TRUSTMARK CORP
Form 10-Q
May 08, 2013

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

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Form 10-Q

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

For the quarterly period ended March 31, 2013

or

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

For the transition period from ___________________ to ___________________

Commission file number 000-03683

Trustmark Corporation
(Exact name of registrant as specified in its charter)

| Mississippi<br>(State or other jurisdiction of incorporation or organization) | 64-0471500<br>(I.R.S. Employer Identification No.) |
|---|---|
| 248 East Capitol Street, Jackson, Mississippi<br>(Address of principal executive offices) | 39201<br>(Zip Code) |

(601) 208-5111
(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes þ No o

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting

company” in Rule 12b of the Exchange Act.

| | |
|---|---|
| Large accelerated filer þ | Accelerated filer o |
| Non-accelerated filer o (Do not check if a smaller reporting company) | Smaller reporting company o |

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

As of April 30, 2013, there were 67,162,685 shares outstanding of the registrant’s common stock (no par value).

Forward-Looking Statements

Certain statements contained in this document constitute forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. You can identify forward-looking statements by words such as “may,” “hope,” “will,” “should,” “expect,” “plan,” “anticipate,” “intend,” “believe,” “estimate,” “predict,” “potential,” “continue,” “cou negative of those terms or other words of similar meaning. You should read statements that contain these words carefully because they discuss our future expectations or state other “forward-looking” information. These forward-looking statements include, but are not limited to, statements relating to anticipated future operating and financial performance measures, including net interest margin, credit quality, business initiatives, growth opportunities and growth rates, among other things, and encompass any estimate, prediction, expectation, projection, opinion, anticipation, outlook or statement of belief included therein as well as the management assumptions underlying these forward-looking statements. You should be aware that the occurrence of the events described under the caption “Risk Factors” in Trustmark’s filings with the Securities and Exchange Commission could have an adverse effect on our business, results of operations and financial condition. Should one or more of these risks materialize, or should any such underlying assumptions prove to be significantly different, actual results may vary significantly from those anticipated, estimated, projected or expected.

Risks that could cause actual results to differ materially from current expectations of Management include, but are not limited to, changes in the level of nonperforming assets and charge-offs, local, state and national economic and market conditions, including the extent and duration of the current volatility in the credit and financial markets, changes in our ability to measure the fair value of assets in our portfolio, material changes in the level and/or volatility of market interest rates, the performance and demand for the products and services we offer, including the level and timing of withdrawals from our deposit accounts, the costs and effects of litigation and of unexpected or adverse outcomes in such litigation, our ability to attract noninterest-bearing deposits and other low-cost funds, competition in loan and deposit pricing, as well as the entry of new competitors into our markets through de novo expansion and acquisitions, economic conditions, including the potential impact of the European financial crisis on the U.S. economy and the markets we serve, and monetary and other governmental actions designed to address the level and volatility of interest rates and the volatility of securities, currency and other markets, the enactment of legislation and changes in existing regulations, or enforcement practices, or the adoption of new regulations, changes in accounting standards and practices, including changes in the interpretation of existing standards, that affect our consolidated financial statements, changes in consumer spending, borrowings and savings habits, technological changes, changes in the financial performance or condition of our borrowers, changes in our ability to control expenses, changes in our compensation and benefit plans, greater than expected costs or difficulties related to the integration of acquisitions or new products and lines of business, natural disasters, environmental disasters, acts of war or terrorism, the ability to maintain relationships with customers, employees or suppliers as well as the ability to successfully integrate the business and realize cost savings and any other synergies from the BancTrust Financial Group, Inc., (BancTrust) merger as well as the risk that the credit ratings of the combined company or its subsidiaries may be different from what the companies expect, and other risks described in our filings with the Securities and Exchange Commission.

Although we believe that the expectations reflected in such forward-looking statements are reasonable, we can give no assurance that such expectations will prove to be correct. Except as required by law, we undertake no obligation to update or revise any of this information, whether as the result of new information, future events or developments or otherwise.

PART I. FINANCIAL INFORMATION
ITEM 1. FINANCIAL STATEMENTS

Trustmark Corporation and Subsidiaries
Consolidated Balance Sheets
($ in thousands)

| | (Unaudited) March 31, 2013 | December 31, 2012 |
|---|---|---|
| Assets | | |
| Cash and due from banks (noninterest-bearing) | $242,896 | $231,489 |
| Federal funds sold and securities purchased under reverse repurchase agreements | 5,926 | 7,046 |
| Securities available for sale (at fair value) | 3,546,083 | 2,657,745 |
| Securities held to maturity (fair value: $78,096-2013; $46,888-2012) | 73,666 | 42,188 |
| Loans held for sale (LHFS) | 207,758 | 257,986 |
| Loans held for investment (LHFI) | 5,474,396 | 5,592,754 |
| Less allowance for loan losses, LHFI | 76,900 | 78,738 |
| Net LHFI | 5,397,496 | 5,514,016 |
| Acquired loans: | | |
| Noncovered loans | 1,003,127 | 81,523 |
| Covered loans | 47,589 | 52,041 |
| Less allowance for loan losses, acquired loans | 6,458 | 6,075 |
| Net acquired loans | 1,044,258 | 127,489 |
| Net LHFI and acquired loans | 6,441,754 | 5,641,505 |
| Premises and equipment, net | 210,789 | 154,841 |
| Mortgage servicing rights | 51,529 | 47,341 |
| Goodwill | 366,366 | 291,104 |
| Identifiable intangible assets | 49,361 | 17,306 |
| Other real estate, excluding covered other real estate | 118,406 | 78,189 |
| Covered other real estate | 5,879 | 5,741 |
| FDIC indemnification asset | 20,198 | 21,774 |
| Other assets | 509,904 | 374,412 |
| Total Assets | $11,850,515 | $9,828,667 |
| | | |
| Liabilities | | |
| Deposits: | | |
| Noninterest-bearing | $2,534,287 | $2,254,211 |
| Interest-bearing | 7,375,144 | 5,642,306 |
| Total deposits | 9,909,431 | 7,896,517 |
| Federal funds purchased and securities sold under repurchase agreements | 219,769 | 288,829 |
| Short-term borrowings | 46,325 | 86,920 |
| Long-term FHLB advances | 10,969 | - |
| Subordinated notes | 49,879 | 49,871 |
| Junior subordinated debt securities | 94,856 | 61,856 |
| Other liabilities | 166,340 | 157,305 |
| Total Liabilities | 10,497,569 | 8,541,298 |

| | | |
|---|---|---|
| Shareholders' Equity | | |
| Common stock, no par value: | | |
| Authorized: 250,000,000 shares | | |
| Issued and outstanding: 67,151,087 shares - 2013; 64,820,414 shares - 2012 | 13,992 | 13,506 |
| Capital surplus | 342,233 | 285,905 |
| Retained earnings | 991,012 | 984,563 |
| Accumulated other comprehensive income, net of tax | 5,709 | 3,395 |
| Total Shareholders' Equity | 1,352,946 | 1,287,369 |
| Total Liabilities and Shareholders' Equity | $11,850,515 | $9,828,667 |

See notes to consolidated financial statements.

Trustmark Corporation and Subsidiaries
Consolidated Statements of Income
($ in thousands except per share data)
(Unaudited)

| | Three Months Ended March 31, | |
|---|---|---|
| | 2013 | 2012 |
| Interest Income | | |
| Interest and fees on LHFI & LHFS | $64,463 | $72,859 |
| Interest and fees on acquired loans | 12,782 | 2,937 |
| Interest on securities: | | |
| Taxable | 16,539 | 18,384 |
| Tax exempt | 1,312 | 1,366 |
| Interest on federal funds sold and securities purchased under reverse repurchase agreements | 4 | 6 |
| Other interest income | 355 | 330 |
| Total Interest Income | 95,455 | 95,882 |
| | | |
| Interest Expense | | |
| Interest on deposits | 4,909 | 7,353 |
| Interest on federal funds purchased and securities sold under repurchase agreements | 81 | 171 |
| Other interest expense | 1,490 | 1,414 |
| Total Interest Expense | 6,480 | 8,938 |
| Net Interest Income | 88,975 | 86,944 |
| Provision for loan losses, LHFI | (2,968) | 3,293 |
| Provision for loan losses, acquired loans | 130 | (194) |
| Net Interest Income After Provision for Loan Losses | 91,813 | 83,845 |
| | | |
| Noninterest Income | | |
| Service charges on deposit accounts | 11,681 | 12,211 |
| Bank card and other fees | 7,945 | 7,364 |
| Mortgage banking, net | 11,583 | 7,295 |
| Insurance commissions | 7,242 | 6,606 |
| Wealth management | 6,875 | 5,501 |
| Other, net | (1,191) | 3,758 |
| Securities gains, net | 204 | 1,050 |
| Total Noninterest Income | 44,339 | 43,785 |
| | | |
| Noninterest Expense | | |
| Salaries and employee benefits | 53,592 | 46,432 |
| Services and fees | 13,032 | 10,747 |
| Net occupancy - premises | 5,955 | 4,938 |
| Equipment expense | 5,674 | 4,912 |
| ORE/Foreclosure expense | 3,820 | 3,902 |
| FDIC assessment expense | 2,021 | 1,775 |
| Other expense | 18,051 | 13,068 |
| Total Noninterest Expense | 102,145 | 85,774 |
| Income Before Income Taxes | 34,007 | 41,856 |

| | | |
|---|---|---|
| Income taxes | 9,141 | 11,536 |
| Net Income | $24,866 | $30,320 |
| | | |
| Earnings Per Common Share | | |
| Basic | $0.38 | $0.47 |
| | | |
| Diluted | $0.38 | $0.47 |
| | | |
| Dividends Per Common Share | $0.23 | $0.23 |

See notes to consolidated financial statements.

Trustmark Corporation and Subsidiaries
Consolidated Statements of Comprehensive Income
($ in thousands)
(Unaudited)

| | Three Months Ended March 31, | |
|---|---|---|
| | 2013 | 2012 |
| Net income per consolidated statements of income | $24,866 | $30,320 |
| Other comprehensive income (loss), net of tax: | | |
| Unrealized gains (losses) on available for sale securities: | | |
| Unrealized holding gains (losses) arising during the period | 1,380 | (1,916) |
| Less: adjustment for net gains realized in net income | (126) | (648) |
| Pension and other postretirement benefit plans: | | |
| Change in the net actuarial loss during the period | 1,060 | 980 |
| Other comprehensive income (loss), net of tax: | 2,314 | (1,584) |
| Comprehensive income | $27,180 | $28,736 |

See notes to consolidated financial statements.

