FIRST FINANCIAL BANCORP /OH/
Form 10-Q
May 05, 2016
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FORM 10-Q
UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington D.C. 20549

x QUARTERLY REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended March 31, 2016

OR

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

For the transition period from ____________________ to ____________________

Commission file number 001-34762

FIRST FINANCIAL BANCORP.
(Exact name of registrant as specified in its charter)

Ohio	31-1042001
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
255 East Fifth Street, Suite 700 Cincinnati, Ohio	45202
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number, including area code (877) 322-9530

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 x 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 x No o

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

Large accelerated filer x Accelerated filer o

Non-accelerated filer o Smaller reporting company o

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Class	Outstanding at 5/4/2016
Common stock, No par value	61,858,864

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FIRST FINANCIAL BANCORP.

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Glossary of Abbreviations and Acronyms

First Financial Bancorp. has identified the following list of abbreviations and acronyms that are used in the Notes to Consolidated Financial Statements and the Management's Discussion and Analysis of Financial Condition and Results of Operations.

the Act	Private Securities Litigation Reform Act	FDIC	Federal Deposit Insurance Corporation
ALLL	Allowance for loan and lease losses	FHLB	Federal Home Loan Bank
ASC	Accounting standards codification	First Financial	First Financial Bancorp.
ASU	Accounting standards update	First Financial Bank	First Financial Bank, N.A.
ATM	Automated teller machine	Form 10-K	First Financial Bancorp. Annual Report on Form 10-K
Bank	First Financial Bank, N.A.	GAAP	U.S. Generally Accepted Accounting Principles
Basel III	Basel Committee regulatory capital reforms, Third Basel Accord	IRLC	Interest Rate Lock Commitment
BP	basis point	N/A	Not applicable
CDs	certificates of deposits	NII	Net interest income
Company	First Financial Bancorp.	Oak Street	Oak Street Holdings Corporation
ERM	Enterprise Risk Management	OREO	Other real estate owned
EVE	Economic value of equity	SEC	United States Securities and Exchange Commission
FASB	Financial Accounting Standards Board	TDR	Troubled debt restructuring
Fair Value Topic	FASB ASC Topic 825, Financial Instruments		

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PART I - FINANCIAL INFORMATION
ITEM I - FINANCIAL STATEMENTS
FIRST FINANCIAL BANCORP. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
(Dollars in thousands)

	March 31, 2016 (Unaudited)	December 31, 2015
Assets		
Cash and due from banks	$102,675	$114,841
Interest-bearing deposits with other banks	15,582	33,734
Investment securities available-for-sale, at fair value (amortized cost $1,165,093 at March 31, 2016 and $1,203,065 at December 31, 2015)	1,164,319	1,190,642
Investment securities held-to-maturity (fair value $718,277 at March 31, 2016 and $731,951 at December 31, 2015)	702,315	726,259
Other investments	53,255	53,725
Loans held for sale	15,369	20,957
Loans and leases		
Commercial and industrial	1,744,732	1,663,102
Lease financing	101,135	93,986
Real estate-construction	341,453	311,712
Real estate-commercial	2,261,857	2,258,297
Real estate-residential	508,512	512,311
Home equity	466,010	466,629
Installment	41,627	41,506
Credit card	39,283	41,217
Total loans and leases	5,504,609	5,388,760
Less: Allowance for loan and lease losses	53,732	53,398
Net loans and leases	5,450,877	5,335,362
Premises and equipment	138,036	136,603
Goodwill and other intangibles	211,533	211,865
FDIC indemnification asset	16,256	17,630
Accrued interest and other assets	323,337	305,793
Total assets	$8,193,554	$8,147,411
Liabilities		
Deposits		
Interest-bearing	$1,430,963	$1,414,291
Savings	1,922,892	1,945,805
Time	1,414,313	1,406,124
Total interest-bearing deposits	4,768,168	4,766,220
Noninterest-bearing	1,408,609	1,413,404
Total deposits	6,176,777	6,179,624
Federal funds purchased and securities sold under agreements to repurchase	75,499	89,325
Federal Home Loan Bank short-term borrowings	894,400	849,100
Total short-term borrowings	969,899	938,425
Long-term debt	119,556	119,540
Total borrowed funds	1,089,455	1,057,965

