FIRST FINANCIAL CORP /IN/
Form 10-Q
May 10, 2013

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE

SECURITIES EXCHANGE ACT OF 1934

For The Quarterly Period Ended March 31, 2013

Commission File Number 0-16759

FIRST FINANCIAL CORPORATION

(Exact name of registrant as specified in its charter)

INDIANA (State or other jurisdiction incorporation or organization)	35-1546989 (I.R.S. Employer Identification No.)
One First Financial Plaza, Terre Haute, IN (Address of principal executive office)	47807 (Zip Code)

(812)238-6000

(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 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 ¨.

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 during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes x No ¨.

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

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

As of May 7, 2013, the registrant had outstanding 13,307,498 shares of common stock, without par value.

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Part I – Financial Information

Item 1. Financial Statements

FIRST FINANCIAL CORPORATION

CONSOLIDATED BALANCE SHEETS

(Dollar amounts in thousands, except per share data)

	March 31, 2013 (unaudited)	December 31, 2012
ASSETS		
Cash and due from banks	$78,399	$ 87,230
Federal funds sold	54,384	20,800
Securities available-for-sale	769,949	691,000
Loans:		
Commercial	1,061,798	1,088,144
Residential	494,001	496,237
Consumer	266,744	268,507
	1,822,543	1,852,888
Less:		
Unearned Income	(1,012)	(952)
Allowance for loan losses	(25,272)	(21,958)
	1,796,259	1,829,978
Restricted Stock	21,292	21,292
Accrued interest receivable	11,622	12,024
Premises and equipment, net	46,940	47,308
Bank-owned life insurance	77,787	77,295
Goodwill	37,612	37,612
Other intangible assets	3,601	3,893
Other real estate owned	7,752	7,722
FDIC Indemnification Asset	1,770	2,632
Other assets	57,585	56,622
TOTAL ASSETS	$2,964,952	$ 2,895,408
LIABILITIES AND SHAREHOLDERS' EQUITY		
Deposits:		
Non-interest-bearing	$454,935	$ 465,954
Interest-bearing:		
Certificates of deposit of $100 or more	211,529	213,610
Other interest-bearing deposits	1,683,312	1,596,570
	2,349,776	2,276,134

Short-term borrowings	39,952	40,551
Other borrowings	114,608	119,705
Other liabilities	82,233	86,896
TOTAL LIABILITIES	2,586,569	2,523,286
Shareholders' equity		
Common stock, $.125 stated value per share;		
Authorized shares-40,000,000		
Issued shares-14,516,113 in 2013 and 14,490,609 in 2012		
Outstanding shares-13,307,498 in 2013 and 13,287,348 in 2012	1,809	1,808
Additional paid-in capital	70,171	69,989
Retained earnings	346,035	338,342
Accumulated other comprehensive income (loss)	(8,925)	(7,472)
Less: Treasury shares at cost-1,208,615 in 2013 and 1,203,261 in 2012	(30,707)	(30,545)
TOTAL SHAREHOLDERS' EQUITY	378,383	372,122
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	$2,964,952	$ 2,895,408

See accompanying notes.

FIRST FINANCIAL CORPORATION

CONSOLIDATED STATEMENTS OF INCOME AND COMPREHENSIVE INCOME

(Dollar amounts in thousands, except per share data)

	Three Months Ended March 31,	
	2013 (unaudited)	2012 (unaudited)
INTEREST INCOME:		
Loans, including related fees	$ 23,454	$ 25,198
Securities:		
Taxable	3,214	3,523
Tax-exempt	1,770	1,805
Other	504	623
TOTAL INTEREST INCOME	28,942	31,149
INTEREST EXPENSE:		
Deposits	1,742	2,664
Short-term borrowings	20	46
Other borrowings	1,007	1,274
TOTAL INTEREST EXPENSE	2,769	3,984
NET INTEREST INCOME	26,173	27,165
Provision for loan losses	3,021	2,956
NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES	23,152	24,209
NON-INTEREST INCOME:		
Trust and financial services	1,526	1,480
Service charges and fees on deposit accounts	2,254	2,204
Other service charges and fees	2,500	2,455
Securities gains/(losses), net	4	(4)
Insurance commissions	1,963	1,891
Gain on sales of mortgage loans	963	925
Other	667	560
TOTAL NON-INTEREST INCOME	9,877	9,511
NON-INTEREST EXPENSE:		
Salaries and employee benefits	13,596	14,419
Occupancy expense	1,522	1,417
Equipment expense	1,501	1,282
FDIC Insurance	557	428

Other	5,023	5,874
TOTAL NON-INTEREST EXPENSE	22,199	23,420
INCOME BEFORE INCOME TAXES	10,830	10,300
Provision for income taxes	3,137	2,857
NET INCOME	7,693	7,443
OTHER COMPREHENSIVE INCOME		
Change in unrealized gains/losses on securities, net of reclassifications	(2,778)	70
Tax effect	1,111	(28)
	(1,667)	42
Change in funded status of post retirement benefits	357	617
Tax effect	(143)	(247)
	214	370
TOTAL OTHER COMPREHENSIVE INCOME	(1,453)	412
COMPREHENSIVE INCOME	$ 6,240	$ 7,855
EARNINGS PER SHARE:		
BASIC AND DILUTED	$ 0.58	$ 0.56
Weighted average number of shares outstanding (in thousands)	13,300	13,223

See accompanying notes.

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FIRST FINANCIAL CORPORATION

CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY

Three Months Ended

March 31, 2013, and 2012

(Dollar amounts in thousands, except per share data)

(Unaudited)

	Common Stock	Additional Capital	Retained Earnings	Accumulated Other Comprehensive Income/(Loss)	Treasury Stock	Total
Balance, January 1, 2012	$ 1,806	$ 69,328	$318,130	($ 10,494)	($31,809)	$346,961
Net income	-	-	7,443	-	-	7,443
Change in other comprehensive income	-	-	-	412	-	412
Omnibus Equity Incentive Plan	1	120	-	-		121
Balance, March 31, 2012	$ 1,807	$ 69,448	$325,573	($ 10,082)	($31,809)	$354,937
Balance, January 1, 2013	$ 1,808	$ 69,989	$338,342	($ 7,472)	($30,545)	$372,122
Net income	-	-	7,693	-	-	7,693
Change in other comprehensive income	-	-	-	(1,453)		(1,453)
Omnibus Equity Incentive Plan	1	182	-	-		183
Treasury stock purchase (5,354 shares)					(162)	(162)
Balance, March 31, 2013	$ 1,809	$ 70,171	$346,035	($ 8,925)	($30,707)	$378,383

See accompanying notes.

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FIRST FINANCIAL CORPORATION

CONSOLIDATED STATEMENTS OF CASH FLOWS

(Dollar amounts in thousands, except per share data)

	Three Months Ended March 31, 2013 (Unaudited)	2012 (Unaudited)
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net Income	$7,693	$ 7,443
Adjustments to reconcile net income to net cash provided by operating activities:		
Net amortization (accretion) of premiums and discounts on investments	652	827
Provision for loan losses	3,021	2,956
Securities (gains) losses	(4)	4
Restricted stock compensation	183	121
(Gain) loss on sale of other real estate	51	5
Depreciation and amortization	1,352	1,193
Other, net	3,014	10,183
NET CASH FROM OPERATING ACTIVITIES	15,962	22,732
CASH FLOWS FROM INVESTING ACTIVITIES:		
Proceeds from sales of securities available-for-sale	4,369	4,553
Calls, maturities and principal reductions on securities available-for-sale	44,334	26,665
Purchases of securities available-for-sale	(131,176)	(30,510)
Loans made to customers, net of repayment	30,338	37,836
Proceeds from sales of other real estate owned	362	525
Redemption of retricted stock	-	1,172
Net change in federal funds sold	(33,584)	(96,403)
Additions to premises and equipment	(692)	(1,354)
NET CASH FROM INVESTING ACTIVITIES	(86,049)	(57,516)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Net change in deposits	73,395	4,737
Net change in short-term borrowings	(599)	(35,053)
Maturities of other borrowings	(5,000)	-
Purchase of treasury stock	(162)	-
Dividends paid	(6,378)	(6,203)
NET CASH FROM FINANCING ACTIVITIES	61,256	(36,519)
NET CHANGE IN CASH AND CASH EQUIVALENTS	(8,831)	(71,303)
CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD	87,230	134,280

CASH AND CASH EQUIVALENTS, END OF PERIOD	$78,399	$ 62,977

See accompanying notes.