Trustmark Corporation and Subsidiaries
Consolidated Statements of Changes in Shareholders' Equity
($ in thousands)
(Unaudited)

| | 2013 | 2012 |
|---|---|---|
| Balance, January 1, | $1,287,369 | $1,215,037 |
| Net income per consolidated statements of income | 24,866 | 30,320 |
| Other comprehensive income (loss) | 2,314 | (1,584) |
| Common stock dividends paid | (15,560) | (14,900) |
| Common stock issued-net, long-term incentive plans: | | |
| Stock options | 109 | 33 |
| Restricted stock | (938) | (1,187) |
| Excess tax benefit from stock-based compensation arrangements | 269 | 674 |
| Compensation expense, long-term incentive plans | 1,022 | 1,127 |
| Common stock issued, business combinations | 53,495 | 12,000 |
| Balance, March 31, | $1,352,946 | $1,241,520 |

See notes to consolidated financial statements.

Trustmark Corporation and Subsidiaries
Consolidated Statements of Cash Flows
($ in thousands)
(Unaudited)

| | Three Months Ended March 31, | |
|---|---|---|
| | 2013 | 2012 |
| Operating Activities | | |
| Net income | $24,866 | $30,320 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Provision for loan losses, net | (2,838) | 3,099 |
| Depreciation and amortization | 8,380 | 6,589 |
| Net amortization of securities | 1,868 | 1,618 |
| Securities gains, net | (204) | (1,050) |
| Gains on sales of loans, net | (10,165) | (6,460) |
| Bargain purchase gain on acquisition | - | (2,754) |
| Deferred income tax provision | 2,157 | 1,880 |
| Proceeds from sales of loans held for sale | 402,159 | 378,255 |
| Purchases and originations of loans held for sale | (382,425) | (388,370) |
| Originations and sales of mortgage servicing rights, net | (5,521) | (4,478) |
| Net (increase) decrease in other assets | (45,074) | 4,000 |
| Net (decrease) increase in other liabilities | (5,740) | 10,674 |
| Other operating activities, net | 1,903 | 2,993 |
| Net cash (used in) provided by operating activities | (10,634) | 36,316 |
| | | |
| Investing Activities | | |
| Proceeds from calls and maturities of securities held to maturity | 3,580 | 5,699 |
| Proceeds from calls and maturities of securities available for sale | 272,858 | 234,155 |
| Proceeds from sales of securities available for sale | 38,742 | - |
| Purchases of securities held to maturity | (35,045) | - |
| Purchases of securities available for sale | (667,299) | (374,785) |
| Net decrease in federal funds sold and securities purchased under reverse repurchase agreements | 1,120 | 2,957 |
| Net decrease in loans | 145,517 | 74,593 |
| Purchases of premises and equipment | (2,228) | (6,909) |
| Proceeds from sales of other real estate | 8,297 | 10,039 |
| Net cash received in business combinations | 89,037 | 78,151 |
| Net cash (used in) provided by investing activities | (145,421) | 23,900 |
| | | |
| Financing Activities | | |
| Net increase in deposits | 272,660 | 315,587 |
| Net decrease in federal funds purchased and securities sold under repurchase agreements | (69,060) | (349,622) |
| Net (decrease) increase in short-term borrowings | (19,936) | 74 |
| Payments on long-term FHLB advances | (82) | - |
| Common stock dividends | (15,560) | (14,900) |
| Common stock issued-net, long-term incentive plans | (829) | (1,154) |
| Excess tax benefit from stock-based compensation arrangements | 269 | 674 |
| Net cash provided by (used in) financing activities | 167,462 | (49,341) |

| | | |
|---|---|---|
| Increase in cash and cash equivalents | 11,407 | 10,875 |
| Cash and cash equivalents at beginning of period | 231,489 | 202,625 |
| Cash and cash equivalents at end of period | $242,896 | $213,500 |

See notes to consolidated financial statements.

Trustmark Corporation and Subsidiaries
Notes to Consolidated Financial Statements
(Unaudited)

Note 1 – Business, Basis of Financial Statement Presentation and Principles of Consolidation

Trustmark Corporation (Trustmark) is a multi-bank holding company headquartered in Jackson, Mississippi. Through its subsidiaries, Trustmark operates as a financial services organization providing banking and financial solutions to corporate institutions and individual customers through approximately 220 offices in Alabama, Florida, Mississippi, Tennessee and Texas.

The consolidated financial statements in this quarterly report on Form 10-Q include the accounts of Trustmark and all other entities in which Trustmark has a controlling financial interest. All significant intercompany accounts and transactions have been eliminated in consolidation.

The accompanying unaudited condensed consolidated financial statements have been prepared in conformity with U.S. generally accepted accounting principles (GAAP) for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by U.S. GAAP for complete financial statements and should be read in conjunction with the consolidated financial statements, and notes thereto, included in Trustmark's 2012 annual report on Form 10-K.

Operating results for the interim periods disclosed herein are not necessarily indicative of the results that may be expected for a full year or any future period. Certain reclassifications have been made to prior period amounts to conform to the current period presentation. In the opinion of Management, all adjustments (consisting of normal recurring accruals) considered necessary for the fair presentation of these consolidated financial statements have been included. The preparation of financial statements in conformity with these accounting principles requires Management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and income and expense during the reporting period and the related disclosures. Although Management's estimates contemplate current conditions and how they are expected to change in the future, it is reasonably possible that in 2013 actual conditions could vary from those anticipated, which could affect our results of operations and financial condition. The allowance for loan losses, the amount and timing of expected cash flows from acquired loans and the Federal Deposit Insurance Corporation (FDIC) indemnification asset, the valuation of other real estate, the fair value of mortgage servicing rights, the valuation of goodwill and other identifiable intangibles, the status of contingencies and the fair values of financial instruments are particularly subject to change. Actual results could differ from those estimates.

Note 2 – Business Combinations

Oxford, Mississippi Branches

On March 29, 2013, Trustmark National Bank (TNB), a subsidiary of Trustmark, announced the signing of a definitive Branch Purchase and Assumption Agreement (the Agreement) pursuant to which TNB will acquire the two branches of SOUTHBank, F.S.B. (SOUTHBank), serving the Oxford, Mississippi market. The Agreement contemplates the assumption of selected deposit accounts of approximately $11.8 million as well as the purchase of the physical branch offices. The proposed transaction, which is subject to regulatory approval and customary closing conditions, is expected to be completed during the summer of 2013. The proposed transaction is not material to Trustmark's consolidated financial statements and is not considered a business combination in accordance with FASB ASC Topic 805, "Business Combinations."

BancTrust Financial Group, Inc.

On February 15, 2013, Trustmark completed its merger with BancTrust Financial Group, Inc. (BancTrust), a 26-year-old bank holding company headquartered in Mobile, Alabama. In accordance with the terms of the definitive agreement, the holders of BancTrust common stock received 0.125 of a share of Trustmark common stock for each share of BancTrust common stock in a tax-free exchange. Trustmark issued approximately 2.24 million shares of its common stock for all issued and outstanding shares of BancTrust common stock. The total value of the 2.24 million shares of Trustmark common stock issued to the BancTrust shareholders on the acquisition date was approximately $53.5 million, based on a closing stock price of $23.83 per share of Trustmark common stock on February 15, 2013. At closing, Trustmark repurchased the $50.0 million of BancTrust preferred stock and associated warrant issued to the U.S. Department of Treasury under the Capital Purchase Program for approximately $52.6 million.

This acquisition was accounted for under the acquisition method in accordance with FASB ASC Topic 805. Accordingly, the assets and liabilities, both tangible and intangible, are recorded at their estimated fair values as of the acquisition date. The estimated fair values were considered preliminary as of March 31, 2013 and are subject to refinement as additional information relative to the closing date fair values becomes available through the measurement period, which is not to exceed one year from the acquisition date of February 15, 2013.



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The acquisition of BancTrust is consistent with Trustmark's strategic plan to selectively expand the Trustmark franchise. The acquisition of BancTrust provided Trustmark entry into more than 15 markets in Alabama and enhanced the Trustmark franchise in the Florida Panhandle. The statement of assets purchased and liabilities assumed in the BancTrust acquisition is presented below at their estimated fair values as of the acquisition date of February 15, 2013 ($ in thousands):

| | | |
|---|---|---|
| Assets: | | |
| Cash and due from banks | $ | 141,616 |
| Securities | | 528,016 |
| Loans held for sale | | 1,050 |
| Acquired noncovered loans | | 951,011 |
| Premises and equipment, net | | 57,146 |
| Identifiable intangible assets | | 33,498 |
| Other real estate | | 41,168 |
| Other assets | | 98,373 |
| Total Assets | | 1,851,878 |
| | | |
| Liabilities: | | |
| Deposits | | 1,740,254 |
| Other borrowings | | 64,051 |
| Other liabilities | | 16,761 |
| Total Liabilities | | 1,821,066 |
| | | |
| Net identified assets acquired at fair value | | 30,812 |
| Goodwill | | 75,262 |
| Net assets acquired at fair value | $ | 106,074 |

The excess of the consideration paid over the estimated fair value of the net assets acquired was $75.3 million, which was recorded as goodwill under FASB ASC Topic 805. The identifiable intangible assets acquired represent the core deposit intangible at fair value at the acquisition date. The core deposit intangible is being amortized on an accelerated basis over the estimated useful life, currently expected to be approximately 10 years.

Loans acquired from BancTrust were evaluated under a fair value process involving various degrees of deterioration in credit quality since origination, and also for those loans for which it was probable at acquisition that Trustmark would not be able to collect all contractually required payments. These loans, with the exception of revolving credit agreements and leases, are referred to as acquired impaired loans and are accounted for in accordance with FASB ASC Topic 310-30, "Loans and Debt Securities Acquired with Deteriorated Credit Quality." Refer to Note 5 – Acquired Loans for further information on acquired loans.

