NBT BANCORP INC
Form 10-Q
May 10, 2011

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D. C. 20549
FORM 10-Q

(Mark One)
x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended March 31, 2011.
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 0-14703

NBT BANCORP INC.
(Exact Name of Registrant as Specified in its Charter)

DELAWARE	16-1268674
(State of Incorporation)	(I.R.S. Employer Identification No.)

52 SOUTH BROAD STREET, NORWICH, NEW YORK 13815
(Address of Principal Executive Offices) (Zip Code)

Registrant's Telephone Number, Including Area Code: (607) 337-2265

None
(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 x No o

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, 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 x   Accelerated filer o   Non-accelerated filer o   Smaller reporting company o

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

As of April 30, 2011, there were 34,440,354 shares outstanding of the Registrant's common stock, $0.01 par value per share.

NBT BANCORP INC.
FORM 10-Q--Quarter Ended March 31, 2011

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Item 1 – FINANCIAL STATEMENTS

NBT Bancorp Inc. and Subsidiaries
Consolidated Balance Sheets (unaudited)

(In thousands, except share and per share data)		March 31, 2011		December 31, 2010
Assets				
Cash and due from banks	$	84,599	$	99,673
Short-term interest bearing accounts		237,347		69,119
Securities available for sale, at fair value		1,105,606		1,129,368
Securities held to maturity (fair value $91,426 and $98,759, respectively)		90,008		97,310
Trading securities		3,119		2,808
Federal Reserve and Federal Home Loan Bank stock		27,246		27,246
Loans and leases		3,626,994		3,610,006
Less allowance for loan and lease losses		69,934		71,234
Net loans and leases		3,557,060		3,538,772
Premises and equipment, net		67,109		67,404
Goodwill		114,841		114,841
Intangible assets, net		17,016		17,543
Bank owned life insurance		76,336		75,301
Other assets		97,325		99,471
Total assets	$	5,477,612	$	5,338,856
Liabilities				
Demand (noninterest bearing)	$	909,833	$	911,741
Savings, NOW, and money market		2,418,748		2,291,833
Time		930,361		930,778
Total deposits		4,258,942		4,134,352
Short-term borrowings		167,461		159,434
Long-term debt		370,032		369,874
Trust preferred debentures		75,422		75,422
Other liabilities		66,679		66,202
Total liabilities		4,938,536		4,805,284
Stockholders’ equity				
Preferred stock, $0.01 par value. Authorized 2,500,000 shares at March 31, 2011 and December 31, 2010		—		—
Common stock, $0.01 par value. Authorized 50,000,000 shares at March 31, 2011 and December 31, 2010; issued 38,035,539 shares at March 31, 2011 and December 31, 2010		380		380
Additional paid-in-capital		314,787		314,023
Retained earnings		307,056		299,797
Accumulated other comprehensive loss		(6,702)		(5,335)
Common stock in treasury, at cost, 3,581,272 and 3,532,732 shares at March 31, 2011 and December 31, 2010, respectively		(76,445)		(75,293)
Total stockholders’ equity		539,076		533,572
Total liabilities and stockholders’ equity	$	5,477,612	$	5,338,856

See accompanying notes to unaudited interim consolidated financial statements.

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NBT Bancorp Inc. and Subsidiaries Consolidated Statements of Income (unaudited) (In thousands, except per share data)	Three months ended March 31, 2011	 2010
Interest, fee, and dividend income		
Interest and fees on loans and leases	$50,860	$53,692
Securities available for sale	7,904	10,046
Securities held to maturity	800	1,137
Other	493	596
Total interest, fee, and dividend income	60,057	65,471
Interest expense		
Deposits	6,287	8,454
Short-term borrowings	58	124
Long-term debt	3,571	5,065
Trust preferred debentures	889	1,027
Total interest expense	10,805	14,670
Net interest income	49,252	50,801
Provision for loan and lease losses	3,965	9,243
Net interest income after provision for loan and lease losses	45,287	41,558
Noninterest income		
Service charges on deposit accounts	5,072	6,130
Insurance and other financial services revenue	5,773	5,245
Trust	2,036	1,766
Net securities gains	27	28
Bank owned life insurance	1,035	981
ATM and debit card fees	2,668	2,367
Retirement plan administration fees	2,171	2,390
Other	1,344	1,434
Total noninterest income	20,126	20,341
Noninterest expense		
Salaries and employee benefits	25,004	22,204
Occupancy	4,522	4,152
Equipment	2,190	2,100
Data processing and communications	2,914	3,218
Professional fees and outside services	2,066	2,284
Office supplies and postage	1,545	1,542
Amortization of intangible assets	733	781
Loan collection and other real estate owned	719	1,059
Advertising	568	667
FDIC expenses	1,496	1,553
Other	3,304	2,600
Total noninterest expense	45,061	42,160
Income before income tax expense	20,352	19,739
Income tax expense	6,045	5,763
Net income	$14,307	$13,976
Earnings per share		
Basic	$0.42	$0.41
Diluted	$0.41	$0.41

See accompanying notes to unaudited interim consolidated financial statements.

