Home Loan Bank advances and other borrowings	1,506,528	770,367	3,505,199	2,352,501
Total interest expense	5,133,013	3,244,495	12,215,190	9,965,475
Net interest income	62,059,101	49,537,061	165,158,165	142,671,277
Provision for loan losses	2,227,937	851,194	3,729,144	1,593,180
Net interest income after provision for loan losses	59,831,164	48,685,867	161,429,021	141,078,097
Noninterest income:				
Service charges on deposit accounts	3,258,058	2,912,617	9,246,262	8,669,229
Investment services	2,525,980	2,353,118	7,184,474	6,645,362
Insurance sales commissions	1,102,859	1,037,043	3,721,260	3,566,835
Gain on mortgage loans sold, net	1,894,731	1,352,976	5,488,096	4,256,451
Investment gains on sales, net	-	29,221	562,017	29,221
Trust fees	1,437,039	1,109,278	3,979,439	3,326,877
Income from equity method investment	5,285,000	-	12,752,456	-
Other noninterest income	5,906,747	4,094,200	16,988,490	11,724,284
Total noninterest income	21,410,414	12,888,453	59,922,494	38,218,259
Noninterest expense:				
Salaries and employee benefits	27,745,643	21,721,663	75,051,061	65,244,092
Equipment and occupancy	6,932,758	6,477,076	18,856,952	18,103,458
Other real estate expense, net	(686,071)	417,197	(405,350)	1,294,355
Marketing and other business development	1,252,270	945,805	3,398,185	2,919,696
Postage and supplies	795,403	569,707	2,175,873	1,674,515
Amortization of intangibles	602,545	236,163	1,057,372	711,514
Merger related expense	2,248,569	-	2,307,622	-
Other noninterest expense	6,215,863	3,991,944	16,243,612	11,959,708
Total noninterest expense	45,106,980	34,359,555	118,685,327	101,907,338
Income before income taxes	36,134,598	27,214,765	102,666,188	77,389,018
Income tax expense	11,985,846	9,017,943	34,010,894	25,655,089
Net income	$24,148,752	$18,196,822	$68,655,294	$51,733,929
Per share information:				

Basic net income per common share	$0.64	$0.52	$1.91	$1.49
Diluted net income per common share	$0.62	$0.52	$1.86	$1.48
Weighted average shares outstanding:				
Basic	37,828,329	34,762,206	36,009,659	34,688,064
Diluted	38,792,787	35,155,224	36,944,171	35,069,764

See accompanying notes to consolidated financial statements (unaudited).

PINNACLE FINANCIAL PARTNERS, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2015	2014	2015	2014
Net income	$24,148,752	$18,196,892	$68,655,294	$51,733,929
Other comprehensive income (loss), net of tax:				
Change in fair value on available-for-sale securities, net of tax	2,117,326	(739,313)	(892,254)	9,311,318
Change in fair value of cash flow hedges, net of tax	(845,615)	273,312	(1,430,041)	(2,556,206)
Net gain on sale of investment securities reclassified from other comprehensive income into net income, net of tax	-	(17,758)	(341,538)	(17,758)
Total other comprehensive income (loss), net of tax	1,271,711	(483,759)	(2,663,833)	6,737,354
Total comprehensive income	$25,420,463	$17,713,133	$65,991,461	$58,471,283

See accompanying notes to consolidated financial statements (unaudited).

PINNACLE FINANCIAL PARTNERS, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY
(Unaudited)

	Common Stock					
	Shares	Amount	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comp. Income (Loss), net	Total Stockholders' Equity
Balances, December 31, 2013	35,221,941	$35,221,941	$550,212,135	$142,298,199	$(4,024,614)	$723,707,661
Exercise of employee common stock options and related tax benefits	218,108	218,108	6,347,045	-	-	6,565,153
Common dividends paid	-	-	-	(8,535,894)	-	(8,535,894)
Issuance of restricted common shares, net of forfeitures	281,416	281,416	(281,416)	-	-	-
Restricted shares withheld for taxes and related tax benefit	(66,924)	(66,924)	(2,177,101)	-	-	(2,244,025)
Compensation expense for restricted shares	-	-	3,969,973	-	-	3,969,973
Net income	-	-	-	51,733,929	-	51,733,929
Other comprehensive income	-	-	-	-	6,737,354	6,737,354
Balances, September 30, 2014	35,654,541	$35,654,541	$558,070,636	$185,496,234	$2,712,740	$781,934,151
Balances, December 31, 2014	35,732,483	$35,732,483	$561,431,449	$201,371,081	$4,158,368	$802,693,381
Exercise of employee common stock options and related tax benefits	205,628	205,628	4,869,810	-	-	5,075,438
Common dividends paid	-	-	-	(13,378,246)		(13,378,246)
Issuance of restricted common shares, net of forfeitures	251,196	251,196	(251,196)	-	-	-
Common stock issued in conjunction with CapitalMark acquisition	3,306,184	3,306,184	202,648,875	-	-	205,955,059
Common stock issued in conjunction with Magna acquisition	1,371,717	1,371,717	62,166,214	-	-	63,537,931
Restricted shares withheld for taxes and related tax benefit	(64,304)	(64,304)	(890,194)	-	-	(954,498)

Compensation expense for restricted shares	-	-	5,305,028	-	-	5,305,028
Net income	-	-	-	68,655,294	-	68,655,294
Other comprehensive loss	-	-	-	-	(2,663,833)	(2,663,833)
Balances, September 30, 2015	40,802,904	$40,802,904	$835,279,986	$256,648,129	$1,494,535	$1,134,225,554

See accompanying notes to consolidated financial statements (unaudited).
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PINNACLE FINANCIAL PARTNERS, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

