

CITY NATIONAL CORP
Form 10-Q
May 08, 2015
[Table of Contents](#)

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended March 31, 2015

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 1-10521

CITY NATIONAL CORPORATION

(Exact name of registrant as specified in its charter)

Edgar Filing: CITY NATIONAL CORP - Form 10-Q

Delaware
(State of Incorporation)

95-2568550
(I.R.S. Employer Identification No.)

City National Plaza

555 South Flower Street, Los Angeles, California, 90071

(Address of principal executive offices)(Zip Code)

(213) 673-7700

(Registrant's telephone number, including area code)

(Former name, former address and former fiscal year, if changed since last report)

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

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

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

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

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

As of April 30, 2015, there were 55,605,256 shares of Common Stock outstanding (including unvested restricted shares).

Table of Contents

TABLE OF CONTENTS

PART I

<u>Item 1.</u>	<u>Financial Statements</u>	3
<u>Item 2.</u>	<u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	50
<u>Item 3.</u>	<u>Quantitative and Qualitative Disclosures about Market Risk</u>	81
<u>Item 4.</u>	<u>Controls and Procedures</u>	86

PART II

<u>Item 1A.</u>	<u>Risk Factors</u>	87
<u>Item 2.</u>	<u>Unregistered Sales of Equity Securities and Use of Proceeds</u>	87
<u>Item 6.</u>	<u>Exhibits</u>	87

Table of Contents**PART I - FINANCIAL INFORMATION****ITEM 1. FINANCIAL STATEMENTS**

CITY NATIONAL CORPORATION
CONSOLIDATED BALANCE SHEETS
(Unaudited)

(in thousands, except share amounts)	March 31, 2015	December 31, 2014
Assets		
Cash and due from banks	\$ 433,670	\$ 336,470
Due from banks - interest-bearing	334,014	119,981
Federal funds sold and securities purchased under resale agreements	200,000	200,000
Securities available-for-sale - cost \$5,201,001 and \$5,894,509 at March 31, 2015 and December 31, 2014, respectively:		
Securities pledged as collateral	21,068	14,654
Held in portfolio	5,189,320	5,868,329
Securities held-to-maturity - fair value \$3,510,553 and \$3,484,647 at March 31, 2015 and December 31, 2014, respectively:		
Securities pledged as collateral	521,963	521,262
Held in portfolio	2,891,843	2,905,769
Trading securities	102,546	173,188
Loans and leases, excluding covered loans	20,910,355	20,337,206
Less: Allowance for loan and lease losses	308,858	310,149
Loans and leases, excluding covered loans, net	20,601,497	20,027,057
Covered loans, net of allowance for loan losses	470,484	502,371
Net loans and leases	21,071,981	20,529,428
Premises and equipment, net	202,208	207,700
Deferred tax asset	228,273	233,811
Goodwill	635,868	635,868
Customer-relationship intangibles, net	33,454	34,831
Affordable housing investments	190,347	186,423
Customers acceptance liability	2,390	17,664
Other real estate owned (\$11,552 and \$12,760 covered by FDIC loss share at March 31, 2015 and December 31, 2014, respectively)	17,509	23,496
FDIC indemnification asset	43,256	50,511
Other assets	579,189	537,847
Total assets	\$ 32,698,899	\$ 32,597,232
Liabilities		
Demand deposits	\$ 18,579,674	\$ 18,030,021
Interest checking deposits	2,751,487	2,736,391
Money market deposits	6,011,679	6,198,798
Savings deposits	506,188	469,931
Time deposits-under \$100,000	152,121	155,568
Time deposits-\$100,000 and over	515,999	517,394
Total deposits	28,517,148	28,108,103
Short-term borrowings	4,400	322,861