The following table illustrates loans (including LHFS) and other real estate acquired from BancTrust, the credit mark and the resulting fair values as of February 15, 2013 ($ in thousands):

| | | Balance 2/15/2013 | | Total Credit Mark $ | | % | | Fair Value 2/15/2013 |
|---|---|---|---|---|---|---|---|---|
| Loans secured by real estate: | | | | | | | | |
| Construction, land development and other land loans | $ | 236,237 | $ | 100,045 | 42.3 | % | $ | 136,192 |
| Secured by 1-4 family residential properties | | 216,444 | | 22,914 | 10.6 | % | | 193,530 |
| Secured by nonfarm, nonresidential properties | | 329,026 | | 28,140 | 8.6 | % | | 300,886 |

| | | | | |
|---|---|---|---|---|
| Other real estate secured | 34,715 | 2,751 | 7.9 % | 31,964 |
| Commercial and industrial loans | 262,536 | 25,489 | 9.7 % | 237,047 |
| Consumer loans | 40,808 | 2,152 | 5.3 % | 38,656 |
| Other loans | 14,248 | 462 | 3.2 % | 13,786 |
| Total loans acquired from BancTrust | 1,134,014 | 181,953 | 16.0 % | 952,061 |
| Other real estate | 58,083 | 16,915 | 29.1 % | 41,168 |
| Total loans and other real estate acquired from BancTrust | $ 1,192,097 | $ 198,868 | 16.7 % | $ 993,229 |

The operations of BancTrust are included in Trustmark's operating results from February 15, 2013, and added revenue of $9.4 million and net income available to common shareholders, excluding non-routine transaction expenses, of approximately $2.0 million through March 31, 2013. Included in noninterest expense during the first quarter of 2013 are non-routine BancTrust transaction expenses totaling approximately $9.4 million (change in control and severance expense of $1.4 million included in salaries and benefits; professional fees, contract termination and other expenses of $7.9 million included in other expense). Such operating results are not necessarily indicative of future operating results.

The following table presents the unaudited pro forma financial information as if the acquisition of BancTrust had occurred on January 1, 2012. The unaudited pro forma information for the three months ended March 31, 2013 and 2012, contains certain adjustments, including acquisition accounting fair value adjustments, amortization of the core deposit intangible and related income tax effects. The non-routine transaction expenses related to the BancTrust acquisition incurred during the first three months of 2013 as well as potential cost savings from the acquisition are not reflected in the unaudited pro forma amounts. The unaudited pro forma financial information is not necessarily indicative of the results of operations that would have occurred had the acquisition been effected on the assumed date ($ in thousands except per share data).

| | Pro Forma Three Months Ended March 31, | |
|---|---|---|
| | 2013 | 2012 |
| Net Interest Income | $96,514 | $102,872 |
| Total Noninterest Income | 46,202 | 47,634 |
| Net Income | 32,675 | 34,531 |
| Pro Forma Earnings Per Common Share | | |
| Basic | $0.49 | $0.52 |
| Diluted | $0.49 | $0.52 |

Bay Bank & Trust Company

On March 16, 2012, Trustmark completed its merger with Bay Bank & Trust Co. (Bay Bank), a 76-year old financial institution headquartered in Panama City, Florida. Trustmark acquired all outstanding common stock of Bay Bank for approximately $22 million in cash and stock, comprised of $10 million in cash and the issuance of approximately 510 thousand shares of Trustmark common stock valued at $12 million. This acquisition was accounted for under the acquisition method in accordance with FASB ASC Topic 805. Accordingly, the assets and liabilities, both tangible and intangible, are recorded at their estimated fair values as of the acquisition date. The purchase price allocation was deemed preliminary as of March 31, 2012 and was finalized in the second quarter of 2012.

The statement of assets purchased and liabilities assumed in the Bay Bank acquisition is presented below at their estimated fair values as of the acquisition date of March 16, 2012 ($ in thousands):

| | |
|---|---|
| Assets: | |
| Cash and due from banks | $ 88,154 |
| Securities available for sale | 26,369 |
| Acquired noncovered loans | 97,914 |
| Premises and equipment, net | 9,466 |
| Identifiable intangible assets | 7,017 |
| Other real estate | 2,569 |
| Other assets | 3,471 |
| Total Assets | 234,960 |
| | |
| Liabilities: | |
| Deposits | 208,796 |
| Other liabilities | 526 |
| Total Liabilities | 209,322 |
| | |
| Net assets acquired at fair value | 25,638 |
| Consideration paid to Bay Bank | 22,003 |
| | |
| Bargain purchase gain | 3,635 |
| Income taxes | - |
| Bargain purchase gain, net of taxes | $ 3,635 |

The bargain purchase gain represents the excess of the net of the estimated fair value of the assets acquired and liabilities assumed over the consideration paid to Bay Bank. Initially, Trustmark recognized a bargain purchase gain of $2.8 million during the first quarter of 2012 and subsequently increased the bargain purchase gain $881 thousand during the second quarter of 2012 as the fair values associated with the Bay Bank acquisition were finalized. The gain of $3.6 million recognized by Trustmark is considered a gain from a bargain purchase under FASB ASC Topic 805 and is included in other noninterest income. Included in noninterest expense during the first quarter of 2012 are non-routine Bay Bank transaction expenses totaling approximately $2.6 million (change in control and severance expense of $672 thousand included in salaries and benefits; contract termination and other expenses of $1.9 million included in other expense).

The identifiable intangible assets represent the core deposit intangible at fair value at the acquisition date. The core deposit intangible is being amortized on an accelerated basis over the estimated useful life, currently expected to be approximately 10 years.

Loans acquired from Bay Bank were evaluated under a fair value process involving various degrees of deterioration in credit quality since origination, and also for those loans for which it was probable at acquisition that Trustmark would not be able to collect all contractually required payments. These loans, with the exception of revolving credit agreements, are referred to as acquired impaired loans and are accounted for in accordance with FASB ASC Topic 310-30. Refer to Note 5 – Acquired Loans for further information on acquired loans.

Fair Value of Acquired Financial Instruments

For financial instruments measured at fair value, Trustmark utilized Level 2 inputs to determine the fair value of securities available for sale, time deposits (included in deposits above) and FHLB advances.  Level 3 inputs were used to determine the fair value of acquired loans, identifiable intangible assets, and other real estate.  The methodology and significant assumptions used in estimating the fair values of these financial assets and liabilities are as follows:

Securities Available for Sale

Estimated fair values for securities available for sale are based on quoted market prices where available.  If quoted market prices are not available, estimated fair values are based on quoted market prices of comparable instruments.

Acquired Loans

Fair value of acquired loans is determined using a discounted cash flow model based on assumptions regarding the amount and timing of principal and interest payments, estimated prepayments, estimated default rates, estimated loss severity in the event of defaults and current market rates.

Identifiable Intangible Assets

The fair value assigned to the identifiable intangible assets, in this case core deposit intangibles, represent the future economic benefit of the potential cost savings from acquiring core deposits in the acquisition compared to the cost of obtaining alternative funding from market sources.

Other Real Estate

Other real estate was initially recorded at its estimated fair value on the acquisition date based on similar market comparable valuations less estimated selling costs.

Time Deposits

Time deposits were valued by projecting expected cash flows into the future based on each account's contracted rate and then determining the present value of those expected cash flows using current rates for deposits with similar maturities.

FHLB Advances

FHLB advances were valued by projecting expected cash flows into the future based on each account's contracted rate and then determining the present value of those expected cash flows using current rates for advances with similar maturities.

Please refer to Note 16 – Fair Value for more information on Trustmark's classification of financial instruments based on valuation inputs within the fair value hierarchy.

Note 3 – Securities Available for Sale and Held to Maturity

The following table is a summary of the amortized cost and estimated fair value of securities available for sale and held to maturity ($ in thousands):

| | Securities Available for Sale | | | | Securities Held to Maturity | | | |
|---|---|---|---|---|---|---|---|---|
| March 31, 2013 | Amortized Cost | Gross Unrealized Gains | Gross Unrealized (Losses) | Estimated Fair Value | Amortized Cost | Gross Unrealized Gains | Gross Unrealized (Losses) | Estimated Fair Value |
| U.S. Treasury securities | $506 | $ - | $ - | $506 | $- | $ - | $ - | $- |
| U.S. Government agency obligations | | | | | | | | |
| Issued by U.S. Government agencies | 138,449 | 2,896 | (119 ) | 141,226 | - | - | - | - |
| Issued by U.S. Government sponsored agencies | 185,541 | 938 | (186 ) | 186,293 | - | - | - | - |
| Obligations of states and political subdivisions | 206,189 | 12,295 | (17 ) | 218,467 | 33,071 | 4,058 | - | 37,129 |
| Mortgage-backed securities | | | | | | | | |
| Residential mortgage pass-through securities | | | | | | | | |
| Guaranteed by GNMA | 50,560 | 768 | (190 ) | 51,138 | 2,932 | 207 | - | 3,139 |
| Issued by FNMA and FHLMC | 234,806 | 6,577 | (18 ) | 241,365 | 569 | 49 | - | 618 |
| Other residential mortgage-backed securities | | | | | | | | |
| Issued or guaranteed by FNMA, FHLMC or GNMA | 2,059,567 | 31,724 | (775 ) | 2,090,516 | - | - | - | - |
| Commercial mortgage-backed securities | | | | | | | | |
| Issued or guaranteed by FNMA, FHLMC or GNMA | 359,650 | 17,701 | (281 ) | 377,070 | 37,094 | 208 | (92 ) | 37,210 |
| Asset-backed securities | 236,016 | 3,486 | - | 239,502 | - | - | - | - |
| Total | $3,471,284 | $ 76,385 | $ (1,586 ) | $3,546,083 | $73,666 | $ 4,522 | $ (92 ) | $ 78,096 |

December 31, 2012

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| U.S. Government agency obligations | | | | | | | | |
| Issued by U.S. Government agencies | $10 | $ - | $ - | $10 | $- | $ - | $ - | $ - |
| Issued by U.S. Government sponsored agencies | 105,396 | 339 | - | 105,735 | - | - | - | - |
| Obligations of states and political subdivisions | 202,877 | 12,900 | (16 ) | 215,761 | 36,206 | 4,184 | - | 40,390 |
| Mortgage-backed securities | | | | | | | | |
| Residential mortgage pass-through securities | | | | | | | | |
| Guaranteed by GNMA | 18,981 | 921 | - | 19,902 | 3,245 | 227 | - | 3,472 |
| Issued by FNMA and FHLMC | 201,493 | 7,071 | - | 208,564 | 572 | 52 | - | 624 |
| Other residential mortgage-backed securities | | | | | | | | |
| Issued or guaranteed by FNMA, FHLMC or GNMA | 1,436,812 | 29,574 | (20 ) | 1,466,366 | - | - | - | - |
| Commercial mortgage-backed securities | | | | | | | | |
| Issued or guaranteed by FNMA, FHLMC or GNMA | 380,514 | 19,420 | (154 ) | 399,780 | 2,165 | 237 | - | 2,402 |
| Asset-backed securities | 238,893 | 2,755 | (21 ) | 241,627 | - | - | - | - |
| Total | $2,584,976 | $ 72,980 | $ (211 ) | $2,657,745 | $42,188 | $ 4,700 | $ - | $46,888 |

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Temporarily Impaired Securities