Accrued interest and other liabilities	100,735	100,446
Total liabilities	7,366,967	7,338,035
Shareholders' equity		
Common stock - no par value		
Authorized - 160,000,000 shares; Issued - 68,730,731 shares in 2016 and 2015	567,497	571,155
Retained earnings	398,224	388,240
Accumulated other comprehensive loss	(23,209)	(30,580)
Treasury stock, at cost, 6,875,704 shares in 2016 and 7,089,051 shares in 2015	(115,925)	(119,439)
Total shareholders' equity	826,587	809,376
Total liabilities and shareholders' equity	$ 8,193,554	$ 8,147,411

See Notes to Consolidated Financial Statements.

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FIRST FINANCIAL BANCORP. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF INCOME
(Dollars in thousands, except per share data)
(Unaudited)

	Three months ended March 31,	
	2016	2015
Interest income		
Loans, including fees	$63,399	$ 54,464
Investment securities		
Taxable	11,373	9,608
Tax-exempt	1,162	1,117
Total interest on investment securities	12,535	10,725
Other earning assets	(1,139)	(1,181)
Total interest income	74,795	64,008
Interest expense		
Deposits	5,530	4,820
Short-term borrowings	1,170	303
Long-term borrowings	1,540	299
Total interest expense	8,240	5,422
Net interest income	66,555	58,586
Provision for loan and lease losses	1,655	2,060
Net interest income after provision for loan and lease losses	64,900	56,526
Noninterest income		
Service charges on deposit accounts	4,381	4,523
Trust and wealth management fees	3,440	3,634
Bankcard income	2,882	2,620
Client derivative fees	1,095	962
Net gains from sales of loans	1,181	1,464
Net gains on sales of investment securities	24	0
FDIC loss sharing income	(565)	(1,046)
Accelerated discount on covered/formerly covered loans	971	2,092
Other	2,103	3,364
Total noninterest income	15,512	17,613
Noninterest expenses		
Salaries and employee benefits	29,615	26,941
Net occupancy	4,957	5,005
Furniture and equipment	2,213	2,153
Data processing	2,718	2,772
Marketing	1,065	888
Communication	481	570
Professional services	1,813	1,970
State intangible tax	639	577
FDIC assessments	1,132	1,090
Loss (gain) - other real estate owned	(190)	474
Loss sharing expense	297	301
Other	5,980	5,327
Total noninterest expenses	50,720	48,068

Income before income taxes	29,692	26,071
Income tax expense	9,878	8,450
Net income	$19,814	$ 17,621
Net earnings per common share - basic	$0.32	$ 0.29
Net earnings per common share - diluted	$0.32	$ 0.29
Cash dividends declared per share	$0.16	$ 0.16
Average common shares outstanding - basic	61,036,797	61,013,489
Average common shares outstanding - diluted	61,840,247	61,731,844

See Notes to Consolidated Financial Statements.

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FIRST FINANCIAL BANCORP. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(Dollars in thousands)
(Unaudited)

	Three months ended March 31,	
	2016	2015
Net income	$19,814	$17,621
Other comprehensive income (loss), net of tax:		
Unrealized gains (losses) on investment securities arising during the period	7,043	5,008
Change in retirement obligation	200	183
Unrealized gain (loss) on derivatives	128	(816)
Unrealized gain (loss) on foreign currency exchange	0	(20)
Other comprehensive income (loss)	7,371	4,355
Comprehensive income	$27,185	$21,976

See Notes to Consolidated Financial Statements.

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FIRST FINANCIAL BANCORP. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY
(Dollars in thousands except per share data)
(Unaudited)

