

CAPITAL CITY BANK GROUP INC
Form 10-Q
November 06, 2014

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

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

For the Quarterly Period Ended September 30, 2014

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: 0-13358

(Exact name of registrant as specified in its charter)

Florida **59-2273542**
(State or other jurisdiction of incorporation or organization) (I.R.S. Employer Identification No.)

217 North Monroe Street, Tallahassee, Florida 32301
(Address of principal executive office) (Zip Code)

(850) 402-7000

(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 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
(Do not check if 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

At October 31, 2014, 17,432,887 shares of the Registrant's Common Stock, \$.01 par value, were outstanding.

CAPITAL CITY BANK GROUP, INC.

QUARTERLY REPORT ON FORM 10-Q

FOR THE PERIOD ENDED SEPTEMBER 30, 2014

TABLE OF CONTENTS

PART I – Financial Information	Page
Item 1. <u>Consolidated Financial Statements (Unaudited)</u>	
<u>Consolidated Statements of Financial Condition – September 30, 2014 and December 31, 2013</u>	4
<u>Consolidated Statements of Operations – Three and Nine Months Ended September 30, 2014 and 2013</u>	5
<u>Consolidated Statements of Comprehensive Income – Three and Nine Months Ended September 30, 2014 and 2013</u>	6
<u>Consolidated Statements of Changes in Shareowners’ Equity – Nine Months Ended September 30, 2014 and 2013</u>	7
<u>Consolidated Statements of Cash Flows – Nine Months Ended September 30, 2014 and 2013</u>	8
<u>Notes to Consolidated Financial Statements</u>	9
Item 2. <u>Management’s Discussion and Analysis of Financial Condition and Results of Operations</u>	28
Item 3. <u>Quantitative and Qualitative Disclosure About Market Risk</u>	44
Item 4. <u>Controls and Procedures</u>	44
PART II – Other Information	
Item 1. <u>Legal Proceedings</u>	44
Item 1A. <u>Risk Factors</u>	44
Item 2. <u>Unregistered Sales of Equity Securities and Use of Proceeds</u>	44
Item 3. <u>Defaults Upon Senior Securities</u>	45
Item 4. <u>Mine Safety Disclosure</u>	45
Item 5. <u>Other Information</u>	45
Item 6. <u>Exhibits</u>	45
Signatures	46

INTRODUCTORY NOTE

Caution Concerning Forward-Looking Statements

This Quarterly Report on Form 10-Q contains “forward-looking statements” within the meaning of the Private Securities Litigation Reform Act of 1995. These forward-looking statements include, among others, statements about our beliefs, plans, objectives, goals, expectations, estimates and intentions that are subject to significant risks and uncertainties and are subject to change based on various factors, many of which are beyond our control. The words “may,” “could,” “should,” “would,” “believe,” “anticipate,” “estimate,” “expect,” “intend,” “plan,” “target,” “goal,” and similar expressions are used to identify forward-looking statements.

All forward-looking statements, by their nature, are subject to risks and uncertainties. Our actual future results may differ materially from those set forth in our forward-looking statements.

Our ability to achieve our financial objectives could be adversely affected by the factors discussed in detail in Part I, Item 2. “Management’s Discussion and Analysis of Financial Condition and Results of Operations” and Part II, Item 1A. “Risk Factors” in this Quarterly Report on Form 10-Q and the following sections of our Annual Report on Form 10-K for the year ended December 31, 2013 (the “2013 Form 10-K”): (a) “Introductory Note” in Part I, Item 1. “Business”; (b) “Risk Factors” in Part I, Item 1A, as updated in our subsequent quarterly reports filed on Form 10-Q; and (c) “Introduction” in “Management’s Discussion and Analysis of Financial Condition and Results of Operations,” in Part II, Item 7, as well as:

- § legislative or regulatory changes, including the Dodd-Frank Act and Basel III;
- § our ability to successfully manage interest rate risk, liquidity risk, and other risks inherent to our industry;
- § the effects of security breaches and computer viruses that may affect our computer systems;
- § the accuracy of our financial statement estimates and assumptions, including the estimates used for our loan loss provision, deferred tax asset valuation allowance, and pension plan;
- § the frequency and magnitude of foreclosure of our loans;
- § the effects of our lack of a diversified loan portfolio, including the risks of geographic and industry concentrations;
- § the strength of the United States economy in general and the strength of the local economies in which we conduct operations;
- § our need and our ability to incur additional debt or equity financing;
- § our ability to declare and pay dividends and repurchase shares of the Company’s common stock under our repurchase plan;
- § changes in the securities and real estate markets;
- § changes in monetary and fiscal policies of the U.S. Government;
- § inflation, interest rate, market and monetary fluctuations;
- § the effects of harsh weather conditions, including hurricanes, and man-made disasters;
- § our ability to comply with the extensive laws and regulations to which we are subject;
- § our ability to comply with the laws for each jurisdiction where we operate;
- § the willingness of clients to accept third-party products and services rather than our products and services and vice versa;
- § increased competition and its effect on pricing;
- § technological changes;

- § negative publicity and the impact on our reputation;
- § changes in consumer spending and saving habits;
- § growth and profitability of our noninterest income;
- § changes in accounting principles, policies, practices or guidelines;
- § the limited trading activity of our common stock;
- § the concentration of ownership of our common stock;
- § anti-takeover provisions under federal and state law as well as our Articles of Incorporation and our Bylaws;
- § other risks described from time to time in our filings with the Securities and Exchange Commission; and
- § our ability to manage the risks involved in the foregoing.

However, other factors besides those listed in *Item 1A Risk Factors* or discussed in this Form 10-Q also could adversely affect our results, and you should not consider any such list of factors to be a complete set of all potential risks or uncertainties. Any forward-looking statements made by us or on our behalf speak only as of the date they are made. We do not undertake to update any forward-looking statement, except as required by applicable law.

PART I. FINANCIAL INFORMATION**Item 1. CONSOLIDATED FINANCIAL STATEMENTS****CAPITAL CITY BANK GROUP, INC.****CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION**

(Dollars in Thousands)	(Unaudited) September 30, 2014	December 31, 2013
ASSETS		
Cash and Due From Banks	\$ 50,049	\$ 55,209
Federal Funds Sold and Interest Bearing Deposits	253,974	474,719
Total Cash and Cash Equivalents	304,023	529,928
Investment Securities, Available for Sale, at fair value	322,297	251,420
Investment Securities, Held to Maturity, at amortized cost (fair value of \$172,717 and \$146,961)	173,188	148,211
Total Investment Securities	495,485	399,631
Loans Held For Sale	8,700	11,065
Loans, Net of Unearned Income	1,414,375	1,388,604
Allowance for Loan Losses	(19,093)	(23,095)
Loans, Net	1,395,282	1,365,509
Premises and Equipment, Net	102,546	103,385
Goodwill	84,811	84,811
Other Intangible Assets	—	32
Other Real Estate Owned	41,726	48,071
Other Assets	67,044	69,471
Total Assets	\$ 2,499,617	\$ 2,611,903
LIABILITIES		
Deposits:		
Noninterest Bearing Deposits	\$ 667,616	\$ 641,463
Interest Bearing Deposits	1,365,962	1,494,785
Total Deposits	2,033,578	2,136,248
Short-Term Borrowings	42,586	51,321
Subordinated Notes Payable	62,887	62,887
Other Long-Term Borrowings	32,305	38,043
Other Liabilities	45,008	47,004
Total Liabilities	2,216,364	2,335,503

SHAREOWNERS' EQUITY

Preferred Stock, \$.01 par value; 3,000,000 shares authorized; no shares issued and outstanding	—	—
Common Stock, \$.01 par value; 90,000,000 shares authorized; 17,432,884 and 17,360,960 shares issued and outstanding at September 30, 2014 and December 31, 2013, respectively	174	174
Additional Paid-In Capital	41,637	41,152
Retained Earnings	249,907	243,614
Accumulated Other Comprehensive Loss, Net of Tax	(8,465	) (8,540)
Total Shareowners' Equity	283,253	276,400
Total Liabilities and Shareowners' Equity	\$ 2,499,617	\$ 2,611,903

The accompanying Notes to Consolidated Financial Statements are an integral part of these statements.

CAPITAL CITY BANK GROUP, INC.**CONSOLIDATED STATEMENTS OF OPERATIONS****(Unaudited)**

	Three Months Ended September 30,		Nine Months Ended September 30,	
(Dollars in Thousands, Except Per Share Data)	2014	2013	2014	2013
INTEREST INCOME				
Loans, including Fees	\$ 18,528	\$ 19,264	\$ 54,778	\$ 59,127
Investment Securities:				
Taxable	921	571	2,440	1,739
Tax Exempt	113	146	380	392
Funds Sold	204	269	752	818
Total Interest Income	19,766	20,250	58,350	62,076
INTEREST EXPENSE				
Deposits	255	335	856	1,117
Short-Term Borrowings	17	46	54	189
Subordinated Notes Payable	333	339	995	1,020
Other Long-Term Borrowings	263	330	823	1,010
Total Interest Expense	868	1,050	2,728	3,336
NET INTEREST INCOME	18,898	19,200	55,622	58,740
Provision for Loan Losses	424	555	1,282	3,075
Net Interest Income After Provision For Loan Losses	18,474	18,645	54,340	55,665
NONINTEREST INCOME				
Deposit Fees	6,211	6,474	18,293	18,856
Bank Card Fees	2,707	2,715	8,234	8,130
Wealth Management Fees	2,050	2,130	5,820	5,946
Mortgage Banking Fees	911	869	2,274	2,880
Data Processing Fees	336	662	1,265	1,985
Other	1,136	1,176	3,597	3,487
Total Noninterest Income	13,351	14,026	39,483	41,284
NONINTEREST EXPENSE				
Compensation	15,378	16,158	46,365	49,544
Occupancy, Net	4,575	4,403	13,378	12,982
Intangible Amortization	—	46	32	162
Other Real Estate	1,783	1,868	5,458	6,981
Other	6,871	7,678	20,816	22,087
Total Noninterest Expense	28,607	30,153	86,049	91,756
INCOME BEFORE INCOME TAXES	3,218	2,518	7,774	5,193
Income Tax Expense	1,103	927	435	1,920

Edgar Filing: CAPITAL CITY BANK GROUP INC - Form 10-Q

NET INCOME	\$ 2,115	\$ 1,591	\$ 7,339	\$ 3,273
BASIC NET INCOME PER SHARE	\$ 0.12	\$ 0.09	\$ 0.42	\$ 0.19
DILUTED NET INCOME PER SHARE	\$ 0.12	\$ 0.09	\$ 0.42	\$ 0.19
Average Basic Shares Outstanding	17,440	17,336	17,422	17,319
Average Diluted Shares Outstanding	17,519	17,396	17,482	17,381

The accompanying Notes to Consolidated Financial Statements are an integral part of these statements.

CAPITAL CITY BANK GROUP, INC.**CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME****(Unaudited)**

(Dollars in Thousands)	Three Months Ended		Nine Months Ended	
	September 30, 2014	2013	September 30, 2014	2013
NET INCOME	\$ 2,115	\$ 1,591	\$ 7,339	\$ 3,273
Other comprehensive income, before tax:				
Change in net unrealized gain (loss) on securities available for sale	(173)	459	78	(1,149)
Unrealized losses on securities transferred from available for sale to held to maturity	—	(523)	—	(523)
Amortization of unrealized losses on securities transferred from available for sale to held to maturity	17	7	53	7
Reclassification adjustment for impairment loss realized in net income	—	210	—	410
Other comprehensive income (loss), before tax	(156)	153	131	(1,255)
Deferred tax (benefit) expense related to other comprehensive income	(54)	136	56	(486)
Other comprehensive income (loss), net of tax	(102)	17	75	(769)
TOTAL COMPREHENSIVE INCOME	\$ 2,013	\$ 1,608	\$ 7,414	\$ 2,504

The accompanying Notes to Consolidated Financial Statements are an integral part of these statements.