Edgar Filing: CITY NATIONAL CORP - Form 10-Q

Long-term debt	634,425	638,600
Reserve for off-balance sheet credit commitments	28,660	27,811
Acceptances outstanding	2,390	17,664
Other liabilities	456,180	499,514
Total liabilities	29,643,203	29,614,553
Redeemable noncontrolling interest	37,326	39,978
Commitments and contingencies		
Shareholders' equity		
Preferred stock, par value \$1.00 per share; 5,000,000 shares authorized; 275,000 shares issued at March 31, 2015 and December 31, 2014	267,616	267,616
Common stock, par value \$1.00 per share; 75,000,000 shares authorized; 55,510,321 and 55,162,455 shares issued at March 31, 2015 and December 31, 2014, respectively	55,510	55,162
Additional paid-in capital	599,800	578,046
Accumulated other comprehensive income (loss)	5,031	(7,074)
Retained earnings	2,109,157	2,071,230
Treasury shares, at cost - 313,965 and 377,224 shares at March 31, 2015 and December 31, 2014, respectively	(18,744)	(22,279)
Total common shareholders' equity	2,750,754	2,675,085
Total shareholders' equity	3,018,370	2,942,701
Total liabilities and shareholders' equity	\$ 32,698,899	\$ 32,597,232

See accompanying Notes to the Unaudited Consolidated Financial Statements.

Table of Contents

CITY NATIONAL CORPORATION
CONSOLIDATED STATEMENTS OF INCOME
(Unaudited)

(in thousands, except per share amounts)	For the three months ended March 31,	
	2015	2014
Interest income		
Loans and leases	\$ 184,032	\$ 169,696
Securities	42,072	41,576
Due from banks - interest-bearing	136	443
Federal funds sold and securities purchased under resale agreements	1,241	1,370
Total interest income	227,481	213,085
Interest expense		
Deposits	1,920	2,134
Federal funds purchased and securities sold under repurchase agreements	71	
Subordinated debt	3,746	6,104
Other long-term debt	5,164	5,049
Total interest expense	10,901	13,287
Net interest income	216,580	199,798
Provision for credit losses on loans and leases, excluding covered loans		
Provision for losses on covered loans	497	4,655
Net interest income after provision	216,083	195,143
Noninterest income		
Trust and investment fees	55,521	53,306
Brokerage and mutual fund fees	10,598	10,042
Cash management and deposit transaction charges	12,633	12,033
International services	10,668	10,395
FDIC loss sharing expense, net	(6,688)	(7,083)
Gain on disposal of assets	110	2,826
Gain on sale of securities	3,376	2,122
Other	24,922	17,607
Impairment loss on securities:		
Total other-than-temporary impairment loss on securities	(293)	
Less: Portion of loss recognized in other comprehensive income	228	
Net impairment loss recognized in earnings	(65)	
Total noninterest income	111,075	101,248
Noninterest expense		
Salaries and employee benefits	144,568	136,833
Net occupancy of premises	16,073	16,094
Legal and professional fees	16,938	12,950
Information services	9,860	9,346
Depreciation and amortization	14,982	7,828
Amortization of intangibles	1,377	1,487
Marketing and advertising	8,830	9,775
Office services and equipment	5,136	4,910
Other real estate owned	2,731	1,433
FDIC assessments	5,094	1,391
Other operating	8,853	8,805
Total noninterest expense	234,442	210,852
Income before income taxes	92,716	85,539

Edgar Filing: CITY NATIONAL CORP - Form 10-Q

Income taxes		30,597		31,010
Net income	\$	62,119	\$	54,529
Less: Net income attributable to noncontrolling interest		553		699
Net income attributable to City National Corporation	\$	61,566	\$	53,830
Less: Dividends on preferred stock		4,094		4,094
Net income available to common shareholders	\$	57,472	\$	49,736
Net income per common share, basic	\$	1.03	\$	0.90
Net income per common share, diluted	\$	1.01	\$	0.89
Weighted-average common shares outstanding, basic		55,422		54,689
Weighted-average common shares outstanding, diluted		56,306		55,429
Dividends per common share	\$	0.35	\$	0.33

See accompanying Notes to the Unaudited Consolidated Financial Statements.

Table of Contents

CITY NATIONAL CORPORATION
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(Unaudited)

(in thousands)	For the three months ended March 31,			
	2015		2014	
Net income	\$	62,119	\$	54,529
Other comprehensive income, net of tax:				
Securities available-for-sale:				
Net unrealized gains arising during the period		14,217		12,553
Reclassification adjustment for net gains included in net income		(1,969)		(1,275)
Non-credit related impairment loss		(133)		
Foreign currency translation adjustments		(10)		
Total other comprehensive income		12,105		11,278
Comprehensive income	\$	74,224	\$	65,807
Less: Comprehensive income attributable to noncontrolling interest		553		699
Comprehensive income attributable to City National Corporation	\$	73,671	\$	65,108

See accompanying Notes to the Unaudited Consolidated Financial Statements.