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NBT Bancorp Inc. and Subsidiaries
Consolidated Statements of Stockholders' Equity (unaudited)

(in thousands, except share and per share data)	Common Stock	Additional Paid-in-Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Common Stock in Treasury	Total
Balance at December 31, 2009	$ 380	$ 311,164	$ 270,232	$ 1,163	$ (77,816)	$ 505,123
Net income	—	—	13,976	—	—	13,976
Cash dividends - $0.20 per share	—	—	(6,883)	—	—	(6,883)
Net issuance of 37,931 shares to employee benefit plans and other stock plans, including tax benefit	—	760	(167)	—	720	1,313
Stock-based compensation	—	514	—	—	—	514
Issuance of 13,055 shares of restricted stock awards	—	(364)	—	—	364	—
Forfeiture of 2,000 shares of restricted stock	—	46	—	—	(46)	—
Other comprehensive income	—	—	—	1,433	—	1,433
Balance at March 31, 2010	$ 380	$ 312,120	$ 277,158	$ 2,596	$ (76,778)	$ 515,476
Balance at December 31, 2010	$ 380	$ 314,023	$ 299,797	$ (5,335)	$ (75,293)	$ 533,572
Net income	—	—	14,307	—	—	14,307
Cash dividends - $0.20 per share	—	—	(6,913)	—	—	(6,913)
Purchase of 107,871 treasury shares	—	—	—	—	(2,369)	(2,369)
Net issuance of 38,868 shares to employee benefit plans and other stock plans, including tax benefit	—	49	(135)	—	787	701
Stock-based compensation	—	1,145	—	—	—	1,145
Issuance of 25,463 shares of restricted stock awards	—	(542)	—	—	542	—
Forfeiture of 5,000 shares of restricted stock	—	112	—	—	(112)	—

Other comprehensive loss	—	—	—	(1,367)	—	(1,367)
Balance at March 31, 2011	$ 380	$ 314,787	$ 307,056	$ (6,702)	$ (76,445)	$ 539,076

See accompanying notes to unaudited interim consolidated financial statements.

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NBT Bancorp Inc. and Subsidiaries Consolidated Statements of Cash Flows (unaudited) (In thousands, except per share data)	Three Months Ended March 31, 2011	2010
Operating activities		
Net income	$14,307	$13,976
Adjustments to reconcile net income to net cash provided by operating activities		
Provision for loan and lease losses	3,965	9,243
Depreciation and amortization of premises and equipment	1,324	1,324
Net accretion on securities	254	152
Amortization of intangible assets	733	781
Stock based compensation	1,145	514
Bank owned life insurance income	(1,035)	(981)
Purchases of trading securities	(208)	(80)
Unrealized gains in trading securities	(103)	(103)
Deferred income tax benefit	(2,876)	(3,588)
Proceeds from sales of loans held for sale	2,043	21,789
Originations and purchases of loans held for sale	(503)	(21,277)
Net gains on sales of loans held for sale	—	(263)
Net security gains	(27)	(28)
Net gain on sales of other real estate owned	(257)	(118)
Net decrease in other assets	2,084	1,541
Net increase (decrease) in other liabilities	3,230	(3,979)
Net cash provided by operating activities	24,076	18,903
Investing activities		
Securities available for sale:		
Proceeds from maturities, calls, and principal paydowns	145,683	145,182
Proceeds from sales	—	702
Purchases	(124,835)	(160,683)
Securities held to maturity:		
Proceeds from maturities, calls, and principal paydowns	12,576	15,400
Purchases	(4,246)	(12,578)
Net (increase) decrease in loans	(23,893)	1,539
Net decrease in Federal Reserve and FHLB stock	—	2,251
Purchases of premises and equipment	(1,029)	(1,332)
Proceeds from sales of other real estate owned	628	811
Net cash provided by (used in) investing activities	4,884	(8,708)
Financing activities		
Net increase in deposits	124,590	84,133
Net increase in short-term borrowings	8,027	10,965
Repayments of long-term debt	—	(50,108)
Issuance of long-term debt	158	—
Excess tax benefit from exercise of stock options	103	809
Proceeds from the issuance of shares to employee benefit plans and other stock plans	598	504
Purchase of treasury stock	(2,369)	—
Cash dividends and payment for fractional shares	(6,913)	(6,883)
Net cash provided by financing activities	124,194	39,420
Net increase in cash and cash equivalents	153,154	49,615
Cash and cash equivalents at beginning of period	168,792	187,161

Cash and cash equivalents at end of period	$321,946	$236,776
Supplemental disclosure of cash flow information		
Cash paid during the period for:		
Interest	$10,731	$15,530
Income taxes paid, net of refunds received	1,275	3,421
Noncash investing activities:		
Loans transferred to OREO	$100	$324
Increase in securities purchases in process	—	18,315

See accompanying notes to unaudited interim consolidated financial statements.