CAPITAL CITY BANK GROUP, INC.**CONSOLIDATED STATEMENTS OF CHANGES IN SHAREOWNERS' EQUITY****(Unaudited)**

<i>(Dollars In Thousands, Except Share Data)</i>	Shares Outstanding	Common Stock	Additional Paid-In Capital	Retained Earnings	Accumulated Other Comprehensive Loss, Net of Taxes	Total
Balance, January 1, 2013	17,232,380	\$ 172	\$ 38,707	\$237,569	\$ (29,559)	\$246,889
Net Income		—	—	3,273	—	3,273
Other Comprehensive Income, Net of Tax		—	—	—	(769)	(769)
Stock Based Compensation		—	914	—	—	914
Impact of Transactions Under Compensation Plans, net	103,898	1	860	—	—	861
Balance, September 30, 2013	17,336,278	\$ 173	\$ 40,481	\$240,842	\$ (30,328)	\$251,168
Balance, January 1, 2014	17,360,960	\$ 174	\$ 41,152	\$243,614	\$ (8,540)	\$276,400
Net Income		—	—	7,339	—	7,339
Other Comprehensive Income, Net of Tax		—	—	—	75	75
Cash Dividends (\$0.0600 per share)		—	—	(1,046)	—	(1,046)
Repurchase of Common Stock	(19,600)	—	(269)	—	—	(269)
Stock Based Compensation		—	635	—	—	635
Impact of Transactions Under Compensation Plans, net	91,524	—	119	—	—	119
Balance, September 30, 2014	17,432,884	\$ 174	\$ 41,637	\$249,907	\$ (8,465)	\$283,253

The accompanying Notes to Consolidated Financial Statements are an integral part of these statements.

CAPITAL CITY BANK GROUP, INC.**CONSOLIDATED STATEMENTS OF CASH FLOWS****(Unaudited)**

(Dollars in Thousands)	Nine Months Ended September 30,	
	2014	2013
CASH FLOWS FROM OPERATING ACTIVITIES		
Net Income	\$ 7,339	\$ 3,273
Adjustments to Reconcile Net Income to Cash Provided by Operating Activities:		
Provision for Loan Losses	1,282	3,075
Depreciation	4,869	4,830
Amortization of Premiums, Discounts, and Fees (net)	3,619	3,422
Amortization of Intangible Assets	32	162
Impairment Loss on Security	—	410
Net Decrease in Loans Held-for-Sale	2,365	367
Stock Based Compensation	635	914
Deferred Income Taxes	1,280	1,802
Loss on Disposal of Fixed Assets	12	18
Loss on Sales and Write-Downs of Other Real Estate Owned	3,423	4,042
Net Decrease in Other Assets	1,144	1,197
Net (Decrease) Increase in Other Liabilities	(2,248)	) 6,470
Net Cash Provided By Operating Activities	23,752	29,982
CASH FLOWS FROM INVESTING ACTIVITIES		
Securities Held to Maturity:		
Purchases	(56,249)	) (39,115)
Payments, Maturities, and Calls	30,078	4,141
Securities Available for Sale:		
Purchases	(159,741)	) (142,336)
Payments, Maturities, and Calls	86,149	99,708
Net (Increase) Decrease in Loans	(42,808)	) 61,354
Proceeds From Sales of Other Real Estate Owned	15,043	17,397
Purchases of Premises and Equipment	(4,042)	) (1,458)
Net Cash Used In Investing Activities	(131,570)	) (309)
CASH FLOWS FROM FINANCING ACTIVITIES		
Net Decrease in Deposits	(102,670)	) (128,110)
Net (Decrease) Increase in Short-Term Borrowings	(10,263)	) 55
Increase in Other Long-Term Borrowings	—	1,303
Repayment of Other Long-Term Borrowings	(4,210)	) (3,490)
Dividends Paid	(1,046)) —
Payments to Repurchase Common Stock	(269)) —
Issuance of Common Stock Under Compensation Plans	371	842
Net Cash Used In Financing Activities	(118,087)	) (129,400)

Edgar Filing: CAPITAL CITY BANK GROUP INC - Form 10-Q

NET DECREASE IN CASH AND CASH EQUIVALENTS	(225,905)	(99,727)
Cash and Cash Equivalents at Beginning of Period	529,928	509,732
Cash and Cash Equivalents at End of Period	\$ 304,023	\$ 410,005
Supplemental Cash Flow Disclosures:		
Interest Paid	\$ 2,678	\$ 2,364
Income Taxes Paid (Refunded)	\$ 2,660	\$ (2,201)
Noncash Investing and Financing Activities:		
Transfer of Securities Available for Sale to Held to Maturity	\$ —	\$ 62,488
Loans Transferred to Other Real Estate Owned	\$ 12,121	\$ 21,030
Transfer of Current Portion of Long-Term Borrowings	\$ 1,528	\$ 4,428

The accompanying Notes to Consolidated Financial Statements are an integral part of these statements.

CAPITAL CITY BANK GROUP, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES

Nature of Operations. Capital City Bank Group, Inc. (“CCBG” or the “Company”) provides a full range of banking and banking-related services to individual and corporate clients through its wholly-owned subsidiary, Capital City Bank (“CCB” or the “Bank” and together with the Company), with banking offices located in Florida, Georgia, and Alabama. The Company is subject to competition from other financial institutions, is subject to regulation by certain government agencies and undergoes periodic examinations by those regulatory authorities.

Basis of Presentation. The consolidated financial statements in this Quarterly Report on Form 10-Q include the accounts of CCBG and CCB. All material inter-company transactions and accounts have been eliminated.

The accompanying unaudited consolidated financial statements have been prepared in accordance with generally accepted accounting principles 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 generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included.

The consolidated statement of financial condition at December 31, 2013 has been derived from the audited consolidated financial statements at that date but does not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. 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, 2013.

NOTE 2 – INVESTMENT SECURITIES

Investment Portfolio Composition. The amortized cost and related market value of investment securities available-for-sale were as follows:

September 30, 2014

December 31, 2013

Edgar Filing: CAPITAL CITY BANK GROUP INC - Form 10-Q

	Amortized Cost	Unrealized Gains	Unrealized Losses	Market Value	Amortized Cost	Unrealized Gain	Unrealized Losses	Market Value
Available for Sale								
U.S. Treasury	\$ 165,055	\$ 97	\$ 95	\$ 165,057	\$ 71,791	\$ 82	\$ 40	\$ 71,833
U.S. Government Agency States and Political Subdivisions	94,925	259	190	94,994	75,275	127	256	75,146
Mortgage-Backed Securities	51,052	99	11	51,140	91,605	167	19	91,753
Equity Securities ⁽¹⁾	2,167	194	—	2,361	2,583	212	—	2,795
Total	8,745	—	—	8,745	9,893	—	—	9,893
	321,944	\$ 649	\$ 296	\$ 322,297	\$ 251,147	\$ 588	\$ 315	\$ 251,420
Held to Maturity								
U.S. Treasury	\$ 76,235	\$ 108	\$ 63	\$ 76,280	\$ 43,533	\$ 84	\$ 38	\$ 43,579
U.S. Government Agency States and Political Subdivisions	22,322	28	37	22,313	15,794	38	22	15,810
Mortgage-Backed Securities	30,244	63	5	30,302	33,216	53	4	33,265
Total	44,387	14	579	43,822	55,668	12	1,373	54,307
	\$ 173,188	\$ 213	\$ 684	\$ 172,717	\$ 148,211	\$ 187	\$ 1,437	\$ 146,961

⁽¹⁾ Includes Federal Home Loan Bank and Federal Reserve Bank stock recorded at cost of \$3.9 million and \$4.8 million, respectively, at September 30, 2014 and \$5.0 million and \$4.8 million, respectively, at December 31, 2013.

Securities with an amortized cost of \$225.5 million and \$258.5 million at September 30, 2014 and December 31, 2013, respectively, were pledged to secure public deposits and for other purposes.

The Bank, as a member of the Federal Home Loan Bank of Atlanta (“FHLB”), is required to own capital stock in the FHLB based generally upon the balances of residential and commercial real estate loans, and FHLB advances. FHLB stock which is included in other securities is pledged to secure FHLB advances. No ready market exists for this stock, and it has no quoted market value; however, redemption of this stock has historically been at par value.

Maturity Distribution. As of September 30, 2014, the Company's investment securities are presented below by contractual maturity. Expected maturities may differ from contractual maturities because issuers may have the right to call or prepay obligations. Mortgage-backed securities, certain amortizing U.S. government agency securities, and equity securities are shown separately since they are not due at a single maturity date.

(Dollars in Thousands)	Available for Sale		Held to Maturity	
	Amortized Cost	Market Value	Amortized Cost	Market Value
Due in one year or less	\$67,038	\$67,110	\$17,588	\$17,616
Due after one through five years	173,739	173,766	111,213	111,279
Mortgage-Backed Securities	2,167	2,361	44,387	43,822
U.S. Government Agency	70,255	70,315	—	—
Equity Securities	8,745	8,745	—	—
Total	\$321,944	\$322,297	\$173,188	\$172,717

Unrealized Losses on Investment Securities. The following table summarizes the investment securities with unrealized losses aggregated by major security type and length of time in a continuous unrealized loss position:

(Dollars in Thousands)	Less Than 12 Months		Greater Than 12 Months		Total	
	Market Value	Unrealized Losses	Market Value	Unrealized Losses	Market Value	Unrealized Losses
September 30, 2014						
Available for Sale						
U.S. Government Treasury	\$95,417	\$ 95	\$—	\$ —	\$95,417	\$ 95
U.S. Government Agency	21,896	71	21,702	119	43,598	190
States and Political Subdivisions	3,549	6	507	5	4,056	11
Total	\$120,862	\$ 172	\$22,209	\$ 124	\$143,071	\$ 296
Held to Maturity						
U.S. Government Treasury	\$47,915	\$ 63	\$—	\$ —	\$47,915	\$ 63
U.S. Government Agency	13,486	37	—	—	13,486	37
States and Political Subdivisions	3,717	5	—	—	3,717	5
Mortgage-Backed Securities	33,309	508	3,935	71	37,244	579
Total	\$98,427	\$ 613	\$3,935	\$ 71	\$102,362	\$ 684
December 31, 2013						
Available for Sale						
U.S. Government Treasury	\$24,924	\$ 40	\$—	\$ —	\$24,924	\$ 40
U.S. Government Agency	40,944	235	4,842	21	45,786	256
States and Political Subdivisions	4,101	7	511	12	4,612	19
Total	\$69,969	\$ 282	\$5,353	\$ 33	\$75,322	\$ 315
Held to Maturity						
U.S. Government Treasury	\$10,054	\$ 38	\$—	\$ —	\$10,054	\$ 38

Edgar Filing: CAPITAL CITY BANK GROUP INC - Form 10-Q

U.S. Government Agency	5,676	22	—	—	5,676	22
States and Political Subdivisions	3,316	4	—	—	3,316	4
Mortgage-Backed Securities	44,031	1,373	—	—	44,031	1,373
Total	\$63,077	\$ 1,437	\$—	\$ —	\$63,077	\$ 1,437

Management evaluates securities for other than temporary impairment at least quarterly, and more frequently when economic or market concerns warrant such evaluation. Consideration is given to: 1) the length of time and the extent to which the fair value has been less than amortized cost, 2) the financial condition and near-term prospects of the issuer, and 3) the intent and ability of the Company to retain its investment in the issuer for a period of time sufficient to allow for any anticipated recovery in cost. In analyzing an issuer's financial condition, management considers whether the securities are issued by the federal government or its agencies, whether downgrades by rating agencies have occurred, regulatory issues, and analysts' reports.