FIRST FINANCIAL CORPORATION

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The accompanying March 31, 2013 and 2012 consolidated financial statements are unaudited. The December 31, 2012 consolidated financial statements are as reported in the First Financial Corporation (the "Corporation") 10-K. The information presented does not include all information and footnotes required by U.S. generally accepted accounting principles for complete financial statements. The following notes should be read together with notes to the consolidated financial statements included in the 10-K filed with the Securities and Exchange Commission for the fiscal year ended December 31, 2012.

1. Significant Accounting Policies

The significant accounting policies followed by the Corporation and its subsidiaries for interim financial reporting are consistent with the accounting policies followed for annual financial reporting. All adjustments which are, in the opinion of management, necessary for a fair statement of the results for the periods reported have been included in the accompanying consolidated financial statements and are of a normal recurring nature. The Corporation reports financial information for only one segment, banking. Some items in the prior year financials were reclassified to conform to the current presentation.

The Omnibus Equity Incentive Plan is a long-term incentive plan that was designed to align the interests of participants with the interests of shareholders. Under the plan, awards may be made based on certain performance measures. The grants are made in restricted stock units that are subject to a vesting schedule. These shares vest over 3 years in increments of 33%, 33%, and 34% respectively. In 2013 and 2012, 30,219 and 39,643 shares were awarded, respectively. These shares had a grant date value of $0.9 million and $1.4 million for 2013 and 2012, vest over three years and their grant in not subject to future performance measures. Outstanding shares are increased at the award date for the total shares awarded.

2. Allowance for Loan Losses

The following tables present the activity of the allowance for loan losses by portfolio segment at March 31.

Allowance for Loan Losses:	March 31, 2013				
(Dollar amounts in thousands)	Commercial	Residential	Consumer	Unallocated	Total

Beginning balance	$10,987	$ 5,426	$ 3,879	$ 1,666	$21,958
Provision for loan losses*	1,264	197	233	581	2,275
Loans charged -off	(450)	(272)	(1,026)	-	(1,748)
Recoveries	2,343	49	395	-	2,787
Ending Balance	$14,144	$ 5,400	$ 3,481	$ 2,247	$25,272

* Provision before increase of $746 thousand in 2012 for decrease in FDIC indemnification asset

Allowance for Loan Losses:	March 31, 2012				
(Dollar amounts in thousands)	Commercial	Residential	Consumer	Unallocated	Total
Beginning balance	$12,119	$ 2,728	$ 3,889	$ 505	$19,241
Provision for loan losses*	997	683	319	461	2,460
Loans charged -off	(1,858)	(1,336)	(783)	-	(3,977)
Recoveries	190	17	381	-	588
Ending Balance	$11,448	$ 2,092	$ 3,806	$ 966	$18,312

* Provision before increase of $496 thousand in 2012 for decrease in FDIC indemnification asset

The following table presents the allocation of the allowance for loan losses and the recorded investment in loans by portfolio segment and based on the impairment method at March 31, 2013 and December 31, 2012.

Ending Balance Attributable to Loans:	March 31, 2013				
(Dollar amounts in thousands)	Commercial	Residential	Consumer	Unallocated	Total
Individually evaluated for impairment	6,610	3,920	-	-	10,530
Collectively evaluated for impairment	6,320	1,361	3,481	2,247	13,409
Acquired with deteriorated credit quality	1,214	119	-	-	1,333
Ending Balance	$14,144	$ 5,400	$ 3,481	$ 2,247	$25,272

Loans:	March 31, 2013			
(Dollar amounts in thousands)	Commercial	Residential	Consumer	Total
Individually evaluated for impairment	27,839	6,989	-	34,828
Collectively evaluated for impairment	1,026,231	485,157	268,056	1,779,444
Acquired with deteriorated credit quality	13,104	3,489	4	16,597
Ending Balance	$1,067,174	$495,635	$268,060	$1,830,869

Allowance for Loan Losses:	December 31, 2012				
(Dollar amounts in thousands)	Commercial	Residential	Consumer	Unallocated	Total
Individually evaluated for impairment	3,453	3,920	-	-	7,373
Collectively evaluated for impairment	7,286	1,506	3,879	1,666	14,337
Acquired with deteriorated credit quality	248	-	-	-	248
Ending Balance	$10,987	$ 5,426	$ 3,879	$ 1,666	$21,958

Loans	December 31, 2012			
(Dollar amounts in thousands)	Commercial	Residential	Consumer	Total
Individually evaluated for impairment	23,721	6,973	-	30,694
Collectively evaluated for impairment	1,056,861	487,486	269,882	1,814,229
Acquired with deteriorated credit quality	13,582	3,421	6	17,009
Ending Balance	$1,094,164	$497,880	$269,888	$1,861,932

The following tables present loans individually evaluated for impairment by class of loans.

	March 31, 2013					
(Dollar amounts in thousands)	Unpaid Principal Balance	Recorded Investment	Allowance for Loan Losses Allocated	Average Recorded Investment	Interest Income Recognized	Cash Basis Interest Recognized
With no related allowance recorded:						
Commercial						
Commercial & Industrial	$563	$ 399	$ -	$ 200	$ -	$ -
Farmland	-	-	-	-	-	-
Non Farm, Non Residential	-	-	-	-	-	-
Agriculture	-	-	-	-	-	-
All Other Commercial	-	-	-	-	-	-
Residential						
First Liens	-	-	-	-	-	-
Home Equity	-	-	-	-	-	-
Junior Liens	-	-	-	-	-	-
Multifamily	-	-	-	-	-	-
All Other Residential	-	-	-	-	-	-
Consumer						
Motor Vehicle	-	-	-	-	-	-
All Other Consumer	-	-	-	-	-	-
With an allowance recorded:						
Commercial						
Commercial & Industrial	16,171	16,171	3,721	16,635	-	-
Farmland	891	891	191	891	-	-
Non Farm, Non Residential	8,710	8,644	1,500	8,015	-	-
Agriculture	-	-	-	-	-	-
All Other Commercial	4,326	4,326	1,297	2,768	-	-

Residential						
First Liens	1,253	1,253	126	1,254	-	-
Home Equity	196	196	-	188	-	-
Junior Liens	-	-	-	-	-	-
Multifamily	-	-	-	-	-	-
All Other Residential	5,540	5,540	3,794	5,540	-	-
Consumer						
Motor Vehicle	-	-	-	-	-	-
All Other Consumer	-	-	-	-	-	-
TOTAL	$37,650	$ 37,420	$ 10,629	$ 35,491	$ -	$ -

	December 31, 2012					
(Dollar amounts in thousands)	Unpaid Principal Balance	Recorded Investment	Allowance for Loan Losses Allocated	Average Recorded Investment	Interest Income Recognized	Cash Basis Interest Income Recognized
With no related allowance recorded:						
Commercial						
Commercial & Industrial	$ -	$ -	$ -	$ 1,013	$ -	$ -
Farmland	-	-	-	-	-	-
Non Farm, Non Residential	-	-	-	1,679	-	-
Agriculture	-	-	-	-	-	-
All Other Commercial	-	-	-	-	-	-
Residential						
First Liens	-	-	-	150	-	-
Home Equity	-	-	-	-	-	-
Junior Liens	-	-	-	-	-	-
Multifamily	-	-	-	50	-	-
All Other Residential	-	-	-	-	-	-
Consumer						
Motor Vehicle	-	-	-	-	-	-
All Other Consumer	-	-	-	-	-	-
With an allowance recorded:						
Commercial						
Commercial & Industrial	17,262	17,098	3,153	16,738	-	-
Farmland	891	891	191	891	-	-
Non Farm, Non Residential	7,438	7,386	293	5,000	179	-
Agriculture	-	-	-	-	-	-
All Other Commercial	1,209	1,209	52	1,362	-	-
Residential						
First Liens	1,254	1,254	126	1,230	-	-
Home Equity	179	179	-	75	-	-
Junior Liens	-	-	-	176	-	-
Multifamily	5,540	5,540	3,794	2,216	-	-
All Other Residential	-	-	-	-	-	-
Consumer						
Motor Vehicle	-	-	-	-	-	-
All Other Consumer	-	-	-	-	-	-
TOTAL	$ 33,773	$ 33,557	$ 7,609	$ 30,580	$ 179	$ -

The table below presents non-performing loans.