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Consolidated Statements of Comprehensive Income (unaudited)	Three months ended March 31, 2011	2010
(In thousands)		
Net income	$14,307	$13,976
Other comprehensive (loss) income, net of tax		
Unrealized net holding (losses) gains arising during the period (pre-tax amounts of ($2,651) and $2,010)	(1,600)	1,213
Reclassification adjustment for net gains related to securities available for sale included in net income (pre-tax amounts of $27 and $28))	(17)	(17)
Pension and other benefits:		
Amortization of prior service cost and actuarial gains (pre-tax amounts of $415 and $393)	250	237
Total other comprehensive (loss) income	(1,367)	1,433
Comprehensive income	$12,940	$15,409

See accompanying notes to unaudited interim consolidated financial statements

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NBT BANCORP INC. and Subsidiaries
NOTES TO UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS
March 31, 2011

Note 1. Description of Business

NBT Bancorp Inc. (the "Registrant") is a registered financial holding company incorporated in the State of Delaware in 1986, with its principal headquarters located in Norwich, New York. The Registrant is the parent holding company of NBT Bank, N.A. (the "Bank"), NBT Financial Services, Inc. ("NBT Financial"), NBT Holdings, Inc. ("NBT Holdings"), CNBF Capital Trust I, NBT Statutory Trust I and NBT Statutory Trust II (the "Trusts"). Through the Bank, the Company is focused on community banking operations. Through NBT Financial, the Company operates EPIC Advisors, Inc. ("EPIC"), a retirement plan administrator. Through NBT Holdings, the Company operates Mang Insurance Agency, LLC ("Mang"), a full-service insurance agency. The Trusts were organized to raise additional regulatory capital and to provide funding for certain acquisitions. The Registrant's primary business consists of providing commercial banking and financial services to customers in its market area. The principal assets of the Registrant are all of the outstanding shares of common stock of its direct subsidiaries, and its principal sources of revenue are the management fees and dividends it receives from the Bank, NBT Financial, and NBT Holdings.

The Bank is a full service commercial bank formed in 1856, which provides a broad range of financial products to individuals, corporations and municipalities throughout the upstate New York, northeastern Pennsylvania, and greater Burlington, Vermont market areas.

Note 2. Basis of Presentation

The accompanying unaudited interim consolidated financial statements include the accounts of the Registrant and its wholly owned subsidiaries, the Bank, NBT Financial and NBT Holdings. Collectively, the Registrant and its subsidiaries are referred to herein as "the Company." All intercompany transactions have been eliminated in consolidation. Amounts in the prior period financial statements are reclassified whenever necessary to conform to current period presentation.

Note 3. Use of Estimates

Preparing financial statements in conformity with accounting principles generally accepted in the United States of America (U.S. GAAP) requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period, as well as the disclosures provided. Actual results could differ from those estimates. Estimates associated with the allowance for loan and lease losses, other real estate owned ("OREO"), income taxes, pension expense, fair values of financial instruments and status of contingencies are particularly susceptible to material change in the near term.

The allowance for loan and lease losses is the amount which, in the opinion of management, is necessary to absorb probable losses inherent in the loan and lease portfolio. The allowance is determined based upon numerous considerations, including local and national economic conditions, the growth and composition of the loan portfolio with respect to the mix between the various types of loans and their related risk characteristics, a review of the value of collateral supporting the loans, comprehensive reviews of the loan portfolio by the independent loan review staff and management, as well as consideration of volume and trends of delinquencies, nonperforming loans, and loan charge-offs. As a result of the review of these factors and historical and current indicators, required additions or reductions to the allowance for loan and lease losses are made periodically by charges to the provision for loan and lease losses.

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The allowance for loan and lease losses related to impaired loans is based on discounted cash flows using the loan's initial effective interest rate or the fair value of the collateral for certain loans where repayment of the loan is expected to be provided solely by the underlying collateral (collateral dependent loans). The Company's impaired loans are generally collateral dependent loans. The Company considers the estimated cost to sell, on a discounted basis, when determining the fair value of collateral in the measurement of impairment if those costs are expected to reduce the cash flows available to repay or otherwise satisfy the loans.