Approximately \$22.2 million of investment securities comprised of 26 Small Business Administration securities and one municipal bond, with an unrealized loss of approximately \$124,000, have been in a loss position for greater than 12 months. Approximately \$3.9 million of held to maturity investment securities, comprised of 7 collateralized mortgage obligations, with an unrealized loss of approximately \$71,000 have been in a loss position for greater than 12 months. All of these debt securities are in a loss position because they were acquired when the general level of interest rates was lower than that on September 30, 2014. The Company believes that the unrealized losses in these debt securities are temporary in nature and that the full principal will be collected as anticipated. Because the declines in the market value of these investments are attributable to changes in interest rates and not credit quality and because the Company has the present ability and intent to hold these investments until there is a recovery in fair value, which may be at maturity, the Company does not consider these investments to be other-than-temporarily impaired at September 30, 2014.

NOTE 3 – LOANS, NET

Loan Portfolio Composition. The composition of the loan portfolio was as follows:

(Dollars in Thousands)	September 30, 2014	December 31, 2013
Commercial, Financial and Agricultural	\$ 133,756	\$ 126,607
Real Estate – Construction	38,121	31,012
Real Estate – Commercial Mortgage	501,863	533,871
Real Estate – Residential ⁽¹⁾	308,295	309,692
Real Estate – Home Equity	228,968	227,922
Consumer	203,372	159,500
Loans, Net of Unearned Income	\$ 1,414,375	\$ 1,388,604

⁽¹⁾ *Includes loans in process with outstanding balances of \$5.5 million and \$6.8 million at September 30, 2014 and December 31, 2013, respectively.*

Net deferred fees included in loans were \$1.5 million at September 30, 2014 and December 31, 2013.

The Company has pledged a blanket floating lien on all 1-4 family residential mortgage loans, commercial real estate mortgage loans, and home equity loans to support available borrowing capacity at the FHLB of Atlanta and has pledged a blanket floating lien on all consumer loans, commercial loans, and construction loans to support available borrowing capacity at the Federal Reserve Bank of Atlanta.

Nonaccrual Loans. Loans are generally placed on nonaccrual status if principal or interest payments become 90 days past due and/or management deems the collectability of the principal and/or interest to be doubtful. Loans are returned to accrual status when the principal and interest amounts contractually due are brought current or when future

payments are reasonably assured.

The following table presents the recorded investment in nonaccrual loans and loans past due over 90 days and still on accrual by class of loans.

(Dollars in Thousands)	September 30, 2014		December 31, 2013	
	Nonaccrual	90 + Days	Nonaccrual	90 + Days
Commercial, Financial and Agricultural	\$933	\$ —	\$188	\$ —
Real Estate – Construction	860	—	426	—
Real Estate – Commercial Mortgage	11,920	—	25,227	—
Real Estate – Residential	7,416	—	6,440	—
Real Estate – Home Equity	2,018	—	4,084	—
Consumer	335	62	599	—
Total	\$23,482	\$ 62	\$36,964	\$ —

11

Loan Portfolio Aging. A loan is defined as a past due loan when one full payment is past due or a contractual maturity is over 30 days past due (“DPD”).

The following table presents the aging of the recorded investment in past due loans by class of loans.

<i>(Dollars in Thousands)</i>	30-59 DPD	60-89 DPD	90 + DPD	Total Past Due	Total Current	Total Loans
September 30, 2014						
Commercial, Financial and Agricultural	\$296	\$59	\$ —	\$355	\$132,468	\$133,756
Real Estate – Construction	—	—	—	—	37,261	38,121
Real Estate – Commercial Mortgage	711	26	—	737	489,206	501,863
Real Estate – Residential	1,193	1,094	—	2,287	298,592	308,295
Real Estate – Home Equity	255	119	—	374	226,576	228,968
Consumer	795	178	62	1,035	202,002	203,372
Total	\$3,250	\$1,476	\$ 62	\$4,788	\$1,386,105	\$1,414,375
December 31, 2013						
Commercial, Financial and Agricultural	\$258	\$100	\$ —	\$358	\$126,062	\$126,607
Real Estate – Construction	—	—	—	—	30,587	31,012
Real Estate – Commercial Mortgage	1,548	672	—	2,220	506,424	533,871
Real Estate – Residential	1,647	1,090	—	2,737	300,514	309,692
Real Estate – Home Equity	848	212	—	1,060	222,778	227,922
Consumer	1,127	244	—	1,371	157,529	159,500
Total	\$5,428	\$2,318	\$ —	\$7,746	\$1,343,894	\$1,388,604

Edgar Filing: CAPITAL CITY BANK GROUP INC - Form 10-Q

Allowance for Loan Losses. The allowance for loan losses is a reserve established through a provision for loan losses charged to expense, which represents management's best estimate of probable losses within the existing portfolio of loans. Loans are charged-off to the allowance when facts and circumstances of the individual loan confirm the loan is not fully collectible and the loss is reasonably quantifiable.

The following table details the activity in the allowance for loan losses by portfolio class. Allocation of a portion of the allowance to one category of loans does not preclude its availability to absorb losses in other categories.

<i>(Dollars in Thousands)</i>	Commercial Financial, Agricultural	Real Estate Construction	Real Estate Commercial Mortgage	Real Estate Residential	Real Estate Home Equity	Consumer	Unallocated	Total
Three Months Ended								
September 30, 2014								
Beginning Balance	\$ 706	\$ 1,267	\$ 6,147	\$ 8,214	\$ 3,066	\$ 1,143	\$ —	\$ 20,543
Provision for Loan Losses	387	(280)	386	(505)	331	105	—	424
Charge-Offs	(86)	—	(1,208)	(212)	(621)	(386)	—	(2,513)
Recoveries	28	2	213	93	37	266	—	639
Net Charge-Offs	(58)	2	(955)	(119)	(584)	(120)	—	(1,874)
Ending Balance	\$ 1,035	\$ 989	\$ 5,538	\$ 7,590	\$ 2,813	\$ 1,128	\$ —	\$ 19,093
Three Months Ended								
September 30, 2013								
Beginning Balance	\$ 895	\$ 2,243	\$ 9,951	\$ 9,258	\$ 2,879	\$ 1,042	\$ 1,026	\$ 27,294
Provision for Loan Losses	(171)	(237)	(630)	1,044	277	297	(25)	555
Charge-Offs	(138)	(278)	(882)	(1,178)	(362)	(674)	—	(3,512)
Recoveries	87	1	167	167	13	238	—	673
Net Charge-Offs	(51)	(277)	(715)	(1,011)	(349)	(436)	—	(2,839)
Ending Balance	\$ 673	\$ 1,729	\$ 8,606	\$ 9,291	\$ 2,807	\$ 903	\$ 1,001	\$ 25,010
Nine Months Ended								
September 30, 2013								
Beginning Balance	\$ 1,253	\$ 2,856	\$ 11,081	\$ 8,678	\$ 2,945	\$ 1,327	\$ 1,027	\$ 29,167
Provision for Loan Losses	(345)	(130)	151	2,868	404	153	(26)	3,075
Charge-Offs	(411)	(998)	(2,975)	(2,914)	(797)	(1,321)	—	(9,416)
Recoveries	176	1	349	659	255	744	—	2,184
Net Charge-Offs	(235)	(997)	(2,626)	(2,255)	(542)	(577)	—	(7,232)

Edgar Filing: CAPITAL CITY BANK GROUP INC - Form 10-Q

Ending Balance	\$ 673	\$ 1,729	\$ 8,606	\$ 9,291	\$ 2,807	\$ 903	\$ 1,001	\$ 25,010
----------------	--------	----------	----------	----------	----------	--------	----------	-----------

13

Edgar Filing: CAPITAL CITY BANK GROUP INC - Form 10-Q

The following table details the amount of the allowance for loan losses by portfolio class disaggregated on the basis of the Company's impairment methodology.

<i>(Dollars in Thousands)</i>	Commercial Financial, Agricultural	Real Estate Construction	Real Estate Commercial Mortgage	Real Estate Residential	Real Estate Home Equity	Consumer	Unallocated	Total
September 30, 2014								
Period-end amount Allocated to:								
Loans Individually Evaluated for Impairment	\$ 576	\$ 94	\$ 3,359	\$ 2,526	\$ 471	\$ 12	\$ —	\$ 7,038
Loans Collectively Evaluated for Impairment	459	895	2,179	5,064	2,342	1,116	—	12,055
Ending Balance	\$ 1,035	\$ 989	\$ 5,538	\$ 7,590	\$ 2,813	\$ 1,128	\$ —	\$ 19,093
December 31, 2013								
Period-end amount Allocated to:								
Loans Individually Evaluated for Impairment	\$ 75	\$ 66	\$ 4,336	\$ 2,047	\$ 682	\$ 23	\$ —	\$ 7,229
Loans Collectively Evaluated for Impairment	624	1,514	3,374	7,026	2,369	959	—	15,866
Ending Balance	\$ 699	\$ 1,580	\$ 7,710	\$ 9,073	\$ 3,051	\$ 982	\$ —	\$ 23,095
September 30, 2013								
Period-end amount Allocated to:								
Loans Individually Evaluated for Impairment	\$ 218	\$ 124	\$ 5,045	\$ 2,184	\$ 508	\$ 31	\$ —	\$ 8,110
Loans Collectively Evaluated for Impairment	455	1,605	3,561	7,107	2,299	872	1,001	16,900
Ending Balance	\$ 673	\$ 1,729	\$ 8,606	\$ 9,291	\$ 2,807	\$ 903	\$ 1,001	\$ 25,010

The Company's recorded investment in loans related to each balance in the allowance for loan losses by portfolio class and disaggregated on the basis of the Company's impairment methodology was as follows:

<i>(Dollars in Thousands)</i>	Commercial Financial, Agricultural	Real Estate Construction	Real Estate Commercial Mortgage	Real Estate Residential	Real Estate Home Equity	Consumer	Unallocated	Total
September 30, 2014								
Individually Evaluated for Impairment	\$ 1,489	\$ 835	\$ 37,524	\$ 22,087	\$ 2,796	\$ 271	\$ —	\$ 65,002
Collectively Evaluated for Impairment	132,267	37,286	464,339	286,208	226,172	203,101	—	1,349,373

Edgar Filing: CAPITAL CITY BANK GROUP INC - Form 10-Q

Total	\$133,756	\$38,121	\$501,863	\$308,295	\$228,968	\$203,372	\$—	\$ 1,414,375
December 31, 2013								
Individually Evaluated for Impairment	\$1,580	\$557	\$49,973	\$20,470	\$3,359	\$355	\$—	\$ 76,294
Collectively Evaluated for Impairment	125,027	30,455	483,898	289,222	224,563	159,145	—	1,312,310
Total	\$126,607	\$31,012	\$533,871	\$309,692	\$227,922	\$159,500	\$—	\$ 1,388,604
September 30, 2013								
Individually Evaluated for Impairment	\$3,546	\$773	\$57,820	\$20,894	\$3,977	\$416	\$—	\$ 87,426
Collectively Evaluated for Impairment	119,707	30,681	512,916	290,137	226,235	150,740	—	1,330,416
Total	\$123,253	\$31,454	\$570,736	\$311,031	\$230,212	\$151,156	\$—	\$ 1,417,842

Impaired Loans. Loans are deemed to be impaired when, based on current information and events, it is probable that the Company will not be able to collect all amounts due (principal and interest payments), according to the contractual terms of the loan agreement. Loans, for which the terms have been modified, and for which the borrower is experiencing financial difficulties, are considered troubled debt restructurings and classified as impaired.