	March 31, 2013		
(Dollar amounts in thousands)	Loans Past Due Over 90 Day Still Accruing	Restructured	Nonaccrual
Commercial			
Commercial & Industrial	$26	$ 11,283	$ 8,383
Farmland	47	-	920
Non Farm, Non Residential	385	4,787	8,475
Agriculture	-	-	92
All Other Commercial	-	-	4,802
Residential			
First Liens	678	4,202	6,910
Home Equity	36	-	205
Junior Liens	149	-	783
Multifamily	-	-	5,743
All Other Residential	-	-	145
Consumer			
Motor Vehicle	73	700	132
All Other Consumer	5	-	1,542
TOTAL	$1,399	$ 20,972	$ 38,132

	December 31, 2012		
(Dollar amounts in thousands)	Loans Past Due Over 90 Day Still Accruing	Restructured	Nonaccrual
Commercial			
Commercial & Industrial	$724	$ 11,573	$ 9,360
Farmland	231	-	907
Non Farm, Non Residential	491	4,836	6,718
Agriculture	69	-	104
All Other Commercial	-	-	4,811
Residential			
First Liens	1,237	4,126	6,852
Home Equity	24	-	196
Junior Liens	538	-	405

Multifamily	101	-	5,598
All Other Residential	-	-	150
Consumer			
Motor Vehicle	133	685	174
All Other Consumer	3	16	1,519
TOTAL	$3,551	$ 21,236	$ 36,794

Covered loans included in loans past due over 90 days still on accrual are $27 thousand at March 31, 2013 and $630 thousand at December 31, 2012. Covered loans included in non-accrual loans are $3.7 million at March 31, 2013 and $4.3 million at December 31, 2012. Covered loans of $2.6 million at March 31, 2013 and $2.9 million at December 31, 2012 are deemed impaired and have allowance for loan loss allocated to them of $99 thousand and $236 thousand, respectively for March 31, 2013 and December 31, 2012. Non-performing loans include both smaller balance homogeneous loans that are collectively evaluated for impairment and individually classified impaired loans.

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

(Dollar amounts in thousands)	March 31, 2013 30-59 Days Past Due	60-89 Days Past Due	Greater than 90 days Past Due	Total Past Due	Current	Total
Commercial						
Commercial & Industrial	$4,884	$ 863	$ 2,948	$8,695	$487,621	$496,316
Farmland	48	-	941	989	84,378	85,367
Non Farm, Non Residential	2,955	1,774	2,106	6,835	284,252	291,087
Agriculture	736	82	5	823	103,184	104,007
All Other Commercial	134	24	3,473	3,631	86,766	90,397
Residential						
First Liens	4,380	748	4,032	9,160	337,766	346,926
Home Equity	155	42	36	233	42,172	42,405
Junior Liens	335	8	565	908	34,666	35,574
Multifamily	361	-	5,639	6,000	57,359	63,359
All Other Residential	177	-	-	177	7,194	7,371
Consumer						
Motor Vehicle	2,313	162	84	2,559	243,505	246,064
All Other Consumer	128	22	6	156	21,840	21,996
TOTAL	$16,606	$ 3,725	$ 19,835	$40,166	$1,790,703	$1,830,869

(Dollar amounts in thousands)	December 31, 2012 30-59 Days Past Due	60-89 Days Past Due	Greater than 90 days Past Due	Total Past Due	Current	Total
Commercial						
Commercial & Industrial	$1,315	$ 861	$ 3,616	$5,792	$487,160	$492,952
Farmland	534	-	1,122	1,656	87,270	88,926
Non Farm, Non Residential	5,618	1,004	2,449	9,071	290,023	299,094
Agriculture	137	-	78	215	130,404	130,619
All Other Commercial	568	202	350	1,120	81,453	82,573
Residential						
First Liens	8,359	1,659	4,599	14,617	336,230	350,847
Home Equity	143	15	24	182	43,317	43,499
Junior Liens	555	98	586	1,239	36,535	37,774
Multifamily	52	-	5,641	5,693	49,019	54,712
All Other Residential	214	-	-	214	10,834	11,048
Consumer						
Motor Vehicle	4,164	600	182	4,946	241,303	246,249

All Other Consumer	225	93	3	321	23,318	23,639
TOTAL	$21,884	$ 4,532	$ 18,650	$45,066	$1,816,866	$1,861,932

The Corporation has allocated $3.1 million and $1.6 million of specific reserves to customers whose loan terms have been modified in troubled debt restructurings as of March 31, 2013 and December 31, 2012. The Corporation has not committed to lend additional amounts as of March 31, 2013 and December 31, 2012 to customers with outstanding loans that are classified as troubled debt restructurings. There were $73 thousand of modifications and $9 thousand of charge offs in the quarter ended March 31, 2013 that were troubled debt restructurings and the resulting impact to the allowance for loan losses was not material. There were $162 thousand of modifications in the quarter ended March 31, 2012 that were troubled debt restructurings and the resulting impact to the allowance for loan losses was not material. There were no defaults of troubled debt restructurings in the first quarter of 2013 or 2012 of loans restructured in the previous 12 months.

Credit Quality Indicators:

The Corporation 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 experience, credit documentation, public information, and current economic trends, among other factors. The Corporation analyzes loans individually by classifying the loans as to credit risk. This analysis includes non-homogeneous loans, such as commercial loans, with an outstanding balance greater than $50 thousand. Any consumer loans outstanding to a borrower who had commercial loans analyzed will be similarly risk rated. This analysis is performed on a quarterly basis. The Corporation uses the following definitions for risk ratings:

Special Mention: Loans classified as special mention have a potential weakness that deserves management's close attention. If left uncorrected, these potential weaknesses may result in deterioration of the repayment prospects for the loan or of the institution's credit position at some future date.

Substandard: Loans classified as substandard are inadequately protected by the current net worth and debt service capacity of the borrower or of any pledged collateral. These loans have a well-defined weakness or weaknesses which have clearly jeopardized repayment of principal and interest as originally intended. They are characterized by the distinct possibility that the institution will sustain some future loss if the deficiencies are not corrected.

Doubtful: Loans classified as doubtful have all the weaknesses inherent in those graded substandard, with the added characteristic that the severity of the weaknesses makes collection or liquidation in full highly questionable or improbable based upon currently existing facts, conditions, and values.

Furthermore, non-homogeneous loans which were not individually analyzed, but are 90+ days past due or on non-accrual are classified as substandard. Loans included in homogeneous pools, such as residential or consumer, may be classified as substandard due to 90+ days delinquency, non-accrual status, bankruptcy, or loan restructuring.

Loans not meeting the criteria above that are analyzed individually as part of the above described process are considered to be pass rated loans. Loans listed as not rated are either less than $50 thousand or are included in groups of homogeneous loans. As of March 31, 2013 and December 31, 2012, and based on the most recent analysis performed, the risk category of loans by class of loans are as follows:

	March 31, 2013					
(Dollar amounts in thousands)	Pass	Special Mention	Substandard	Doubtful	Not Rated	Total
Commercial						
Commercial & Industrial	$418,380	$32,385	$ 30,372	$ 7,213	$6,621	$494,971
Farmland	79,939	2,627	1,588	-	37	84,191
Non Farm, Non Residential	255,651	11,479	22,099	1,058	44	290,331
Agriculture	94,414	7,800	117	-	75	102,406
All Other Commercial	76,560	1,022	11,537	52	728	89,899
Residential						
First Liens	112,920	10,006	10,584	1,269	210,901	345,680
Home Equity	12,565	643	1,365	117	27,638	42,328
Junior Liens	9,263	56	723	70	25,328	35,440
Multifamily	52,566	3,352	7,133	155	2	63,208
All Other Residential	1,149	-	-	-	6,196	7,345
Consumer						
Motor Vehicle	11,586	322	290	11	232,680	244,889
All Other Consumer	4,081	74	72	20	17,608	21,855
TOTAL	$1,129,074	$69,766	$ 85,880	$ 9,965	$527,858	$1,822,543

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	December 31, 2012					
(Dollar amounts in thousands)	Pass	Special Mention	Substandard	Doubtful	Not Rated	Total
Commercial						
Commercial & Industrial	$414,680	$31,368	$ 31,442	$ 7,138	$7,025	$491,653
Farmland	81,977	2,718	1,616	-	805	87,116
Non Farm, Non Residential	249,614	25,764	22,038	831	42	298,289
Agriculture	119,789	8,921	134	-	62	128,906
All Other Commercial	69,952	132	11,239	54	803	82,180
Residential						
First Liens	113,360	8,986	11,516	689	215,034	349,585
Home Equity	13,035	469	1,631	23	28,267	43,425
Junior Liens	10,419	50	515	70	26,575	37,629
Multifamily	42,719	3,328	8,481	59	-	54,587
All Other Residential	2,840	-	35	-	8,136	11,011
Consumer	-					
Motor Vehicle	11,695	262	311	25	232,727	245,020
All Other Consumer	4,614	73	104	21	18,675	23,487
TOTAL	$1,134,694	$82,071	$ 89,062	$ 8,910	$538,151	$1,852,888

3. <u>Securities</u>

The amortized cost and fair value of the Corporation’s investments are shown below. All securities are classified as available-for-sale.