Management believes that the allowance for loan and lease losses is adequate. While management uses available information to recognize loan and lease losses, future additions or reductions to the allowance for loan and lease losses may be necessary based on changes in economic conditions or changes in the values of properties securing loans in the process of foreclosure. In addition, various regulatory agencies, as an integral part of their examination process, periodically review the Company's allowance for loan and lease losses. Such agencies may require the Company to recognize additions to the allowance for loan and lease losses based on their judgments about information available to them at the time of their examination which may not be currently available to management.

OREO consists of properties acquired through foreclosure or by acceptance of a deed in lieu of foreclosure. These assets are recorded at the lower of fair value of the asset acquired less estimated costs to sell or "cost" (cost is defined as the fair value less costs to sell at initial foreclosure). At the time of foreclosure, or when foreclosure occurs in-substance, the excess, if any, of the loan over the fair value of the assets received, less estimated selling costs, is charged to the allowance for loan and lease losses and any subsequent valuation write-downs are charged to other expense. Operating costs associated with the properties are charged to expense as incurred. Gains on the sale of OREO are included in income when title has passed and the sale has met the minimum down payment requirements prescribed by U.S. GAAP.

Income taxes are accounted for under the asset and liability method. The Company files consolidated tax returns on the accrual basis. Deferred income taxes are recognized for the future tax consequences and benefits attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. Realization of deferred tax assets is dependent upon the generation of future taxable income or the existence of sufficient taxable income within the available carryback period. A valuation allowance is provided when it is more likely than not that some portion of the deferred tax asset will not be realized. Based on available carrybacks and expected future income, gross deferred tax assets will ultimately be realized and a valuation allowance was not deemed necessary at March 31, 2011 or December 31, 2010. The effect of a change in tax rates on deferred taxes is recognized in income in the period that includes the enactment date. Uncertain tax positions are recognized only when it is more likely than not (likelihood of greater than 50%), based on technical merits, that the position would be sustained upon examination by taxing authorities. Tax positions that meet the more than likely than not threshold are measured using a probability-weighted approach as the largest amount of tax benefit that is greater than 50% likely of being realized upon settlement.

Management is required to make various assumptions in valuing its pension assets and liabilities. These assumptions include the expected long-term rate of return on plan assets, the discount rate, and the rate of increase in future compensation levels. Changes to these assumptions could impact earnings in future periods. The Company takes into account the plan asset mix, funding obligations, and expert opinions in determining the various assumptions used to compute pension expense. The Company also considers relevant indices and market interest rates in selecting an appropriate discount rate. A cash flow analysis for expected benefit payments from the plan is performed each year to assist in selecting the discount rate. In addition, the Company reviews expected inflationary and merit increases to compensation in determining the expected rate of increase in future compensation levels.

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Note 4. Commitments and Contingencies

The Company is a party to financial instruments in the normal course of business to meet the financing needs of its customers and to reduce its own exposure to fluctuating interest rates. These financial instruments include commitments to extend credit, unused lines of credit, and standby letters of credit. Exposure to credit loss in the event of nonperformance by the other party to the financial instrument for commitments to make loans and standby letters of credit is represented by the contractual amount of those instruments. The Company uses the same credit policy to make such commitments as it uses for on-balance-sheet items. Commitments to extend credit and unused lines of credit totaled $594.7 million at March 31, 2011 and $643.6 million at December 31, 2010. Since commitments to extend credit and unused lines of credit may expire without being fully drawn upon, this amount does not necessarily represent future cash commitments. Collateral obtained upon exercise of the commitment is determined using management's credit evaluation of the borrower and may include accounts receivable, inventory, property, land and other items.

The Company guarantees the obligations or performance of customers by issuing standby letters of credit to third parties. These standby letters of credit are frequently issued in support of third party debt, such as corporate debt issuances, industrial revenue bonds and municipal securities. The credit risk involved in issuing standby letters of credit is essentially the same as the credit risk involved in extending loan facilities to customers, and they are subject to the same credit origination guidelines, portfolio maintenance and management procedures as other credit and off-balance sheet products. Typically, these instruments have terms of five years or less and expire unused; therefore, the total amounts do not necessarily represent future cash commitments. Standby letters of credit totaled $25.9 million at March 31, 2011 and $26.2 million at December 31, 2010. As of March 31, 2011, the fair value of standby letters of credit was not significant to the Company's consolidated financial statements.