	Common Stock	Common Stock	Retained	Accumulated other comprehensive	Treasury stock		
	Shares	Amount	Earnings	income (loss)	Shares	Amount	Total
Balance at January 1, 2015	68,730,731	$574,643	$352,587	$ (21,409)	(7,274,184)	$(122,050)	$783,771
Net income			17,621				17,621
Other comprehensive income (loss)				4,355			4,355
Cash dividends declared:							
Common stock at $0.16 per share			(9,818)				(9,818)
Excess tax benefit on share-based compensation		99					99
Exercise of stock options, net of shares purchased		(170)			15,217	256	86
Restricted stock awards, net of forfeitures		(4,807)			215,123	3,577	(1,230)
Share-based compensation expense		858					858
Balance at March 31, 2015	68,730,731	$570,623	$360,390	$ (17,054)	(7,043,844)	$(118,217)	$795,742
Balance at January 1, 2016	68,730,731	$571,155	$388,240	$ (30,580)	(7,089,051)	$(119,439)	$809,376
Net income			19,814				19,814
Other comprehensive income (loss)				7,371			7,371
Cash dividends declared:							
Common stock at $0.16 per share			(9,830)				(9,830)
Excess tax benefit on share-based compensation		105					105
Exercise of stock options, net of shares purchased		(85)			9,937	167	82
Restricted stock awards, net of forfeitures		(4,685)			203,410	3,347	(1,338)
Share-based compensation expense		1,007					1,007
Balance at March 31, 2016	68,730,731	$567,497	$398,224	$ (23,209)	(6,875,704)	$(115,925)	$826,587

See Notes to Consolidated Financial Statements.

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FIRST FINANCIAL BANCORP. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Dollars in thousands)
(Unaudited)

	Three months ended March 31,	
	2016	2015
Operating activities		
Net income	$19,814	$17,621
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for loan and lease losses	1,655	2,060
Depreciation and amortization	3,287	3,208
Stock-based compensation expense	1,007	858
Pension expense (income)	(225)	(300)
Net amortization of premiums/accretion of discounts on investment securities	1,911	1,741
Gains on sales of investment securities	(24)	0
Originations of loans held for sale	(42,935)	(59,541)
Net gains from sales of loans held for sale	(1,181)	(1,464)
Proceeds from sales of loans held for sale	49,381	56,816
Deferred income taxes	0	2,313
Decrease (increase) in interest receivable	(2,471)	(2,354)
Decrease (increase) in cash surrender value of life insurance	(493)	(480)
Decrease (increase) in indemnification asset	1,374	2,269
(Decrease) increase in interest payable	(1,353)	0
Decrease (increase) in other assets	(15,305)	(13,435)
(Decrease) increase in other liabilities	(3,923)	5,790
Net cash provided by (used in) operating activities	10,519	15,102
Investing activities		
Proceeds from sales of securities available-for-sale	42,696	25
Proceeds from calls, paydowns and maturities of securities available-for-sale	31,974	26,103
Purchases of securities available-for-sale	(36,851)	(55,005)
Proceeds from calls, paydowns and maturities of securities held-to-maturity	22,881	27,155
Net decrease (increase) in interest-bearing deposits with other banks	18,152	(2,720)
Net decrease (increase) in loans and leases	(117,755)	8,883
Proceeds from disposal of other real estate owned	2,035	4,557
Purchases of premises and equipment	(4,900)	(2,255)
Net cash provided by (used in) investing activities	(41,768)	6,743
Financing activities		
Net (decrease) increase in total deposits	(2,847)	58,848
Net (decrease) increase in short-term borrowings	31,474	(69,750)
Payments on long-term debt	0	(532)
Cash dividends paid on common stock	(9,760)	(9,745)
Proceeds from exercise of stock options	111	124
Excess tax benefit on share-based compensation	105	99
Net cash provided by (used in) financing activities	19,083	(20,956)
Cash and due from banks		

Net increase (decrease) in cash and due from banks	(12,166)	889
Cash and due from banks at beginning of period	114,841	110,122
Cash and due from banks at end of period	$102,675	$111,011

See Notes to Consolidated Financial Statements.

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FIRST FINANCIAL BANCORP. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
March 31, 2016
(Unaudited)

NOTE 1: BASIS OF PRESENTATION

The Consolidated Financial Statements of First Financial Bancorp., a bank holding company, principally serving Ohio, Indiana and Kentucky, include the accounts and operations of First Financial and its wholly-owned subsidiary, First Financial Bank, N.A. All significant intercompany transactions and accounts have been eliminated in consolidation. Certain reclassifications of prior periods' amounts have been made to conform to current year presentation. Such reclassifications had no effect on net earnings.

The preparation of financial statements in conformity with GAAP requires management to make estimates, assumptions and judgments that affect the amounts reported in the Consolidated Financial Statements and accompanying Notes. These estimates, assumptions and judgments are inherently subjective and may be susceptible to significant change. Actual realized amounts could differ materially from these estimates.