		(000's) March 31, 2013		
	Amortized	Unrealized		
(Dollar amounts in thousands)	Cost	Gains	Losses	Fair Value
U.S. Government sponsored entities and entity mortgage-backed securities	$ 1,722	$71	$ -	$ 1,793
Mortgage Backed Securities-residential	228,731	12,086	(123)	240,694
Mortgage Backed Securities-commercial	5,026	1	(65)	4,962
Collateralized mortgage obligations	318,085	2,518	(799)	319,804
State and municipal	184,761	11,732	(188)	196,305
Collateralized debt obligations	11,698	1,828	(7,554)	5,972
Equities	320	99	-	419
TOTAL	$ 750,343	$28,335	($8,729)	$ 769,949

		December 31, 2012		
	Amortized	Unrealized		
(Dollar amounts in thousands)	Cost	Gains	Losses	Fair Value

U.S. Government sponsored entities				
and entity mortgage-backed securities	$ 1,807	$ 79	$ -	$ 1,886
Mortgage Backed Securities-residential	231,316	13,373	(13)	244,676
Mortgage Backed Securities-commercial	5,146	1	(16)	5,131
Collateralized mortgage obligations	230,739	2,827	(246)	233,320
State and municipal	187,044	12,518	(77)	199,485
Collateralized debt obligations	12,243	1,761	(7,882)	6,122
Equities	320	60	-	380
TOTAL	$ 668,615	$ 30,619	($ 8,234)	$ 691,000

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Contractual maturities of debt securities at March 31, 2013 were as follows. Securities not due at a single maturity or with no maturity date, primarily mortgage-backed and equity securities are shown separately.

	Available-for-Sale	
(Dollar amounts in thousands)	Amortized Cost	Fair Value
Due in one year or less	$14,986	$15,195
Due after one but within five years	31,614	33,420
Due after five but within ten years	86,775	92,113
Due after ten years	382,891	383,146
	516,266	523,874
Mortgage-backed securities and equities	234,077	246,075
TOTAL	$750,343	$769,949

There were $4 thousand in gains and no losses realized by the Corporation on investment sales for the three months ended March 31, 2013. There were $4 thousand in losses and no gains realized by the Corporation on investment sales for the three months ended March 31, 2012.

The following tables show the securities' gross unrealized losses and fair value, aggregated by investment category and length of time that individual securities have been in continuous unrealized loss position, at March 31, 2013 and December 31, 2012.

	March 31, 2013					
	Less Than 12 Months		More Than 12 Months		Total	
(Dollar amounts in thousands)	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
Mortgage Backed Securities - Residential	$ 19,004	$ (123)	$ -	$ -	$ 19,004	($ 123)
Mortgage Backed Securities - Commercial	4,920	(65)	-	-	4,920	(65)
Collateralized mortgage obligations	107,099	(799)	-	-	107,099	(799)
State and municipal obligations	11,080	(146)	1,048	(42)	12,128	(188)
Collateralized Debt Obligations	-	-	3,887	(7,554)	3,887	(7,554)
Total temporarily impaired securities	$ 142,103	($ 1,133)	$ 4,935	($ 7,596)	$ 147,038	($ 8,729)

	December 31, 2012					
	Less Than 12 Months		More Than 12 Months		Total	
(Dollar amounts in thousands)	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses

Mortgage Backed Securities - Residential	$ 7,245	$ (13)	$ -	$ -	$ 7,245	$ (13)
Mortgage Backed Securities - Commercial	5,086	(16)	-	-	5,086	(16)
Collateralized mortgage obligations	46,121	(246)	-	-	46,121	(246)
State and municipal obligations	8,611	(77)	-	-	8,611	(77)
Collateralized Debt Obligations	-	-	4,032	(7,882)	4,032	(7,882)
Total temporarily impaired securities	$ 67,063	($ 352)	$ 4,032	($ 7,882)	$ 71,095	($ 8,234)

Management evaluates securities for other-than-temporary impairment (“OTTI”) at least on a quarterly basis, and more frequently when economic or market conditions warrant such an evaluation. The investment securities portfolio is evaluated for OTTI by segregating the portfolio into two general segments and applying the appropriate OTTI model. Investment securities are generally evaluated for OTTI under FASB ASC 320, *Investments - Debt and Equity Securities*. However, certain purchased beneficial interests, including non-agency mortgage-backed securities, asset-backed securities, and collateralized debt obligations, that had credit ratings at the time of purchase of below AA are evaluated using the model outlined in FASB ASC 325-40, *Beneficial Interests in Securitized Financial Assets.*

In determining OTTI under the FASB ASC 320 model, management considers many factors, including: (1) the length of time and the extent to which the fair value has been less than cost, (2) the financial condition and near-term prospects of the issuer, (3) whether the market decline was affected by macroeconomic conditions, and (4) whether the entity has the intent to sell the security or more likely than not will be required to sell the security before its anticipated recovery. The assessment of whether an other-than-temporary decline exists involves a high degree of subjectivity and judgment and is based on the information available to management at a point in time.

The second segment of the portfolio uses the OTTI guidance provided by FASB ASC 325 that is specific to purchased beneficial interests that, on the purchase date, were rated below AA. Under the FASB ASC 325 model, the Corporation compares the present value of the remaining cash flows as estimated at the preceding evaluation date to the current expected remaining cash flows. An OTTI is deemed to have occurred if there has been an adverse change in the remaining expected future cash flows.

When OTTI occurs under either model, the amount of the OTTI recognized in earnings depends on whether an entity intends to sell the security or it is more likely than not it will be required to sell the security before recovery of its amortized cost basis, less any current-period credit loss. If an entity intends to sell or it is more likely than not it will be required to sell the security before recovery of its amortized cost basis, less any current-period credit loss, the OTTI shall be recognized in earnings equal to the entire difference between the investment's amortized cost basis and its fair value at the balance sheet date. If an entity does not intend to sell the security and it is not more likely than not that the entity will be required to sell the security before recovery of its amortized cost basis less any current-period loss, the OTTI shall be separated into the amount representing the credit loss and the amount related to all other factors. The amount of the total OTTI related to the credit loss is determined based on the present value of cash flows expected to be collected and is recognized in earnings. The amount of the total OTTI related to other factors is recognized in other comprehensive income, net of applicable taxes. The previous amortized cost basis less the OTTI recognized in earnings becomes the new amortized cost basis of the investment.

Gross unrealized losses on investment securities were $8.7 million as of March 31, 2013 and $8.2 million as of December 31, 2012. A majority of these losses represent negative adjustments to market value relative to the illiquidity in the markets on the securities and not losses related to the creditworthiness of the issuer. Based upon our review of the issuers, we do not believe these investments to be other than temporarily impaired. Management does not intend to sell these securities and it is not more likely than not that we will be required to sell them before their anticipated recovery.

A significant portion of the total unrealized loss in investment securities relates to collateralized debt obligations that were separately evaluated under FASB ASC 325-40, Beneficial Interests in Securitized Financial Assets. Based upon qualitative considerations, such as a down grade in credit rating or further defaults of underlying issuers during the quarter, and an analysis of expected cash flows, we have determined that three of the CDO's included in collateralized debt obligations were other-than-temporarily impaired, though no impairment was identified during the first quarter of 2013. Those three CDO's have a contractual balance of $27.1 million at March 31, 2013 which has been reduced to $5.4 million by $1.1 million of interest payments received, $14.9 million of cumulative OTTI charges recorded through earnings to date, and $5.7 million recorded in other comprehensive income. The severity of the OTTI recorded varies by security, based on the analysis described below, and ranges at March 31, 2013 from 28% to 91%. The losses recorded in other comprehensive income represents temporary impairment due to factors other than credit loss, mainly current market illiquidity. The issuers in these securities are primarily banks, but some of the pools do include a limited number of insurance companies. The market for these securities has remained very illiquid, there are very few new issuances of trust preferred securities and the credit spreads implied by current prices have increased dramatically and remain very high, resulting in significant non-credit related impairment. The Corporation uses the OTTI evaluation model to compare the present value of expected cash flows to the previous estimate to ensure there are no adverse changes in cash flows during the quarter. The OTTI model considers the structure and term of the CDO and the financial condition of the underlying issuers. Specifically, the model details interest rates, principal balances of note classes and underlying issuers, the timing and amount of interest and principal payments of the underlying issuers, and the allocation of the payments to the note classes. Cash flows are projected using a forward rate LIBOR curve, as these CDOs are variable rate instruments. An average rate is then computed using this same forward rate curve to determine an appropriate discount rate (3 month LIBOR plus margin ranging from 160 to 180 basis points). The current estimate of expected cash flows is based on the most recent trustee reports and any other relevant market information including announcements of interest payment deferrals or defaults of underlying trust preferred securities. Assumptions used in the model include expected future default rates and prepayments. We assume no recoveries on defaults and treat all interest payment deferrals as defaults. In addition we use the model to "stress" each CDO, or make assumptions more severe than expected activity, to determine the degree to which assumptions could deteriorate before the CDO could no longer fully support repayment of the Corporation's note class.