The table below includes securities with gross unrealized losses segregated by length of impairment ($ in thousands):

| | Less than 12 Months | | 12 Months or More | | Total | |
|---|---|---|---|---|---|---|
| March 31, 2013 | Estimated Fair Value | Gross Unrealized (Losses) | Estimated Fair Value | Gross Unrealized (Losses) | Estimated Fair Value | Gross Unrealized (Losses) |
| U.S. Government agency obligations | | | | | | |
| Issued by U.S. Government agencies | $11,007 | $(119) | $- | $- | $11,007 | $(119) |
| Issued by U.S. Government sponsored agencies | 39,920 | (186) | - | - | 39,920 | (186) |
| Obligations of states and political subdivisions | 3,689 | (16) | 573 | (1) | 4,262 | (17) |
| Mortgage-backed securities | | | | | | |
| Residential mortgage pass-through securities | | | | | | |
| Guaranteed by GNMA | 30,062 | (190) | - | - | 30,062 | (190) |
| Issued by FNMA and FHLMC | 39,551 | (18) | - | - | 39,551 | (18) |
| Other residential mortgage-backed securities | | | | | | |
| Issued or guaranteed by FNMA, FHLMC or GNMA | 263,436 | (775) | - | - | 263,436 | (775) |
| Commercial mortgage-backed securities | | | | | | |
| Issued or guaranteed by FNMA, FHLMC or GNMA | 64,343 | (373) | - | - | 64,343 | (373) |
| Total | $452,008 | $(1,677) | $573 | $(1) | $452,581 | $(1,678) |
| | | | | | | |
| December 31, 2012 | | | | | | |
| Obligations of states and political subdivisions | $5,878 | $(16) | $- | $- | $5,878 | $(16) |
| Mortgage-backed securities | | | | | | |
| Other residential mortgage-backed securities | | | | | | |
| Issued or guaranteed by FNMA, FHLMC or GNMA | 3,055 | (20) | - | - | 3,055 | (20) |
| Commercial mortgage-backed securities | | | | | | |
| Issued or guaranteed by FNMA, FHLMC or GNMA | - | - | 16,339 | (154) | 16,339 | (154) |
| Asset-backed securities | 16,412 | (21) | - | - | 16,412 | (21) |
| Total | $25,345 | $(57) | $16,339 | $(154) | $41,684 | $(211) |

Declines in the fair value of held-to-maturity and available-for-sale securities below their cost that are deemed to be other than temporary are reflected in earnings as realized losses to the extent the impairment is related to credit losses. The amount of the impairment related to other factors is recognized in other comprehensive income (loss). In

estimating other-than-temporary impairment losses, Management considers, among other things, the length of time and the extent to which the fair value has been less than cost, the financial condition and near-term prospects of the issuer and the intent and ability of Trustmark to hold the security for a period of time sufficient to allow for any anticipated recovery in fair value. The unrealized losses shown above are primarily due to increases in market rates over the yields available at the time of purchase of the underlying securities and not credit quality. Because Trustmark does not intend to sell these securities and it is more likely than not that Trustmark will not be required to sell the investments before recovery of their amortized cost bases, which may be maturity, Trustmark does not consider these investments to be other-than-temporarily impaired at March 31, 2013. There were no other-than-temporary impairments for the three months ended March 31, 2013 and 2012.

Security Gains and Losses

Gains and losses as a result of calls and dispositions of securities were as follows ($ in thousands):

| | Three Months Ended March 31, | |
|---|---|---|
| Available for Sale | 2013 | 2012 |
| Proceeds from calls and sales of securities | $ 35,748 | $ - |
| Gross realized gains | 204 | 1,050 |

Realized gains and losses are determined using the specific identification method and are included in noninterest income as securities gains, net.

Contractual Maturities

The amortized cost and estimated fair value of securities available for sale and held to maturity at March 31, 2013, by contractual maturity, are shown below ($ in thousands). 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.

| | Securities Available for Sale | | Securities Held to Maturity | |
|---|---|---|---|---|
| | Amortized Cost | Estimated Fair Value | Amortized Cost | Estimated Fair Value |
| Due in one year or less | $12,298 | $12,349 | $1,622 | $1,634 |
| Due after one year through five years | 106,600 | 110,902 | 15,450 | 16,744 |
| Due after five years through ten years | 389,757 | 399,690 | 14,772 | 17,456 |
| Due after ten years | 258,046 | 263,053 | 1,227 | 1,295 |
| | 766,701 | 785,994 | 33,071 | 37,129 |
| Mortgage-backed securities | 2,704,583 | 2,760,089 | 40,595 | 40,967 |
| Total | $3,471,284 | $3,546,083 | $73,666 | $78,096 |

Note 4 – Loans Held for Investment (LHFI) and Allowance for Loan Losses, LHFI

For the periods presented, LHFI consisted of the following ($ in thousands):

| | March 31, 2013 | December 31, 2012 |
|---|---|---|
| Loans secured by real estate: | | |
| Construction, land development and other land loans | $485,419 | $468,975 |
| Secured by 1-4 family residential properties | 1,372,901 | 1,497,480 |
| Secured by nonfarm, nonresidential properties | 1,385,669 | 1,410,264 |
| Other | 174,680 | 189,949 |
| Commercial and industrial loans | 1,206,851 | 1,169,513 |
| Consumer loans | 160,253 | 171,660 |
| Other loans | 688,623 | 684,913 |
| LHFI | 5,474,396 | 5,592,754 |
| Less allowance for loan losses, LHFI | 76,900 | 78,738 |
| Net LHFI | $5,397,496 | $5,514,016 |

Loan Concentrations

Trustmark does not have any loan concentrations other than those reflected in the preceding table, which exceed 10% of total LHFI. At March 31, 2013, Trustmark's geographic loan distribution was concentrated primarily in its five key market regions, Alabama, Florida, Mississippi, Tennessee and Texas. Accordingly, the ultimate collectability of a substantial portion of these loans and the recovery of a substantial portion of the carrying amount of other real estate are susceptible to changes in market conditions in these areas.

Nonaccrual/Impaired LHFI

At March 31, 2013 and December 31, 2012, the carrying amounts of nonaccrual LHFI, which are individually evaluated for impairment, were $83.3 million and $82.4 million, respectively. Of this total, all commercial nonaccrual

LHFI over $500 thousand were specifically evaluated for impairment (specifically evaluated impaired LHFI) using a fair value approach. The remaining nonaccrual LHFI were not all specifically reviewed and written down to fair value less cost to sell. No material interest income was recognized in the income statement on impaired or nonaccrual loans for each of the periods ended March 31, 2013 and 2012.

All of Trustmark's specifically evaluated impaired LHFI are collateral dependent loans. At March 31, 2013 and December 31, 2012, specifically evaluated impaired LHFI totaled $33.0 million and $40.6 million, respectively. In addition, these specifically evaluated impaired LHFI had a related allowance of $3.5 million and $5.9 million at the end of the respective periods. For collateral dependent loans, when a loan is deemed impaired, the full difference between the carrying amount of the loan and the most likely estimate of the asset's fair value less cost to sell is charged off. Charge-offs related to specifically evaluated impaired LHFI totaled $986 thousand and $1.4 million for the first three months of 2013 and 2012, respectively. Provision recapture on specifically evaluated impaired LFHI totaled $1.3 million and $864 thousand for the first three months of 2013 and 2012, respectively.

Fair value estimates for specifically evaluated impaired LHFI are derived from appraised values based on the current market /as is value of the property, normally from recently received and reviewed appraisals. If an appraisal with an inspection date within the past 12 months using the necessary assumptions is not in the file, a new appraisal is ordered. Appraisals are obtained from state-certified appraisers and are based on certain assumptions, which may include construction or development status and the highest and best use of the property. These appraisals are reviewed by Trustmark's Appraisal Review Department to ensure they are acceptable, and values are adjusted down for costs associated with asset disposal. Once this estimated net realizable value has been determined, the value used in the impairment assessment is updated. At the time a specifically evaluated impaired LHFI is deemed to be impaired, the full difference between book value and the most likely estimate of the asset's net realizable value is charged off. As subsequent events dictate and estimated net realizable values decline, required reserves may be established or further adjustments recorded.

At March 31, 2013 and December 31, 2012, nonaccrual LHFI not specifically reviewed for impairment and written down to fair value less cost to sell, totaled $50.3 million and $41.8 million, respectively. In addition, these nonaccrual LHFI had allocated allowance for loan losses of $7.6 million and $4.6 million at the end of the respective periods.

The following table details LHFI individually and collectively evaluated for impairment at March 31, 2013 and December 31, 2012 ($ in thousands):

| | March 31, 2013 | | |
|---|---|---|---|
| | LHFI Evaluated for Impairment | | |
| | Individually | Collectively | Total |
| Loans secured by real estate: | | | |
| Construction, land development and other land loans | $24,443 | $460,976 | $485,419 |
| Secured by 1-4 family residential properties | 27,149 | 1,345,752 | 1,372,901 |
| Secured by nonfarm, nonresidential properties | 17,880 | 1,367,789 | 1,385,669 |
| Other | 1,040 | 173,640 | 174,680 |
| Commercial and industrial loans | 9,053 | 1,197,798 | 1,206,851 |
| Consumer loans | 277 | 159,976 | 160,253 |
| Other loans | 3,480 | 685,143 | 688,623 |
| Total | $83,322 | $5,391,074 | $5,474,396 |

| | December 31, 2012 | | |
|---|---|---|---|
| | LHFI Evaluated for Impairment | | |
| | Individually | Collectively | Total |
| Loans secured by real estate: | | | |
| Construction, land development and other land loans | $27,105 | $441,870 | $468,975 |
| Secured by 1-4 family residential properties | 27,114 | 1,470,366 | 1,497,480 |
| Secured by nonfarm, nonresidential properties | 18,289 | 1,391,975 | 1,410,264 |
| Other | 3,956 | 185,993 | 189,949 |
| Commercial and industrial loans | 4,741 | 1,164,772 | 1,169,513 |
| Consumer loans | 360 | 171,300 | 171,660 |
| Other loans | 798 | 684,115 | 684,913 |
| Total | $82,363 | $5,510,391 | $5,592,754 |