The following table presents loans individually evaluated for impairment by class of loans.

<i>(Dollars in Thousands)</i>	Unpaid Principal Balance	Recorded Investment With No Allowance	Recorded Investment With Allowance	Related Allowance
September 30, 2014				
Commercial, Financial and Agricultural	\$ 1,489	\$ 195	\$ 1,294	\$ 576
Real Estate – Construction	835	—	835	94
Real Estate – Commercial Mortgage	37,524	11,062	26,462	3,359
Real Estate – Residential	22,087	5,265	16,822	2,526
Real Estate – Home Equity	2,796	792	2,004	471
Consumer	271	20	251	12
Total	\$ 65,002	\$ 17,334	\$ 47,668	\$ 7,038
December 31, 2013				
Commercial, Financial and Agricultural	\$ 1,580	\$ 443	\$ 1,137	\$ 75
Real Estate – Construction	557	—	557	66
Real Estate – Commercial Mortgage	49,973	19,860	30,113	4,336
Real Estate – Residential	20,470	4,330	16,140	2,047
Real Estate – Home Equity	3,359	646	2,713	682
Consumer	355	90	265	23
Total	\$ 76,294	\$ 25,369	\$ 50,925	\$ 7,229

The following table summarizes the average recorded investment and interest income recognized by class of impaired loans.

<i>(Dollars in Thousands)</i>	Three Months Ended September 30,				Nine Months Ended September 30,			
	2014		2013		2014		2013	
	Average Recorded Investment	Total Interest Income	Average Recorded Investment	Total Interest Income	Average Recorded Investment	Total Interest Income	Average Recorded Investment	Total Interest Income
Commercial, Financial and Agricultural	\$1,433	15	\$2,750	34	\$1,482	50	\$2,633	110
Real Estate - Construction	828	1	935	2	738	4	1,317	5
Real Estate - Commercial Mortgage	39,020	381	59,657	510	42,671	1,298	60,785	1,575
Real Estate - Residential	22,180	284	20,992	217	21,610	800	21,353	637
Real Estate - Home Equity	2,680	18	4,050	19	2,906	52	4,056	54

Edgar Filing: CAPITAL CITY BANK GROUP INC - Form 10-Q

Consumer	293	2	472	3	314	7	529	7
Total	\$66,434	701	\$88,856	785	\$69,721	2,211	\$90,673	2,388

Credit Risk Management. The Company has adopted comprehensive lending policies, underwriting standards and loan review procedures designed to maximize loan income within an acceptable level of risk. Management and the Board of Directors review and approve these policies and procedures on a regular basis (at least annually).

Reporting systems have been implemented to monitor loan originations, loan quality, concentrations of credit, loan delinquencies and nonperforming loans and potential problem loans. Management and the Credit Risk Oversight Committee periodically review our lines of business to monitor asset quality trends and the appropriateness of credit policies. In addition, total borrower exposure limits are established and concentration risk is monitored. As part of this process, the overall composition of the portfolio is reviewed to gauge diversification of risk, client concentrations, industry group, loan type, geographic area, or other relevant classifications of loans. Specific segments of the loan portfolio are monitored and reported to the Board on a quarterly basis and have strategic plans in place to supplement Board approved credit policies governing exposure limits and underwriting standards. Detailed below are the types of loans within the Company's loan portfolio and risk characteristics unique to each.

Commercial, Financial, and Agricultural – Loans in this category are primarily made based on identified cash flows of the borrower with consideration given to underlying collateral and personal or other guarantees. Lending policy establishes debt service coverage ratio limits that require a borrower’s cash flow to be sufficient to cover principal and interest payments on all new and existing debt. The majority of these loans are secured by the assets being financed or other business assets such as accounts receivable, inventory, or equipment. Collateral values are determined based upon third party appraisals and evaluations. Loan to value ratios at origination are governed by established policy guidelines.

Real Estate Construction – Loans in this category consist of short-term construction loans, revolving and non-revolving credit lines and construction/permanent loans made to individuals and investors to finance the acquisition, development, construction or rehabilitation of real property. These loans are primarily made based on identified cash flows of the borrower or project and generally secured by the property being financed, including 1-4 family residential properties and commercial properties that are either owner-occupied or investment in nature. These properties may include either vacant or improved property. Construction loans are generally based upon estimates of costs and value associated with the completed project. Collateral values are determined based upon third party appraisals and evaluations. Loan to value ratios at origination are governed by established policy guidelines. The disbursement of funds for construction loans is made in relation to the progress of the project and as such these loans are closely monitored by on-site inspections.

Real Estate Commercial Mortgage – Loans in this category consists of commercial mortgage loans secured by property that is either owner-occupied or investment in nature. These loans are primarily made based on identified cash flows of the borrower or project with consideration given to underlying real estate collateral and personal guarantees. Lending policy establishes debt service coverage ratios and loan to value ratios specific to the property type. Collateral values are determined based upon third party appraisals and evaluations.

Real Estate Residential – Residential mortgage loans held in the Company’s loan portfolio are made to borrowers that demonstrate the ability to make scheduled payments with full consideration to underwriting factors such as current income, employment status, current assets, and other financial resources, credit history, and the value of the collateral. Collateral consists of mortgage liens on 1-4 family residential properties. Collateral values are determined based upon third party appraisals and evaluations. The Company does not originate sub-prime loans.

Real Estate Home Equity – Home equity loans and lines are made to qualified individuals and are generally secured by senior or junior mortgage liens on owner-occupied 1-4 family homes or vacation homes. Borrower qualifications include favorable credit history combined with supportive income and debt ratio requirements and combined loan to value ratios within established policy guidelines. Collateral values are determined based upon third party appraisals and evaluations.

Consumer Loans – This loan portfolio includes personal installment loans, direct and indirect automobile financing, and overdraft lines of credit. The majority of the consumer loan portfolio consists of indirect and direct automobile loans. Lending policy establishes maximum debt to income ratios, minimum credit scores, and includes guidelines for

verification of applicants' income and receipt of credit reports.

Credit Quality Indicators. As part of the ongoing monitoring of the Company's loan portfolio quality, management categorizes loans into risk categories based on relevant information about the ability of borrowers to service their debt such as: current financial information, historical payment performance, credit documentation, and current economic/market trends, among other factors. Risk ratings are assigned to each loan and revised as needed through established monitoring procedures for individual loan relationships over a predetermined amount and review of smaller balance homogenous loan pools. The Company uses the definitions noted below for categorizing and managing its criticized loans. Loans categorized as "Pass" do not meet the criteria set forth for the Special Mention, Substandard, or Doubtful categories and are not considered criticized.

Special Mention – Loans in this category are presently protected from loss, but weaknesses are apparent which, if not corrected, could cause future problems. Loans in this category may not meet required underwriting criteria and have no mitigating factors. More than the ordinary amount of attention is warranted for these loans.

Substandard – Loans in this category exhibit well-defined weaknesses that would typically bring normal repayment into jeopardy. These loans are no longer adequately protected due to well-defined weaknesses that affect the repayment capacity of the borrower. The possibility of loss is much more evident and above average supervision is required for these loans.

Doubtful – Loans in this category have all the weaknesses inherent in a loan categorized as Substandard, with the characteristic that the weaknesses make collection or liquidation in full, on the basis of currently existing facts, conditions, and values, highly questionable and improbable.

The following table presents the risk category of loans by segment.

(Dollars in Thousands)	Commercial, Financial, Agriculture	Real Estate	Consumer	Total Criticized Loans
September 30, 2014				
Special Mention	\$ 4,225	\$43,372	\$ 179	\$47,776
Substandard	3,994	84,526	910	89,430
Doubtful	420	—	—	420
Total Criticized Loans	\$ 8,639	\$127,898	\$ 1,089	\$ 137,626
December 31, 2013				
Special Mention	\$ 3,656	\$45,870	\$ 115	\$49,641
Substandard	4,243	108,990	1,496	114,729
Doubtful	—	900	—	900
Total Criticized Loans	\$ 7,899	\$155,760	\$ 1,611	\$ 165,270

Troubled Debt Restructurings (“TDRs”). TDRs are loans in which the borrower is experiencing financial difficulty and the Company has granted an economic concession to the borrower that it would not otherwise consider. In these instances, as part of a work-out alternative, the Company will make concessions including the extension of the loan term, a principal moratorium, a reduction in the interest rate, or a combination thereof. The impact of the TDR modifications and defaults are factored into the allowance for loan losses on a loan-by-loan basis as all TDRs are, by definition, impaired loans. Thus, specific reserves are established based upon the results of either a discounted cash flow analysis or the underlying collateral value, if the loan is deemed to be collateral dependent. In the limited circumstances that a loan is removed from TDR classification it is the Company’s policy to also remove it from the impaired loan category, but to continue to individually evaluate loan impairment based on the contractual terms specified by the loan agreement.

The following table presents loans classified as TDRs.

(Dollars in Thousands)	September 30, 2014		December 31, 2013	
	Accruing	Nonaccruing	Accruing	Nonaccruing
Commercial, Financial and Agricultural	\$783	\$ —	\$1,511	\$ —
Real Estate – Construction	—	—	156	—
Real Estate – Commercial Mortgage	24,916	4,645	24,735	10,308
Real Estate – Residential	15,756	1,556	16,441	458
Real Estate – Home Equity	1,856	181	1,576	241
Consumer	267	—	345	—
Total TDRs	\$43,578	\$ 6,382	\$44,764	\$ 11,007

Loans classified as TDRs during the periods indicated are presented in the table below. The modifications made during the reporting period involved either an extension of the loan term, an interest rate adjustment, or a principal moratorium, and the financial impact of these modifications was not material.

(Dollars in Thousands)	Three Months Ended September 30, 2014			Nine Months Ended September 30, 2014		
	Number of Contracts	Pre-Modified Recorded Investment	Post-Modified Recorded Investment	Number of Contracts	Pre-Modified Recorded Investment	Post-Modified Recorded Investment
		\$	\$		\$	\$
Commercial, Financial and Agricultural	—	\$ —	\$ —	1	\$ 51	\$ 54
Real Estate - Construction	—	—	—	—	—	—
Real Estate - Commercial Mortgage	1	303	1,125	3	947	1,769
Real Estate - Residential	2	201	182	8	1,308	1,390
Real Estate - Home Equity	5	453	438	8	701	686
Consumer	—	—	—	1	34	33
Total TDRs	8	\$ 957	\$ 1,745	21	\$ 3,041	\$ 3,932

(Dollars in Thousands)	Three Months Ended September 30, 2013			Nine Months Ended September 30, 2013		
	Number of Contracts	Pre-Modified Recorded Investment	Post-Modified Recorded Investment	Number of Contracts	Pre-Modified Recorded Investment	Post-Modified Recorded Investment
		\$	\$		\$	\$
Commercial, Financial and Agricultural	—	\$ —	\$ —	4	\$ 294	\$ 337
Real Estate - Construction	—	—	—	—	—	—
Real Estate - Commercial Mortgage	3	4,264	4,250	12	9,385	9,403
Real Estate - Residential	6	581	642	16	1,757	1,856
Real Estate - Home Equity	2	85	85	8	429	427
Consumer	—	—	—	6	112	93
Total TDRs	11	\$ 4,930	\$ 4,977	46	\$ 11,977	\$ 12,116

Loans modified as TDRs within the previous 12 months that have subsequently defaulted during the periods indicated are presented in the table below.