The Company has also entered into commercial letter of credit agreements on behalf of its customers. Under these agreements, the Company, on the request of its customer, opens the letter of credit and makes a commitment to honor draws made under the agreement, whereby the beneficiary is normally the provider of goods and/or services and the Company essentially replaces the customer as the payee. The credit risk involved in issuing commercial letters of credit is essentially the same as the credit risk involved in extending loan facilities to customers, and they are subject to the same credit origination guidelines, portfolio maintenance and management procedures as other credit and off-balance sheet products. Typically, these agreements vary in terms and the total amounts do not necessarily represent future cash commitments. Commercial letters of credit totaled $16.2 million at March 31, 2011 and $16.3 million at December 31, 2010. As of March 31, 2011, the fair value of commercial letters of credit was not significant to the Company's consolidated financial statements.

Note 5. Allowance for Loan and Lease Losses and Credit Quality of Loans and Leases

Allowance for Loan and Lease Losses

The allowance for loan and lease losses is maintained at a level estimated by management to provide adequately for risk of probable losses inherent in the current loan and lease portfolio. The adequacy of the allowance for loan and lease losses is continuously monitored. It is assessed for adequacy using a methodology designed to ensure the level of the allowance reasonably reflects the loan and lease portfolio's risk profile. It is evaluated to ensure that it is sufficient to absorb all reasonably estimable credit losses inherent in the current loan and lease portfolio.

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To develop and document a systematic methodology for determining the allowance for loan and lease losses, the Company has divided the loan portfolio into three portfolio segments, each with different risk characteristics and methodologies for assessing risk. Each portfolio segment is broken down into class segments where appropriate. Class segments contain unique measurement attributes, risk characteristics and methods for monitoring and assessing risk that are necessary to develop the allowance for loan and lease losses. Unique characteristics such as borrower type, loan type, collateral type, and risk characteristics define each class segment. The following table illustrates the portfolio and class segments for the Company's loan portfolio:

Portfolio	Class
Commercial Loans	Commercial
	Commercial Real Estate
	Agricultural
	Agricultural Real Estate
	Small Business
Consumer Loans and Leases	Indirect
	Home Equity
	Direct
Residential Real Estate Mortgages	

Commercial – The Company offers a variety of loan options to meet the specific needs of our commercial customers including term loans, time notes and lines of credit. Such loans are made available to businesses for working capital such as inventory and receivables, business expansion and equipment purchases. Generally, a collateral lien is placed on equipment or other assets owned by the borrower. These loans carry a higher risk than commercial real estate loans due to the nature of the underlying collateral, which can be business assets such as equipment and accounts receivable and is generally less liquid than real estate. To reduce the risk, management also attempts to secure real estate as collateral and obtain personal guarantees of the borrowers.

Commercial Real Estate – The Company offers commercial real estate loans to finance real estate purchases, refinancings, expansions and improvements to commercial properties. Commercial real estate loans are made to finance the purchases of real property which generally consists of real estate with completed structures. These commercial real estate loans are secured by first liens on the real estate, which may include apartments, commercial structures, housing businesses, healthcare facilities, and other non owner-occupied facilities. These loans are typically less risky than commercial loans, since they are secured by real estate and buildings. The Company's underwriting analysis includes credit verification, independent appraisals, a review of the borrower's financial condition, and a detailed analysis of the borrower's underlying cash flows. These loans are typically originated in amounts of no more than 80% of the appraised value of the property.

Agricultural – The Company offers a variety of agricultural loans to meet the needs of our agricultural customers including term loans, time notes, and lines of credit. These loans are made to purchase livestock, purchase and modernize equipment, and finance seasonal crop expenses. Generally, a collateral lien is placed on the livestock, equipment, produce inventories, and/or receivables owned by the borrower. These loans may carry a higher risk than commercial and agricultural real estate loans due to the industry price volatility, and in some cases, the perishable nature of the underlying collateral. To reduce these risks, management may attempt to secure these loans with additional real estate collateral, obtain personal guarantees of the borrowers, or obtain government loan guarantees to provide further support.

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Agricultural Real Estate – The Company offers real estate loans to our agricultural customers to finance farm related real estate purchases, refinancings, expansions, and improvements to agricultural properties such as barns, production facilities, and land. The agricultural real estate loans are secured by first liens on the farm real estate. Because they are secured by land and buildings, these loans may be less risky than agricultural loans. The Company's underwriting analysis includes credit verification, independent appraisals, a review of the borrower's financial condition, and a detailed analysis of the borrower's underlying cash flows. These loans are typically originated in amounts of no more than 75% of the appraised value of the property. Government loan guarantees may be obtained to provide further support.

Small Business - The Company offers a variety of loan options to meet the specific needs of our small business customers including term loans, small business mortgages and lines of credit. Such loans are generally less than $350 thousand and are made available to businesses for working capital such as inventory and receivables, business expansion, equipment purchases, and agricultural needs. Generally, a collateral lien is placed on equipment or other assets owned by the borrower such as inventory and/or receivables. These loans carry a higher risk than commercial loans due to the smaller size of the borrower and lower levels of capital. To reduce the risk, the Company obtains personal guarantees of the owners for a majority of the loans.