	Nine Months Ended September 30, 2015	2014
Operating activities:		
Net income	$68,655,294	$51,733,929
Adjustments to reconcile net income to net cash provided by operating activities:		
Net amortization/accretion of premium/discount on securities	3,476,415	3,353,794
Depreciation and amortization	4,987,259	6,987,533
Provision for loan losses	3,729,144	1,593,180
Gain on mortgage loans sold, net	(5,488,096)	(4,256,451)
Gain on sale of investment securities	(562,017)	(29,221)
Stock-based compensation expense	5,305,028	3,969,973
Deferred tax expense (benefit)	249,179	(361,424)
(Gains) losses on dispositions of other real estate and other investments, net	(426,069)	(92,577)
(Gains) losses from equity method investment	(12,752,456)	-
Excess tax benefit from stock compensation	(2,537,097)	(1,526,772)
Changes in other loans held for sale	(20,236,426)	-
Mortgage loans held for sale:		
Loans originated	(361,610,268)	(242,784,212)
Loans sold	354,142,000	240,761,000
Increase in other assets	17,774,166	3,978,907
Decrease in other liabilities	(19,804,697)	(2,526,028)
Net cash provided by operating activities	34,901,359	60,801,631
Investing activities:		
Activities in securities available-for-sale:		
Purchases	(263,963,695)	(97,806,318)
Sales	125,020,082	2,360,478
Maturities, prepayments and calls	103,815,445	86,531,771
Activities in securities held-to-maturity:		
Purchases	(1,550,995)	-
Maturities, prepayments and calls	8,005,000	1,094,966
Increase in loans, net	(455,811,945)	(283,931,233)
Purchases of software, premises and equipment	(7,907,943)	(3,991,211)
Proceeds from sales of software, premises and equipment	654,069	-
Acquisitions of CapitalMark and Magna, net of cash acquired	5,876,592	-
Increase in equity-method investment	(69,011,530)	-
(Increase) decrease in other investments	(708,018)	31,553
Net cash used in investing activities	(555,582,938)	(295,709,994)
Financing activities:		
Net increase in deposits	412,421,421	128,858,023
Net decrease in securities sold under agreements to repurchase	(43,791,132)	(5,692,815)
Advances from Federal Home Loan Bank:		
Issuances	1,135,000,000	585,000,000
Payments/maturities	(847,251,755)	(460,063,036)
Increase (decrease) in subordinated debt and other borrowings, net	46,317,708	(1,875,000)

Cash paid to redeem senior preferred stock at acquired entities	(36,607,714)	-
Exercise of common stock options and stock appreciation rights, net of repurchase of restricted shares	4,564,967	4,321,128
Excess tax benefit from stock compensation	2,537,097	1,526,772
Common stock dividends paid	(13,378,246)	(8,535,894)
Net cash provided by financing activities	659,812,346	243,539,178
Net increase in cash and cash equivalents	139,130,767	8,630,815
Cash and cash equivalents, beginning of period	187,907,510	208,938,737
Cash and cash equivalents, end of period	$327,038,277	$217,569,552

See accompanying notes to consolidated financial statements (unaudited).

PINNACLE FINANCIAL PARTNERS, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

Note 1. Summary of Significant Accounting Policies

Nature of Business — Pinnacle Financial Partners, Inc. (Pinnacle Financial) is a bank holding company whose primary business is conducted by its wholly-owned subsidiary, Pinnacle Bank. Pinnacle Bank is a commercial bank headquartered in Nashville, Tennessee. Pinnacle Financial completed its acquisitions of CapitalMark Bank and Trust (CapitalMark) and Magna Bank (Magna) (jointly, the acquisitions) on July 31, 2015 and September 1, 2015, respectively. Pinnacle Bank provides a full range of banking services in its primary market areas of the Nashville-Davidson-Murfreesboro-Franklin, TN, the Knoxville, TN, the Chattanooga, TN-GA and Memphis, TN-MS-AR Metropolitan Statistical Areas.

Basis of Presentation — The accompanying unaudited consolidated financial statements have been prepared in accordance with instructions to Form 10-Q and therefore do not include all information and footnotes necessary for a fair presentation of financial position, results of operations, and cash flows in conformity with U.S. generally accepted accounting principles (U.S. GAAP). All adjustments consisting of normally recurring accruals that, in the opinion of management, are necessary for a fair presentation of the financial position and results of operations for the periods covered by the report have been included. The accompanying unaudited consolidated financial statements should be read in conjunction with the Pinnacle Financial consolidated financial statements and related notes appearing in the 2014 Annual Report previously filed on Form 10-K.

These consolidated financial statements include the accounts of Pinnacle Financial and its wholly-owned subsidiaries. PNFP Statutory Trust I, PNFP Statutory Trust II, PNFP Statutory Trust III and PNFP Statutory Trust IV are affiliates of Pinnacle Financial and are included in these consolidated financial statements pursuant to the equity method of accounting. Significant intercompany transactions and accounts are eliminated in consolidation.

The financial statements and footnotes accompanying this Form 10-Q and the financial condition and results of operations described herein reflect the impact of the acquisitions beginning on the respective acquisition dates and are subject to future refinements to the firm's purchase accounting adjustments.

Use of Estimates — The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities as of the balance sheet date and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change in the near term include the determination of the allowance for loan losses, the valuation of purchased loan, deferred tax assets, other real estate owned and our investment portfolio, including other-than-temporary impairment, and any potential impairment of intangible assets, including goodwill. These financial statements should be read in conjunction with Pinnacle Financial's Annual Report on Form 10-K for the year ended December 31, 2014. There have been no significant changes to Pinnacle Financial's significant accounting policies as disclosed in Pinnacle Financial's Annual Report on Form 10-K for the year ended December 31, 2014.