(Dollars in Thousands)	Three Months Ended September 30, 2014		Nine Months Ended September 30, 2014	
	Number of Contracts	Post-Modified Recorded Investment ⁽¹⁾	Number of Contracts	Post-Modified Recorded Investment ⁽¹⁾
Commercial, Financial and Agricultural	—	\$ —	—	\$ —
Real Estate - Construction	—	—	—	—
Real Estate - Commercial Mortgage	—	—	—	—
Real Estate - Residential	3	334	4	451
Real Estate - Home Equity	—	—	1	153
Consumer	—	—	—	—
Total TDRs	3	\$ 334	5	\$ 604

(Dollars in Thousands)	Three Months Ended September 30, 2013		Nine Months Ended September 30, 2013	
	Number of Contracts	Post-Modified Recorded Investment ⁽¹⁾	Number of Contracts	Post-Modified Recorded Investment ⁽¹⁾
Commercial, Financial and Agricultural	—	\$ —	1	\$ 83
Real Estate - Construction	—	—	—	366
Real Estate - Commercial Mortgage	1	304	2	728
Real Estate - Residential	5	445	7	50
Real Estate - Home Equity	1	50	1	—
Consumer	—	—	—	—
Total TDRs	7	\$ 799	11	\$ 1,227

⁽¹⁾Recorded investment reflects charge-offs and additional funds advanced at time of restructure, if applicable.

The following table provides information on how TDRs were modified during the periods indicated.

(Dollars in Thousands)	Three Months Ended September 30, 2014		Nine Months Ended September 30, 2014	
	Number of Contracts	Recorded Investment ⁽¹⁾	Number of Contracts	Recorded Investment ⁽¹⁾
Extended amortization	2	\$ 158	8	\$ 1,736
Interest rate adjustment	—	—	1	156
	2	231	5	488

Extended amortization and interest rate adjustment

Other	4	1,356	7	1,552
Total TDRs	8	\$ 1,745	21	\$ 3,932

(Dollars in Thousands)	Three Months Ended September 30, 2013		Nine Months Ended September 30, 2013	
	Number of Contracts	Recorded Investment ⁽¹⁾	Number of Contracts	Recorded Investment ⁽¹⁾
Extended amortization	4	\$ 2,633	13	\$ 3,924
Interest rate adjustment	1	97	8	883
Extended amortization and interest rate adjustment	4	473	16	5,263
Principal Moratorium	1	1,700	1	1,700
Other	1	74	8	346
Total TDRs	11	\$ 4,977	46	\$ 12,116

⁽¹⁾ Recorded investment reflects charge-offs and additional funds advanced at time of restructure, if applicable.

NOTE 4 - INTANGIBLE ASSETS

The Company had net intangible assets of \$84.8 million at September 30, 2014 and December 31, 2013, respectively. Intangible assets were as follows:

(Dollars in Thousands)	September 30, 2014		December 31, 2013	
	Gross Amount	Accumulated Amortization	Gross Amount	Accumulated Amortization
Core Deposit Intangibles	\$47,176	\$ 47,176	\$47,176	\$ 47,176
Goodwill	84,811	—	84,811	—
Customer Relationship Intangible	1,867	1,867	1,867	1,835
Total Intangible Assets	\$133,854	\$ 49,043	\$133,854	\$ 49,011

Goodwill: As of September 30, 2014 and December 31, 2013, the Company had goodwill, net of accumulated amortization, of \$84.8 million. Goodwill is tested for impairment on an annual basis, or more often if impairment indicators exist. A goodwill impairment test consists of two steps. Step One compares the estimated fair value of the reporting unit to its carrying amount. If the carrying amount exceeds the estimated fair value, Step Two is performed by comparing the fair value of the reporting unit's implied goodwill to the carrying value of goodwill. If the carrying value of the reporting unit's goodwill exceeds the estimated fair value, an impairment charge is recorded equal to the excess.

As of September 30, 2014, the Company's net book value, including goodwill, exceeded its market capitalization, and as such, the Company evaluated goodwill impairment. The Step One test indicated that the carrying amount (including goodwill) of the Company's reporting unit was less than its estimated fair value; therefore, no impairment was recorded. The Company will continue to evaluate goodwill for impairment as defined by ASC Topic 350.

NOTE 5 – OTHER REAL ESTATE OWNED

The following table presents other real estate owned activity for the periods indicated.

(Dollars in Thousands)	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
Beginning Balance	\$ 42,579	\$ 55,087	\$ 48,071	\$ 53,426
Additions	2,854	3,697	12,121	21,030
Valuation Write-downs	(664)	(604)	(2,216)	(2,808)
Sales	(2,693)	(5,162)	(15,900)	(18,531)

Edgar Filing: CAPITAL CITY BANK GROUP INC - Form 10-Q

Other	(350	)	—	(350	)	(99)
Ending Balance	\$ 41,726		\$ 53,018	\$ 41,726		\$ 53,018	

Net expenses applicable to other real estate owned include the following:

(Dollars in Thousands)	Three Months Ended September 30,		Nine Months Ended September 30,					
	2014	2013	2014	2013				
Gains from the Sale of Properties	\$ (107	)	\$ (280	)	\$ (441	)	\$ (458)
Losses from the Sale of Properties	483		402		1,648		1,691	
Rental Income from Properties	(81	)	(39	)	(356	)	(167)
Property Carrying Costs	824		1,181		2,391		3,107	
Valuation Adjustments	664		604		2,216		2,808	
Total	\$ 1,783		\$ 1,868		\$ 5,458		\$ 6,981	

20

NOTE 6 - DEPOSITS

The composition of the Company's interest bearing deposits were as follows:

(Dollars in Thousands)	September 30, 2014	December 31, 2013
NOW Accounts	\$ 665,493	\$ 794,746
Money Market Accounts	270,131	268,449
Savings Deposits	231,301	211,668
Other Time Deposits	199,037	219,922
Total Interest Bearing Deposits	\$ 1,365,962	\$ 1,494,785

NOTE 7 - EMPLOYEE BENEFIT PLANS

The Company has a defined benefit pension plan covering substantially all full-time and eligible part-time associates and a Supplemental Executive Retirement Plan ("SERP") covering its executive officers.

The components of the net periodic benefit costs for the Company's qualified benefit pension plan were as follows:

(Dollars in Thousands)	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
Service Cost	\$ 1,500	\$ 1,750	\$ 4,500	\$ 5,250
Interest Cost	1,400	1,392	4,200	4,175
Expected Return on Plan Assets	(1,875)	(1,843)	(5,625)	(5,529)
Prior Service Cost Amortization	75	79	225	237
Net Loss Amortization	325	1,079	975	3,237
Net Periodic Cost	\$ 1,425	\$ 2,457	\$ 4,275	\$ 7,370
Discount Rate	5.00	% 4.25	% 5.00	% 4.25
Long-Term Rate of Return on Assets	7.50	% 8.00	% 7.50	% 8.00

The components of the net periodic benefit costs for the Company's SERP were as follows:

(Dollars in Thousands)	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
Interest Cost	\$ 28	\$ 35	\$ 84	\$ 105

Edgar Filing: CAPITAL CITY BANK GROUP INC - Form 10-Q

Prior Service Cost Amortization	40		47		120		141	
Net Gain Amortization	(183	)	(59	)	(549	)	(177)
Net Periodic (Benefit) Cost	\$ (115	)	\$ 23		\$ (349	)	\$ 69	
Discount Rate	5.00	%	4.25	%	5.00	%	4.25	%

NOTE 8 - COMMITMENTS AND CONTINGENCIES

Lending Commitments. The Company is a party to financial instruments with off-balance sheet risks in the normal course of business to meet the financing needs of its clients. These financial instruments consist of commitments to extend credit and standby letters of credit.

The Company's maximum exposure to credit loss under standby letters of credit and commitments to extend credit is represented by the contractual amount of those instruments. The Company uses the same credit policies in establishing commitments and issuing letters of credit as it does for on-balance sheet instruments. The amounts associated with the Company's off-balance sheet obligations were as follows:

(Dollars in Thousands)	September 30, 2014			December 31, 2013		
	Fixed	Variable	Total	Fixed	Variable	Total
Commitments to Extend Credit ⁽¹⁾	\$30,106	\$289,703	\$319,809	\$36,927	\$234,342	\$271,269
Standby Letters of Credit	8,729	—	8,729	10,979	—	10,979
Total	\$38,835	\$289,703	\$328,538	\$47,906	\$234,342	\$282,248

⁽¹⁾ *Commitments include unfunded loans, revolving lines of credit, and other unused commitments.*

Commitments to extend credit are agreements to lend to a client so long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements.

Standby letters of credit are conditional commitments issued by the Company to guarantee the performance of a client to a third party. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities. In general, management does not anticipate any material losses as a result of participating in these types of transactions. However, any potential losses arising from such transactions are reserved for in the same manner as management reserves for its other credit facilities.

For both on- and off-balance sheet financial instruments, the Company requires collateral to support such instruments when it is deemed necessary. The Company evaluates each client's creditworthiness on a case-by-case basis. The amount of collateral obtained upon extension of credit is based on management's credit evaluation of the counterparty. Collateral held varies, but may include deposits held in financial institutions; U.S. Treasury securities; other marketable securities; real estate; accounts receivable; property, plant and equipment; and inventory.

Contingencies. The Company is a party to lawsuits and claims arising out of the normal course of business. In management's opinion, there are no known pending claims or litigation, the outcome of which would, individually or in the aggregate, have a material effect on the consolidated results of operations, financial position, or cash flows of the Company.

Indemnification Obligation. The Company is a member of the Visa U.S.A. network. Visa U.S.A believes that its member banks are required to indemnify it for potential future settlement of certain litigation (the "Covered Litigation") that relates to several antitrust lawsuits challenging the practices of Visa and MasterCard International. In 2008, the Company, as a member of the Visa U.S.A. network, obtained Class B shares of Visa, Inc. upon its initial public offering. Since its initial public offering, Visa, Inc. has funded a litigation reserve for the Covered Litigation resulting in a reduction in the Class B shares held by the Company. During the first quarter of 2011, the Company sold its remaining Class B shares resulting in a \$3.2 million pre-tax gain. Associated with this sale, the Company entered into a swap contract with the purchaser of the shares that requires a payment to the counterparty in the event that Visa, Inc. makes subsequent revisions to the conversion ratio for its Class B shares. Fixed quarterly charges under the swap contract are reflected in earnings until the litigation reserve is fully liquidated and at which time the aforementioned swap contract will be terminated. In December 2013, a settlement agreement was approved by the court in resolution of the aforementioned Covered Litigation matter. Visa's share of the settlement is to be paid from the litigation reserve account which was further funded during the third quarter of 2014. Accordingly, a liability in the amount of \$161,000 was accrued as payment to the counterparty for the change in the Class B share conversion ratio.

