

INDEPENDENT BANK CORP

Form 10-Q

May 06, 2015

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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

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

For the quarterly period ended March 31, 2015

Commission File Number: 1-9047

Independent Bank Corp.

(Exact name of registrant as specified in its charter)

Massachusetts

04-2870273

(State or other jurisdiction of
incorporation or organization)

(I.R.S. Employer
Identification No.)

Office Address: 2036 Washington Street, Hanover Massachusetts 02339

Mailing Address: 288 Union Street, Rockland, Massachusetts 02370

(Address of principal executive offices, including zip code)

(781) 878-6100

(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 No

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large Accelerated Filer

Accelerated Filer

Non-accelerated Filer

Smaller Reporting Company

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

As of May 1, 2015, there were 26,148,263 shares of the issuer's common stock outstanding, par value \$0.01 per share.

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PART 1. FINANCIAL INFORMATION

Item 1. Financial Statements

INDEPENDENT BANK CORP.

CONSOLIDATED BALANCE SHEETS

(Unaudited—Dollars in thousands, except share data)

	March 31, 2015	December 31, 2014
Assets		
Cash and due from banks	\$108,804	\$143,342
Interest-earning deposits with banks	47,470	34,912
Securities		
Securities - trading	494	—
Securities - available for sale	387,038	348,554
Securities - held to maturity (fair value \$402,322 and \$379,699)	394,745	375,453
Total securities	782,277	724,007
Loans held for sale (at fair value)	9,507	6,888
Loans		
Commercial and industrial	829,380	860,839
Commercial real estate	2,606,444	2,347,323
Commercial construction	291,666	265,994
Small business	87,709	85,247
Residential real estate	681,379	530,259
Home equity - first position	519,978	513,518
Home equity - subordinate positions	356,938	350,345
Other consumer	19,624	17,208
Total loans	5,393,118	4,970,733
Less: allowance for loan losses	(54,515)	(55,100)
Net loans	5,338,603	4,915,633
Federal Home Loan Bank stock	37,485	33,233
Bank premises and equipment, net	73,315	64,074
Goodwill	201,083	170,421
Identifiable intangible assets	13,975	9,885
Cash surrender value of life insurance policies	131,643	109,854
Other real estate owned and other foreclosed assets	6,285	7,743
Other assets	160,638	144,920
Total assets	\$6,911,085	\$6,364,912
Liabilities and Stockholders' Equity		
Deposits		
Demand deposits	1,603,124	1,462,200
Savings and interest checking accounts	2,232,832	2,108,486
Money market	1,088,223	990,160
Time certificates of deposit of \$100,000 and over	304,952	254,718
Other time certificates of deposits	441,581	394,902
Total deposits	5,670,712	5,210,466
Borrowings		
Federal Home Loan Bank borrowings	108,246	70,080
Customer repurchase agreements and other short-term borrowings	128,138	147,890

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Wholesale repurchase agreements	50,000	50,000
Junior subordinated debentures	73,631	73,685
Subordinated debentures	35,000	65,000
Total borrowings	395,015	406,655
Other liabilities	112,472	107,264
Total liabilities	6,178,199	5,724,385
Commitments and contingencies		
Stockholders' equity		
Preferred stock, \$.01 par value. authorized: 1,000,000 shares, outstanding: none	—	—
Common stock, \$.01 par value. authorized: 75,000,000 shares, issued and outstanding: 26,123,576 shares at March 31, 2015 and 23,998,738 shares at December 31, 2014 (includes 241,660 and 254,500 shares of unvested participating restricted stock awards, respectively)	259	237
Shares held in rabbi trust at cost: 169,262 shares at March 31, 2015 and 176,849 shares at December 31, 2014	(3,700	) (3,666
Deferred compensation and other retirement benefit obligations	3,700	3,666
Additional paid in capital	399,936	311,978
Retained earnings	333,104	330,444
Accumulated other comprehensive loss, net of tax	(413	) (2,132
Total stockholders' equity	732,886	640,527
Total liabilities and stockholders' equity	\$6,911,085	\$6,364,912

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

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INDEPENDENT BANK CORP.
CONSOLIDATED STATEMENTS OF INCOME
(Unaudited—Dollars in thousands, except per share data)