These interim financial statements have been prepared in accordance with the instructions to Form 10-Q and Article 10 of Regulation S-X, and serve to update the Form 10-K for the year ended December 31, 2015. These interim financial statements may not include all information and notes necessary to constitute a complete set of financial statements under GAAP applicable to annual periods and it is suggested that these interim statements be read in conjunction with the Form 10-K. Management believes these unaudited consolidated financial statements reflect all adjustments of a normal recurring nature which are necessary for a fair presentation of the results for the interim periods presented. The results of operations for the interim periods are not necessarily indicative of the results that may be expected for the full year or any other interim period. The Consolidated Balance Sheet as of December 31, 2015 has been derived from the audited financial statements in the Company’s 2015 Form 10-K.

NOTE 2: RECENTLY ADOPTED AND ISSUED ACCOUNTING STANDARDS

In April 2015, the FASB issued an update (ASU 2015-03, Interest-Imputation of Interest: Simplifying the Presentation of Debt Issuance Costs) that requires debt issuance costs to be presented as a deduction from the corresponding debt liability. Upon adoption, an entity must apply the new guidance retrospectively to all prior periods presented in the financial statements. The provisions of this update became effective January 1, 2016. First Financial early adopted this accounting standard during the third quarter of 2015. Management concluded that the debt issuance costs capitalized in prior periods was immaterial as a component of other assets, total assets, total long-term debt and total liabilities, and as such, the Company's prior periods have not been restated.

In September 2015, the FASB issued an update (ASU 2015-16, Business Combinations: Simplifying the Accounting for Measurement-Period Adjustments) which eliminates the requirement for an acquirer in a business combination to account for measurement-period adjustments retrospectively. This update requires acquiring companies to recognize measurement-period adjustments during the period in which they determine the amounts, including the effect on earnings of any amounts they would have recorded in previous periods if the accounting had been completed at the acquisition date. The guidance in this ASU became effective January 1, 2016 and did not have a material impact on the Company's Consolidated Financial Statements.

In January 2016, the FASB issued an update (ASU 2016-01, Financial Instruments-Overall: Recognition and Measurement of Financial Assets and Financial Liabilities) which will require entities to measure many equity investments at fair value and recognize changes in fair value in net income. This update does not apply to equity investments that result in consolidation, those accounted for under the equity method and certain others, and will eliminate use of the available for sale classification for equity securities while providing a new measurement alternative for equity investments that do not have readily determinable fair values and do not qualify for the net asset value practical expedient. The guidance in this ASU will become effective for interim and annual reporting periods beginning after December 15, 2017, with early adoption permitted. First Financial does not anticipate this update will have a material impact on its Consolidated Financial Statements.

In February 2016, the FASB issued an update (ASU 2016-02, Leases) which will require lessees to record most leases on their balance sheet and recognize leasing expenses in the income statement. Operating leases, except for short-term leases that are subject to an accounting policy election, will be recorded on the balance sheet for lessees by establishing a lease liability and corresponding right-of-use asset. The guidance in this ASU will become effective for interim and annual reporting periods

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beginning after December 15, 2018, with early adoption permitted. First Financial is currently evaluating the impact of this update on its Consolidated Financial Statements.

In March 2016, the FASB issued an update (ASU 2016-05, Derivatives and Hedging: Effect of Derivative Contract Novations on Existing Hedge Accounting Relationships) which clarifies that the novation of a derivative contract in a hedge accounting relationship does not, in and of itself, require de-designation of that hedge accounting relationship. In the event of a novation, hedge accounting relationships could continue if all other hedge accounting criteria are met, including the expectation that the hedge will be highly effective when the creditworthiness of the new counterparty to the derivative contract is considered. The guidance in this ASU will become effective for interim and annual reporting periods beginning after December 15, 2016, with early adoption permitted. First Financial does not anticipate this update will have a material impact on its Consolidated Financial Statements.

In March 2016, the FASB issued an update (ASU 2016-06, Derivatives and Hedging: Contingent Put and Call Options in Debt Instruments) which clarifies that an assessment of whether an embedded contingent put or call option is clearly and closely related to the debt host requires only an analysis of the four-step decision sequence in ASC 815-15-25-42. Entities are required to apply the guidance to existing debt instruments (or hybrid financial instruments that are determined to have a debt host) using a modified retrospective transition method as of the period of adoption. The guidance in this ASU will become effective for interim and annual reporting periods beginning after December 15, 2016, with early adoption permitted. First Financial does not anticipate this update will have a material impact on its Consolidated Financial Statements.