Goodwill — ASC 350-35-3 provides an entity the option to first perform a qualitative assessment to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount. If an entity determines that this is the case, it is required to perform the quantitative two-step goodwill impairment test to identify potential goodwill impairment and measure the amount of goodwill impairment loss to be recognized for that reporting unit (if any). Based on the qualitative assessment, if an entity determines that the fair value of a reporting unit is more than its carrying amount, the quantitative two-step goodwill impairment test is not required. Pinnacle Financial performed its annual qualitative assessment as of September 30, 2014. No impairment was noted as a result of this assessment.

Cash Flow Information — Supplemental cash flow information addressing certain cash and noncash transactions for each of the nine months ended September 30, 2015 and 2014 was as follows:

	For the nine months ended September 30,	
	2015	2014
Cash Transactions:		
Interest paid	$11,807,394	$10,186,045
Income taxes paid, net	30,186,000	22,150,000
Noncash Transactions:		
Loans charged-off to the allowance for loan losses	11,732,626	5,634,327
Loans foreclosed upon and transferred to other real estate owned	252,896	1,672,459
Loans foreclosed upon and transferred to other repossessed assets	5,947,634	1,398,823

Income Per Common Share — Basic net income per common share (EPS) is computed by dividing net income by the weighted average common shares outstanding for the period. Diluted EPS reflects the dilution that could occur if securities or other contracts to issue common stock were exercised or converted. The difference between basic and diluted weighted average shares outstanding is attributable to common stock options, common stock appreciation rights, restricted share awards, and restricted share unit awards. The dilutive effect of outstanding options, common stock appreciation rights, restricted share awards, and restricted share unit awards is reflected in diluted EPS by application of the treasury stock method.

The following is a summary of the basic and diluted net income per share calculations for the three and nine months ended September 30, 2015 and 2014:

	Three months ended September 30,		Nine months ended September 30,	
	2015	2014	2015	2014
Basic net income per share calculation:				
Numerator - Net income	$24,148,752	$18,196,892	$68,655,294	$51,733,929
Denominator - Average common shares outstanding	37,828,329	34,762,206	36,009,659	34,688,064
Basic net income per share	$0.64	$0.52	$1.91	$1.49
Diluted net income per share calculation:				
Numerator – Net income	$24,148,752	$18,196,892	$68,655,294	$51,733,929
Denominator - Average common shares outstanding	37,828,329	34,762,206	36,009,659	34,688,064
Dilutive shares contingently issuable	964,458	393,018	934,512	381,700
Average diluted common shares outstanding	38,792,787	35,155,224	36,944,171	35,069,764
Diluted net income per share	$0.62	$0.52	$1.86	$1.48

Purchased Loans — Purchased loans, including loans acquired through a merger, are initially recorded at fair value on the date of purchase. Purchased loans that contain evidence of post-origination credit deterioration as of the purchase date are carried at the net present value of expected future cash flows. All other purchased loans are recorded at their initial fair value, and adjusted for subsequent advances, pay downs, amortization or accretion of any premium or discount on purchase, charge-offs and any other adjustment to carrying value. Pursuant to U.S. GAAP, management has up to 12 months following the date of the acquisition to finalize the fair values of acquired assets and assumed liabilities as of the acquisition date. Once management has finalized the fair values of acquired assets and assumed liabilities within this 12-month period, management considers such values to be the day 1 fair values (Day 1 Fair Values).

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At the time of acquisition, management evaluates all purchased loans using a variety of factors such as current classification or risk rating, past due status and history as a component of the fair value determination. For those purchased loans without evidence of credit deterioration, management evaluates each reviewed loan using an internal grading system with a grade assigned to each loan at the date of acquisition. To the extent that any purchased loan is not specifically reviewed, such loan is assumed to have characteristics similar to the characteristics of the specifically reviewed acquired portfolio of purchased loans. The grade for each purchased loan without evidence of credit deterioration is reviewed subsequent to the date of acquisition any time a loan is renewed or extended or at any time information becomes available to Pinnacle Financial that provides material insight regarding the loan's performance, the borrower's capacity to repay or the underlying collateral. To the extent that current information indicates it is probable that Pinnacle Financial will collect all amounts according to the contractual terms thereof, such loan is not considered impaired and is not considered in the determination of the required allowance for loan losses (ALL). To the extent that current information indicates it is probable that Pinnacle Financial will not be able to collect all amounts according to the contractual terms thereon, such loan is considered in the determination of the required level of ALL.

In determining the Day 1 Fair Values of purchased loans without evidence of post-origination credit deterioration at the date of acquisition, management includes (i) no carry over of any previously recorded ALL and (ii) an adjustment of the unpaid principal balance to reflect an appropriate market rate of interest and expected loss, given the risk profile and grade assigned to each loan. This adjustment is accreted into earnings as a yield adjustment, using the effective yield method, over the remaining life of each loan.

Purchased loans that contain evidence of credit deterioration on the date of purchase are individually evaluated by management to determine the estimated fair value of each loan. This evaluation includes no carryover of any previously recorded ALL. In determining the estimated fair value of purchased loans with evidence of credit deterioration, management considers a number of factors including, among other things, the remaining life of the acquired loans, estimated prepayments, estimated loss ratios, estimated value of the underlying collateral, estimated holding periods, and net present value of cash flows expected to be received.