Indirect – The Company maintains relationships with many dealers primarily in the communities that we serve. Through these relationships, the company finances the purchases of automobiles and recreational vehicles (such as campers, boats, etc.) indirectly through dealer relationships. Approximately 69% of the indirect relationships represent automobile financing. Most of these loans carry a fixed rate of interest with principal repayment terms typically ranging from three to six years, based upon the nature of the collateral and the size of the loan. The majority of indirect consumer loans are underwritten on a secured basis using the underlying collateral being financed.

Home Equity – The Company offers fixed home equity loans as well as home equity lines of credit to consumers to finance home improvements, debt consolidation, education and other uses. Consumers are able to borrower up to 85% of the equity in their homes. The Company originates home equity lines of credit and second mortgage loans (loans secured by a second [junior] lien position on one-to-four-family residential real estate). These loans carry a higher risk than first mortgage residential loans as they are in a second position with respect to collateral. Risk is reduced through underwriting criteria, which include credit verification, appraisals, a review of the borrower's financial condition, and personal cash flows. A security interest, with title insurance when necessary, is taken in the underlying real estate.

Direct – The Company offers a variety of consumer installment loans to finance vehicle purchases, mobile home purchases and personal expenditures. Most of these loans carry a fixed rate of interest with principal repayment terms typically ranging from one to ten years, based upon the nature of the collateral and the size of the loan. The majority of consumer loans are underwritten on a secured basis using the underlying collateral being financed or a customer's deposit account. In addition to installment loans, the Company also offers personal lines of credit and overdraft protection. A minimal amount of loans are unsecured, which carry a higher risk of loss.

Residential Real Estate – Residential real estate loans consist primarily of loans secured by first or second deeds of trust on primary residences. We originate adjustable-rate and fixed-rate, one-to-four-family residential real estate loans for the construction, purchase or refinancing of a mortgage. These loans are collateralized by owner-occupied properties located in the Company's market area. When market conditions are favorable, for longer term, fixed-rate residential mortgages without escrow, the Company retains the servicing, but sells the right to receive principal and interest to Freddie Mac. This practice allows the Company to manage interest rate risk, liquidity risk, and credit risk. Loans on one-to-four-family residential real estate are generally originated in amounts of no more than 85% of the purchase price or appraised value (whichever is lower), or have private mortgage insurance. Mortgage title insurance and hazard insurance are normally required. Construction loans have a unique risk, because they are secured by an incomplete dwelling. This risk is reduced through periodic site inspections, including one at each loan draw period.

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Allowance for Loan and Lease Loss Calculation

Management considers the accounting policy related to the allowance for loan and lease losses to be a critical accounting policy given the inherent uncertainty in evaluating the levels of the allowance required to cover credit losses in the portfolio and the material effect that such judgments can have on the consolidated results of operations.

For purposes of evaluating the adequacy of the allowance, the Company considers a number of significant factors that affect the collectibility of the portfolio. For individually analyzed loans, these include estimates of loss exposure, which reflect the facts and circumstances that affect the likelihood of repayment of such loans as of the evaluation date. For homogeneous pools of loans and leases, estimates of the Company's exposure to credit loss reflect a current assessment of a number of factors, which could affect collectibility. These factors include: past loss experience; size, trend, composition, and nature of loans; changes in lending policies and procedures, including underwriting standards and collection, charge-offs and recoveries; trends experienced in nonperforming and delinquent loans; current economic conditions in the Company's market; portfolio concentrations that may affect loss experienced across one or more components of the portfolio; the effect of external factors such as competition, legal and regulatory requirements; and the experience, ability, and depth of lending management and staff. In addition, various regulatory agencies, as an integral component of their examination process, periodically review the Company's allowance for loan and lease losses. Such agencies may require the Company to make loan grade changes as well as recognize additions to the allowance based on their examinations.