Table of Contents

CITY NATIONAL CORPORATION
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

(in thousands)	For the three months ended March 31,	
	2015	2014
Cash Flows From Operating Activities		
Net income	\$ 62,119	\$ 54,529
Adjustments to net income:		
Provision for losses on covered loans	497	4,655
Depreciation and amortization	14,982	7,828
Amortization of intangibles	1,377	1,487
Share-based employee compensation expense	6,227	5,397
Deferred income tax benefit	(3,211)	(3,237)
Gain on disposal of assets	(110)	(2,826)
Gain on sale of securities	(3,376)	(2,122)
Impairment loss on securities	65	
Other, net	9,583	4,948
Net change in:		
Trading securities	70,633	20,678
Other assets and other liabilities, net	(92,959)	(88,563)
Net cash provided by operating activities	65,827	2,774
Cash Flows From Investing Activities		
Purchase of securities available-for-sale	(83,767)	(330,444)
Sales of securities available-for-sale	398,166	377,115
Maturities and paydowns of securities available-for-sale	375,712	823,410
Purchase of securities held-to-maturity	(42,637)	(282,679)
Maturities and paydowns of securities held-to-maturity	54,856	36,337
Loan originations, net of principal collections	(530,516)	(523,514)
Net payments for premises and equipment	(10,008)	(8,831)
Other investing activities, net	(851)	6,676
Net cash provided by investing activities	160,955	98,070
Cash Flows From Financing Activities		
Net increase in deposits	409,045	52,329
Net decrease in federal funds purchased	(320,000)	
Issuance of long-term debt	8,439	7,907
Repayment of long-term debt	(11,071)	(10,088)
Proceeds from exercise of stock options	21,320	13,207
Tax benefit from exercise of stock options	3,474	2,970
Cash dividends paid	(23,449)	(22,141)
Other financing activities, net	(3,307)	(16,250)
Net cash provided by financing activities	84,451	27,934
Net increase in cash and cash equivalents	311,233	128,778
Cash and cash equivalents at beginning of year	656,451	935,946
Cash and cash equivalents at end of period	\$ 967,684	\$ 1,064,724
Supplemental Disclosures of Cash Flow Information:		
Cash paid during the period for:		
Interest	\$ 18,504	\$ 22,121
Income taxes	39,022	39,399

Edgar Filing: CITY NATIONAL CORP - Form 10-Q

Non-cash investing activities:

Transfer of loans to other real estate owned	\$	1,085	\$	2,033
----------------------------------------------	----	-------	----	-------

See accompanying Notes to the Unaudited Consolidated Financial Statements.

Table of Contents

CITY NATIONAL CORPORATION

CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS EQUITY

(Unaudited)