In determining the Day 1 Fair Values of purchased loans with evidence of credit deterioration, management calculates a non-accretable difference (the credit risk component of the purchased loans) and an accretable difference (the yield component of the purchased loans). The non-accretable difference is the difference between the contractually required payments and the cash flows expected to be collected in accordance with management's determination of the Day 1 Fair Values. Subsequent increases in expected cash flows will result in an adjustment to accretable yield, which will have a positive impact on interest income. Subsequent decreases in expected cash flows will generally result in increased provision for loan losses. Subsequent increases in expected cash flows following any previous decrease will result in a reversal of the provision for loan losses to the extent of prior charges and then an adjustment to accretable yield. The accretable difference on purchased loans with evidence of credit deterioration is the difference between the expected cash flows and the net present value of expected cash flows. Such difference is accreted into earnings using the effective yield method over the term of the loans. For purchased loans with evidence of credit deterioration for which the expected cash flows cannot be forecasted, these loans are deemed to be collateral dependent are recorded at their fair value and are placed on nonaccrual.

Mortgage Servicing Rights — In conjunction with the acquisition of Magna, Pinnacle acquired a commercial and residential mortgage servicing portfolio which was recorded at fair value in conjunction with purchase accounting. The rights to service loans (MSRs) represent an intangible financial asset which going forward will be reported at the lower of amortized cost or fair market value in the accompanying balance sheet.

Additions to our MSRs are recorded at fair value, while MSRs retained in connection with the sale of the principal due on a mortgage loan are capitalized at fair value. The value of servicing rights is initially measured using a discounted cash flow model. All servicing rights capitalized have involved the retention of servicing rights only; Pinnacle Financial does not retain residual interest, "first loss" obligations, or other similar on-going financial interests in the loans it sells to third parties, nor have we participated any securitizations with any special purpose entities.

U.S. GAAP requires periodic evaluation of the fair value of the residential mortgage servicing rights. When fair value is less than amortized cost, a valuation allowance is created through a charge to earnings to reduce the carrying value of residential servicing rights to fair value. The carrying value of residential servicing may be increased (not to exceed amortized cost) through a credit to income to reduce or remove the valuation allowance if subsequent valuations indicate that fair value exceeds amortized cost.

Except for recovery of amounts invested in acquiring servicing rights, servicing mortgage loans for others does not generally impose significant financial risks to the servicer. There are, however, certain investors for whom servicing does involve some risk of loss. For example, servicing Federal Housing Administration (FHA) insured or Veterans Administration (VA) guaranteed loans can result in the servicer advancing principal and interest payments for delinquent borrowers, or incurring a shortfall in the total amount of principal collected under certain foreclosure circumstances.

Subordinated Debt Issuance— On July 30, 2015, Pinnacle Bank issued $60.0 million in aggregate principal amount of Fixed–to-Floating Rate Subordinated Notes due 2025 (the Notes) in a private placement transaction to accredited institutional investors. The maturity date of the notes is July 30, 2025, although Pinnacle Bank may redeem some or all of the Notes beginning on the interest payment date of July 30, 2020 and on any interest payment date thereafter at a redemption price equal to 100% of the principal amount of the Notes to be redeemed plus accrued and unpaid interest to the date of redemption, subject to the prior approval of the Federal Deposit Insurance Corporation (the FDIC).

From the date of the issuance through July 29, 2020, the Notes will bear interest at the rate of 4.875% per year and will be payable semi-annually in arrears on January 30 and July 30 of each year, beginning on January 30, 2016. From July 30, 2020, the Notes will bear interest at a rate per annum equal to the three-month LIBOR rate plus 3.128%, payable quarterly in arrears on each January 30, April 30, July 30, and October 30, beginning on July 30, 2020, through the maturity date or the early redemption date of the Notes.

The sale of the Notes yielded net proceeds of approximately $59.1 million after deducting the placement agents' fees and estimated expenses payable by Pinnacle Bank. Pinnacle Bank used the net proceeds from the offering, together with available cash, to pay the cash portion of the merger consideration payable to the shareholders of CapitalMark, to pay the cash portion of the merger consideration payable to Magna shareholders in connection with the mergers, to pay the amounts necessary to redeem the preferred shares that each of CapitalMark and Magna issued to the United States Department of the Treasury in connection with their participation in the Treasury's Small Business Lending Fund and for general corporate purposes.

Note 2. Acquisitions

Acquisition of CapitalMark Bank & Trust

On July 31, 2015, Pinnacle Financial consummated its previously announced acquisition of CapitalMark Bank & Trust (CapitalMark). Pursuant to the terms of the Agreement and Plan of Merger dated as of April 7, 2015 by and among Pinnacle Financial, Pinnacle Bank, and CapitalMark (the CapitalMark Merger Agreement), CapitalMark merged with and into Pinnacle Bank, with Pinnacle Bank continuing as the surviving corporation (the CapitalMark Merger).

By virtue of the CapitalMark Merger, each holder of an issued and outstanding share of common stock of CapitalMark had the right to elect, for each share of CapitalMark common stock held by such holder, to receive either (i) 0.50 shares of Pinnacle Financial's common stock, (ii) an amount in cash equal to the value of 0.50 shares of Pinnacle Financial's common stock, based on the 10-day average closing price for Pinnacle Financial's common stock prior to July 31, 2015 (which such amount equaled $26.78), or (iii) a combination of stock and cash.

Approximately 90% and 10%, respectively, of CapitalMark's outstanding shares of common stock as of the effective time of the CapitalMark Merger were converted into shares of Pinnacle Financial common stock and cash, respectively. As a result, Pinnacle Financial issued approximately 3.3 million shares of its common stock and paid approximately $19.7 million in cash (including payments related to fractional shares) to the CapitalMark shareholders. Fractional shares were converted to cash based on the 10-day average closing price for Pinnacle Financial's common stock prior to July 31, 2015. All of CapitalMark's outstanding stock options vested upon consummation of the CapitalMark Merger and were converted into options to purchase shares of Pinnacle Financial's common stock at the common stock exchange rates. The fair market value of stock options assumed was $30.4 million.