Collateralized debt obligations include an investment in a CDO consisting of pooled trust preferred securities in which the issuers are primarily banks. This CDO with an amortized cost of $646 thousand and a fair value of $582 thousand is rated BAA3 and is the senior tranche, is not in the scope of FASB ASC 325, as it was rated high investment grade at purchase, and is not considered to be other-than-temporarily impaired based on its credit quality. Its fair value is negatively impacted by the factors described above.

Management has consistently used Standard & Poors pricing to value these investments. There are a number of other pricing sources available to determine fair value for these investments. These sources utilize a variety of methods to determine fair value. The result is a wide range of estimates of fair value for these securities. The Standard & Poors pricing ranges from 4.29 to 90.15 while Moody Investor Service pricing ranges from 3.15 to 92.97, with others falling somewhere in between. We recognize that the Standard & Poors pricing utilized is likely a conservative estimate, but have been consistent in using this source and its estimate of fair value.

The table below presents a rollforward of the credit losses recognized in earnings for the three month periods ended March 31, 2013 and 2012:

(Dollar amounts in thousands)	Three Months Ended March 31, 2013	2012
Beginning balance	$ 14,983	$ 15,180
Increases to the amount related to the credit loss for which other-than-temporary was previously recognized	-	-
Ending balance	$ 14,983	$ 15,180

4. Fair Value

FASB ASC No. 820-10 establishes a fair value hierarchy which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The standard describes three levels of inputs that may be used to measure fair value:

Level 1: Quoted prices (unadjusted) of identical assets or liabilities in active markets that the entity has the ability to access as of the measurement date.

Level 2: Significant other observable inputs other than Level I prices such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data.

Level 3: Significant unobservable inputs that reflect a reporting entity’s own assumptions about the assumptions that market participants would use in pricing an asset or liability.

The fair value of most securities available for sale is determined by obtaining quoted prices on nationally recognized securities exchanges (Level 1 inputs) or matrix pricing, which is a mathematical technique widely used in the industry to value debt securities without relying exclusively on quoted prices for the specific securities but rather by relying on the securities’ relationship to other benchmark quoted securities (Level 2 inputs).

For those securities that cannot be priced using quoted market prices or observable inputs a Level 3 valuation is determined. These securities are primarily trust preferred securities, which are priced using Level 3 due to current market illiquidity and certain investments in and state and municipal securities. The fair value of the trust preferred securities is obtained from a third party provider without adjustment. As described previously, management obtains values from other pricing sources to validate the Standard & Poors pricing that they currently utilize. The fair value of state and municipal obligations are derived by comparing the securities to current market rates plus an appropriate credit spread to determine an estimated value. Illiquidity spreads are then considered. Credit reviews are performed on each of the issuers. The significant unobservable inputs used in the fair value measurement of the Corporation's state and municipal obligations are credit spreads related to specific issuers. Significantly higher credit spread assumptions would result in significantly lower fair value measurement. Conversely, significantly lower credit spreads would result in a significantly higher fair value measurements.

The fair value of derivatives is based on valuation models using observable market data as of the measurement date (Level 2 inputs).

	March 31, 2013 Fair Value Measurements Using Significant Unobservable Inputs (Level 3)			
(Dollar amounts in thousands)	Level 1	Level 2	Level 3	Carrying Value
U.S. Government entity mortgage-backed securities	$ -	$ 1,793	$ -	$ 1,793
Mortgage Backed Securities-residential	-	240,694	-	240,694
Mortgage Backed Securities-commercial	-	$ 4,962	-	4,962
Collateralized mortgage obligations	-	319,804	-	319,804
State and municipal	-	189,803	6,502	196,305
Collateralized debt obligations	-	-	5,972	5,972
Equities	419	-	0	419
TOTAL	$ 419	$ 757,056	$ 12,474	$ 769,949
Derivative Assets		1,876		
Derivative Liabilities		(1,876)		

(Dollar amounts in thousands)	December 31, 2012 Fair Value Measurements Using Significant Unobservable Inputs (Level 3) Level 1	Level 2	Level 3	Carrying Value
U.S. Government entity mortgage-backed securities	$ -	$ 1,886	$ -	$ 1,886
Mortgage Backed Securities-residential	-	244,676	-	244,676
Mortgage Backed Securities-commercial	-	$ 5,131	-	5,131
Collateralized mortgage obligations	-	233,320	-	233,320
State and municipal	-	189,574	9,911	199,485
Collateralized debt obligations	-	-	6,122	6,122
Equities	380	-	0	380
TOTAL	$ 380	$ 674,587	$ 16,033	$ 691,000
Derivative Assets		2,053		
Derivative Liabilities		(2,053)		

There were no transfer between Level 1 and Level 2 during 2013 and 2012.

The table below presents a reconciliation and income statement classification of gains and losses for all assets measured at fair value on a recurring basis using significant unobservable inputs (Level 3) for the three months ended March 31, 2013 and December 31, 2012.

	Fair Value Measurements Using SignificantUnobservable Inputs (Level 3) March 31, 2013		
	State and municipal obligations	Collateralized debt obligations	Total
Beginning balance, January 1	$ 9,911	$ 6,122	$ 16,033
Total realized/unrealized gains or losses			
Included in earnings	-	-	-
Included in other comprehensive income	-	395	395
Transfers & Purchases	-	-	-
Settlements	(3,409)	(545)	(3,954)
Ending balance, March 31	$ 6,502	$ 5,972	$ 12,474

	Fair Value Measurements Using SignificantUnobservable Inputs (Level 3) December 31, 2012			
	Equities	State and municipal obligations	Collateralized debt obligations	Total
Beginning balance, January 1	$ 1,711	$ 9,525	$ 4,771	$ 16,007
Total realized/unrealized gains or losses				

Included in earnings	(446)	-	(96)	(542)
Included in other comprehensive income	-	-	1,556	1,556
Transfers & Purchases	-	1,186	-	1,186
Settlements	(1,265)	(800)	(109)	(2,174)
Ending balance, December 31	$ -	$ 9,911	$ 6,122	$ 16,033

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The following table presents quantitative information about recurring Level 3 fair value measurements at March 31, 2013.

	Fair Value	Valuation Technique(s)	Unobservable Input(s)	Range	
State and municipal obligations	$ 6,502	Discounted cash flow	Discount rate	3.05%-5.50	%
			Probability of default	0	%
Other real estate	7,752	Sales comparison/income approach	Discount rate for age	5.00%-20.00	%
			of appraisal and market conditions		
Impaired Loans	26,789	Sales comparison/income approach	Discount rate for age		
			of appraisal and market conditions	0.00%-50.00	%

All impaired loans disclosed in footnote 2, which are measured for impairment using the fair value of collateral, are valued at Level 3. They are carried at a fair value of $26.8 million, net of a valuation allowance of $10.6 million at March 31, 2013. At December 31, 2012 impaired loans valued at Level 3 were carried at a fair value of $26.0 million, net of a valuation allowance of $7.6 million. The impact to the provision for loan losses was $3.0 million for the three months ended March 31, 2013, and was $4.2 million for the year ended December 31, 2012. Other real estate owned is valued at Level 3. Other real estate owned at March 31, 2013, with a value of $7.8 million was reduced $267 thousand for fair value adjustment. Other real estate owned at December 31, 2012, with a value of $7.7 million was reduced $234 thousand for fair value adjustment.

Fair value is measured based on the value of the collateral securing those loans, and is determined using several methods. Generally the fair value of real estate is determined based on appraisals by qualified licensed appraisers. Appraisals for real estate generally use three methods to derive value: cost, sales or market comparison and income approach. The cost method bases value on the cost to replace current property. The market comparison evaluates the sales price of similar properties in the same market area. The income approach considers net operating income generated by the property and the investor’s required return. The final fair value is based on a reconciliation of these three approaches. If an appraisal is not available, the fair value may be determined by using a cash flow analysis, a broker’s opinion of value, the net present value of future cash flows, or an observable market price from an active market. Fair value of other real estate is based upon the current appraised values of the properties as determined by qualified licensed appraisers and the Company’s judgment of other relevant market conditions. Appraisals are obtained annually and reductions in value are recorded as a valuation through a charge to expense. The primary unobservable input used by management in estimating fair value are additional discounts to the appraised value to consider selling costs and the age of the appraisal. These discounts range from 5% to20% for costs to sell and marketability. Other real estate and impaired loans carried at fair value are primarily comprised of smaller balance properties.

The following tables presents loans identified as impaired by class of loans as of March 31, 2013 and December 31, 2012.