At March 31, 2013 and December 31, 2012, the carrying amount of LHFI individually evaluated for impairment consisted of the following ($ in thousands):

| | March 31, 2013 | | | | | |
|---|---|---|---|---|---|---|
| | LHFI | | | | | |
| | Unpaid Principal Balance | With No Related Allowance Recorded | With an Allowance Recorded | Total Carrying Amount | Related Allowance | Average Recorded Investment |
| Loans secured by real estate: | | | | | | |
| Construction, land development and other land loans | $39,955 | $10,483 | $13,960 | $24,443 | $3,514 | $25,774 |
| Secured by 1-4 family residential properties | 35,509 | 2,461 | 24,688 | 27,149 | 1,117 | 27,131 |
| Secured by nonfarm, nonresidential properties | 20,528 | 7,976 | 9,904 | 17,880 | 2,170 | 18,085 |
| Other | 1,543 | 555 | 485 | 1,040 | 32 | 2,498 |
| Commercial and industrial loans | 11,629 | 2,100 | 6,953 | 9,053 | 3,584 | 6,897 |
| Consumer loans | 525 | - | 277 | 277 | 2 | 319 |
| Other loans | 3,586 | 50 | 3,430 | 3,480 | 594 | 2,139 |
| Total | $113,275 | $23,625 | $59,697 | $83,322 | $11,013 | $82,843 |

| | December 31, 2012 | | | | | |
|---|---|---|---|---|---|---|
| | LHFI | | | | | |
| | Unpaid Principal Balance | With No Related Allowance Recorded | With an Allowance Recorded | Total Carrying Amount | Related Allowance | Average Recorded Investment |
| Loans secured by real estate: | | | | | | |
| Construction, land development and other land loans | $46,558 | $9,571 | $17,534 | $27,105 | $4,992 | $33,759 |
| Secured by 1-4 family residential properties | 35,155 | 2,533 | 24,581 | 27,114 | 1,469 | 25,731 |
| Secured by nonfarm, nonresidential properties | 23,337 | 8,184 | 10,105 | 18,289 | 2,296 | 21,135 |
| Other | 6,036 | 566 | 3,390 | 3,956 | 760 | 4,914 |
| Commercial and industrial loans | 7,251 | 2,336 | 2,405 | 4,741 | 640 | 9,444 |
| Consumer loans | 624 | - | 360 | 360 | 5 | 592 |
| Other loans | 857 | - | 798 | 798 | 342 | 835 |
| Total | $119,818 | $23,190 | $59,173 | $82,363 | $10,504 | $96,410 |

A troubled debt restructuring (TDR) occurs when a borrower is experiencing financial difficulties, and for related economic or legal reasons, a concession is granted to the borrower that Trustmark would not otherwise consider. Whatever the form of a concession granted by Trustmark, the objective is to make the best of a difficult situation by obtaining more cash or other value from the borrower or by increasing the probability of receipt by granting the concession than by not granting it. Other concessions may arise from court proceedings or may be imposed by law. In addition, TDRs also include those credits that are extended or renewed to a borrower who is not able to obtain funds from sources other than Trustmark at a market interest rate for new debt with similar risk.

A formal TDR may include, but is not necessarily limited to, one or a combination of the following situations:

- Trustmark accepts a third-party receivable or other asset(s) of the borrower, in lieu of the receivable from the borrower.
- Trustmark accepts an equity interest in the borrower in lieu of the receivable.
- Trustmark accepts modification of the terms of the debt including but not limited to:
  - Reduction of (absolute or contingent) the stated interest rate to below the current market rate.
  - Extension of the maturity date or dates at a stated interest rate lower than the current market rate for new debt with similar risk.
  - Reduction (absolute or contingent) of the face amount or maturity amount of the debt as stated in the note or other agreement.
  - Reduction (absolute or contingent) of accrued interest.

Troubled debt restructurings are addressed in Trustmark's loan policy, and in accordance with that policy, any modifications or concessions that may result in a TDR are subject to a special approval process which allows for control, identification, and monitoring of these arrangements. Prior to granting a concession, a revised borrowing arrangement is proposed which is structured so as to improve collectability of the loan in accordance with a reasonable repayment schedule with any loss promptly identified. It is supported by a thorough evaluation of the borrower's financial condition and prospects for repayment under those revised terms. Other TDRs arising from renewals or extensions of existing debt are routinely identified through the processes utilized in the Problem Loan Committees and in the Credit Quality Review Committee. All TDRs are subsequently reported to the Director Credit Policy Committee on a quarterly basis and are disclosed in Trustmark's consolidated financial statements in accordance with GAAP and regulatory reporting guidance.

All loans whose terms have been modified in a troubled debt restructuring are evaluated for impairment under FASB ASC Topic 310. Accordingly, Trustmark measures any loss on the restructuring in accordance with that guidance. A TDR in which Trustmark receives physical possession of the borrower's assets, regardless of whether formal foreclosure or repossession proceedings take place, is accounted for in accordance with FASB ASC Subtopic 310-40, "Troubled Debt Restructurings by Creditors." Thus, the loan is treated as if assets have been received in satisfaction of the loan and reported as a foreclosed asset.

A TDR may be returned to accrual status if Trustmark is reasonably assured of repayment of principal and interest under the modified terms and the borrower has demonstrated sustained performance under those terms for a period of at least six months. Otherwise, the restructured loan must remain on nonaccrual.

At March 31, 2013 and December 31, 2012, LHFI classified as TDRs totaled $24.7 million and $24.3 million, respectively, and were primarily comprised of credits with interest-only payments for an extended period of time totaling $16.8 million and $21.6 million, respectively. The remaining TDRs at March 31, 2013 and December 31, 2012 resulted from real estate loans discharged through Chapter 7 bankruptcy that were not reaffirmed or from payment or maturity extensions.

For TDRs, Trustmark had a related loan loss allowance of $4.0 million and $4.3 million at the end of each respective period. Specific charge-offs related to TDRs totaled $60 thousand and $563 thousand for the three months ended March 31, 2013 and 2012, respectively. LHFI that are TDRs are charged down to the most likely fair value estimate less an estimated cost to sell for collateral dependent loans, which would approximate net realizable value.

The following table illustrates the impact of modifications classified as TDRs for the three months ended March 31, 2013 and 2012 as well as those TDRs modified within the last 12 months for which there was a payment default during the period ($ in thousands):

| | Three Months Ended March 31, 2013 | | |
|---|---|---|---|
| Troubled Debt Restructurings | Number of Contracts | Pre-Modification Outstanding Recorded Investment | Post-Modification Outstanding Recorded Investment |
| Secured by 1-4 family residential properties | 2 | 249 | 193 |
| Secured by nonfarm, nonresidential properties | 1 | 952 | 952 |
| Commercial and industrial | 2 | 944 | 937 |
| Other loans | 1 | 2,490 | 2,490 |
| Total | 6 | $ 4,635 | $ 4,572 |

| | Three Months Ended March 31, 2012 | | |
|---|---|---|---|
| Troubled Debt Restructurings | Number of Contracts | Pre-Modification Outstanding Recorded Investment | Post-Modification Outstanding Recorded Investment |
| Construction, land development and other land loans | 8 | $ 3,611 | $ 3,611 |
| Secured by 1-4 family residential properties | 2 | 1,009 | 1,009 |
| Secured by nonfarm, nonresidential properties | 2 | 1,210 | 1,210 |
| Total | 12 | $ 5,830 | $ 5,830 |

| | Three Months Ended March 31, | | | |
|---|---|---|---|---|
| | 2013 | | 2012 | |
| Troubled Debt Restructurings that Subsequently Defaulted | Number of Contracts | Recorded Investment | Number of Contracts | Recorded Investment |
| Construction, land development and other land loans | 4 | $236 | 1 | $299 |
| Secured by 1-4 family residential properties | 19 | 1,506 | 3 | 1,382 |
| Total | 23 | $1,742 | 4 | $1,681 |

Trustmark's TDRs have resulted primarily from allowing the borrower to pay interest-only for an extended period of time rather than from forgiveness. Accordingly, as shown above, these TDRs have a similar recorded investment for both the pre-modification and post-modification disclosure. Trustmark has utilized loans 90 days or more past due to define payment default in determining TDRs that have subsequently defaulted.

At March 31, 2013 and December 31, 2012, the following table details LHFI classified as TDRs by loan type ($ in thousands):

| | March 31, 2013 | | |
|---|---|---|---|
| | Accruing | Nonaccrual | Total |
| Construction, land development and other land loans | $231 | $10,720 | $10,951 |
| Secured by 1-4 family residential properties | 1,163 | 5,528 | 6,691 |
| Secured by nonfarm, nonresidential properties | - | 3,454 | 3,454 |
| Other loans secured by real estate | - | 2,677 | 2,677 |
| Commercial and industrial | - | 936 | 936 |
| Total Troubled Debt Restructurings by Type | $1,394 | $23,315 | $24,709 |

| | December 31, 2012 | | |
|---|---|---|---|
| | Accruing | Nonaccrual | Total |
| Construction, land development and other land loans | $233 | $12,073 | $12,306 |
| Secured by 1-4 family residential properties | 1,280 | 5,908 | 7,188 |
| Secured by nonfarm, nonresidential properties | - | 4,582 | 4,582 |
| Other loans secured by real estate | - | 197 | 197 |
| Total Troubled Debt Restructurings by Type | $1,513 | $22,760 | $24,273 |

Credit Quality Indicators

Trustmark's loan portfolio credit quality indicators focus on six key quality ratios that are compared against bank tolerances. The loan indicators are total classified outstanding, total criticized outstanding, nonperforming loans, nonperforming assets, delinquencies and net loan losses. Due to the homogenous nature of consumer loans, Trustmark does not assign a formal internal risk rating to each credit and therefore the criticized and classified measures are unique to commercial loans.

In addition to monitoring portfolio credit quality indictors, Trustmark also measures how effectively the lending process is being managed and risks are being identified. As part of an ongoing monitoring process, Trustmark grades the commercial portfolio as it relates to credit file completion and financial statement exceptions, total policy exceptions, collateral exceptions and violations of law as shown below:

- Credit File Completeness and Financial Statement Exceptions – evaluates the quality and condition of credit files in terms of content, completeness and organization and focuses on efforts to obtain and document sufficient information to determine the quality and status of credits. Also included is an evaluation of the systems/procedures used to insure compliance with policy such as financial statements, review memos and loan agreements.
- Underwriting/Policy – evaluates whether credits are adequately analyzed, appropriately structured and properly approved within requirements of bank loan policy. A properly approved credit is approved by adequate authority in a timely manner with all conditions of approval fulfilled. Total policy exceptions measures the level of underwriting and other policy exceptions within a loan portfolio.
- Collateral Documentation – focuses on the adequacy of documentation to support the obligation, perfect Trustmark's collateral position and protect collateral value. There are two parts to this measure:

ü Collateral exceptions are where certain collateral documentation is either not present, is not considered current or has expired.

ü 90 days and over collateral exceptions are where certain collateral documentation is either not present, is not considered current or has expired and the exception has been identified in excess of 90 days.

- Compliance with Law – focuses on underwriting, documentation, approval and reporting in compliance with banking laws and regulations. Primary emphasis is directed to Financial Institutions Reform, Recovery and Enforcement

Act of 1989 (FIRREA) and Regulation O requirements.