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With this acquisition, Pinnacle Financial expanded its presence in the East Tennessee region by expanding into Chattanooga. Pinnacle Financial believes that cost savings will be recognized in future periods through the elimination of redundant operations. The following summarizes consideration paid and a preliminary allocation of purchase price to net assets acquired (in thousands):

	Number of Shares	Amount
Equity consideration:		
Common stock issued	3,306,184	$175,525
Fair value of stock options assumed		30,430
Total equity consideration		$205,955
Non-equity consideration - Cash		$ 19,675
Total consideration paid		$225,630
Allocation of total consideration paid:		
Preliminary fair value of net assets assumed including estimated identifiable intangible assets		$69,018
Goodwill		$156,612

Acquisition of Magna Bank

On September 1, 2015, Pinnacle Financial consummated its previously announced acquisition of Magna Bank (Magna). Pursuant to the terms of the Agreement and Plan of Merger dated as of April 28, 2015 by and among Pinnacle Financial, Pinnacle Bank and Magna (the Magna Merger Agreement), Magna merged with and into Pinnacle Bank, with Pinnacle Bank continuing as the surviving corporation (the Magna Merger and together with the CapitalMark Merger, the Mergers).

By virtue of the Magna Merger, each holder of an issued and outstanding share of common stock of Magna (including shares of Magna's common stock issued automatically upon conversion of Magna's Series D preferred stock immediately prior to the effective time of the Magna Merger) had the right to elect, for each share of Magna common stock held by such holder (including shares of Magna's common stock issued automatically upon conversion of Magna's Series D preferred stock immediately prior to the effective time of the Magna Merger), to receive either (i) 0.3369 shares of Pinnacle Financial's common stock, (ii) an amount in cash equal to $14.32, or (iii) a combination of stock and cash.

In total, Magna common shareholders (including holders of shares of Magna's common stock issued automatically upon conversion of Magna's Series D preferred stock immediately prior to the effective time of the Merger) had approximately 75% of their shares of Magna common stock as of the effective time of the Merger (including shares of Magna's common stock issued automatically upon conversion of Magna's Series D preferred stock immediately prior to the effective time of the Merger) converted into shares of common stock of the Company and approximately 25% of their shares converted into cash. As a result, Pinnacle Financial issued approximately 1.4 million shares of its common stock and paid approximately $19.5 million in cash (including payments related to fractional shares) to the Magna shareholders. Additionally, at the time of the merger there were 139,417 unexercised stock options that were exchanged for cash equal to $14.32 less the respective exercise price. This consideration totaled approximately $848,000, including all applicable payroll taxes.

With this acquisition, Pinnacle Financial expanded its presence in the Memphis market of Tennessee. Pinnacle Financial believes that cost savings will be recognized in future periods through the elimination of redundant operations. The following summarizes consideration paid and a preliminary allocation of purchase price to net assets acquired (in thousands):

	Number of Shares	Amount
Equity consideration:		
Common stock issued	1,371,717	$63,538
Total equity consideration		$63,538
Non-Equity Consideration:		
Cash paid to redeem common stock		$19,453
Cash paid to exchange outstanding stock options		847
Total consideration paid		$83,838
Allocation of total consideration paid:		
Preliminary fair value of net assets assumed including estimated identifiable intangible assets		54,132
Goodwill		29,706

Pinnacle Financial accounted for the Mergers under the acquisition method in accordance with ASC Topic 805. Accordingly, the purchase price is allocated to the fair value of the assets acquired and liabilities assumed as of the date of the Mergers. The following purchase price allocations on the Mergers are preliminary and will be finalized upon the receipt of final valuations on certain assets and liabilities. Upon receipt of final fair value estimates, which must be within one year of the merger dates, Pinnacle Financial will make any final adjustments to the purchase price allocation and prospectively adjust any goodwill recorded. Material adjustments to estimated fair values as of the date of the Mergers would be recorded in the period in which the Merger occurred, and as a result, previously reported results are subject to change. Information regarding Pinnacle Financial's loan discount and related deferred tax asset, core deposit intangible asset and related deferred tax liability, as well as income taxes payable and the related deferred tax balances, and potentially other account balances recorded in the Mergers may be adjusted as Pinnacle Financial refines its estimates. Determining the fair value of assets and liabilities, particularly illiquid assets and liabilities, is a complicated process involving significant judgment regarding estimates and assumptions used to calculate estimated fair value. Fair value adjustments based on updated estimates could materially affect the goodwill recorded on the Mergers. Pinnacle Financial may incur losses on the acquired loans that are materially different from losses Pinnacle Financial originally projected.

The acquired assets and liabilities, as well as the preliminary adjustments to record the assets and liabilities at their estimated fair values, are presented in the following tables (in thousands):

CapitalMark

	As of July 31, 2015			
	CapitalMark Historical Cost Basis	Preliminary Fair Value Adjustments		As Recorded by Pinnacle Financial
Assets				
Cash and cash equivalents	$28,021	$ -		$28,021
Investment securities[1]	150,799	(399	)	150,400
Loans, net of allowance for loan losses[2]	881,906	(20,704	)	861,202
Other real estate owned	1,728	-		1,728
Core deposit intangible[3]	-	6,193		6,452
Other assets	36,113	6,239		42,352
Total Assets	$1,098,826	$ (8,671	)	$1,090,155
Liabilities				
Interest-bearing deposits[4]	$758,492	$ 891		$759,383
Non-interest bearing deposits	193,798	-		193,798
Borrowings[5]	32,874	228		33,102
Other liabilities	34,854	-		34,854
Total Liabilities	$1,020,018	$ 1,119		$1,021,137
Net Assets Acquired	$78,808	$ (9,790	)	$69,018

Explanation of certain fair value adjustments

(1) The amount represents the adjustment of the book value of CapitalMark's investment securities to their estimated fair value on the date of acquisition.