NOTE 9 – FAIR VALUE MEASUREMENTS

The fair value of an asset or liability is the price that would be received to sell that asset or paid to transfer that liability in an orderly transaction occurring in the principal market (or most advantageous market in the absence of a principal market) for such asset or liability. In estimating fair value, the Company utilizes valuation techniques that are consistent with the market approach, the income approach and/or the cost approach. Such valuation techniques are consistently applied. Inputs to valuation techniques include the assumptions that market participants would use in pricing an asset or liability. ASC Topic 820 establishes a fair value hierarchy for valuation inputs that gives the highest priority to quoted prices in active markets for identical assets or liabilities and the lowest priority to unobservable inputs. The fair value hierarchy is as follows:

§ *Level 1 Inputs* - Unadjusted quoted prices in active markets for identical assets or liabilities that the reporting entity has the ability to access at the measurement date.

§ *Level 2 Inputs* - Inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly or indirectly. These might include quoted prices for similar assets or liabilities in active markets, § quoted prices for identical or similar assets or liabilities in markets that are not active, inputs other than quoted prices that are observable for the asset or liability (such as interest rates, volatilities, prepayment speeds, credit risks, etc.) or inputs that are derived principally from, or corroborated, by market data by correlation or other means.

§ *Level 3 Inputs* - Unobservable inputs for determining the fair values of assets or liabilities that reflect an entity's own § assumptions about the assumptions that market participants would use in pricing the assets or liabilities.

Assets and Liabilities Measured at Fair Value on a Recurring Basis

Securities Available for Sale. U.S. Treasury securities and certain U.S. Government Agency securities are reported at fair value utilizing Level 1 inputs. Other securities classified as available for sale are reported at fair value utilizing Level 2 inputs. For these securities, the Company obtains fair value measurements from an independent pricing service. The fair value measurements consider observable data that may include dealer quotes, market spreads, cash flows, the U.S. Treasury yield curve, live trading levels, trade execution data, credit information and the bond's terms and conditions, among other things.

In general, the Company does not purchase securities that have a complicated structure. The Company's entire portfolio consists of traditional investments, nearly all of which are U.S. Treasury obligations, federal agency bullet or mortgage pass-through securities, or general obligation or revenue based municipal bonds. Pricing for such instruments is easily obtained. From time to time, the Company will validate, on a sample basis, prices supplied by the independent pricing service by comparison to prices obtained from third-party sources or derived using internal models.

Fair Value Swap. The Company entered into a stand-alone derivative contract with the purchaser of its Visa Class B shares. The valuation represents the amount due and payable to the counterparty based upon the revised share conversion rate, if any, during the period.

A summary of fair values for assets and liabilities consisted of the following:

(Dollars in Thousands)	Level 1 Inputs	Level 2 Inputs	Level 3 Inputs	Total Fair Value
September 30, 2014				
ASSETS:				
Securities Available for Sale:				
U.S. Treasury	\$165,057	\$—	\$ —	\$165,057
U.S. Government Agency States and Political Subdivisions	—	94,994	—	94,994
Mortgage-Backed Securities	—	51,140	—	51,140
Equity Securities	—	2,361	—	2,361
	—	8,745	—	8,745
LIABILITIES:				
Fair Value Swap	—	—	161	161
December 31, 2013				
ASSETS:				
Securities Available for Sale:				
U.S. Treasury	\$71,833	\$—	\$ —	\$71,833

U.S. Government Agency	—	75,146	—	75,146
State and Political Subdivisions	—	91,753	—	91,753
Mortgage-Backed Securities	—	2,795	—	2,795
Equity Securities	—	9,893	—	9,893

Assets Measured at Fair Value on a Non-Recurring Basis

Certain assets are measured at fair value on a non-recurring basis (i.e., the assets are not measured at fair value on an ongoing basis but are subject to fair value adjustments in certain circumstances). An example would be assets exhibiting evidence of impairment. The following is a description of valuation methodologies used for assets measured on a non-recurring basis.

Impaired Loans. Impairment for collateral dependent loans is measured using the fair value of the collateral less selling costs. The fair value of collateral is determined by an independent valuation or professional appraisal in conformance with banking regulations. Collateral values are estimated using Level 3 inputs due to the volatility in the real estate market, and the judgment and estimation involved in the real estate appraisal process. Impaired loans are reviewed and evaluated on at least a quarterly basis for additional impairment and adjusted accordingly. Valuation techniques are consistent with those techniques applied in prior periods. Impaired collateral dependent loans had a carrying value of \$22.0 million with a valuation allowance of \$3.2 million at September 30, 2014 and \$31.5 million and \$3.1 million, respectively, at December 31, 2013.

Loans Held for Sale. These loans are carried at the lower of cost or fair value and are adjusted to fair value on a non-recurring basis. Fair value is based on observable markets rates for comparable loan products, which is considered a Level 2 fair value measurement.

Other Real Estate Owned. During the first nine months of 2014, certain foreclosed assets, upon initial recognition, were measured and reported at fair value through a charge-off to the allowance for loan losses based on the fair value of the foreclosed asset less estimated cost to sell. The fair value of the foreclosed asset is determined by an independent valuation or professional appraisal in conformance with banking regulations. On an ongoing basis, we obtain updated appraisals on foreclosed assets and realize valuation adjustments as necessary. The fair value of foreclosed assets is estimated using Level 3 inputs due to the judgment and estimation involved in the real estate valuation process.

Assets and Liabilities Disclosed at Fair Value

The Company is required to disclose the estimated fair value of financial instruments, both assets and liabilities, for which it is practical to estimate fair value and the following is a description of valuation methodologies used for those assets and liabilities.

Cash and Short-Term Investments. The carrying amount of cash and short-term investments is used to approximate fair value, given the short time frame to maturity and as such assets do not present unanticipated credit concerns.

Securities Held to Maturity. Securities held to maturity are valued in accordance with the methodology previously noted in the caption “Assets and Liabilities Measured at Fair Value on a Recurring Basis – Securities Available for Sale”.

Loans. The loan portfolio is segregated into categories and the fair value of each loan category is calculated using present value techniques based upon projected cash flows and estimated discount rates that reflect the credit, interest rate, and liquidity risks inherent in each loan category. The calculated present values are then reduced by an allocation of the allowance for loan losses against each respective loan category.

Deposits. The fair value of Noninterest Bearing Deposits, NOW Accounts, Money Market Accounts and Savings Accounts are the amounts payable on demand at the reporting date. The fair value of fixed maturity certificates of deposit is estimated using present value techniques and rates currently offered for deposits of similar remaining maturities.

Subordinated Notes Payable. The fair value of each note is calculated using present value techniques, based upon projected cash flows and estimated discount rates as well as rates being offered for similar obligations.

Short-Term and Long-Term Borrowings. The fair value of each note is calculated using present value techniques, based upon projected cash flows and estimated discount rates as well as rates being offered for similar debt.

A summary of estimated fair values of significant financial instruments consisted of the following:

(Dollars in Thousands)	September 30, 2014			
	Carrying Value	Level 1 Inputs	Level 2 Inputs	Level 3 Inputs
ASSETS:				
Cash	\$50,049	\$50,049	\$—	\$—
Short-Term Investments	253,974	253,974	—	—
Investment Securities, Available for Sale	322,297	165,057	157,240	—
Investment Securities, Held to Maturity	173,188	76,280	96,437	—
Loans Held for Sale	8,700	—	8,700	—
Loans, Net of Allowance for Loan Losses	1,395,282	—	—	1,326,357
LIABILITIES:				
Deposits	\$2,033,578	\$—	\$2,033,271	\$—
Short-Term Borrowings	42,586	—	41,998	—
Subordinated Notes Payable	62,887	—	62,890	—
Long-Term Borrowings	32,305	—	33,495	—

(Dollars in Thousands)	December 31, 2013			
	Carrying Value	Level 1 Inputs	Level 2 Inputs	Level 3 Inputs
ASSETS:				
Cash	\$55,209	\$55,209	\$—	\$—
Short-Term Investments	474,719	474,719	—	—
Investment Securities, Available for Sale	251,420	71,833	179,587	—
Investment Securities, Held to Maturity	148,211	43,579	103,382	—
Loans Held for Sale	11,065	—	11,065	—
Loans, Net of Allowance for Loan Losses	1,365,509	—	—	1,265,827
LIABILITIES:				
Deposits	\$2,136,248	\$—	\$2,136,737	\$—
Short-Term Borrowings	51,321	—	50,754	—
Subordinated Notes Payable	62,887	—	62,886	—
Long-Term Borrowings	38,043	—	39,450	—

All non-financial instruments are excluded from the above table. The disclosures also do not include certain intangible assets such as client relationships, deposit base intangibles and goodwill. Accordingly, the aggregate fair value amounts presented do not represent the underlying value of the Company.

NOTE 10 – OTHER COMPREHENSIVE INCOME (LOSS)

The amounts allocated to other comprehensive income (loss) are presented in the table below. Reclassification adjustments related to securities held for sale are included in net gain (loss) on securities transactions in the accompanying consolidated statements of comprehensive income. For the periods presented, reclassifications adjustments related to securities held for sale was not material.

<i>(Dollars in Thousands)</i>	Before Tax Amount	Tax (Expense) Benefit	Net of Tax Amount
Three Months Ended September 30, 2014			
Investment Securities:			
Change in net unrealized gain/loss on securities available for sale	\$ (173)	\$ 61	\$ (112)
Amortization of losses on securities transferred from available for sale to held to maturity	17	(7)	10
Total Other Comprehensive Loss	\$ (156)	\$ 54	\$ (102)
Nine Months Ended September 30, 2014			
Investment Securities:			
Change in net unrealized gain/ loss on securities available for sale	\$ 78	\$ (36)	\$ 42
Amortization of losses on securities transferred from available for sale to held to maturity	53	(20)	33
Total Other Comprehensive Income	\$ 131	\$ (56)	\$ 75
<i>(Dollars in Thousands)</i>	Before Tax Amount	Tax (Expense) Benefit	Net of Tax Amount
Three Months Ended September 30, 2013			
Investment Securities:			
Change in net unrealized gain/loss on securities available for sale	\$ 459	\$ (177)	\$ 282
Unrealized losses on securities transferred from available for sale to held to maturity	(523)	202	(321)
Amortization of losses on securities transferred from available for sale to held to maturity	7	(3)	4
Reclassification adjustment for impairment loss realized in net income	210	(158)	52
Total Other Comprehensive Income	\$ 153	\$ 136	\$ 17
Nine Months Ended September 30, 2013			
Investment Securities:			
Change in net unrealized gain/loss on securities available for sale	\$(1,149)	\$ 445	\$ (704)
Unrealized losses on securities transferred from available for sale to held to maturity	(523)	202	(321)
Amortization of losses on securities transferred from available for sale to held to maturity	7	(3)	4
Reclassification adjustment for impairment loss realized in net income	410	(158)	252
Total Other Comprehensive Loss	\$ (1,255)	\$ 486	\$ (769)

Accumulated other comprehensive loss was comprised of the following components:

<i>(Dollars in Thousands)</i>	Securities Available for Sale	Retirement Plans	Accumulated Other Comprehensive Loss	
Balance as of January 1, 2014	\$ (132)	\$ (8,408)	\$ (8,540)	
Other comprehensive income during the period	75	—	75	
Balance as of September 30, 2014	\$ (57)	\$ (8,408)	\$ (8,465)	
Balance as of January 1, 2013	\$ 573	\$ (30,132)	\$ (29,559)	
Other comprehensive loss during the period	(769)	—	(769)	
Balance as of September 30, 2013	\$ (196)	\$ (30,132)	\$ (30,328)	

NOTE 11 – ACCOUNTING STANDARDS UPDATES

ASU 2014-01 “Investments – Equity Method and Joint Ventures (Topic 323) – Accounting for Investments in Qualified Affordable Housing Projects.” ASU 2014-01 provides guidance related to the accounting for investments in qualified affordable housing projects. The guidance allows the holder of low income housing tax credit investments to apply a proportional amortization method that would recognize the cost of the investment as a part of income tax expense, provided that the investment meets certain criteria. The guidance is silent regarding statement of financial position classification, although it would not be appropriate to classify the investment as a deferred tax asset. The decision to apply the proportional amortization method is an accounting policy election. Entities may also elect to continue to account for these investments using the equity method. The guidance will be applied retrospectively and is effective for fiscal years, and interim periods within those years, beginning after December 15, 2014. Early adoption is permitted. The Company does not believe this pronouncement will have a significant impact on its financial statements.