Commercial Credits

Trustmark has established a loan grading system that consists of ten individual credit risk grades (risk ratings) that encompass a range from loans where the expectation of loss is negligible to loans where loss has been established. The model is based on the risk of default for an individual credit and establishes certain criteria to delineate the level of risk across the ten unique credit risk grades. Credit risk grade definitions are as follows:

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- Risk Rate (RR) 1 through RR 6 – Grades one through six represent groups of loans that are not subject to adverse criticism as defined in regulatory guidance. Loans in these groups exhibit characteristics that represent low to moderate risk measured by using a variety of credit risk criteria such as cash flow coverage, debt service coverage, balance sheet leverage, liquidity, management experience, industry position, prevailing economic conditions, support from secondary sources of repayment and other credit factors that may be relevant to a specific loan. In general, these loans are supported by properly margined collateral and guarantees of principal parties.
- Other Assets Especially Mentioned (OAEM) (RR 7) – a loan that has a potential weakness that if not corrected will lead to a more severe rating. This rating is for credits that are currently protected but potentially weak because of an adverse feature or condition that if not corrected will lead to a further downgrade.
- Substandard (RR 8) – a loan that has at least one identified weakness that is well defined. This rating is for credits where the primary sources of repayment are not viable at this time or where either the capital or collateral is not adequate to support the loan and the secondary means of repayment do not provide a sufficient level of support to offset the identified weakness. Loss potential exists in the aggregate amount of substandard loans but does not necessarily exist in individual loans.
- Doubtful (RR 9) – a loan with an identified weakness that does not have a valid secondary source of repayment. Generally these credits have an impaired primary source of repayment and secondary sources are not sufficient to prevent a loss in the credit. The exact amount of the loss has not been determined at this time.
- Loss (RR 10) – a loan or a portion of a loan that is deemed to be uncollectible.

By definition, credit risk grades OAEM (RR 7), substandard (RR 8), doubtful (RR 9) and loss (RR 10) are criticized loans while substandard (RR 8), doubtful (RR 9) and loss (RR 10) are classified loans. These definitions are standardized by all bank regulatory agencies and are generally equally applied to each individual lending institution. The remaining credit risk grades are considered pass credits and are solely defined by Trustmark.

The credit risk grades represent the probability of default (PD) for an individual credit and as such are not a direct indication of loss given default (LGD). The LGD aspect of the subject risk ratings is neither uniform across the nine primary commercial loan groups or constant between the geographic areas. To account for the variance in the LGD aspects of the risk rate system, the loss expectations for each risk rating is integrated into the allowance for loan loss methodology where the calculated LGD is allotted for each individual risk rating with respect to the individual loan group and unique geographic area. The LGD aspect of the reserve methodology is calculated each quarter as a component of the overall reserve factor for each risk grade by loan group and geographic area.

To enhance this process, loans of a certain size that are rated in one of the criticized categories are routinely reviewed to establish an expectation of loss, if any, and if such examination indicates that the level of reserve is not adequate to cover the expectation of loss, a special reserve or impairment is generally applied.

The distribution of the losses is accomplished by means of a loss distribution model that assigns a loss factor to each risk rating (1 to 9) in each commercial loan pool. A factor is not applied to risk rate 10 (Loss) as loans classified as Losses are not carried on the bank’s books over quarter ends as they are charged off within the period that the loss is determined.

The expected loss distribution is spread across the various risk ratings by the perceived level of risk for loss. The nine grade scale above ranges from a negligible risk of loss to an identified loss across its breadth. The loss distribution factors are graduated through the scale on a basis proportional to the degree of risk that appears manifest in each individual rating and assumes that migration through the loan grading system will occur.

Each loan officer assesses the appropriateness of the internal risk rating assigned to their credits on an ongoing basis. Trustmark’s Asset Review area conducts independent credit quality reviews of the majority of the bank’s commercial loan portfolio concentrations both on the underlying credit quality of each individual loan portfolio as

well as the adherence to bank loan policy and the loan administration process. In general, Asset Review conducts reviews of each lending area within a six to eighteen month window depending on the overall credit quality results of the individual area.

In addition to the ongoing internal risk rate monitoring described above, Trustmark conducts monthly credit quality reviews (CQR) for the credits described below, as well as semi-annual analysis and stress testing on all residential real estate development credits and non-owner occupied commercial real estate (CRE) credits of $1.0 million or more as described below:

- Trustmark's Credit Quality Review Committee meets monthly and performs the following functions: detailed review and evaluation of all loans of $100 thousand or more that are either delinquent thirty days or more or on nonaccrual, including determination of appropriate risk ratings, accrual status, and appropriate servicing officer; review of risk rate changes for relationships of $100 thousand or more; quarterly review of all nonaccruals less than $100 thousand to determine whether the credit should be charged off, returned to accrual, or remain in nonaccrual status; monthly/quarterly review of continuous action plans for all credits rated seven or worse for relationships of $100 thousand or more; monthly review of all commercial charge-offs of $25 thousand or more for the preceding month.

- Residential real estate developments - a development project analysis is performed on all projects regardless of size. Performance of the development is assessed through an evaluation of the number of lots remaining, the payout ratios, and the loan-to-value ratios. Results are stress tested as to absorption and price of lots. This information is reviewed by each senior credit officer for that market to determine the need for any risk rate or accrual status changes.

- Non-owner occupied commercial real estate – a cash flow analysis is performed on all projects with an outstanding balance of $1.0 million or more. In addition, credits are stress tested for vacancies and rate sensitivity. Confirmation is obtained that guarantor financial statements are current, taxes have been paid, and that there are no other issues that need to be addressed. This information is reviewed by each senior credit officer for that market to determine the need for any risk rate or accrual status changes.

Consumer Credits

Loans that do not meet a minimum custom credit score are reviewed quarterly by Management. The Retail Credit Review Committee reviews the volume and percentage of approvals that did not meet the minimum passing custom score by region, individual location, and officer. To assure that Trustmark continues to originate quality loans, this process allows Management to make necessary changes such as revisions to underwriting procedures and credit policies, or changes in loan authority to Trustmark personnel.

Trustmark monitors the levels and severity of past due consumer loans on a daily basis through its collection activities. A detailed assessment of consumer loan delinquencies is performed monthly at both a product and market level by delivery channel, which incorporates the perceived level of risk at time of underwriting. Trustmark also monitors its consumer loan delinquency trends by comparing them to quarterly industry averages.

The table below illustrates the carrying amount of LHFI by credit quality indicator at March 31, 2013 and December 31, 2012 ($ in thousands):

| | March 31, 2013 | | | | |
|---|---|---|---|---|---|
| | Commercial LHFI | | | | |
| | Pass - Categories 1-6 | Special Mention - Category 7 | Substandard - Category 8 | Doubtful - Category 9 | Subtotal |
| Loans secured by real estate: | | | | | |
| Construction, land development and other land loans | $360,197 | $23,060 | $59,289 | $229 | $442,775 |
| Secured by 1-4 family residential properties | 110,110 | 2,288 | 11,387 | 131 | 123,916 |
| Secured by nonfarm, nonresidential properties | 1,279,133 | 12,323 | 92,932 | 313 | 1,384,701 |
| Other | 167,063 | 340 | 2,577 | - | 169,980 |
| Commercial and industrial loans | 1,131,149 | 41,159 | 32,776 | 1,545 | 1,206,629 |
| Consumer loans | 366 | - | - | - | 366 |
| Other loans | 676,708 | 50 | 4,327 | 756 | 681,841 |
| | $3,724,726 | $79,220 | $203,288 | $2,974 | $4,010,208 |

| | Consumer LHFI | | | | | |
|---|---|---|---|---|---|---|
| | Current | Past Due 30-89 Days | Past Due 90 Days or More | Nonaccrual | Subtotal | Total LHFI |
| Loans secured by real estate: | | | | | | |
| Construction, land development and other land loans | $41,948 | $491 | $- | $205 | $42,644 | $485,419 |
| Secured by 1-4 family residential properties | 1,217,358 | 8,634 | 1,284 | 21,709 | 1,248,985 | 1,372,901 |
| Secured by nonfarm, nonresidential properties | 968 | - | - | - | 968 | 1,385,669 |
| Other | 4,533 | 147 | - | 20 | 4,700 | 174,680 |
| Commercial and industrial loans | 195 | 17 | - | 10 | 222 | 1,206,851 |
| Consumer loans | 157,200 | 2,183 | 228 | 276 | 159,887 | 160,253 |
| Other loans | 6,782 | - | - | - | 6,782 | 688,623 |
| | $1,428,984 | $11,472 | $1,512 | $22,220 | $1,464,188 | $5,474,396 |

| | December 31, 2012 | | | | |
|---|---|---|---|---|---|
| | Commercial LHFI | | | | |
| | Pass - Categories 1-6 | Special Mention - Category 7 | Substandard - Category 8 | Doubtful - Category 9 | Subtotal |
| Loans secured by real estate: | | | | | |
| | $335,179 | $23,812 | $63,832 | $143 | $422,966 |

| | | | | | |
|---|---|---|---|---|---|
| Construction, land development and other land loans | | | | | |
| Secured by 1-4 family residential properties | 110,333 | 1,012 | 13,303 | 432 | 125,080 |
| Secured by nonfarm, nonresidential properties | 1,298,820 | 12,156 | 98,082 | - | 1,409,058 |
| Other | 178,790 | 444 | 5,768 | - | 185,002 |
| Commercial and industrial loans | 1,091,356 | 36,992 | 39,479 | 1,334 | 1,169,161 |
| Consumer loans | 404 | - | - | - | 404 |
| Other loans | 676,618 | 59 | 1,714 | 784 | 679,175 |
| | $3,691,500 | $74,475 | $222,178 | $2,693 | $3,990,846 |

| | Consumer LHFI | | | | | |
|---|---|---|---|---|---|---|
| | Current | Past Due 30-89 Days | Past Due 90 Days or More | Nonaccrual | Subtotal | Total LHFI |
| Loans secured by real estate: | | | | | | |
| Construction, land development and other land loans | $44,131 | $1,109 | $- | $769 | $46,009 | $468,975 |
| Secured by 1-4 family residential properties | 1,339,000 | 10,332 | 2,630 | 20,438 | 1,372,400 | 1,497,480 |
| Secured by nonfarm, nonresidential properties | 1,206 | - | - | - | 1,206 | 1,410,264 |
| Other | 4,746 | 150 | - | 51 | 4,947 | 189,949 |
| Commercial and industrial loans | 313 | 29 | - | 10 | 352 | 1,169,513 |
| Consumer loans | 167,131 | 3,481 | 285 | 359 | 171,256 | 171,660 |
| Other loans | 5,738 | - | - | - | 5,738 | 684,913 |
| | $1,562,265 | $15,101 | $2,915 | $21,627 | $1,601,908 | $5,592,754 |