(2) The amount represents the adjustment of the net book value of CapitalMark's loans to their estimated fair value based on current interest rates and expected cash flows, which includes estimates of expected credit losses inherent in the portfolio.

(3) The amount represents the fair value of the core deposit intangible asset created in the acquisition.

(4) The adjustment is necessary because the weighted average interest rate of CapitalMark's deposits exceeded the cost of similar funding at the time of acquisition. The fair value adjustment will be amortized to reduce future interest expense over the life of the portfolio.

(5) The adjustment is necessary because the weighted average interest rate of CapitalMark's FHLB advances exceeded the cost of similar funding at the time of acquisition. The fair value adjustment will be amortized to reduce future interest expense over the life of the portfolio.

Magna

	As of September 1, 2015		
	Magna Historical Cost Basis	Preliminary Fair Value Adjustments	As Recorded by Pinnacle Financial
Assets			
Cash and cash equivalents	$17,832	$ -	$17,832
Investment securities[1]	59,719	(281)	59,438
Loans, net of allowance for loan losses[2]	471,994	(10,009)	461,985
Other real estate owned[3]	1,471	139	1,610
Core deposit intangible[4]	-	3,169	3,169
Other assets[5]	36,794	5,300	42,094
Total Assets	$587,810	$ (1,682)	$586,128
Liabilities			
Interest-bearing deposits[6]	$402,535	$ 1,268	$403,803
Non-interest bearing deposits	48,851	-	48,851
Borrowings[7]	46,900	506	47,406
Other liabilities	31,936	-	31,936
Total Liabilities	$530,222	$ 1,774	$531,996
Net Assets Acquired	$57,888	$ (3,456)	$54,132

Explanation of certain fair value adjustments:

(1) The amount represents the adjustment of the book value of Magna's investment securities to their estimated fair value on the date of acquisition.

(2) The amount represents the adjustment of the net book value of Magna's loans to their estimated fair value based on current interest rates and expected cash flows, which includes estimates of expected credit losses inherent in the portfolio.

(3) The amount represents the adjustment to the book value of Magna's OREO to fair value on the date of acquisition.

(4) The amount represents the fair value of the core deposit intangible asset created in the acquisition.

(5) The amount represents the deferred tax asset recognized on the fair value adjustment of Magna's acquired assets and assumed liabilities as well as the fair value adjustment for the mortgage servicing right and property and equipment.

(6) The adjustment is necessary because the weighted average interest rate of Magna's deposits exceeded the cost of similar funding at the time of acquisition. The fair value adjustment will be amortized to reduce future interest expense over the life of the portfolio.

(7) The adjustment is necessary because the weighted average interest rate of Magna's FHLB advances exceeded the cost of similar funding at the time of acquisition. The fair value adjustment will be amortized to reduce future interest expense over the life of the portfolio.

Note 3. Equity method investment

On February 1, 2015, Pinnacle Bank acquired a 30% interest in Bankers Healthcare Group, LLC (BHG) for $75 million. Pinnacle Bank accounts for this investment pursuant to the equity method for unconsolidated subsidiaries and recognizes its interest in BHG's profits and losses in noninterest income with corresponding adjustments to the BHG investment account. Currently, the equity method of accounting requires that this investment is reported as a net investment on the financial statements, but that embedded goodwill and intangibles should be identified, tested for impairment and amortized over their useful life within the equity method investment line of the balance sheet. Amortization expense associated with BHG's customer list and data processing capabilities is recorded in income from equity method investments. Pinnacle has not yet completed the purchase accounting for this equity method investment. On the acquisition date, Pinnacle Bank estimated its investment included embedded goodwill of $40.8 million and $14.4 million of technology, trade name and customer relationship intangibles. However, the FASB has issued an exposure draft, "Proposed Accounting Standards Update 2015-280 - Investments - Equity Method and Joint Ventures (Topic 323)", that may result in equity method investments moving from the currently prescribed method of accounting to an impairment based model. Pinnacle Bank recorded earnings of $12.7 million, net of approximately $1.6 million in intangible amortization expense for the first nine months of 2015. During the third quarter of 2015, Pinnacle Bank received a $6.4 million dividend from BHG, which under the equity method of accounting reduced the carrying amount of our investment in BHG. Earnings from BHG are included in Pinnacle Bank and Pinnacle Financial's consolidated tax return.

A summary of BHG's financial position and results of operations as of and for the nine months ended September 30, 2015 were as follows (in thousands):

Banker's Healthcare Group

	September 30, 2015
Assets	$ 211,451
Liabilities	130,689
Equity interests	80,762
Total liabilities and equity	$ 211,451

	For the nine months ended September 30, 2015
Revenues	$ 102,574
Net income, pre-tax	$ 53,002

In connection with the BHG acquisition, Pinnacle Bank borrowed $40 million pursuant to a loan agreement which requires Pinnacle Financial and Pinnacle Bank to maintain certain financial covenants including minimum capital ratios, liquidity requirements and other non-financial covenants. The loan had a 5-year maturity and bore interest at approximately 2.95% per annum. This loan was paid in full during the third quarter of 2015.

While Pinnacle Bank's investment in BHG is expected to have a modest impact on Pinnacle Financial's balance sheet volumes throughout the remainder of 2015, this investment primarily serves to increase and diversify Pinnacle Financial's fee income. Additionally, Pinnacle Financial utilizes BHG's marketing platform to distribute certain of its financial services through BHG's national distribution channel.