	Three Months Ended	
	March 31	
	2015	2014
Interest income		
Interest and fees on loans	\$51,687	\$48,204
Taxable interest and dividends on securities	4,627	4,650
Nontaxable interest and dividends on securities	34	37
Interest on loans held for sale	51	51
Interest on federal funds sold and short-term investments	30	38
Total interest and dividend income	56,429	52,980
Interest expense		
Interest on deposits	2,763	2,791
Interest on borrowings	2,417	2,583
Total interest expense	5,180	5,374
Net interest income	51,249	47,606
Provision (benefit) for loan losses	(500	) 4,502
Net interest income after provision for loan losses	51,749	43,104
Noninterest income		
Deposit account fees	4,166	4,359
Interchange and ATM fees	3,100	2,975
Investment management	5,107	4,603
Mortgage banking income	1,126	487
Gain on life insurance benefits	—	1,627
Increase in cash surrender value of life insurance policies	778	722
Loan level derivative income	418	746
Net gain on sale of equity securities	—	91
Other noninterest income	1,862	1,906
Total noninterest income	16,557	17,516
Noninterest expenses		
Salaries and employee benefits	25,288	23,080
Occupancy and equipment expenses	6,394	6,146
Data processing and facilities management	1,122	1,253
FDIC assessment	956	905
Advertising expense	834	824
Consulting expense	755	559
Merger and acquisition expense	10,230	77
Software maintenance	625	662
Other noninterest expenses	8,773	8,381
Total noninterest expenses	54,977	41,887
Income before income taxes	13,329	18,733
Provision for income taxes	3,869	5,350
Net income	\$9,460	\$13,383
Basic earnings per share	\$0.38	\$0.56
Diluted earnings per share	\$0.38	\$0.56
Weighted average common shares (basic)	24,959,865	23,819,065
Common shares equivalents	80,215	100,173

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Weighted average common shares (diluted)	25,040,080	23,919,238
Cash dividends declared per common share	\$0.26	\$0.24

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

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INDEPENDENT BANK CORP.
 CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
 (Unaudited—Dollars in thousands)

	Three Months Ended March 31	
	2015	2014
Net income	\$9,460	\$13,383
Other comprehensive income, net of tax		
Net change in fair value of securities available for sale	1,561	1,917
Net change in fair value of cash flow hedges	82	502
Net change in other comprehensive income for defined benefit postretirement plans	76	(39)
Total other comprehensive income	1,719	2,380
Total comprehensive income	\$11,179	\$15,763

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

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INDEPENDENT BANK CORP.
CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY
(Unaudited—Dollars in thousands, except per share data)

	Common Stock Outstanding	Common Stock	Value of Shares Held in Rabbi Trust at Cost	Deferred Compensation and Other Retirement Benefit Obligations	Additional Paid in Capital	Retained Earnings	Accumulated Other Comprehensive Loss	Total
Balance December 31, 2014	23,998,738	\$237	\$ (3,666)	\$ 3,666	\$311,978	\$330,444	\$ (2,132)	\$640,527
Net income	—	—	—	—	—	9,460	—	9,460
Other comprehensive income	—	—	—	—	—	—	1,719	1,719
Common dividend declared (\$0.26 per share)	—	—	—	—	—	(6,800)	—	(6,800)
Common stock issued for acquisition	2,052,137	21	—	—	86,394	—	—	86,415
Proceeds from exercise of stock options, net of cash paid	23,436	—	—	—	321	—	—	321
Tax benefit related to equity award activity	—	—	—	—	337	—	—	337
Stock based compensation	—	—	—	—	739	—	—	739
Restricted stock awards issued, net of awards surrendered	33,491	1	—	—	(636)	—	—	(635)
Shares issued under direct stock purchase plan	15,774	—	—	—	638	—	—	638
Deferred compensation and other retirement benefit obligations	—	—	(34)	34	—	—	—	—
Tax benefit related to deferred compensation distributions	—	\$—	\$—	\$—	165	—	—	165
Balance March 31, 2015	26,123,576	\$259	\$ (3,700)	\$ 3,700	\$399,936	\$333,104	\$ (413)	\$732,886

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Balance at December 31, 2013	23,805,984	\$235	\$ (3,404)	\$ 3,404	\$305,179	\$293,560	\$ (7,434)	\$591,540
Net income	—	—	—	—	—	13,383	—	13,383
Other comprehensive income	—	—	—	—	—	—	2,380	2,380
Common dividend declared (\$0.24 per share)	—	—	—	—	—	(5,725)	—	(5,725)
Proceeds from exercise of stock options, net of cash paid	7,911	—	—	—	133	—	—	133
Tax benefit related to equity award activity	—	—	—	—	193	—	—	193
Stock based compensation	—	—	—	—	677	—	—	677
Restricted stock awards issued, net of awards surrendered	55,761	1	—	—	(473)	—	—	(472)
Shares issued under direct stock purchase plan	8,400	—	—	—	319	—	—	319
Deferred compensation and other retirement benefit obligations	—	—	(52)	52	—	—	—	—
Tax benefit related to deferred compensation distributions	—	\$—	\$—	\$—	\$128	\$—	\$—	\$128
Balance March 31, 2014	23,878,056	236	(3,456)	3,456	306,156	301,218	(5,054)	602,556