Past Due LHFI and Loans Held for Sale (LHFS)

LHFI past due 90 days or more totaled $2.8 million and $6.4 million at March 31, 2013 and December 31, 2012, respectively. The following table provides an aging analysis of past due and nonaccrual LHFI by class at March 31, 2013 and December 31, 2012 ($ in thousands):

| | March 31, 2013 | | | | | |
|---|---|---|---|---|---|---|
| | 30-89 Days | Past Due 90 Days or More (1) | Total | Nonaccrual | Current Loans | Total LHFI |
| Loans secured by real estate: | | | | | | |
| Construction, land development and other land loans | $3,700 | $477 | $4,177 | $24,443 | $456,799 | $485,419 |
| Secured by 1-4 family residential properties | 9,205 | 1,285 | 10,490 | 27,149 | 1,335,262 | 1,372,901 |
| Secured by nonfarm, nonresidential properties | 7,666 | 250 | 7,916 | 17,880 | 1,359,873 | 1,385,669 |
| Other | 546 | 1 | 547 | 1,040 | 173,093 | 174,680 |
| Commercial and industrial loans | 1,258 | 533 | 1,791 | 9,053 | 1,196,007 | 1,206,851 |
| Consumer loans | 2,184 | 227 | 2,411 | 277 | 157,565 | 160,253 |
| Other loans | 499 | - | 499 | 3,480 | 684,644 | 688,623 |
| Total | $25,058 | $2,773 | $27,831 | $83,322 | $5,363,243 | $5,474,396 |

(1) - Past due 90 days or more but still accruing interest.

| | December 31, 2012 | | | | | |
|---|---|---|---|---|---|---|
| | 30-89 Days | Past Due 90 Days or More (1) | Total | Nonaccrual | Current Loans | Total LHFI |
| Loans secured by real estate: | | | | | | |
| Construction, land development and other land loans | $4,957 | $438 | $5,395 | $27,105 | $436,475 | $468,975 |
| Secured by 1-4 family residential properties | 12,626 | 3,131 | 15,757 | 27,114 | 1,454,609 | 1,497,480 |
| Secured by nonfarm, nonresidential properties | 9,460 | - | 9,460 | 18,289 | 1,382,515 | 1,410,264 |
| Other | 172 | - | 172 | 3,956 | 185,821 | 189,949 |
| Commercial and industrial loans | 4,317 | 2,525 | 6,842 | 4,741 | 1,157,930 | 1,169,513 |
| Consumer loans | 3,480 | 284 | 3,764 | 360 | 167,536 | 171,660 |
| Other loans | 181 | - | 181 | 798 | 683,934 | 684,913 |
| Total | $35,193 | $6,378 | $41,571 | $82,363 | $5,468,820 | $5,592,754 |

(1) - Past due 90 days or more but still accruing interest.

LHFS past due 90 days or more totaled $4.5 million and $43.1 million at March 31, 2013 and December 31, 2012, respectively. LHFS past due 90 days or more are serviced loans eligible for repurchase, which are fully guaranteed by

GNMA. GNMA optional repurchase programs allow financial institutions to buy back individual delinquent mortgage loans that meet certain criteria from the securitized loan pool for which the institution provides servicing. At the servicer's option and without GNMA's prior authorization, the servicer may repurchase such a delinquent loan for an amount equal to 100 percent of the remaining principal balance of the loan. This buy-back option is considered a conditional option until the delinquency criteria are met, at which time the option becomes unconditional. When Trustmark is deemed to have regained effective control over these loans under the unconditional buy-back option, the loans can no longer be reported as sold and must be brought back onto the balance sheet as loans held for sale, regardless of whether Trustmark intends to exercise the buy-back option. These loans are reported as held for sale with the offsetting liability being reported as short-term borrowings.

During the first quarter of 2013, Trustmark exercised its option to repurchase approximately $58.0 million delinquent loans serviced for GNMA. These loans were subsequently sold to a third party under different repurchase provisions. Trustmark retained the servicing for these loans, which are fully guaranteed by FHA/VA. As a result of this repurchase and sale, the loans are no longer carried as LHFS. The transaction resulted in a gain of $542 thousand, which is included in gain on sales of loans, net for the first three months of 2013. Trustmark did not exercise its buy-back option on any delinquent loans serviced for GNMA during the first three months of 2012.

Allowance for Loan Losses, LHFI

Trustmark’s allowance for loan loss methodology for commercial loans is based upon regulatory guidance from its primary regulator and GAAP. The methodology segregates the commercial purpose and commercial construction loan portfolios into nine separate loan types (or pools) which have similar characteristics such as repayment, collateral and risk profiles. The nine basic loan pools are further segregated into Trustmark’s five key market regions, Alabama, Florida, Mississippi, Tennessee and Texas, to take into consideration the uniqueness of each market. A 10-point risk rating system is utilized for each separate loan pool to apply a reserve factor consisting of quantitative and qualitative components to determine the needed allowance by each loan type. As a result, there are 450 risk rate factors for commercial loan types. The nine separate pools are shown below:

Commercial Purpose Loans

- Real Estate – Owner Occupied
- Real Estate – Non-Owner Occupied
- Working Capital
- Non-Working Capital
- Land
- Lots and Development
- Political Subdivisions

Commercial Construction Loans

- 1 to 4 Family
- Non-1 to 4 Family

The quantitative factors of the allowance methodology reflect a twelve-quarter rolling average of net charge-offs, one quarter in arrears, by loan type within each key market region. This allows for a greater sensitivity to current trends, such as economic changes, as well as current loss profiles and creates a more accurate depiction of historical losses.

Qualitative factors used in the allowance methodology include the following:

- National and regional economic trends and conditions
- Impact of recent performance trends
- Experience, ability and effectiveness of management
- Adherence to Trustmark's loan policies, procedures and internal controls
- Collateral, financial and underwriting exception trends
- Credit concentrations
- Acquisitions
- Catastrophe

Each qualitative factor is converted to a scale ranging from 0 (No risk) to 100 (High Risk), other than the last two factors, which are applied on a dollar-for-dollar basis to ensure that the combination of such factors is proportional. The resulting ratings from the individual factors are weighted and summed to establish the weighted average qualitative factor of a specific loan portfolio within each key market region. This weighted average qualitative factor is then distributed over the nine primary loan pools within each key market region based on the ranking by risk of each.

During the fourth quarter of 2012, Trustmark revised the quantitative portion of the allowance for loan loss methodology for consumer and residential LHFI. Trustmark converted the historical loss factor from a 20-quarter net charge-off rolling average to a 12-quarter rolling average and developed a separate reserve for junior liens on 1-4 family LHFI. The change in quantitative methodology allows the bank to more readily correlate portfolio risk to the current market environment as the impact of more recent experience is emphasized. This change also allows for a greater sensitivity to current trends such as economic and performance changes, which includes current loss profiles and creates a more accurate depiction of historical losses. Loans and lines of credit secured by junior liens on 1-4 family residential properties are being reserved for separately in light of continued uncertainty in the economy and the housing market in particular. An additional provision of approximately $1.4 million was recorded in the fourth quarter of 2012 as a result of this revision to the quantitative portion of the allowance for loan loss methodology for consumer and residential LHFI.

The allowance for loan loss methodology segregates the consumer loan portfolio into homogeneous pools of loans that contain similar structure, repayment, collateral and risk profiles. These homogeneous pools of loans are shown

below:

- Residential Mortgage
- Direct Consumer
- Auto Finance
- Junior Lien on 1-4 Family Residential Properties
- Credit Cards
- Overdrafts

The historical loss experience for these pools is determined by calculating a 12-quarter rolling average of net charge-offs, which is applied to each pool to establish the quantitative aspect of the methodology. Where, in Management's estimation, the calculated loss experience does not fully cover the anticipated loss for a pool, an estimate is also applied to each pool to establish the qualitative aspect of the methodology, which represents the perceived risks across the loan portfolio at the current point in time. This qualitative methodology utilizes five separate factors made up of unique components that when weighted and combined produce an estimated level of reserve for each of the loan pools. The five qualitative factors include the following:

- Economic indicators
- Performance trends
- Management experience
- Lending policy measures
- Credit concentrations

The risk measure for each factor is converted to a scale ranging from 0 (No risk) to 100 (High Risk) to ensure that the combination of such factors is proportional. The determination of the risk measurement for each qualitative factor is done for all markets combined. The resulting estimated reserve factor is then applied to each pool.

The resulting ratings from the individual factors are weighted and summed to establish the weighted average qualitative factor of a specific loan portfolio. This weighted average qualitative factor is then applied over the six loan pools.

Changes in the allowance for loan losses, LHFI were as follows ($ in thousands):

| | Three Months Ended March 31, | |
|---|---|---|
| | 2013 | 2012 |
| Balance at January 1, | $78,738 | $89,518 |
| Loans charged-off | (3,325) | (5,376) |
| Recoveries | 4,455 | 3,444 |
| Net recoveries (charge-offs) | 1,130 | (1,932) |
| Provision for loan losses, LHFI | (2,968) | 3,293 |
| Balance at March 31, | $76,900 | $90,879 |