In March 2016, the FASB issued an update (ASU 2016-07, Investments-Equity Method and Joint Ventures: Simplifying the Transition to the Equity Method of Accounting) which will eliminate the requirement to retrospectively apply the equity method when an investment that had been accounted for utilizing another method qualifies for use of the equity method. The guidance in this ASU will become effective for interim and annual reporting periods beginning after December 15, 2016, with early adoption permitted. First Financial does not anticipate this update will have a material impact on its Consolidated Financial Statements.

In March 2016, the FASB issued an update (ASU 2016-09, Compensation-Stock Compensation: Improvements to Employee Share-Based Payment Accounting) which will require recognition of the income tax effects of share-based awards in the income statement when the awards vest or are settled (i.e., Additional Paid-in-Capital pools will be eliminated). The guidance in this ASU will become effective for interim and annual reporting periods beginning after December 15, 2016, with early adoption permitted. First Financial does not anticipate this update will have a material impact on its Consolidated Financial Statements.

NOTE 3: INVESTMENTS

For the first quarter 2016, proceeds on the sale of $42.7 million of available-for-sale securities resulted in gains of $0.3 million and losses of $0.3 million. For the comparable quarter in 2015, proceeds on the sale of $25 thousand of available-for-sale securities resulted in no gains or losses. No held-to-maturity securities were sold.

The following is a summary of held-to-maturity and available-for-sale investment securities as of March 31, 2016:

	Held-to-maturity				Available-for-sale			
(Dollars in thousands)	Amortized cost	Unrecognized gain	Unrecognized loss	Fair value	Amortized cost	Unrealized gain	Unrealized loss	Fair value
U.S. Treasuries	$0	$ 0	$ 0	$0	$98	$ 3	$0	$101
Securities of U.S. government agencies and corporations	14,935	373	0	15,308	8,183	223	0	8,406

Mortgage-backed securities	655,387	15,615	(410)	670,592	720,407	6,868	(4,493)	722,782
Obligations of state and other political subdivisions	27,180	480	(2)	27,658	103,215	3,437	(443)	106,209
Asset-backed securities	0	0	0	0	258,731	31	(5,266)	253,496
Other securities	4,813	0	(94)	4,719	74,459	632	(1,766)	73,325
Total	$702,315	$ 16,468	$ (506)	$718,277	$1,165,093	$ 11,194	$(11,968)	$1,164,319

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The following is a summary of held-to-maturity and available-for-sale investment securities as of December 31, 2015:

(Dollars in thousands)	Held-to-maturity Amortized cost	Unrecognized gain	Unrecognized loss	Fair value	Available-for-sale Amortized cost	Unrealized gain	Unrealized loss	Fair value
U.S. Treasuries	$0	$ 0	$ 0	$0	$98	$ 0	$(1)	$97
Securities of U.S. government agencies and corporations	15,486	121	0	15,607	8,183	157	0	8,340
Mortgage-backed securities	678,318	7,452	(1,999)	683,771	775,285	2,708	(12,926)	765,067
Obligations of state and other political subdivisions	27,646	338	(99)	27,885	105,212	2,655	(730)	107,137
Asset-backed securities	0	0	0	0	236,411	35	(3,445)	233,001
Other securities	4,809	0	(121)	4,688	77,876	523	(1,399)	77,000
Total	$726,259	$ 7,911	$ (2,219)	$731,951	$1,203,065	$ 6,078	$(18,501)	$1,190,642

The following table provides a summary of investment securities by contractual maturity or estimated weighted average life as of March 31, 2016. Estimated lives on amortizing investment securities may differ from contractual maturities as issuers may have the right to call or prepay obligations with or without call or prepayment penalties.