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

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INDEPENDENT BANK CORP.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited—Dollars in thousands)

	Three Months Ended	
	March 31	
	2015	2014
Cash flow from operating activities		
Net income	\$9,460	\$13,383
Adjustments to reconcile net income to net cash provided by operating activities		
Depreciation and amortization	3,145	2,757
Provision (benefit) for loan losses	(500)	) 4,502
Deferred income tax expense	639	471
Net gain on sale of securities	—	(91)
Net (gain) loss on fixed assets	(2)	) 353
Net loss on other real estate owned and foreclosed assets	666	184
Realized gain on sale leaseback transaction	(258)	) (258)
Stock based compensation	739	677
Excess tax benefit related to equity award activity	(337)	) (193)
Increase in cash surrender value of life insurance policies	(778)	) (722)
Gain on life insurance benefits	—	(1,627)
Change in fair value on loans held for sale	(27)	) (51)
Net change in:		
Trading assets	(494)) —
Loans held for sale	(2,592)	) 2,145
Other assets	3,056	1,904
Other liabilities	(5,292)	) (8,721)
Total adjustments	(2,035)	) 1,330
Net cash provided by operating activities	7,425	14,713
Cash flows provided by (used in) investing activities		
Proceeds from sales of securities available for sale	—	673
Proceeds from maturities and principal repayments of securities available for sale	13,108	11,705
Purchases of securities available for sale	(5,846)	) (766)
Proceeds from maturities and principal repayments of securities held to maturity	12,616	9,083
Purchases of securities held to maturity	(31,890)	) (34,017)
Investments in low income housing projects	(5,002)	) (2,561)
Purchases of life insurance policies	(92)	) (93)
Proceeds from life insurance policies	—	478
Net decrease (increase) in loans	41,330	(93,858)
Cash used in business combinations, net of cash acquired	(13,448)) —
Purchases of bank premises and equipment	(1,481)	) (2,455)
Proceeds from the sale of bank premises and equipment	14	756
Proceeds from the sale of other real estate owned and foreclosed assets	1,641	642
Net capital improvements to other real estate owned	(665)	) (444)
Net cash provided by (used in) investing activities	10,285	(110,857)
Cash flows provided by (used in) financing activities		
Net decrease in time deposits	(19,023)) (18,342)

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Net increase in other deposits	47,019	146,183	
Net repayments of short-term Federal Home Loan Bank borrowings	(10,000) —	
Repayments of long-term Federal Home Loan Bank borrowings	(3,000) —	
Net decrease in customer repurchase agreements	(29,752	) (20,803)
Net increase (decrease) in other short term borrowings	10,000	(5,000)
Repayments of subordinated debentures	(30,000) —	
Proceeds from exercise of stock options, net of cash paid	321	133	
Restricted stock awards issued, net of awards surrendered	(635	) (472)
Excess tax benefit from stock based compensation	337	193	
Tax benefit from deferred compensation distribution	165	128	
Proceeds from shares issued under direct stock purchase plan	638	319	
Common dividends paid	(5,760	) (5,237)
Net cash provided by (used in) financing activities	(39,690	) 97,102	
Net increase (decrease) in cash and cash equivalents	(21,980	) 958	
Cash and cash equivalents at beginning of year	178,254	216,325	
Cash and cash equivalents at end of period	156,274	217,283	
Supplemental schedule of noncash investing and financing activities			
Transfer of loans to other real estate owned & foreclosed assets	\$354	\$746	
Capital commitment relating to low income housing project investments	\$—	\$25,839	
In conjunction with the purchase acquisition detailed in note 2 to the consolidated financial statements, assets were acquired and liabilities were assumed as follows			
Common stock issued for acquisition	\$86,415	\$—	
Fair value of assets acquired, net of cash acquired	\$598,376	\$—	
Fair value of liabilities assumed	\$498,513	\$—	

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

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CONDENSED NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 - BASIS OF PRESENTATION

Independent Bank Corp. (the "Company") is a state chartered, federally registered bank holding company, incorporated in 1985. The Company is the sole stockholder of Rockland Trust Company ("Rockland Trust" or the "Bank"), a Massachusetts trust company chartered in 1907.