	March 31, 2013		
(Dollar amounts in thousands)	Carrying Value	Allowance for Loan Losses Allocated	Fair Value
Commercial			
Commercial & Industrial	$ 16,570	$ 3,721	$ 12,848
Farmland	891	191	700
Non Farm, Non Residential	8,644	1,500	7,143
Agriculture	-	-	
All Other Commercial	4,326	1,297	3,029
Residential			
First Liens	1,253	126	1,127
Home Equity	196	-	196
Junior Liens	-	-	-
Multifamily	5,540	3,794	1,746
All Other Residential	-	-	-
Consumer			
Motor Vehicle	-	-	-
All Other Consumer	-	-	-
TOTAL	$ 37,420	$ 10,629	$ 26,789

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(Dollar amounts in thousands)	December 31, 2012 Carrying Value	Allowance for Loan Losses Allocated	Fair Value
Commercial			
Commercial & Industrial	$ 17,098	$ 3,153	$ 13,945
Farmland	891	191	700
Non Farm, Non Residential	7,386	293	7,093
Agriculture	-	-	
All Other Commercial	1,209	52	1,157
Residential			
First Liens	1,254	126	1,128
Home Equity	179	-	179
Junior Liens	-	-	-
Multifamily	5,540	3,794	1,746
All Other Residential	-		-
Consumer			
Motor Vehicle	-		-
All Other Consumer	-		-
TOTAL	$ 33,557	$ 7,609	$ 25,948

	March 31, 2013 Fair Value Measurment Using			
(Dollar amounts in thousands)	Carrying Value	Level 1	Level 2	Level 3
Other real estate - commercial	$ 5,656	$ -	$ -	$ 5,656
Other real estate - residential	2,096	-	-	2,096
TOTAL	$ 7,752	$ -	$ -	$ 7,752

	December 31, 2012 Fair Value Measurment Using			
(Dollar amounts in thousands)	Carrying Value	Level 1	Level 2	Level 3
Other real estate - commercial	$ 5,588	$ -	$ -	$ 5,588
Other real estate - residential	2,134	-	-	2,134
TOTAL	$ 7,722	$ -	$ -	$ 7,722

The amounts represent only balances measured at fair value during the period and still held as of the reporting date.

The carrying amounts and estimated fair value of financial instruments at March 31, 2013 and December 31, 2012, are shown below. Carrying amount is the estimated fair value for cash and due from banks, federal funds sold, short-term borrowings, accrued interest receivable and payable, demand deposits, short-term debt and variable-rate loans or deposits that reprice frequently and fully. Security fair values were described previously. For fixed-rate, non-impaired loans or deposits, variable rate loans or deposits with infrequent repricing or repricing limits, and for longer-term borrowings, fair value is based on discounted cash flows using current market rates applied to the estimated life and considering credit risk. The valuation of impaired loans was described previously. Loan fair value estimates do not necessarily represent an exit price. Fair values of loans held for sale are based on market bids on the loans or similar loans. It was not practicable to determine the fair value of Federal Home Loan Bank stock due to restrictions placed on its transferability. For the FDIC indemnification asset the carrying value is the estimated fair value as it represents amounts to be received from the FDIC in the near term. Fair value of debt is based on current rates for similar financing. The fair value of off-balance sheet items is not considered material.

The carrying amount and estimated fair value of financial instruments are presented in the table below and were determined based on the above assumptions:

	March 31, 2013				
	Carrying	Fair Value			
(Dollar amounts in thousands)	Value	Level 1	Level 2	Level 3	Total
Cash and due from banks	$78,399	$18,854	$59,545	$-	$78,399
Federal funds sold	54,384	-	54,384	-	54,384
Securities available—for—sale	769,949	419	757,056	12,474	769,949
Restricted stock	21,292	n/a	n/a	n/a	n/a
Loans, net	1,796,259	-	-	1,875,255	1,875,255
FDIC Indemnification Asset	1,770	-	1,770	-	1,770
Accrued interest receivable	11,622	-	3,295	8,327	11,622
Deposits	(2,349,776)	-	(2,353,844)	-	(2,353,844)
Short—term borrowings	(39,952)	-	(39,952)	-	(39,952)
Federal Home Loan Bank advances	(114,608)	-	(119,103)	-	(119,103)
Accrued interest payable	(1,053)	-	(1,053)	-	(1,053)

	December 31, 2012				
	Carrying	Fair Value			
(Dollar amounts in thousands)	Value	Level 1	Level 2	Level 3	Total
Cash and due from banks	$87,230	$21,333	$65,897	$-	$87,230
Federal funds sold	20,800	-	20,800	-	20,800
Securities available—for—sale	691,000	380	674,587	16,033	691,000
Restricted stock	21,292	n/a	n/a	n/a	n/a
Loans, net	1,829,978	-	-	1,916,256	1,916,256
FDIC Indemnification Asset	2,632	-	2,632	-	2,632
Accrued interest receivable	12,024	-	2,980	9,044	12,024
Deposits	(2,276,134)	-	(2,280,910)	-	(2,280,910)
Short—term borrowings	(40,551)	-	(40,551)	-	(40,551)
Federal Home Loan Bank advances	(119,705)	-	(124,933)	-	(124,933)
Accrued interest payable	(1,163)	-	(1,163)	-	(1,163)

5. Short-Term Borrowings

Period–end short-term borrowings were comprised of the following:

(000's) March 31,	December 31,

	2013	2012
Federal Funds Purchased	$4,725	$ 2,750
Repurchase Agreements	35,227	37,801
	$39,952	$ 40,551

6. Other Borrowings

Other borrowings at period-end are summarized as follows:

	(000's) March 31, 2013	December 31, 2012
FHLB Advances	$114,608	$ 119,705
	$114,608	$ 119,705

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7. Components of Net Periodic Benefit Cost

	Three Months ended March 31, (000's)			
	Pension Benefits		Post-Retirement Health Benefits	
	2013	2012	2013	2012
Service cost	$ 559	$ 1,218	$ 17	$ 15
Interest cost	846	917	43	43
Expected return on plan assets	(827)	(815)	-	-
Amortization of transition obligation	-	-	15	15
Net amortization of prior service cost	(4)	41	-	-
Net amortization of net (gain) loss	523	567	-	-
Net Periodic Benefit Cost	$ 1,097	$ 1,928	$ 75	$ 73

Employer Contributions

First Financial Corporation previously disclosed in its financial statements for the year ended December 31, 2012 that it expected to contribute $2.1 and $550 thousand respectively to its Pension Plan and ESOP and $234,000 to the Post Retirement Health Benefits Plan in 2013. Contributions of $52 thousand have been made through the first three months of 2013 for the Post Retirement Health Benefits plan. No contributions have been made in 2013 for the Pension plan or the ESOP. The Pension plan was frozen for most employees at the end of 2012 and for those employees there will be discretionary contributions to the ESOP plan and a 401K plan in place of the former Pension benefit. In the first three months of 2013 there has been $350 thousand of expense accrued for potential contributions to these alternative retirement benefit options.

8. New accounting standards

In February 2013, the Financial Accounting Standards Board (FASB) issued updated guidance related to disclosure of reclassification amounts out of other comprehensive income. The standard requires that companies present either in a single note or parenthetically on the face of the financial statements, the effect of significant amounts reclassified from each component of accumulated other comprehensive income based on its source and the income statement line items affected by the reclassification. The new requirements will take effect for public companies in fiscal years, and interim periods within those years, beginning after December 15, 2012. The Company has adopted this standard and the effect of adopting this standard increased our disclosure surrounding reclassification items out of accumulated other comprehensive income.

In October 2012, the Financial Accounting Standards Board ("FASB") issued guidance on the subsequent accounting for an indemnification asset recognized at the acquisition date as a result of a government assisted acquisition of a financial institution. When an entity recognizes such an indemnification asset and subsequently a change in the cash flows expected to be collected on the indemnification asset occurs as a result of a change in the cash flows expected to be collected on the indemnified asset, the guidance requires the entity to recognize the change in the measurement of the indemnification asset on the same basis as the indemnified assets. Any amortization of changes in value of the indemnification asset should be limited to the lesser of the term of the indemnification agreement and the remaining life of the indemnified assets. The amendments are effective for fiscal years beginning on or after December 15, 2012 and early adoption is permitted. The amendments are to be applied prospectively to any new indemnification assets acquired after the date of adoption and to indemnification assets existing as of the date of adoption arising from a government-assisted acquisition of a financial institution. The effect of adopting this standard did not have a material effect on the Corporation's operating results or financial condition.