ASU 2014-04 “Receivables – Troubled Debt Restructurings by Creditors (Topic 310-40) – Reclassification of Residential Real Estate Collateralized Consumer Loans Upon Foreclosure.” ASU 2014-04 provides guidance regarding the reclassification of residential real estate collateralized consumer mortgage loans upon foreclosures. The guidance requires reclassification of a consumer mortgage loan to other real estate owned upon obtaining legal title to the residential property, which could occur either through foreclosure or through a deed in lieu of foreclosure or similar legal agreement. The existence of a borrower redemption right will not prevent the lender from reclassifying a loan to real estate once the lender obtains legal title to the property. In addition, entities are required to disclose the amount of foreclosed residential real estate properties and the recorded investment in residential real estate mortgage loans in the process of foreclosure on both an interim and annual basis. The guidance may be applied prospectively or on a modified retrospective basis in fiscal years, and interim periods within those fiscal years, beginning after December 15, 2014. Early adoption is permitted. The Company does not believe this pronouncement will have a significant impact on its financial statements.

ASU 2014-09, “Revenue from Contracts with Customers (Topic 606).” ASU 2014-09 implements a common revenue standard that clarifies the principles for recognizing revenue. The core principle of ASU 2014-09 is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. To achieve that core principle, an entity should apply the following steps: (i) identify the contract(s) with a customer, (ii) identify the performance obligations in the contract, (iii) determine the transaction price, (iv) allocate the transaction price to the performance obligations in the contract and (v) recognize revenue when (or as) the entity satisfies a performance obligation. ASU 2014-09 is effective for the Company on January 1, 2017. The Company is still evaluating the potential impact on its financial statements.

ASU 2014-14, “Receivables-Troubled Debt Restructurings by Creditors (Topic 310-40) – Classification of Certain Government-Guaranteed Mortgage Loans Upon Foreclosure.” ASU 2014-14 requires that a mortgage loan be derecognized and that a separate other receivable be recognized upon foreclosure if the following conditions are met: (i) the loan has a government guarantee that is not separable from the loan before foreclosure, (ii) at the time of

foreclosure, the creditor has the intent to convey the real estate property to the guarantor and make a claim on the guarantee, and the creditor has the ability to recover that claim, (iii) at the time of foreclosure, any amount of the claim that is determined on the basis of the fair value of the real estate is fixed. The guidance may be applied prospectively or on a modified retrospective basis in fiscal years, and interim periods within those fiscal years, beginning after December 15, 2014. The Company does not believe that this pronouncement will have a significant impact on its financial statements.

Item 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Management's discussion and analysis ("MD&A") provides supplemental information, which sets forth the major factors that have affected our financial condition and results of operations and should be read in conjunction with the Consolidated Financial Statements and related notes. The following information should provide a better understanding of the major factors and trends that affect our earnings performance and financial condition, and how our performance during 2014 compares with prior periods. Throughout this section, Capital City Bank Group, Inc., and subsidiaries, collectively, are referred to as "CCBG," "Company," "we," "us," or "our."

The following discussion should be read in conjunction with the condensed consolidated financial statements and notes thereto included in this Quarterly Report on Form 10-Q.

CAUTION CONCERNING FORWARD-LOOKING STATEMENTS

This Quarterly Report on Form 10-Q, including this MD&A section, contains "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995. These forward-looking statements include, among others, statements about our beliefs, plans, objectives, goals, expectations, estimates and intentions that are subject to significant risks and uncertainties and are subject to change based on various factors, many of which are beyond our control. The words "may," "could," "should," "would," "believe," "anticipate," "estimate," "expect," "intend," "plan," "target," similar expressions are intended to identify forward-looking statements.

All forward-looking statements, by their nature, are subject to risks and uncertainties. Our actual future results may differ materially from those set forth in our forward-looking statements. Please see the Introductory Note and *Item 1A. Risk Factors* of our 2013 Report on Form 10-K, as updated in our subsequent quarterly reports filed on Form 10-Q, and in our other filings made from time to time with the SEC after the date of this report.

However, other factors besides those listed in our Quarterly Report or in our Annual Report also could adversely affect our results, and you should not consider any such list of factors to be a complete set of all potential risks or uncertainties. Any forward-looking statements made by us or on our behalf speak only as of the date they are made. We do not undertake to update any forward-looking statement, except as required by applicable law.

BUSINESS OVERVIEW

We are a financial holding company headquartered in Tallahassee, Florida, and we are the parent of our wholly-owned subsidiary, Capital City Bank (the “Bank” or “CCB”). The Bank offers a broad array of products and services through a total of 63 full-service offices located in Florida, Georgia, and Alabama. The Bank offers commercial and retail banking services, as well as trust and asset management, retail securities brokerage and data processing services.

Our profitability, like most financial institutions, is dependent to a large extent upon net interest income, which is the difference between the interest and fees received on earning assets, such as loans and securities, and the interest paid on interest-bearing liabilities, principally deposits and borrowings. Results of operations are also affected by the provision for loan losses, operating expenses such as salaries and employee benefits, occupancy and other operating expenses including income taxes, and noninterest income such as deposit fees, wealth management fees, mortgage banking fees, bank card fees, and data processing fees.

A detailed discussion regarding the economic conditions in our markets and our long-term strategic objectives is included as part of the MD&A section of our 2013 Form 10-K.

SELECTED QUARTERLY FINANCIAL DATA (UNAUDITED)

(Dollars in Thousands, Except Per Share Data)	2014			2013			2012	
	Third	Second	First	Fourth	Third	Second	First	Fourth
Summary of Operations:								
Interest Income	\$19,766	\$19,348	\$19,236	\$20,076	\$20,250	\$20,698	\$21,128	\$21,128
Interest Expense	868	910	950	1,080	1,050	1,103	1,183	1,200
Net Interest Income	18,898	18,438	18,286	18,996	19,200	19,595	19,945	20,000
Provision for Loan Losses	424	499	359	397	555	1,450	1,070	2,700
Net Interest Income After Provision for Loan Losses	18,474	17,939	17,927	18,599	18,645	18,145	18,875	17,300
Noninterest Income	13,351	13,347	12,785	13,825	14,026	13,731	13,528	13,500
Noninterest Expense	28,607	29,076	28,366	29,647	30,153	30,464	31,140	29,500
Income Before Income Taxes	3,218	2,210	2,346	2,777	2,518	1,412	1,263	2,400
Income Tax Expense (Benefit)	1,103	737	(1,405)	5	927	569	424	564
Net Income	\$2,115	\$1,473	\$3,751	\$2,772	\$1,591	\$843	\$839	\$1,836
Net Interest Income (FTE)	\$19,020	\$18,567	\$18,424	\$19,141	\$19,355	\$19,744	\$20,079	\$20,000
Per Common Share:								
Net Income Basic	\$0.12	\$0.08	\$0.22	\$0.16	\$0.09	\$0.05	\$0.05	\$0.12
Net Income Diluted	0.12	0.08	0.22	0.16	0.09	0.05	0.05	0.12
Dividends Declared	0.02	0.02	0.02	0.00	0.00	0.00	0.00	0.00
Diluted Book Value	16.18	16.08	16.02	15.85	14.44	14.36	14.35	14.35
Market Price:								
High	14.98	14.71	14.59	12.69	13.08	12.64	12.54	11.50
Low	13.26	12.60	11.56	11.33	11.06	10.12	10.95	9.00
Close	13.54	14.53	13.28	11.77	11.78	11.53	12.35	11.50

Edgar Filing: CAPITAL CITY BANK GROUP INC - Form 10-Q

Selected
Average
Balances:

Loans, Net	\$1,421,327	\$1,411,988	\$1,395,506	\$1,414,909	\$1,436,039	\$1,456,904	\$1,496,432	\$1,500,000
Earning Assets	2,209,429	2,260,885	2,268,320	2,206,286	2,201,390	2,206,694	2,240,889	2,190,000
Total Assets	2,530,571	2,578,993	2,598,307	2,553,653	2,558,395	2,564,528	2,598,680	2,550,000
Deposits	2,062,881	2,109,563	2,124,960	2,050,870	2,059,498	2,067,647	2,102,967	2,050,000
Shareowners' Equity	284,130	282,346	279,729	253,999	251,617	250,485	249,557	253,000
Common Equivalent Average Shares:								
Basic	17,440	17,427	17,399	17,341	17,336	17,319	17,302	17,300
Diluted	17,519	17,488	17,439	17,423	17,396	17,355	17,309	17,300

Performance
Ratios:

Return on Average Assets	0.33	%	0.23	%	0.59	%	0.43	%	0.25	%	0.13	%	0.13	%	0.25
Return on Average Equity	2.95		2.09		5.44		4.33		2.51		1.35		1.36		2.95
Net Interest Margin (FTE)	3.42		3.29		3.29		3.45		3.49		3.59		3.64		3.75
Noninterest Income as % of Operating Revenue	41.78		42.31		42.05		43.85		42.82		41.68		40.62		40.00
Efficiency Ratio	88.44		91.15		91.02		90.22		90.42		91.07		92.67		84.00

Asset Quality:

Allowance for Loan Losses	\$19,093	\$20,543	\$22,110	\$23,095	\$25,010	\$27,294	\$27,803	\$29,000							
Allowance for Loan Losses to Loans	1.34	%	1.45	%	1.57	%	1.65	%	1.75	%	1.89	%	1.90	%	1.90
Nonperforming Assets ("NPAs")	65,208	68,249	78,594	85,035	94,700	96,653	103,869	117,000							
NPAs to Total Assets	2.61		2.66		2.98		3.26		3.77		3.77		3.99		4.40
NPAs to Loans + OREO	4.45		4.67		5.42		5.87		6.38		6.44		6.81		7.40
Allowance to Non-Performing Loans	81.31		80.03		63.98		62.48		60.00		65.66		61.17		45.00
Net Charge-Offs to Average Loans	0.52		0.59		0.39		0.65		0.78		0.54		0.66		1.00

Capital Ratios:

Tier 1 Capital Ratio	16.88	%	16.85	%	16.85	%	16.56	%	15.60	%	15.36	%	14.95	%	14.00
----------------------	-------	---	-------	---	-------	---	-------	---	-------	---	-------	---	-------	---	-------

Edgar Filing: CAPITAL CITY BANK GROUP INC - Form 10-Q

Total								
Risk-Based	18.08	18.10	18.22	17.94	16.97	16.73	16.32	15.
Capital Ratio								
Tangible Capital								
Ratio	8.22	7.93	7.66	7.58	6.84	6.64	6.49	6.3
Leverage Ratio	10.97	10.70	10.47	10.46	10.16	10.07	9.81	9.9

29

FINANCIAL OVERVIEW

A summary overview of our financial performance is provided below.