(Dollars in thousands)	Held-to-maturity Amortized cost	Fair value	Available-for-sale Amortized cost	Fair value
Due in one year or less	$5,105	$5,207	$58,659	$58,493
Due after one year through five years	563,324	574,597	775,602	774,467
Due after five years through ten years	133,886	138,473	303,552	304,623
Due after ten years	0	0	27,280	26,736
Total	$702,315	$718,277	$1,165,093	$1,164,319

The following tables provide the fair value and gross unrealized losses on investment securities in an unrealized loss position, aggregated by investment category and the length of time the individual securities have been in a continuous loss position:

	March 31, 2016					
	Less than 12 months		12 months or more		Total	
(Dollars in thousands)	Fair value	Unrealized loss	Fair value	Unrealized loss	Fair value	Unrealized loss
Mortgage-backed securities	$167,950	$ (1,299)	$235,099	$ (3,604)	$403,049	$(4,903)
Obligations of state and other political subdivisions	6,684	(53)	20,758	(392)	27,442	(445)
Asset-backed securities	215,166	(4,217)	24,018	(1,049)	239,184	(5,266)
Other securities	34,001	(1,123)	16,766	(737)	50,767	(1,860)
Total	$423,801	$ (6,692)	$296,641	$ (5,782)	$720,442	$(12,474)

	December 31, 2015					
	Less than 12 months		12 months or more		Total	
(Dollars in thousands)	Fair value	Unrealized loss	Fair value	Unrealized loss	Fair value	Unrealized loss
Securities of U.S. government agencies and corporations	$97	$ 0	$0	$ 0	$97	$ 0

Mortgage-backed securities	500,768	(5,363)	246,523	(9,563)	747,291	(14,926)
Obligations of state and other political subdivisions	5,800	(65)	29,287	(764)	35,087	(829)
Asset-backed securities	189,066	(3,042)	17,144	(403)	206,210	(3,445)
Other securities	30,828	(592)	24,716	(928)	55,544	(1,520)
Total	$726,559	$ (9,062)	$317,670	$(11,658)	$1,044,229	$(20,720)

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Gains and losses on debt securities are generally due to fluctuations in current market yields relative to the yields of the debt securities at their amortized cost. All securities with unrealized losses are reviewed quarterly to determine if any impairment is considered other than temporary, requiring a write-down to fair value. First Financial considers the percentage loss on a security, duration of the loss, average life or duration of the security, credit rating of the security and payment performance as well as the Company's intent and ability to hold the security to maturity when determining whether any impairment is other than temporary. At this time First Financial does not intend to sell, and it is not more likely than not that the Company will be required to sell debt securities temporarily impaired prior to maturity or recovery of the recorded value. First Financial had no other than temporary impairment related to its investment securities portfolio as of March 31, 2016 or December 31, 2015.

For further detail on the fair value of investment securities, see Note 14 – Fair Value Disclosures.

NOTE 4: LOANS AND LEASES

First Financial offers clients a variety of commercial and consumer loan and lease products with various interest rates and payment terms. Lending activities are primarily concentrated in states where the Bank currently operates banking centers (Ohio, Indiana and Kentucky). Additionally, First Financial has two national lending platforms, one that provides equipment and leasehold improvement financing for franchisees in the quick service and casual dining restaurant sector and another that provides loans secured by commissions and cash collateral accounts primarily to insurance agents and brokers. Commercial loan categories include commercial and industrial, commercial real estate, construction real estate and lease financing. Consumer loan categories include residential real estate, home equity, installment and credit card.

Purchased impaired loans. Loans accounted for under FASB ASC Topic 310-30, Loans and Debt Securities Acquired with Deteriorated Credit Quality, are referred to as purchased impaired loans. First Financial accounts for the majority of loans acquired in FDIC transactions as purchased impaired loans, except for loans with revolving privileges, which are outside the scope of FASB ASC Topic 310-30, and loans for which cash flows could not be estimated, which are accounted for under the cost recovery method. Purchased impaired loans include loans previously covered under loss sharing agreements as well as loans that remain subject to FDIC loss sharing coverage.

Purchased impaired loans are not classified as nonperforming assets as the loans are considered to be performing under FASB ASC Topic 310-30. Therefore, interest income, through accretion of the difference between the carrying value of the loans and the expected cash flows (accretable difference) is recognized on all purchased impaired loans. First Financial had purchased impaired loans totaling $177.0 million and $191.6 million, at March 31, 2016 and December 31, 2015, respectively. The outstanding balance of all purchased impaired loans, including all contractual principal, interest, fees and penalties, was $196.2 million and $213.3 million as of March 31, 2016 and December 31, 2015, respectively. These balances exclude contractual interest not yet accrued.