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The following tables detail the balance in the allowance for loan losses, LHFI by portfolio segment at March 31, 2013 and 2012 ($ in thousands):

| | 2013 | | | | |
|---|---|---|---|---|---|
| | Balance January 1, | Charge-offs | Recoveries | Provision for Loan Losses | Balance March 31, |
| Loans secured by real estate: | | | | | |
| Construction, land development and other land loans | $21,838 | $(297) | $- | $(1,964) | $19,577 |
| Secured by 1-4 family residential properties | 12,957 | (209) | 59 | (1,083) | 11,724 |
| Secured by nonfarm, nonresidential properties | 21,096 | (168) | - | (896) | 20,032 |
| Other | 2,197 | (910) | - | 53 | 1,340 |
| Commercial and industrial loans | 14,319 | (40) | 2,031 | 1,360 | 17,670 |
| Consumer loans | 3,087 | (634) | 1,451 | (876) | 3,028 |
| Other loans | 3,244 | (1,067) | 914 | 438 | 3,529 |
| Total allowance for loan losses, LHFI | $78,738 | $(3,325) | $4,455 | $(2,968) | $76,900 |

| | Disaggregated by Impairment Method | | |
|---|---|---|---|
| | Individually | Collectively | Total |
| Loans secured by real estate: | | | |
| Construction, land development and other land loans | $3,514 | $16,063 | $19,577 |
| Secured by 1-4 family residential properties | 1,117 | 10,607 | 11,724 |
| Secured by nonfarm, nonresidential properties | 2,170 | 17,862 | 20,032 |
| Other | 32 | 1,308 | 1,340 |
| Commercial and industrial loans | 3,584 | 14,086 | 17,670 |
| Consumer loans | 2 | 3,026 | 3,028 |
| Other loans | 594 | 2,935 | 3,529 |
| Total allowance for loan losses, LHFI | $11,013 | $65,887 | $76,900 |

| | 2012 | | | | |
|---|---|---|---|---|---|
| | Balance January 1, | Charge-offs | Recoveries | Provision for Loan Losses | Balance March 31, |
| Loans secured by real estate: | | | | | |
| Construction, land development and other land loans | $27,220 | $(1,526) | $- | $21 | $25,715 |
| Secured by 1-4 family residential properties | 12,650 | (716) | 208 | 598 | 12,740 |
| Secured by nonfarm, nonresidential properties | 24,358 | (127) | - | 3,653 | 27,884 |
| Other | 3,079 | (234) | - | 176 | 3,021 |
| Commercial and industrial loans | 15,868 | (331) | 821 | (320) | 16,038 |
| Consumer loans | 3,656 | (1,038) | 1,352 | (766) | 3,204 |
| Other loans | 2,687 | (1,404) | 1,063 | (69) | 2,277 |
| Total allowance for loan losses, LHFI | $89,518 | $(5,376) | $3,444 | $3,293 | $90,879 |

| | Disaggregated by Impairment Method | | |
|---|---|---|---|
| | Individually | Collectively | Total |
| Loans secured by real estate: | | | |
| Construction, land development and other land loans | $5,963 | $19,752 | $25,715 |
| Secured by 1-4 family residential properties | 1,240 | 11,500 | 12,740 |
| Secured by nonfarm, nonresidential properties | 5,443 | 22,441 | 27,884 |
| Other | 1,002 | 2,019 | 3,021 |
| Commercial and industrial loans | 1,168 | 14,870 | 16,038 |
| Consumer loans | 7 | 3,197 | 3,204 |
| Other loans | 65 | 2,212 | 2,277 |
| Total allowance for loan losses, LHFI | $14,888 | $75,991 | $90,879 |

Note 5 – Acquired Loans

For the periods presented, acquired loans consisted of the following ($ in thousands):

| | March 31, 2013 | | December 31, 2012 | |
|---|---|---|---|---|
| | Covered | Noncovered | Covered | Noncovered |
| Loans secured by real estate: | | | | |
| Construction, land development and other land loans | $3,875 | $138,442 | $3,924 | $10,056 |
| Secured by 1-4 family residential properties | 20,980 | 209,658 | 23,990 | 19,404 |
| Secured by nonfarm, nonresidential properties | 17,355 | 339,953 | 18,407 | 45,649 |
| Other | 3,365 | 32,208 | 3,567 | 669 |
| Commercial and industrial loans | 648 | 235,286 | 747 | 3,035 |
| Consumer loans | 179 | 32,694 | 177 | 2,610 |
| Other loans | 1,187 | 14,886 | 1,229 | 100 |
| Acquired loans | 47,589 | 1,003,127 | 52,041 | 81,523 |
| Less allowance for loan losses, acquired loans | 4,497 | 1,961 | 4,190 | 1,885 |
| Net acquired loans | $43,092 | $1,001,166 | $47,851 | $79,638 |

Acquired loans are accounted for under the acquisition method of accounting.The acquired loans are recorded at their estimated fair value at the time of acquisition. Fair value of acquired loans is determined using a discounted cash flow

model based on assumptions regarding the amount and timing of principal and interest payments, estimated prepayments, estimated default rates, estimated loss severity in the event of defaults and current market rates. Estimated credit losses are included in the determination of fair value; therefore, an allowance for loan losses is not recorded on the acquisition date.

Loans acquired in an FDIC-assisted transaction and covered under loss-share agreements are referred to as "covered loans" and are reported separately in Trustmark's consolidated financial statements. The covered loans were recorded at their estimated fair value at the time of acquisition exclusive of the expected reimbursement cash flows from the FDIC.

Trustmark accounts for acquired impaired loans under FASB ASC Topic 310-30. An acquired loan is considered impaired when there is evidence of credit deterioration since origination and it is probable at the date of acquisition that Trustmark would be unable to collect all contractually required payments. Revolving credit agreements such as home equity lines and commercial leases are excluded from acquired impaired loan accounting requirements. Trustmark acquired $154.8 million of revolving credit agreements and commercial leases, at fair value, in the BancTrust acquisition and $5.9 million of revolving credit agreements, at fair value, in the Bay Bank acquisition, consisting mainly of home equity loans and commercial asset-based lines of credit, where the borrower had revolving privileges on the acquisition date. As such, Trustmark has accounted for such acquired loans in accordance with accounting requirements for acquired nonimpaired loans.

For acquired impaired loans, Trustmark (a) calculates the contractual amount and timing of undiscounted principal and interest payments (the “undiscounted contractual cash flows”) and (b) estimates the amount and timing of undiscounted expected principal and interest payments (the “undiscounted expected cash flows”). Under FASB ASC Topic 310-30, the difference between the undiscounted contractual cash flows and the undiscounted expected cash flows is the nonaccretable difference. The nonaccretable difference represents an estimate of the loss exposure of principal and interest related to the acquired impaired loan portfolio, and such amount is subject to change over time based on the performance of such loans.

The excess of expected cash flows at acquisition over the initial fair value of acquired impaired loans is referred to as the “accretable yield” and is recorded as interest income over the estimated life of the loans using the effective yield method if the timing and amount of the future cash flows is reasonably estimable. Improvements in expected cash flows over those originally estimated increase the accretable yield and are recognized as interest income prospectively. Decreases in the amount and changes in the timing of expected cash flows compared to those originally estimated decrease the accretable yield and result in a provision for loan losses and the establishment of an allowance for loan losses. The carrying value of acquired impaired loans is reduced by payments received, both principal and interest, and increased by the portion of the accretable yield recognized as interest income.

Trustmark aggregates certain acquired loans into pools of loans with common credit risk characteristics such as loan type and risk rating. To establish accounting pools of acquired loans, loans are first categorized by similar purpose, collateral and geographic region. Within each category, loans are further segmented by ranges of risk determinants observed at the time of acquisition. For commercial loans, the primary risk determinant is the risk rating as assigned by Trustmark. For consumer loans, the risk determinants include delinquency, FICO and loan-to-value ratios. Statistical comparison of the pools reflect that each pool is comprised of loans generally of similar characteristics, including loan type, loan risk and weighted average life. Each pool is then reviewed for similarity of the pool constituents, including standard deviation of purchase price, weighted average life and concentration of the largest loans. Loan pools are initially booked at the aggregate fair value of the loan pool constituents, based on the present value of Trustmark's expected cash flows from the loans. An acquired loan is removed from a pool of loans only if the loan is sold, foreclosed, or payment is received in full satisfaction of the loan. The acquired loan is removed from the pool at its carrying value. If an individual acquired loan is removed from a pool of loans, the difference between its relative carrying amount and its cash, fair value of the collateral, or other assets received will be recognized as a gain or loss immediately in interest income on loans and would not affect the effective yield used to recognize the accretable yield on the remaining pool. Certain acquired loans are not pooled and are accounted for individually. Such loans are withheld from pools due to the inherent uncertainty of the timing and amount of their cash flows or because they are not a suitable similar constituent to the established pools.

As required by FASB ASC Topic 310-30, Trustmark periodically re-estimates the expected cash flows to be collected over the life of the acquired impaired loans. If, based on current information and events, it is probable that Trustmark will be unable to collect all cash flows expected at acquisition plus additional cash flows expected to be collected arising from changes in estimate after acquisition, the acquired loans are considered impaired. The decrease in the

expected cash flows reduces the carrying value of the acquired impaired loans as well as the accretable yield and results in a charge to income through the provision for loans losses, acquired loans and the establishment of an allowance for loan losses, acquired loans. If, based on current information and events, it is probable that there is a significant increase in the cash flows previously expected to be collected or if actual cash flows are significantly greater than cash flows previously expected, Trustmark will reduce any remaining allowance for loan losses, acquired loans established on the acquired impaired loans for the increase in the present value of cash flows expected to be collected. The increase in the expected cash flows for the acquired impaired loans over those originally estimated at acquisition increases the carrying value of the acquired impaired loans as well as the accretable yield. The increase in the accretable yield is recognized as interest income over the remaining average life of the acquired impaired loans.

On February 15, 2013, Trustmark completed its merger with BancTrust. Loans acquired in the BancTrust acquisition were evaluated for evidence of credit deterioration since origination and collectability of contractually required payments. Trustmark elected to account for all loans acquired in the BancTrust acquisition as acquired impaired loans under FASB ASC Topic 310-30 except for $154.8 million of acquired loans with revolving privileges and acquired commercial leases, which are outside the scope of the guidance. While not all loans acquired from BancTrust exhibited evidence of significant credit deterioration, accounting for these acquired loans under ASC Topic 310-30 would have materially the same result as the alternative accounting treatment. The purchase price allocation was deemed preliminary as of March 31, 2013.

The following table presents the fair value of loans acquired as of the date of the BancTrust acquisition ($ in thousands):

| At acquisition date: | February 15, 2013 |
|---|---|
| Contractually required principal and interest | $1,228,684 |
| Nonaccretable difference | 180,638 |
| Cash flows expected to be collected | 1,048,046 |
| Accretable yield | 86,221 |
| FAS 91 discount | 10,814 |
| Fair value of loans at acquisition | $951,011 |

On March 16, 2012, Trustmark completed its merger with Bay Bank. Loans acquired in the Bay Bank acquisition were evaluated for evidence of credit deterioration since origination and collectability of contractually required payments. Trustmark elected to account for all loans acquired in the Bay Bank acquisition as acquired impaired loans under FASB ASC Topic 310-30 except for $5.9 million of acquired loans with revolving privileges, which are outside the scope of the guidance. While not all loans acquired from Bay Bank exhibited evidence of significant credit deterioration, accounting for these acquired loans under ASC Topic 310-30 would have materially the same result as the alternative accounting treatment. The purchase price allocation was deemed preliminary as of March 31, 2012 and was finalized in the second quarter of 2012.

The following tables present changes in the carrying value of the acquired loans for the periods presented ($ in thousands):

| | Covered | | Noncovered | |
|---|---|---|---|---|
| | Acquired Impaired | Acquired Not ASC 310-30(1) | Acquired Impaired | Acquired Not ASC 310-30 (1) |
| Carrying value, net at January 1, 2012 | $72,131 | $ 4,171 | $4,350 | |