After a thorough consideration of the factors discussed above, any required additions to the allowance for loan and lease losses are made periodically by charges to the provision for loan and lease losses. These charges are necessary to maintain the allowance at a level which management believes is reasonably reflective of overall inherent risk of probable loss in the portfolio. While management uses available information to recognize losses on loans and leases, additions to the allowance may fluctuate from one reporting period to another. These fluctuations are reflective of changes in risk associated with portfolio content and/or changes in management's assessment of any or all of the determining factors discussed above. The following table illustrates the changes in the allowance for loan and lease losses by portfolio segment for the three months ended March 31, 2011 and March 31, 2010:

Allowance for Loan and Lease Losses
(in thousands)

	Commercial Loans	Consumer Loans and Leases	Residential Real Estate Mortgages	Unallocated	Total
Balance as of January 1, 2011	$ 40,101	$ 26,126	$ 4,627	$ 380	$ 71,234
Charge-offs	(2,870)	(3,294)	(99)	—	(6,263)
Recoveries	420	577	1	—	998
Provision	286	2,810	809	60	3,965
Ending Balance as of March 31, 2011	$ 37,937	$ 26,219	$ 5,338	$ 440	$ 69,934
Balance as of January 1, 2010	$ 36,598	$ 26,664	$ 3,002	$ 286	$ 66,550
Charge-offs	(2,830)	(3,942)	(112)	—	(6,884)
Recoveries	525	710	6	—	1,241
Provision	6,956	2,377	(58)	(32)	9,243
Ending Balance as of March 31, 2010	$ 41,249	$ 25,809	$ 2,838	$ 254	$ 70,150

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The following tables illustrate the allowance for loan and lease losses and the recorded investment by portfolio segment as of March 31, 2011 and December 31, 2010:

Allowance for Loan and Lease Losses and Recorded Investment in Loans and Leases
(in thousands)

As of March 31, 2011	Commercial Loans	Consumer Loans and Leases	Residential Real Estate Mortgages	Unallocated	Total
Allowance loan and lease losses	$ 37,937	$26,219	$5,338	$440	$69,934
Allowance for loans and leases individually evaluated for impairment	$ 1,815	$—	$—		$1,815
Allowance for loans and leases collectively evaluated for impairment	$ 36,122	$26,219	$5,338	$440	$68,119
Ending balance of loans and leases	$ 1,605,394	$1,459,817	$561,783		$3,626,994
Ending balance of loans and leases individually evaluated for impairment	$ 11,157	$—	$—		$11,157
Ending balance of loans and leases collectively evaluated for impairment	$ 1,594,237	$1,459,817	$561,783		$3,615,837

As of December 31, 2010	Commercial Loans	Consumer Loans and Leases	Residential Real Estate Mortgages	Unallocated	Total
Allowance loan and lease losses	$ 40,101	$26,126	$4,627	$380	$71,234
Allowance for loans and leases individually evaluated for impairment	$ 2,211	$—	$—		$2,211
Allowance for loans and leases collectively evaluated for impairment	$ 37,890	$26,126	$4,627	$380	$69,023
Ending balance of loans and leases	$ 1,580,371	$1,481,241	$548,394		$3,610,006
Ending balance of loans and leases individually evaluated for impairment	$ 11,419	$—	$—		$11,419
Ending balance of loans and leases collectively evaluated for impairment	$ 1,568,952	$1,481,241	$548,394		$3,598,587

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Credit Quality of Loans and Leases

Loans and leases are placed on nonaccrual status when timely collection of principal and interest in accordance with contractual terms is doubtful. Loans and leases are transferred to nonaccrual status generally when principal or interest payments become ninety days delinquent, unless the loan is well secured and in the process of collection, or sooner when management concludes or circumstances indicate that borrowers may be unable to meet contractual principal or interest payments. When a loan or lease is transferred to a nonaccrual status, all interest previously accrued in the current period but not collected is reversed against interest income in that period. Interest accrued in a prior period and not collected is charged-off against the allowance for loan and lease losses.

If ultimate repayment of a nonaccrual loan is expected, any payments received are applied in accordance with contractual terms. If ultimate repayment of principal is not expected, any payment received on a nonaccrual loan is applied to principal until ultimate repayment becomes expected. Nonaccrual loans are returned to accrual status when they become current as to principal and interest and demonstrate a period of performance under the contractual terms and, in the opinion of management, are fully collectible as to principal and interest. When in the opinion of management the collection of principal appears unlikely, the loan balance is charged-off in total or in part.

The following table illustrates the Company's nonaccrual loans by loan class:

Loans and Leases on Nonaccrual Status

(In thousands)	March 31, 2011	December 31, 2010
Commercial Loans		
Commercial	$4,344	$5,837
Commercial Real Estate	7,180	5,687
Agricultural	4,002	4,065
Agricultural Real Estate	2,313	2,429
Small Business	7,987	7,033
	25,826	25,051
Consumer Loans and Leases		
Indirect	2,131	1,971
Home Equity	8,936	6,395
Direct	389	399
	11,456	8,765
Residential Real Estate Mortgages	9,409	8,651
Total Nonaccrual	$46,691	$42,467

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The following tables set forth information with regard to past due and nonperforming loans by loan class as of March 31, 2011 and December 31, 2010:

Age Analysis of Past Due Loans and Leases
As of March 31, 2011
(in thousands)