All material intercompany balances and transactions have been eliminated in consolidation. Certain previously reported amounts may have been reclassified to conform to the current year's presentation.

The accompanying unaudited consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America ("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 GAAP for complete financial statements. In the opinion of management, all adjustments considered necessary for a fair presentation of the financial statements, primarily consisting of normal recurring adjustments, have been included. Operating results for the quarter ended March 31, 2015 are not necessarily indicative of the results that may be expected for the year ending December 31, 2015 or any other interim period.

For further information, refer to the consolidated financial statements and footnotes thereto included in the Company's Annual Report on Form 10-K for the year ended December 31, 2014, filed with the Securities and Exchange Commission.

NOTE 2 - RECENT ACCOUNTING STANDARDS UPDATES

FASB ASC Subtopic 835-30 "Interest - Imputation of Interest" Update No. 2015-03. Update No. 2015-03 was issued in April 2015 to simplify presentation of debt issuance costs. The amendments in this Update require that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability, consistent with debt discounts. The recognition and measurement guidance for debt issuances costs are not affected by the amendments in this Update. The amendments in this update are effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2015. Early adoption is permitted. The adoption of this standard is not expected to have a material impact on the Company's consolidated financial position.

FASB ASC Topic 810 "Consolidation" Update No. 2015-02. Update No. 2015-02 was issued in February 2015 to respond to stakeholders' concerns about the current accounting for consolidation of certain legal entities. The amendments in this update affect reporting entities that are required to evaluate whether they should consolidate certain legal entities. All legal entities are subject to reevaluation under the revised consolidation model. Specifically, the amendments: (1) modify the evaluation of whether limited partnerships and similar legal entities are variable interest entities (VIEs) or voting interest entities, (2) eliminate the presumption that a general partner should consolidate a limited partnership, (3) affect the consolidation analysis of reporting entities that are involved with VIEs, particularly those that have fee arrangements and related party relationships, and (4) provide a scope exception from consolidation guidance for reporting entities with interests in legal entities that are required to comply with or operate in accordance with requirements that are similar to those in Rule 2a-7 of the Investment Company Act of 1940 for registered money market funds. The amendments in this update are effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2015. Early adoption is permitted. The adoption of this standard is not expected to have a material impact on the Company's consolidated financial position.

FASB ASC Subtopic 225-20 "Income Statement - Extraordinary and Unusual Items" Update No. 2015-01. Update No. 2015-01 was issued in January 2015 to simplify the income statement presentation requirements in Subtopic 225-20 by eliminating the concept of extraordinary items. Extraordinary items are events and transactions that are distinguished by their unusual nature and by the infrequency of their occurrence. The amendments in this update are effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2015. Early

adoption is permitted. The adoption of this standard is not expected to have a material impact on the Company's consolidated financial position.

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NOTE 3 - ACQUISITIONS

Peoples Federal Bancshares, Inc.

On February 20, 2015, the Company completed its acquisition of Peoples Federal Bancshares, Inc. ("Peoples"), the parent of Peoples Federal Saving Bank. The transaction qualified as a tax-free reorganization for federal income tax purposes and Peoples shareholders received, for each share of Peoples common stock, the right to receive either \$21.00 in cash per share or 0.5523 shares of the Company's stock (valued at \$23.26 per share, based upon the highest trading value of the Company's stock on February 20, 2015 of \$42.11). The total deal consideration was \$141.8 million and was comprised of 40% cash and 60% stock consideration. The cash consideration was \$55.4 million in the aggregate, inclusive of cash paid in lieu of fractional shares. The total stock consideration was \$86.4 million and resulted in an increase to the Company's outstanding shares of 2,052,137 shares.

The Company accounted for the acquisition using the acquisition method pursuant to the Business Combinations Topic of the Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC"). Accordingly, the Company recorded merger and acquisition expenses of \$10.2 million during the three months ended March 31, 2015. Additionally, the acquisition method requires the acquirer to recognize the assets acquired and the liabilities assumed at their fair values as of the acquisition date. The following table summarizes the estimated fair value of the assets acquired and liabilities assumed as of the date of the acquisition:

	Net Assets Acquired at Fair Value (Dollars in thousands)
Assets	
Cash	\$ 41,957
Investments	43,585
Loans	463,927
Premises and equipment	9,346
Goodwill	30,662
Core deposit and other intangibles	3,936
Other assets	46,920
Total assets acquired	640,333
Liabilities	
Deposits	432,250
Borrowings	51,209
Other liabilities	15,054
Total liabilities assumed	498,513
Purchase price	\$ 141,820

Fair value adjustments to assets acquired and liabilities assumed are generally amortized using either an effective yield or straight-line basis over periods consistent with the average life, useful life and/or contractual term of the related assets and liabilities.