Changes in the carrying amount of accretable difference for purchased impaired loans were as follows:

	Three months ended March 31,	
(Dollars in thousands)	2016	2015
Balance at beginning of period	$64,857	$106,622
Reclassification from/(to) nonaccretable difference	318	(1,576)
Accretion	(4,210)	(6,357)
Other net activity [(1)]	(2,241)	(6,701)
Balance at end of period	$58,724	$91,988

(1) Includes the impact of loan repayments and charge-offs.

First Financial regularly reviews its forecast of expected cash flows for purchased impaired loans. The Company recognized reclassifications from nonaccretable to accretable difference of $0.3 million for the first quarter of 2016, however, during the three months ended March 31, 2015, the Company recognized reclassifications from accretable to nonaccretable difference of $1.6 million due to changes in the cash flow expectations related to certain loan pools. These reclassifications can result in impairment and provision expense in the current period or yield adjustments on the related loan pools on a prospective basis.

Covered loans. Loans acquired in FDIC-assisted transactions covered under loss sharing agreements whereby the FDIC will reimburse First Financial for the majority of any losses incurred are referred to as covered loans. Pursuant to the terms of the

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loss sharing agreements, covered loans are subject to a stated loss threshold whereby the FDIC will reimburse First Financial for 80% of losses up to a stated loss threshold and 95% of losses in excess of the threshold. These loss sharing agreements provide for partial loss protection on single-family, residential loans for a period of ten years and First Financial is required to share any recoveries of previously charged-off amounts for the same time period, on the same pro-rata basis with the FDIC. All other loans subject to loss sharing agreements were provided loss protection for a period of five years and recoveries of previously charged-off amounts must be shared with the FDIC for an additional three year period, on the same pro-rata basis.

The Company's loss sharing agreements with the FDIC related to non-single family loans expired effective October 1, 2014, and the ten year period of loss protection on all other covered loans and covered OREO expires October 1, 2019. Covered loans totaled $109.2 million as of March 31, 2016 and $113.3 million as of December 31, 2015.

Credit Quality. To facilitate the monitoring of credit quality for commercial loans, and for purposes of determining an appropriate ALLL, First Financial utilizes the following categories of credit grades:

Pass - Higher quality loans that do not fit any of the other categories described below.

Special Mention - First Financial assigns a special mention rating to loans and leases with potential weaknesses that deserve management's close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the loan or lease or in First Financial's credit position at some future date.

Substandard - First Financial assigns a substandard rating to loans or leases that are inadequately protected by the current sound financial worth and paying capacity of the borrower or of the collateral pledged, if any. Substandard loans and leases have well-defined weaknesses that jeopardize repayment of the debt. Substandard loans and leases are characterized by the distinct possibility that the Company will sustain some loss if the deficiencies are not addressed.

Doubtful - First Financial assigns a doubtful rating to loans and leases with all the attributes of a substandard rating with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently existing facts, conditions and values, highly questionable and improbable. The possibility of loss is extremely high, but because of certain important and reasonably specific pending factors that may work to the advantage and strengthening of the credit quality of the loan or lease, its classification as an estimated loss is deferred until its more exact status may be determined. Pending factors include proposed merger, acquisition or liquidation procedures, capital injection, perfecting liens on additional collateral and refinancing plans.

The credit grades described above, which are derived from standard regulatory rating definitions, are assigned upon initial approval of credit to borrowers and updated periodically thereafter.

First Financial considers repayment performance to be the best indicator of credit quality for consumer loans. Consumer loans that have principal and interest payments that are past due by 90 days or more are generally classified as nonperforming. Additionally, consumer loans that have been modified in a TDR are classified as nonperforming.

Commercial and consumer credit exposure by risk attribute was as follows:

	As of March 31, 2016				
		Real Estate			
(Dollars in thousands)	Commercial	Construction	Commercial	Leasing	Total
Pass	$1,680,764	$337,472	$2,182,683	$99,583	$4,300,502
Special Mention	22,155	3,417	19,754	0	45,326
Substandard	41,813	564	59,420	1,552	103,349

Doubtful	0	0	0	0	0
Total	$1,744,732	$341,453			