Results of Operations

Net income of \$2.1 million, or \$0.12 per diluted share, for the third quarter of 2014 compared to net income of \$1.5 million, or \$0.08 per diluted share, in the second quarter of 2014, and net income of \$1.6 million, or \$0.09 per diluted share for the third quarter of 2013. For the nine month period ended September 30, 2014, we realized net income of \$7.3 million, or \$0.42 per diluted share, compared to net income of \$3.3 million, or \$0.19 per diluted share, for the comparable period of 2013. Year to date earnings reflect a tax benefit of \$2.2 million, or \$0.13 per share related to an adjustment to our reserve for uncertain tax positions in the first quarter of 2014.

Total credit costs (loan loss provision plus other real estate owned (“OREO”) expenses) were \$2.2 million, \$2.8 million, and \$2.4 million for the quarters ended September 30, 2014, June 30, 2014, and September 30, 2013, respectively. Total credit costs for the nine month period of 2014 were \$6.7 million compared to \$10.0 million for the same period of 2013. Slower problem loan migration, lower loan losses and improved credit metrics have resulted in a lower loan loss provision. Continued progress in disposing of OREO properties and firming of property values has favorably impacted our level of OREO costs.

Tax equivalent net interest income for the third quarter of 2014 was \$19.0 million compared to \$18.6 million for the second quarter of 2014 and \$19.4 million for the third quarter of 2013. For the first nine months of 2014, tax equivalent net interest income totaled \$56.0 million compared to \$59.1 million in 2013. The increase compared to the second quarter of 2014 was driven by one additional calendar day, a positive shift in earning asset mix due to growth in the investment and loan portfolios and a slight reduction in interest expense. Compared to both prior year periods, the decrease reflects lower loan income primarily attributable to declining loan balances and unfavorable asset repricing that was partially offset by a reduction in interest expense and a lower level of foregone interest on loans.

Noninterest income for the third quarter of 2014 totaled \$13.4 million, comparable to the second quarter of 2014, and a decrease of \$0.7 million, or 4.8%, from the third quarter of 2013. Compared to the second quarter of 2014, higher wealth management fees and mortgage banking fees were offset by lower bank card fees, data processing fees, and other income. Compared to the third quarter of 2013, the decrease was driven by lower deposit fees, data processing fees, and wealth management fees. For the first nine months of 2014, noninterest income totaled \$39.5 million, a \$1.8 million, or 4.4%, decrease from the same period of 2013 reflective of lower deposit fees, mortgage banking fees, wealth management fees, and data processing fees, partially offset by higher bank card fees and other income.

§

Noninterest expense for the third quarter of 2014 totaled \$28.6 million, a decrease of \$0.5 million, or 1.6%, from the second quarter of 2014 and \$1.5 million, or 5.1%, from the third quarter of 2013. The decrease from the second quarter of 2014 primarily reflects lower OREO expense and legal fees. Compared to the third quarter of 2013, the decrease was primarily driven by lower compensation expense (primarily pension), insurance fees (primarily FDIC), and professional fees. For the first nine months of 2014, noninterest expense totaled \$86.0 million, a decrease of \$5.7 million, or 6.2%, from the same period of 2013 primarily attributable to lower compensation expense (primarily pension), OREO expense, and insurance fees (primarily FDIC).

Financial Condition

§ Average earning assets were \$2.209 billion for the third quarter of 2014, a decrease of \$51.5 million, or 2.3%, from the second quarter of 2014 and an increase of \$3.1 million, or 0.1%, over the fourth quarter of 2013. The change in earning assets from the second quarter of 2014 reflects a lower level of overnight funds attributable to declining balances in both public fund deposits and repurchase agreements. The increase compared to the fourth quarter of 2013 reflects a higher level of investments and loans, which was funded through a reduction in overnight funds and growth in core deposits.

§ Average gross loans increased by \$9.3 million, or 0.7%, over the second quarter of 2014, which represents the second consecutive quarter-over-quarter increase in average loans. Average loans have increased by \$6.4 million when compared to the fourth quarter of 2013. The improvement in loans when compared to both periods was attributable primarily in the consumer and commercial portfolios, while the commercial real estate portfolio continued to decline.

§ Nonperforming assets totaled \$65.2 million at the end of the third quarter of 2014, a decrease of \$3.0 million from the second quarter of 2014 and \$19.8 million from the fourth quarter of 2013. Nonperforming assets represented 2.61% of total assets at September 30, 2014 compared to 2.66% at June 30, 2014 and 3.26% at December 31, 2013.

§ As of September 30, 2014, we are well-capitalized with a total risk-based capital ratio of 18.08% and a tangible common equity ratio of 8.22% compared to 18.10% and 7.93%, respectively, at June 30, 2014, and 17.94% and 7.58%, respectively, at December 31, 2013.

RESULTS OF OPERATIONS**Net Income**

For the third quarter of 2014, we realized net income of \$2.1 million, or \$0.12 per diluted share, compared to net income of \$1.5 million, or \$0.08 per diluted share for the second quarter of 2014, and \$1.6 million, or \$0.09 per diluted share, for the third quarter of 2013. For the first nine months of 2014, we realized net income of \$7.3 million, or \$0.42 per diluted share, compared to net income of \$3.3 million, or \$0.19 per diluted share for the same period of 2013.

Compared to the second quarter of 2014, performance reflects higher net interest income of \$0.4 million, lower noninterest expense of \$0.5 million, and a lower loan loss provision of \$0.1 million, partially offset by higher income tax expense of \$0.4 million.

Compared to the third quarter of 2013, the increase in earnings was due to lower noninterest expense of \$1.5 million and loan loss provision of \$0.2 million, partially offset by lower net interest income of \$0.3 million, a decline in noninterest income of \$0.7 million, and higher income tax expense of \$0.2 million.

The increase in earnings for the first nine months of 2014 versus the comparable period of 2013 was attributable to lower noninterest expense of \$5.7 million, a lower loan loss provision of \$1.8 million, and lower income taxes of \$1.4 million, partially offset by lower net interest income of \$3.1 million and noninterest income of \$1.8 million.

A condensed earnings summary of each major component of our financial performance is provided below:

(Dollars in Thousands, except per share data)	Three Months Ended			Nine Months Ended	
	Sept 30, 2014	June 30, 2014	Sept 30, 2013	Sept 30, 2014	Sept 30, 2013
Interest Income	\$19,766	\$19,348	\$20,250	\$58,350	\$62,076
Taxable Equivalent Adjustments	122	129	155	389	438
Total Interest Income (FTE)	19,888	19,477	20,405	58,739	62,514
Interest Expense	868	910	1,050	2,728	3,336
Net Interest Income (FTE)	19,020	18,567	19,355	56,011	59,178
Provision for Loan Losses	424	499	555	1,282	3,075
Taxable Equivalent Adjustments	122	129	155	389	438
Net Interest Income After provision for Loan Losses	18,474	17,939	18,645	54,340	55,665

Edgar Filing: CAPITAL CITY BANK GROUP INC - Form 10-Q

Noninterest Income	13,351	13,347	14,026	39,483	41,284
Noninterest Expense	28,607	29,076	30,153	86,049	91,756
Income Before Income Taxes	3,218	2,210	2,518	7,774	5,193
Income Tax Expense	1,103	737	927	435	1,920
Net Income	\$2,115	\$1,473	\$1,591	\$7,339	\$3,273
Basic Net Income Per Share	\$0.12	\$0.08	\$0.09	\$0.42	\$0.19
Diluted Net Income Per Share	\$0.12	\$0.08	\$0.09	\$0.42	\$0.19

Net Interest Income

Net interest income represents our single largest source of earnings and is equal to interest income and fees generated by earning assets less interest expense paid on interest bearing liabilities. This information is provided on a “taxable equivalent” basis to reflect the tax-exempt status of income earned on certain loans and investments, the majority of which are state and local government debt obligations. We provide an analysis of our net interest income including average yields and rates in Table I on page 43.

Tax equivalent net interest income for the third quarter of 2014 was \$19.0 million compared to \$18.6 million for the second quarter of 2014 and \$19.4 million for the third quarter of 2013. For the nine months ended September 30, 2014, tax equivalent net interest income totaled \$56.0 million compared to \$59.1 million for the same period of 2013. The increase in tax equivalent net interest income compared to the second quarter of 2014 reflects one additional calendar day, a positive shift in earning asset mix due to growth in the investment and loan portfolios and a slight reduction in interest expense, partially offset by unfavorable asset repricing. The lower net interest income when compared to the third quarter of 2013 reflects a reduction in loan income primarily attributable to unfavorable asset repricing, partially offset by a reduction in interest expense and a lower level of foregone interest on loans.

We experienced higher net interest income for the quarter but pressure still remains on net interest income primarily as a result of the low rate environment. The low rate environment continues to negatively impact the loan portfolio and, going forward, will have minimal to no impact on deposits. Increased lending competition in all markets has also unfavorably impacted the pricing for loans.

The net interest margin for the third quarter of 2014 at 3.42% represents an increase of 13 basis points from the second quarter of 2014 and represented a decline of 7 basis points from the third quarter of 2013. Growth in our investment and loan portfolios helped to improve our margin from the second to third quarter, while the decrease in the margin from the comparable prior year period was attributable to unfavorable asset repricing, partially offset by a lower average cost of funds.

Historically low interest rates (essentially setting a floor on deposit repricing), foregone interest, unfavorable asset repricing without the flexibility to significantly adjust deposit rates and core deposit growth (which has strengthened our liquidity position, but contributed to an unfavorable shift in our earning asset mix), have all placed pressure on our net interest margin. Our current strategy, which is consistent with our historical strategy, is to not accept greater interest rate risk by reaching further out the curve for yield, particularly given the fact that short term rates are at historical lows. We continue to maintain short duration portfolios on both sides of the balance sheet and believe we are well positioned to respond to changing market conditions. Over time, this strategy has historically produced fairly consistent outcomes and a net interest margin that is significantly above peer comparisons.

Provision for Loan Losses

The provision for loan losses for the third quarter of 2014 was \$0.4 million compared to \$0.5 million for the second quarter of 2014 and \$0.6 million for the third quarter of 2013. For the first nine months of 2014, the loan loss provision totaled \$1.3 million compared to \$3.1 million for the same period of 2013. The lower level of provision reflects continued favorable problem loan migration and improvement in key credit metrics. Net charge-offs for the third quarter of 2014 totaled \$1.9 million, or 0.52% (annualized), of average loans compared to \$2.1 million, or 0.59% (annualized), for the second quarter of 2014 and \$2.8 million, or 0.78% (annualized), for the third quarter of 2013. For the first nine months of 2014, net charge-offs totaled \$5.3 million, or 0.50% (annualized), of average loans compared to \$7.2 million, or 0.66%, for the same period of 2013.

Charge-off activity for the respective periods is set forth below:

	Three Months Ended			Nine Months Ended	
(Dollars in Thousands, except per share data)	Sept 30, 2014	June 30, 2014	Sept 30, 2013	Sept 30, 2013	Sept 30, 2013

Edgar Filing: CAPITAL CITY BANK GROUP INC - Form 10-Q

	2014		2014	
CHARGE-OFFS				
Commercial, Financial and Agricultural	\$86	\$ 86	\$ 138	\$183