Fair values of the major categories of assets acquired and liabilities assumed were determined as follows:

Cash and Cash Equivalents

The fair values of cash and cash equivalents approximate the respective carrying amounts because the instruments are payable on demand or have short-term maturities.

Investments

The fair values of securities were based on quoted market prices for identical securities received from an independent, nationally-recognized, third-party pricing service. Prices provided by the independent pricing service were based on recent trading activity and other observable information including, but not limited to, market interest rate curves,

referenced credit spreads and estimated prepayment rates where applicable.

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Loans

The loans acquired were recorded at fair value without a carryover of the allowance for loan losses. Fair value of the loans is determined using market participant assumptions in estimating the amount and timing of both principal and interest cash flows expected to be collected, as adjusted for an estimate of future credit losses and prepayments, and then applying a market-based discount rate to those cash flows. The overall discount on the loans acquired in this transaction was due to anticipated credit loss, as well as considerations for liquidity and market interest rates.

A portion of the loans acquired showed evidence of deterioration of credit quality at the purchase date and it was deemed unlikely that the Bank will be able to collect all contractually required payments. As such, these loans were deemed to be purchased credit impaired ("PCI") and the carrying value and prospective income recognition are predicated upon future cash flows expected to be collected. The following is a summary of these PCI loans associated with the acquisition as of the date acquired:

	(Dollars in thousands)
Contractually required principal and interest at acquisition	\$4,358
Contractual cash flows not expected to be collected	(1,596)
Expected cash flows at acquisition	2,762
Interest component of expected cash flows	(319)
Basis in PCI loans at acquisition - estimated fair value	\$2,443

Premises and Equipment

The fair value of the premises, including land, buildings and improvements, was determined based upon appraisals by licensed real estate appraisers or pending agreed upon sale prices. The appraisals were based upon the best and highest use of the property with final values determined based upon an analysis of the cost, sales comparison and income capitalization approaches for each property appraised.

Core Deposit Intangible

The fair value of the core deposit intangible is derived by comparing the interest rate and servicing costs that the financial institution pays on the core deposit liability versus the current market rate for alternative sources of financing, while factoring in estimates over the remaining life and attrition rate of the deposit accounts. The intangible asset represents the stable and relatively low cost source of funds that the deposits and accompanying relationships provide the Company, when compared to alternative funding sources.

Deposits

The fair value of acquired savings and transaction deposit accounts was assumed to approximate the carrying value as these accounts have no stated maturity and are payable on demand. The fair value of time deposits were determined based on the present value of the contractual cash flows over the remaining period to maturity using a market interest rate.

Borrowings

The fair values of Federal Home Loan Bank ("FHLB") advances were derived based upon the present value of the principal and interest payments using a current market discount rate.

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Selected Pro Forma Results

The following summarizes the unaudited pro forma results of operations as if the Company acquired Peoples on January 1, 2015 (2014 amounts represent combined results for the Company and Peoples). The selected pro forma financial information is presented for illustrative purposes only and is not necessarily indicative of the financial results of the combined companies had the acquisition actually been completed at the beginning of the periods presented, nor does it indicate future results for any other interim or full-year period.

	March 31,	
	2015	2014
	(Dollars in thousands)	
Net interest income after provision for loan losses	\$54,407	\$47,516
Net income	14,161	13,897

Excluded from the pro forma results of operations for the three months ended March 31, 2015 are merger-related costs of \$16.6 million recognized by both the Company and Peoples in the aggregate. These costs were primarily made up of contract terminations arising due to the change in control, the acceleration of certain compensation and benefit costs, and other merger expenses.

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NOTE 4 - SECURITIES

Trading Securities

As of March 31, 2015, the Company had trading securities of \$494,000. These securities are held in a rabbi trust and will be used for future payments associated with the Company's non-qualified 401(k) Restoration Plan and non-qualified deferred compensation plan.

Available for Sale and Held to Maturity Securities

The following table presents a summary of the amortized cost, gross unrealized holding gains and losses, other-than-temporary impairment recorded in other comprehensive income and fair value of securities available for sale and securities held to maturity for the periods below:

	March 31, 2015			December 31, 2014				
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
	(Dollars in thousands)							

Available for sale securities

U.S. government agency securities \$45,848 \$ 656