(in thousands, except share amounts)	Common shares issued	Preferred stock	Common stock	Additional paid-in capital	Accumulated other comprehensive income (loss)	Retained earnings	Treasury shares	Total shareholders equity
Balance, December 31, 2013	54,667,295	\$ 267,616	\$ 54,667	\$ 541,210	\$ (15,641)	\$ 1,918,163	\$ (25,029)	\$ 2,740,986
Adjustment to initially apply Accounting Standards Update 2014-01						(11,941)		(11,941)
Balance, January 1, 2014	54,667,295	267,616	54,667	541,210	(15,641)	1,906,222	(25,029)	2,729,045
Net income (1)						53,830		53,830
Other comprehensive income, net of tax					11,278			11,278
Issuance of shares under share-based compensation plans	231,763		232	6,702			2,492	9,426
Share-based employee compensation expense				4,459				4,459
Tax benefit from share-based compensation plans				2,866				2,866
Dividends:								
Preferred						(4,094)		(4,094)
Common						(18,224)		(18,224)
Net change in deferred compensation plans				181				181
Change in redeemable noncontrolling interest				(5,429)				(5,429)
Balance, March 31, 2014	54,899,058	\$ 267,616	\$ 54,899	\$ 549,989	\$ (4,363)	\$ 1,937,734	\$ (22,537)	\$ 2,783,338
Balance, December 31, 2014	55,162,455	\$ 267,616	\$ 55,162	\$ 578,046	\$ (7,074)	\$ 2,071,230	\$ (22,279)	\$ 2,942,701
Net income (1)						61,566		61,566
Other comprehensive income, net of tax					12,105			12,105
Issuance of shares under share-based compensation plans	347,596		348	14,459			3,536	18,343
Share-based employee compensation expense				4,252				4,252
Tax benefit from share-based compensation plans				3,211				3,211
Dividends:								
Preferred						(4,094)		(4,094)
Common						(19,545)		(19,545)
Net change in deferred compensation plans	270			105			(1)	104
Change in redeemable noncontrolling interest				(273)				(273)
Balance, March 31, 2015	55,510,321	\$ 267,616	\$ 55,510	\$ 599,800	\$ 5,031	\$ 2,109,157	\$ (18,744)	\$ 3,018,370

- (1) Net income excludes net income attributable to redeemable noncontrolling interest of \$553 and \$699 for the three-month periods ended March 31, 2015 and 2014, respectively.
Redeemable noncontrolling interest is reflected in the mezzanine section of the consolidated balance sheets. See Note 17 of the Notes to the Unaudited Consolidated Financial Statements.

See accompanying Notes to the Unaudited Consolidated Financial Statements.

Table of Contents

CITY NATIONAL CORPORATION

NOTES TO THE UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

Note 1. Summary of Significant Accounting Policies

Organization

City National Corporation (the Corporation) is the holding company for City National Bank (the Bank). The Bank delivers banking, investment and trust services through 75 offices in Southern California, the San Francisco Bay area, Nevada, New York City, Nashville, Tennessee and Atlanta, Georgia. As of March 31, 2015, the Corporation had four consolidated investment advisory affiliates and one unconsolidated subsidiary, Business Bancorp Capital Trust I. Because the Bank comprises substantially all of the business of the Corporation, references to the Company mean the Corporation and the Bank together. The Corporation is approved as a financial holding company pursuant to the Gramm-Leach-Bliley Act of 1999.

Consolidation

The consolidated financial statements of the Company include the accounts of the Corporation, its non-bank subsidiaries, the Bank and the Bank's wholly owned subsidiaries, after the elimination of all material intercompany transactions. It also includes noncontrolling interest, which is the portion of equity in a subsidiary not attributable to a parent. Redeemable noncontrolling interests are noncontrolling ownership interests that are redeemable at the option of the holder or outside the control of the issuer. The redeemable noncontrolling interests of third parties in the Corporation's investment advisory affiliates are not considered to be permanent equity and are reflected in the mezzanine section between liabilities and equity in the consolidated balance sheets. Noncontrolling interests' share of subsidiary earnings is reflected as Net income attributable to noncontrolling interest in the consolidated statements of income.

The Company's investment management and wealth advisory affiliates are organized as limited liability companies. The Corporation generally owns a majority position in each affiliate and certain management members of each affiliate own the remaining shares. The Corporation has contractual arrangements with its affiliates whereby a percentage of revenue is allocable to fund affiliate operating expenses (operating share) while the remaining portion of revenue (distributable revenue) is allocable to the Corporation and the noncontrolling owners. All majority-owned affiliates that meet the prescribed criteria for consolidation are consolidated. The Corporation's interests in investment management affiliates in which it holds a noncontrolling share are accounted for using the equity method. Additionally, the Company has various interests in variable interest entities (VIEs) that are not required to be consolidated. See Note 16 for a more detailed discussion on VIEs.