	31-60 Days Past Due Accruing	61-90 Days Past Due Accruing	Greater Than 91 Days Past Due Accruing	Total Past Due Accruing	Non-Accrual	Current	Recorded Total Loans and Leases
Commercial Loans							
Commercial	$290	$—	$—	$290	$ 4,344	$485,031	$489,665
Commercial Real Estate	1,708	27	395	2,130	7,180	743,864	753,174
Agricultural	—	—	—	—	4,002	62,196	66,198
Agricultural Real Estate	617	—	—	617	2,313	31,916	34,846
Small Business	3,167	869	—	4,036	7,987	249,488	261,511
	5,782	896	395	7,073	25,826	1,572,495	1,605,394
Consumer Loans and Leases							
Indirect	6,629	1,431	1,003	9,063	2,131	814,758	825,952
Home Equity	3,145	968	501	4,614	8,936	544,980	558,530
Direct	719	223	89	1,031	389	73,915	75,335
	10,493	2,622	1,593	14,708	11,456	1,433,653	1,459,817
Residential Real Estate Mortgages	1,754	294	19	2,067	9,409	550,307	561,783
	$18,029	$3,812	$2,007	$23,848	$ 46,691	$3,556,455	$3,626,994

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Age Analysis of Past Due Loans and Leases
As of December 31, 2010
(in thousands)

	31-60 Days Past Due Accruing	61-90 Days Past Due Accruing	Greater Than 91 Days Past Due Accruing	Total Past Due Accruing	Non-Accrual	Current	Recorded Total Loans and Leases
Commercial							
Commercial	$136	$55	$94	$285	$ 5,837	$461,633	$467,755
Commercial Real Estate	1,263	—	—	1,263	5,687	730,285	737,235
Agricultural	63	92	—	155	4,065	63,336	67,556
Agricultural Real Estate	108	—	—	108	2,429	33,400	35,937
Small Business	2,570	1,183	—	3,753	7,033	261,102	271,888
	4,140	1,330	94	5,564	25,051	1,549,756	1,580,371
Consumer							
Indirect	9,307	2,193	862	12,362	1,971	814,594	828,927
Home Equity	5,740	1,756	396	7,892	6,395	561,391	575,678
Direct	927	158	54	1,139	399	75,098	76,636
	15,974	4,107	1,312	21,393	8,765	1,451,083	1,481,241
Residential Real Estate Mortgages	3,002	126	919	4,047	8,651	535,696	548,394
	$23,116	$5,563	$2,325	$31,004	$ 42,467	$3,536,535	$3,610,006

There were no material commitments to extend further credit to borrowers with nonperforming loans. Within nonaccrual loans, there are approximately $3.4 million of troubled debt restructured loans at March 31, 2011.

Impaired loans, which primarily consist of nonaccruing commercial, commercial real estate, agricultural, and agricultural real estate loans were $17.2 million at March 31, 2011 and December 31,2010.

The methodology used to establish the allowance for loan and lease losses on impaired loans incorporates specific allocations on loans analyzed individually. Classified loans with outstanding balances of $500 thousand or more are evaluated for impairment through the Company's quarterly status review process. For loans that are impaired as defined by accounting standards, impairment is measured by one of three methods: 1) the fair value of collateral less cost to sell, 2) present value of expected future cash flows or 3) the loan's observable market price. At March 31, 2011, $6.0 million of the total impaired loans had a specific reserve allocation of $1.8 million compared to $5.7 million of impaired loans at December 31, 2010 which had a specific reserve allocation of $2.2 million.

The following table provides additional information on impaired loans and specific reserve allocations as of March 31, 2011 and December 31, 2010:

Impaired Loans

	March 31, 2011			December 31, 2010		
(in thousands)	Recorded Investment Balance (Book)	Unpaid Principal Balance (Legal)	Related Allowance	Recorded Investment Balance (Book)	Unpaid Principal Balance (Legal)	Related Allowance
With no related allowance recorded:						
Commercial Loans						
Commercial	$2,459	$4,197		$1,794	$2,145	
Commercial Real Estate	3,551	4,412		3,787	4,467	
Agricultural	2,665	3,131		2,657	3,145	
Agricultural Real Estate	1,265	1,376		1,283	1,382	
Small Business	1,281	1,608		1,982	2,334	
	11,221	14,724		11,503	13,473	
With an allowance recorded:						
Commercial Loans						
Commercial	$1,877	$2,806	$628	$3,925	$4,962	$1,907
Commercial Real Estate	2,423	2,423	1,020	—	—	—
Agricultural	1,596	1,886	150	1,671	1,918	281
Agricultural Real Estate	72	78	17	73	78	23
	5,968	7,193	1,815	5,669		