In July 2012, the FASB amended existing guidance relating to testing indefinite-lived intangible assets for impairment. The amendment permits an assessment of qualitative factors to determine whether the existence of events and circumstances indicates that it is more likely than not that the indefinite-lived intangible asset is impaired. If, after assessing the totality of events and circumstances, it is concluded that it is not more likely than not that the indefinite-lived intangible asset is impaired, then no further action is required. However, after the same assessment, if it is concluded that it is more like than not that the indefinite-lived intangible asset is impaired, then a quantitative impairment test should be performed whereby the fair value of the indefinite-lived intangible asset is compared to the carrying amount. The amendments in this guidance are effective for annual and interim impairment tests performed for fiscal years beginning after September 15, 2012. Early adoption is permitted. The effect of adopting this standard did not have a material effect on the Corporation's operating results or financial condition.

9. Acquisitions and FDIC Indemnification Asset

On July 2, 2009, the Bank entered into a purchase and assumption agreement with the Federal Deposit Insurance Corporation ("FDIC") to assume all of the deposits (excluding brokered deposits) and certain assets of The First National Bank of Danville, a full-service commercial bank headquartered in Danville, Illinois, that had failed and been placed in receivership with the FDIC. The acquisition consisted of assets worth a fair value of approximately $151.8 million, including $77.5 million of loans, $24.2 million of investment securities, $31.0 million of cash and cash equivalents and $146.3 million of liabilities, including $145.7 million of deposits. A customer related core deposit intangible asset of $4.6 million was also recorded. In addition to the excess of liabilities over assets, the Bank received approximately$14.6 million in cash from the FDIC. Based upon the acquisition date fair values of the net assets acquired, no goodwill was recorded. The transaction resulted in a gain of $5.1 million, which is included in non-interest income in the December 31, 2009 Consolidated Statement of Operations Under the loss-sharing agreement ("LSA"), the Bank will share in the losses on assets covered under the agreement (referred to as covered assets). On losses up to $29 million, the FDIC has agreed to reimburse the Bank for 80 percent of the losses. On losses exceeding $29 million, the FDIC has agreed to reimburse the Bank for 95 percent of the losses. The loss-sharing agreement is subject to following servicing procedures as specified in the agreement with the FDIC. Loans acquired that are subject to the loss-sharing agreement with the FDIC are referred to as covered loans for disclosure purposes. Since the acquisition date the Bank has been reimbursed $18.1 million for losses and carrying expenses and currently carries a balance of $1.8 million in the indemnification asset. Included in the current balance is the estimate of $729 thousand for 80% of the loans subject to the loss-sharing agreement identified in the allowance for loan loss evaluation as probable incurred losses at March 31, 2013.

FASB ASC 310-30, *Loans and Debt Securities Acquired with Deteriorated Credit Quality,* applies to a loan with evidence of deterioration of credit quality since origination, acquired by completion of a transfer for which it is probable, at acquisition, that the investor will be unable to collect all contractually required payments receivable. FASB ASC 310-30 prohibits carrying over or creating an allowance for loan losses upon initial recognition. The carrying amount of covered assets at March 31, 2013 and December 31, 2012, consisted of loans accounted for in accordance with FASB ASC 310-30, loans not subject to FASB ASC 310-30 and other assets as shown in the following table:

	March 31, 2013			
	ASC 310-30	Non ASC 310-30		
(Dollar amounts in thousands)	Loans	Loans	Other	Total
Loans	$3,967	$ 21,770		$25,737
Foreclosed Assets			732	732
Total Covered Assets	$3,967	$ 21,770	$732	$26,469

	December 31, 2012	
	ASC 310-30	Non ASC 310-30

	Loans	Loans	Other	Total
Loans	$4,279	$ 23,475	$ -	$27,754
Foreclosed Assets	-	-	720	720
Total Covered Assets	$4,279	$ 23,475	$720	$28,474

The rollforward of the FDIC Indemnification asset is as follows:

(Dollar amounts in thousands)	Quarter Ended March 31, 2013	Year Ended December 31, 2012
Beginning balance	$ 2,632	$ 2,384
Accretion	-	-
Net changes in losses and expenses added	(702)	2,422
Reimbursements from the FDIC	(160)	(2,174)
TOTAL	$ 1,770	$ 2,632

On the acquisition date, the preliminary estimate of the contractually required payments receivable for all FASB ASC310-30 loans acquired in the acquisition were $31.6 million, the cash flows expected to be collected were $18.4 million including interest, and the estimated fair value of the loans was $16.7 million. These amounts were determined based upon the estimated remaining life of the underlying loans, which include the effects of estimated prepayments. At March 31, 2013, a majority of these loans were valued based on the liquidation value of the underlying collateral, because the expected cash flows are primarily based on the liquidation of underlying collateral and the timing and amount of the cash flows could not be reasonably estimated. On the acquisition date, the preliminary estimate of the contractually required payments receivable for all non FASB ASC310-30 loans acquired in the acquisition was $58.4 million and the estimated fair value of the loans was $60.7 million. The impact to the Corporation from the amortization and accretion of premiums and discounts was immaterial.

On March 18, 2013, First Financial Bank, a subsidiary of First Financial Corporation entered into a Purchase and Assumption Agreement with Bank of America, National Association. Under the terms of the Agreement, First Financial Bank will purchase certain assets and assume certain liabilities of 7 branch offices and 2 drive-up facilities of Bank of America in central and southern Illinois. Pursuant to the terms of the Agreement, First Financial Bank has agreed to assume approximately $250 million in deposit liabilities and to acquire approximately $2.3 million of loans, as well as real property, furniture, and other fixed operating assets associated with the branches. The agreement is expected to close in the third quarter of 2013. Regulatory approval is expected by the June 30, 2013.

10. Accumulated Other Comprehensive Income

The following table summarizes the changes within each classification of accumulated other comprehensive income for the three months ended March 31, 2013 and 2012.

(Dollar amounts in thousands)	Unrealized gains and Losses on available-for-sale Securities	2013 Retirement plans	Total
Beginning balance, January 1	$ 13,431	$(20,903)	$(7,472)
Change in other comprehensive income before reclassification	(1,665)	-	(1,665)
Amounts reclassified from accumulated other comprehensive income	(2)	214	212
Net Current period other comprehensive other income	(1,667)	214	(1,453)
Ending balance, March 31	$ 11,764	$(20,689)	$(8,925)

(Dollar amounts in thousands)	Unrealized gains and Losses on available-for-sale Securities	2012 Retirement plans	Total
Beginning balance, January 1	$ 12,740	$(23,234)	$(10,494)
Change in other comprehensive income before reclassification	368	-	368
Amounts reclassified from accumulated other comprehensive income	2	42	44
Net Current period other comprehensive other income	370	42	412
Ending balance, March 31	$ 13,110	$(23,192)	$(10,082)

(Dollar amounts in thousands)	Balance at 12/31/2012	Current Period Change	Balance at 3/31/2013
Unrealized gains (losses) on securities available-for-sale without other than temporary impairment	$ 17,044	$(1,883)	$ 15,161
Unrealized gains (losses) on securities available-for-sale with other than temporary impairment	(3,613)	216	(3,397)
Total unrealized loss on securities available-for-sale	$ 13,431	$(1,667)	$ 11,764
Unrealized loss on retirement plans	(20,903)	214	(20,689)
TOTAL	$ (7,472)	$(1,453)	$ (8,925)

(Dollar amounts in thousands)	Balance at 12/31/2011	Current Period Change	Balance at 3/31/2012
Unrealized gains (losses) on securities available-for-sale without other than temporary impairment	$ 18,136	$ 367	$ 18,503
Unrealized gains (losses) on securities available-for-sale with other than temporary impairment	(5,396)	3	(5,393)
Total unrealized loss on securities available-for-sale	$ 12,740	$ 370	$ 13,110
Unrealized loss on retirement plans	(23,234)	42	(23,192)
TOTAL	$ (10,494)	$ 412	$ (10,082)

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Details about accumulated other comprehensive income components	2013 Amount reclassified from accumulated other comprehensive income (in thousands)	Affected line item in the statement where net income is presented
Unrealized gains and losses on available-for-sale securities	$ 4	Net securities gains (losses)
	(2)	Income tax expense
	$ 2	Net of tax
Amortization of retirement plan items	$ (357)(a)	
	143	Income tax expense
	$ (214)	Net of tax
Total reclassifications for the period	$ (212)	Net of tax

(a) Included in the computation of net periodic benefit cost. (see Footnoe 7 for additional details).

Details about accumulated other comprehensive income components	2012 Amount reclassified from accumulated other comprehensive income (in thousands)	Affected line item in the statement where net income is presented
Unrealized gains and losses on available-for-sale securities	$ (4)	Net securities gains (losses)
	2	Income tax expense
	$ (2)	Net of tax
Amortization of retirement plan items	$ (70)(a)	
	28	Income tax expense
	$ (42)	Net of tax
Total reclassifications for the period	$ (44)	Net of tax

(a) Included in the computation of net periodic benefit cost. (see Footnoe 7 for additional details).