Note 4. Securities

The amortized cost and fair value of securities available-for-sale and held-to-maturity at September 30, 2015 and December 31, 2014 are summarized as follows (in thousands):

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
September 30, 2015:				
Securities available-for-sale:				
U.S. Treasury securities	$ 9,996	$ 3	$ -	$9,999
U.S. government agency securities	147,268	83	2,548	144,803
Mortgage-backed agency securities	584,066	8,797	1,892	590,971
State and municipal securities	156,469	7,200	175	163,494
Asset-backed securities	51,348	52	509	50,891
Corporate notes and other	11,258	880	1	12,137
	$ 960,405	$ 17,015	$ 5,125	$972,295
Securities held-to-maturity:				
State and municipal securities	$ 31,698	$ 227	$ 75	$31,850
	$ 31,698	$ 227	$ 75	$31,850
December 31, 2014:				
Securities available-for-sale:				
U.S. Treasury securities	$ -	$ -	$ -	$-
U.S. government agency securities	117,098	12	3,654	113,456
Mortgage-backed agency securities	447,757	10,322	2,240	455,839
State and municipal securities	130,545	8,213	180	138,578
Asset-backed securities	13,089	14	85	13,018
Corporate notes and other	10,196	969	2	11,163
	$ 718,685	$ 19,530	6,161	$732,054
Securities held-to-maturity:				
State and municipal securities	$ 38,676	$ 205	$ 92	$38,789
	$ 38,676	$ 205	$ 92	$38,789

At September 30, 2015, approximately $757.2 million of securities within Pinnacle Financial's investment portfolio were either pledged to secure public funds and other deposits or securities sold under agreements to repurchase.

The amortized cost and fair value of debt securities as of September 30, 2015 by contractual maturity are shown below. Actual maturities may differ from contractual maturities of mortgage- and asset-backed securities since the mortgages and assets underlying the securities may be called or prepaid with or without penalty. Therefore, these securities are not included in the maturity categories in the following summary (in thousands):

	Available-for-sale		Held-to-maturity	
	Amortized	Fair	Amortized	Fair
September 30, 2015:	Cost	Value	Cost	Value
Due in one year or less	$17,623	$17,670	$962	$963
Due in one year to five years	38,088	39,631	8,990	9,058
Due in five years to ten years	180,128	184,465	12,863	12,964
Due after ten years	89,152	88,667	8,883	8,865
Mortgage-backed securities	584,066	590,971	-	-
Asset-backed securities	51,348	50,891	-	-
	$960,405	$972,295	$31,698	$31,850

At September 30, 2015 and December 31, 2014, the following investments had unrealized losses. The table below classifies these investments according to the term of the unrealized losses of less than twelve months or twelve months or longer (in thousands):

	Investments with an Unrealized Loss of less than 12 months		Investments with an Unrealized Loss of 12 months or longer		Total Investments with an Unrealized Loss	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
At September 30, 2015:						
U.S. Treasury securities	$-	$ -	$-	$ -	$-	$ -
U.S. government agency securities	60,704	1,206	65,803	1,342	126,507	2,548
Mortgage-backed securities	108,531	762	105,911	1,130	214,442	1,892
State and municipal securities	11,921	78	5,671	172	17,592	250
Asset-backed securities	30,183	487	7,105	22	37,288	509
Corporate notes	502	1	-	-	502	1
Total temporarily-impaired securities	$211,841	$ 2,534	$184,490	$ 2,666	$396,331	$ 5,200
At December 31, 2014:						
U.S. Treasury securities	$-	$ -	$-	$ -	$-	$ -
U.S. government agency securities	3,593	10	103,658	3,644	107,251	3,654
Mortgage-backed securities	91,410	405	102,892	1,835	194,302	2,240
State and municipal securities	3,561	15	16,502	257	20,063	272
Asset-backed securities	-	-	9,289	85	9,289	85
Corporate notes	950	1	154	1	1,104	2
Total temporarily-impaired securities	$99,514	$ 431	$232,495	$ 5,822	$332,009	$ 6,253

The applicable dates for determining when securities are in an unrealized loss position are September 30, 2015 and December 31, 2014. As such, it is possible that a security had a market value that exceeded its amortized cost on other days during the past twelve-month periods ended September 30, 2015 and December 31, 2014, but is in the "Investments with an Unrealized Loss of less than 12 months" category above.

As shown in the tables above, at September 30, 2015, Pinnacle Financial had $5.2 million in unrealized losses on $396.3 million of securities. The unrealized losses associated with these investment securities are driven by changes in interest rates and the unrealized loss is recorded as a component of equity. These securities will continue to be monitored as a part of our ongoing impairment analysis, but are expected to perform even if the rating agencies reduce the credit rating of the bond issuers. Management evaluates the financial performance of the issuers on a quarterly basis to determine if it is probable that the issuers can make all contractual principal and interest payments. If a shortfall in future cash flows is identified, a credit loss will be deemed to have occurred and will be recognized as a charge to earnings and a new cost basis for the security will be established.

Because Pinnacle Financial currently does not intend to sell those securities that have an unrealized loss at September 30, 2015, and it is not more-likely-than-not that Pinnacle Financial will be required to sell the securities before recovery of their amortized cost bases, which may be maturity, Pinnacle Financial does not consider these securities to be other-than-temporarily impaired at September 30, 2015.