Use of Estimates

Edgar Filing: CITY NATIONAL CORP - Form 10-Q

The Company's accounting and reporting policies conform to generally accepted accounting principles (GAAP) and practices in the financial services industry. To prepare the financial statements in conformity with GAAP, management must make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements, and income and expenses during the reporting period. Circumstances and events that differ significantly from those underlying the Company's estimates and assumptions could cause actual financial results to differ from those estimates. The material estimates included in the financial statements relate to the allowance for loan and lease losses, the reserve for off-balance sheet credit commitments, other real estate owned (OREO), valuation of share-based compensation awards, income taxes, goodwill and intangible asset impairment, securities impairment, private equity and alternative investments impairment, valuation of assets and liabilities acquired in business combinations, including contingent consideration liabilities, subsequent valuations of acquired impaired loans, Federal Deposit Insurance Corporation (FDIC) indemnification asset, valuation of noncontrolling interest, and the valuation of financial assets and liabilities reported at fair value.

The Company has applied its critical accounting policies and estimation methods consistently in all periods presented in these financial statements. The Company's estimates and assumptions are expected to change as changes in market conditions and the Company's portfolio occur in subsequent periods.

Table of Contents

Note 1. Summary of Significant Accounting Policies (Continued)

Basis of Presentation

The Company is on the accrual basis of accounting for income and expenses. The results of operations reflect any adjustments, all of which are of a normal recurring nature, unless otherwise disclosed in this Form 10-Q, and which, in the opinion of management, are necessary for a fair presentation of the results for the periods presented. In accordance with the usual practice of banks, assets and liabilities of individual trust, agency and fiduciary funds have not been included in the financial statements. These unaudited consolidated financial statements should be read in conjunction with the audited consolidated financial statements included in the Company's Annual Report on Form 10-K for the year ended December 31, 2014.

The results for the 2015 interim periods are not necessarily indicative of the results expected for the full year. The Company has not made any significant changes in its critical accounting policies or in its estimates and assumptions from those disclosed in its 2014 Annual Report other than the adoption of new accounting pronouncements and other authoritative guidance that became effective for the Company on or after January 1, 2015. Refer to *Accounting Pronouncements* for discussion of accounting pronouncements adopted in 2015.

Certain prior period amounts have been reclassified to conform to the current period presentation.

Accounting Pronouncements

The following is a summary of accounting pronouncements that became effective during the three months ended March 31, 2015:

- In January 2014, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2014-01, *Investments - Equity Method and Joint Ventures (Topic 323), Accounting for Investments in Qualified Affordable Housing Projects* (ASU 2014-01). ASU 2014-01 permits an entity to make an accounting policy election to apply a proportionate amortization method to its low income housing tax credit investments if certain conditions are met. Under the proportionate amortization method, an investor amortizes the initial cost of the investment in proportion to the tax credits and other tax benefits received, and recognizes the amortization in the income statement as a component of income taxes attributable to continuing operations. On January 1, 2015, the Company adopted ASU 2014-01 and elected to apply the proportionate amortization method to its low income housing tax credit investments. Following adoption, the Company recognizes amortization of its tax credit investments as a component of income taxes. The Company previously recognized amortization as a component of noninterest expense. Prior periods presented in the Company's consolidated financial statements have been adjusted to reflect retrospective adoption of ASU 2014-01 as follows:

(in thousands)	Consolidated Balance Sheet As of December 31, 2014	
	As Reported	As Adjusted (Unaudited)

Edgar Filing: CITY NATIONAL CORP - Form 10-Q

Assets			
Deferred tax asset	\$	230,376	\$ 233,811
Affordable housing investments		203,010	186,423
Other assets		537,826	537,847
Shareholders equity			
Retained earnings		2,084,361	2,071,230

Table of Contents**Note 1. Summary of Significant Accounting Policies (Continued)**

Consolidated Income Statement			
For the three months ended			
March 31, 2014			
(in thousands, except per share amounts)	As Reported	As Adjusted	
	(Unaudited)		
Noninterest expense			
Other operating	\$ 12,846	\$	8,805
Income taxes	26,288		31,010
Net income	55,210		54,529
Net income per common share, basic	\$ 0.91	\$	0.90
Net income per common share, diluted	\$ 0.90	\$	0.89

Consolidated Statement of Cash Flows			
For the three months ended			
March 31, 2014			
(in thousands)	As Reported	As Adjusted	
	(Unaudited)		
Cash Flows From Operating Activities			
Net income	\$ 55,210	\$	54,529
Adjustments to net income:			
Deferred income tax benefit	(2,679)		