ITEMS 2. and 3. Management's Discussion and Analysis of Financial Condition and Results of Operations and Quantitative and Qualitative Disclosures About Market Risk

The purpose of this discussion is to point out key factors in the Corporation's recent performance compared with earlier periods. The discussion should be read in conjunction with the financial statements beginning on page three of this report. All figures are for the consolidated entities. It is presumed the readers of these financial statements and of the following narrative have previously read the Corporation's financial statements in the 10-K filed for the fiscal year ended December 31, 2012.

This Quarterly Report on Form 10-Q contains forward-looking statements. Forward-looking statements provide current expectations or forecasts of future events and are not guarantees of future performance, nor should they be relied upon as representing management's views as of any subsequent date. The forward-looking statements are based on management's expectations and are subject to a number of risks and uncertainties. Although management believes that the expectations reflected in such forward-looking statements are reasonable, actual results may differ materially from those expressed or implied in such statements. Risks and uncertainties that could cause actual results to differ materially include, without limitation, the Corporation's ability to effectively execute its business plans; changes in general economic and financial market conditions; changes in interest rates; changes in the competitive environment; continuing consolidation in the financial services industry; new litigation or changes in existing litigation; losses, customer bankruptcy, claims and assessments; changes in banking regulations or other regulatory or legislative requirements affecting the Corporation's business; and changes in accounting policies or procedures as may be required by the Financial Accounting Standards Board or other regulatory agencies. Additional information concerning factors that could cause actual results to differ materially from those expressed or implied in the forward-looking statements is available in the Corporation's Form 10-K for the year ended December 31, 2012, and subsequent filings with the United States Securities and Exchange Commission (SEC). Copies of these filings are available at no cost on the SEC's Web site at www.sec.gov or on the Corporation's Web site at www.first-online.com. Management may elect to update forward-looking statements at some future point; however, it specifically disclaims any obligation to do so.

Critical Accounting Policies

Certain of the Corporation's accounting policies are important to the portrayal of the Corporation's financial condition and results of operations, since they require management to make difficult, complex or subjective judgments, some of which may relate to matters that are inherently uncertain. Estimates associated with these policies are susceptible to material changes as a result of changes in facts and circumstances. Facts and circumstances which could affect these judgments include, without limitation, changes in interest rates, in the performance of the economy or in the financial condition of borrowers. Management believes that its critical accounting policies include determining the allowance for loan losses and the valuation of goodwill and valuing investment securities. See further discussion of these critical accounting policies in the 2012 Form 10-K.

Summary of Operating Results

Net income for the three months ended March 31, 2013 was $7.7 million compared to $7.4 million for the same period of 2012. Basic earnings per share increased to $0.58 for the first quarter of 2013 compared to $0.56 for same period of 2012. Return on Assets and Return on Equity were 1.05% and 8.21% respectively for the three months ended March 31, 2013, compared to 1.02%and 8.46% for the three months ended March 31, 2012.

The primary components of income and expense affecting net income are discussed in the following analysis.

Net Interest Income

The Corporation's primary source of earnings is net interest income, which is the difference between the interest earned on loans and other investments and the interest paid for deposits and other sources of funds. Net interest income decreased $992 thousand in the three months ended March 31, 2013 to $26.2 million from $27.2 million in the same period in 2012. The net interest margin for the first three months of 2013 is 4.09% compared to 4.26% for the same period of 2012, a 4.0% decrease, driven by a greater decline in the rates of return on earning assets than the decrease in funding costs.

Non-Interest Income

Non-interest income for the three months ended March 31, 2013 was $9.9 million compared to the $9.5 million for the same period of 2012. Trust fees, insurance commissions, deposit fees and electronic banking income were all increased in the first quarter of 2013 compared to the same period of 2012.

Non-Interest Expenses

The Corporation’s non-interest expense for the quarter ended March 31, 2013 decreased by $1.2 million compared to the same period in 2012. Reduced personnel expense of $823 thousand was the primary contributor to the decrease as efficiencies are being realized from the acquisition of Freestar Bank on December 30, 2011.

Allowance for Loan Losses

The Corporation's provision for loan losses was virtually the same at $3.0 million with an increase of $65 thousand for the first quarter of 2013 compared to the same period of 2012. Net charge-offs decreased $4.4 million for the three months ended March 31, 2013 compared to the same period of 2012 resulting in net recoveries. Recoveries for the three months ended March 31, 2013 were $2.8 million. The allowance for loan losses increased to 1.39% of gross loans, or $25.3 million at March 31, 2013 compared to 1.19% of gross loans, or $21.9 million at December 31, 2012. While non-performing trends have remained stable, the increase in the allowance allocated to loans individually evaluated for impairment of $3.2 million since December 31, 2012 resulted in a higher overall allowance for loan losses in the current period. Based on management's analysis of the current portfolio, an evaluation that includes consideration of historical loss experience, non-performing loans trends, and probable incurred losses on identified problem loans, management believes the allowance is adequate.

Non-performing Loans

Non-performing loans consist of (1) non-accrual loans on which the ultimate collectability of the full amount of interest is uncertain, (2) loans which have been renegotiated to provide for a reduction or deferral of interest or principal because of a deterioration in the financial position of the borrower, and (3) loans past due ninety days or more as to principal or interest. A summary of non-performing loans at March 31, 2013 and December 31, 2012 follows:

	(000's) March 31, 2013	December 31, 2012
Non-accrual loans	$38,132	$ 36,794
Restructured loans	19,317	19,671
Accruing loans past due over 90 days	1,262	3,362
	$58,711	$ 59,827
Ratio of the allowance for loan losses as a percentage of non-performing loans	43.0 %	36.7 %

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The following loan categories comprise significant components of the nonperforming loans:

	(000's) March 31,	December 31,
Non-accrual loans	2013	2012
Commercial loans	$22,672	$ 21,900
Residential loans	13,786	13,201
Consumer loans	1,674	1,693
	$38,132	$ 36,794
Past due 90 days or more		
Commercial loans	$437	$ 1,481
Residential loans	751	1,750
Consumer loans	74	131
	$1,262	$ 3,362

The following table presents covered non-accrual loans at March 31, 2013 and December 31, 2012 that were from the acquisition of assets from The First National Bank of Danville, which are also included in the table above.

	(000's) March 31,	December 31,
Non-accrual loans	2013	2012
Commercial loans	$3,407	$ 4,114
Residential loans	277	217
Consumer loans	-	-
	$3,684	$ 4,331

Interest Rate Sensitivity and Liquidity

First Financial Corporation has established risk measures, limits and policy guidelines for managing interest rate risk and liquidity. Responsibility for management of these functions resides with the Asset Liability Committee. The primary goal of the Asset Liability Committee is to maximize net interest income within the interest rate risk limits approved by the Board of Directors.

Interest Rate Risk

Management considers interest rate risk to be the Corporation's most significant market risk. Interest rate risk is the exposure to changes in net interest income as a result of changes in interest rates. Consistency in the Corporation's net interest income is largely dependent on the effective management of this risk.

The Asset Liability position is measured using sophisticated risk management tools, including earning simulation and market value of equity sensitivity analysis. These tools allow management to quantify and monitor both short-term and long-term exposure to interest rate risk. Simulation modeling measures the effects of changes in interest rates, changes in the shape of the yield curve and the effects of embedded options on net interest income. This measure projects earnings in the various environments over the next three years. It is important to note that measures of interest rate risk have limitations and are dependent on various assumptions. These assumptions are inherently uncertain and, as a result, the model cannot precisely predict the impact of interest rate fluctuations on net interest income. Actual results will differ from simulated results due to timing, frequency and amount of interest rate changes as well as overall market conditions. The Committee has performed a thorough analysis of these assumptions and believes them to be valid and theoretically sound. These assumptions are continuously monitored for behavioral changes.

The Corporation from time to time utilizes derivatives to manage interest rate risk. Management continuously evaluates the merits of such interest rate risk products but does not anticipate the use of such products to become a major part of the Corporation's risk management strategy.

The table below shows the Corporation's estimated sensitivity profile as of March 31, 2013. The change in interest rates assumes a parallel shift in interest rates of 100 and 200 basis points. Given a 100 basis point increase in rates, net interest income would increase 3.07% over the next 12 months and increase 6.02% over the following 12 months. Given a 100 basis point decrease in rates, net interest income would decrease 1.97% over the next 12 months and decrease 4.91% over the following 12 months. These estimates assume all rate changes occur overnight and management takes no action as a result of this change.

Basis Point	Percentage Change in Net Interest Income					
Interest Rate Change	12 months		24 months		36 months	
Down 200	-2.76	%	-7.34	%	-10.51	%
Down 100	-1.97		-4.91		-6.93	