Periodically, available-for-sale securities may be sold or the composition of the portfolio realigned to improve yields, quality or marketability, or to implement changes in investment or asset/liability strategy, including maintaining collateral requirements and raising funds for liquidity purposes. Additionally, if an available-for-sale security loses its investment grade or tax-exempt status, the underlying credit support is terminated or collection otherwise becomes uncertain based on factors known to management, Pinnacle Financial will consider selling the security, but will review each security on a case-by-case basis as these factors become known. Consistent with the investment policy, available-for-sale securities of $125.0 million were sold and a gain of $562,000 realized during the nine months ended September 30, 2015. The investment portfolios of our acquired institutions were restructured in accordance with our asset liability policies. Of the $125.0 million in available-for-sale securities sold during the nine months ended September 30, 2015, $75.4 million and $16.3 million of the securities were sold to restructure the acquired portfolios of CapitalMark and Magna, respectively. As this restructuring was performed using Day 1 fair values, no gain or loss was recorded on these transactions.

The carrying values of Pinnacle Financial's investment securities could decline in the future if the financial condition of issuers deteriorates and management determines it is probable that Pinnacle Financial will not recover the entire amortized cost bases of the securities. As a result, there is a risk that other-than-temporary impairment charges may occur in the future. Additionally, there is a risk that other-than-temporary impairment charges may occur in the future if management's intention to hold these securities to maturity and or recovery changes.

Note 5. Loans and Allowance for Loan Losses

For financial reporting purposes, Pinnacle Financial classifies its loan portfolio based on the underlying collateral utilized to secure each loan. This classification is consistent with those utilized in the Quarterly Report of Condition and Income filed with the Federal Deposit Insurance Corporation (FDIC).

Pinnacle Financial uses five loan categories: commercial real estate mortgage, consumer real estate mortgage, construction and land development, commercial and industrial, consumer and other.

- Commercial real-estate mortgage loans. Commercial real-estate mortgage loans are categorized as such based on investor exposures where repayment is largely dependent upon the operation, refinance, or sale of the underlying real estate. Commercial real-estate mortgage also includes owner occupied commercial real estate which shares a similar risk profile to our commercial and industrial products.
- Consumer real-estate mortgage loans. Consumer real-estate mortgage consists primarily of loans secured by 1-4 residential properties including home equity lines of credit.
- Construction and land development loans. Construction and land development loans include loans where the repayment is dependent on the successful operation of the related real estate project. Construction and land

development loans include 1-4 family construction projects and commercial construction endeavors such as warehouses, apartments, office and retail space and land acquisition and development.

- Commercial and industrial loans. Commercial and industrial loans include loans to business enterprises issued for commercial, industrial and/or other professional purposes.
- Consumer and other loans. Consumer and other loans include all loans issued to individuals not included in the consumer real-estate mortgage classification. Examples of consumer and other loans are automobile loans, credit cards and loans to finance education, among others.

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Commercial loans receive risk ratings assigned by a financial advisor and approved by a senior credit officer subject to validation by Pinnacle Financial's independent loan review department. Risk ratings are categorized as pass, special mention, substandard, substandard-nonaccrual or doubtful-nonaccrual. Pinnacle Financial believes that its categories follow those used by Pinnacle Bank's primary regulators. At September 30, 2015, approximately 74% of our legacy Pinnacle loan portfolio was analyzed as a commercial loan type with a specifically assigned risk rating in the allowance for loan loss assessment. Consumer loans and small business loans are generally not assigned an individual risk rating but are evaluated as either accrual or nonaccrual based on the performance of the individual loans. However, certain consumer real-estate mortgage loans and certain consumer and other loans receive a specific risk rating due to the loan proceeds being used for commercial purposes even though the collateral may be of a consumer loan nature.

Risk ratings are subject to continual review by a financial advisor and a senior credit officer. At least annually, our credit procedures require that every risk rated loan of $500,000 or more be subject to a formal credit risk review process by the assigned financial advisor. Each loan's risk rating is also subject to review by our independent loan review department, which reviews a substantial portion of our risk rated portfolio annually. Included in the coverage are independent loan reviews of loans in targeted higher-risk portfolio segments such as certain commercial and industrial loans, land loans and/or loan types in certain geographies.

The following table presents our loan balances by primary loan classification and the amount within each risk rating category. Pass rated loans include all credits other than those included in special mention, substandard, substandard-nonaccrual and doubtful-nonaccrual which are defined as follows:

Special mention loans have potential weaknesses that deserve management's close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the asset or in Pinnacle Financial's credit position at some future date.

Substandard loans are inadequately protected by the current sound worth and paying capacity of the obligor or of the collateral pledged, if any. Assets so classified must have a well-defined weakness or weaknesses that jeopardize collection of the debt. Substandard loans are characterized by the distinct possibility that Pinnacle Financial will sustain some loss if the deficiencies are not corrected.

Substandard-nonaccrual loans are substandard loans that have been placed on nonaccrual status.

Doubtful-nonaccrual loans have all the characteristics of substandard-nonaccrual loans with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently existing facts, conditions and values, highly questionable and improbable.

The following table outlines the amount of each loan classification categorized into each risk rating category as of September 30, 2015 and December 31, 2014 (in thousands):

	Commercial real estate - mortgage	Consumer real estate - mortgage	Construction and land development	Commercial and industrial	Consumer and other	Total
September 30, 2015						
Accruing loans						
Pass	$2,138,361	$1,015,126	$ 659,275	$2,081,298	$239,212	$6,133,272
Special Mention	21,038	3,196	5,348	42,527	952	73,061
Substandard (1)	25,297	12,756	3,805	49,376	-	91,234
Total	2,184,696	1,031,078	668,428	2,173,201	240,164	6,297,567
Impaired loans						
Nonaccrual loans(3)						
Substandard-nonaccrual &#1	7,232	9,421	6,498	1,122	5,776	30,049