

FIRST BANCSHARES INC /MS/
Form 10-Q
August 14, 2013

U. S. SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D. C. 20549

FORM 10-Q

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

FOR THE QUARTERLY PERIOD ENDED: June 30, 2013

OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15 (D)
OF THE SECURITIES EXCHANGE ACT OF 1934

COMMISSION FILE NUMBER: 33-94288

THE FIRST BANCSHARES, INC.

(EXACT NAME OF ISSUER AS SPECIFIED IN ITS CHARTER)

MISSISSIPPI 64-0862173
(STATE OF INCORPORATION) (I.R.S. EMPLOYER IDENTIFICATION NO.)

6480 U.S. HIGHWAY 98 WEST
HATTIESBURG, MISSISSIPPI 39402
(ADDRESS OF PRINCIPAL EXECUTIVE OFFICES) (ZIP CODE)

(601) 268-8998

(ISSUER'S TELEPHONE NUMBER, INCLUDING AREA CODE)

NONE

(FORMER NAME, ADDRESS AND FISCAL YEAR, IF CHANGED SINCE LAST REPORT)

INDICATE BY CHECK MARK WHETHER THE ISSUER: (1) HAS FILED ALL REPORTS REQUIRED TO BE FILED BY SECTION 13 OR 15 (D) OF THE SECURITIES EXCHANGE ACT OF 1934 DURING THE PRECEDING 12 MONTHS (OR FOR SUCH SHORTER PERIOD THAT THE REGISTRANT WAS REQUIRED TO FILE SUCH REPORTS), AND (2) HAS BEEN SUBJECT TO SUCH FILING REQUIREMENTS FOR THE PAST 90 DAYS.

YES NO

INDICATE BY CHECK MARK WHETHER THE REGISTRANT IS A LARGE ACCELERATED FILER, AN ACCELERATED FILER, OR A NON-ACCELERATED FILER. SEE DEFINITION OF "ACCELERATED FILER AND LARGE ACCELERATED FILER" IN RULE 12B-2 OF THE EXCHANGE ACT.

LARGE ACCELERATED FILER ACCELERATED FILER NON-ACCELERATED FILER

ON June 30, 2013, 5,093,455 SHARES OF THE ISSUER'S COMMON STOCK, PAR VALUE \$1.00 PER SHARE, WERE ISSUED AND OUTSTANDING.

TRANSITIONAL DISCLOSURE FORMAT (CHECK ONE):

YES NO

INDICATE BY CHECK MARK WHETHER THE REGISTRANT IS A SHELL COMPANY (AS DEFINED IN RULE 12B-2 OF THE EXCHANGE ACT): YES NO

PART I - FINANCIAL INFORMATION

ITEM NO. 1. FINANCIAL STATEMENTS

THE FIRST BANCSHARES, INC.

CONSOLIDATED BALANCE SHEETS

(\$ amounts in thousands)

	(Unaudited)	
	June 30, 2013	December 31, 2012
ASSETS		
Cash and due from banks	\$ 27,811	\$ 20,225
Interest-bearing deposits with banks	49,089	9,588
Federal funds sold	4,941	1,064
Total cash and cash equivalents	81,841	30,877
Securities held-to-maturity, at amortized cost	8,455	8,470
Securities available-for-sale, at fair value	248,030	214,393
Other securities	4,101	3,438
Total securities	260,586	226,301
Loans held for sale	2,933	5,586
Loans	554,838	408,112
Allowance for loan losses	(5,393)	(4,727)
Loans, net	552,378	408,971
Premises and equipment	32,696	22,243
Interest receivable	3,263	2,887
Cash surrender value of life insurance	6,513	6,441
Goodwill	10,713	9,362
Other assets	11,760	7,522

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Other real estate owned	5,687	6,782
TOTAL ASSETS	\$ 965,437	\$ 721,386
LIABILITIES AND STOCKHOLDERS' EQUITY		
LIABILITIES:		
Deposits:		
Noninterest-bearing	\$ 182,324	\$ 109,625
Interest-bearing	661,015	487,002
TOTAL DEPOSITS	843,339	596,627
Interest payable	470	212
Borrowed funds	16,500	36,771
Subordinated debentures	10,310	10,310
Other liabilities	12,201	11,580
TOTAL LIABILITIES	882,820	655,500
STOCKHOLDERS' EQUITY:		
Preferred stock, no par value, \$1,000 per share liquidation, 10,000,000 shares authorized; 17,123 issued and outstanding at June 30, 2013 and December 31, 2012, respectively	17,062	17,021
Common stock, par value \$1 per share, 10,000,000 shares authorized; 5,119,949 shares issued at June 30, 2013 and 3,133,596 at December 31, 2012, respectively	5,120	3,134
Additional paid-in capital	41,902	23,711
Retained earnings	20,538	19,951
Accumulated other comprehensive income (loss)	(1,541)	2,533
Treasury stock, at cost, 26,494 shares at June 30, 2013 and at December 31, 2012	(464)	(464)
TOTAL STOCKHOLDERS' EQUITY	82,617	65,886
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	\$ 965,437	\$ 721,386

THE FIRST BANCSHARES, INC.

CONSOLIDATED STATEMENTS OF INCOME

(\$ amounts in thousands, except earnings and dividends per share)

	(Unaudited) Three Months Ended June 30,		(Unaudited) Six Months Ended June 30,	
	2013	2012	2013	2012
INTEREST INCOME:				
Interest and fees on loans	\$ 6,318	\$ 5,353	\$ 11,549	\$ 10,807
Interest and dividends on securities:				
Taxable interest and dividends	740	729	1,643	1,423
Tax exempt interest	529	507	1,033	1,014
Interest on federal funds sold	22	20	34	31
TOTAL INTEREST INCOME	7,609	6,609	14,259	13,275
INTEREST EXPENSE:				
Interest on deposits	666	834	1,284	1,726
Interest on borrowed funds	157	267	298	556
TOTAL INTEREST EXPENSE	823	1,101	1,582	2,282
NET INTEREST INCOME	6,786	5,508	12,677	10,993
PROVISION FOR LOAN LOSSES	349	221	660	373
NET INTEREST INCOME AFTER PROVISION FOR LOAN LOSSES	6,437	5,287	12,017	10,620
OTHER INCOME:				
Service charges on deposit accounts	1,010	857	1,854	1,727
Other service charges and fees	880	653	1,966	1,258
TOTAL OTHER INCOME	1,890	1,510	3,820	2,985
OTHER EXPENSES:				
Salaries and employee benefits	3,729	2,996	6,912	5,934

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Occupancy and equipment	1,104	949	2,060	1,909
Other	2,412	1,469	4,252	3,093
TOTAL OTHER EXPENSES	7,245	5,414	13,224	10,936
INCOME BEFORE INCOME TAXES	1,082	1,383	2,613	2,669
INCOME TAXES	270	346	576	661
NET INCOME	812	1,037	2,037	2,008
PREFERRED STOCK ACCRETION AND DIVIDENDS	106	106	212	212
NET INCOME APPLICABLE TO COMMON STOCKHOLDERS	\$ 706	\$ 931	\$ 1,825	\$ 1,796
NET INCOME APPLICABLE TO COMMON STOCKHOLDERS:				
BASIC	\$.18	\$.30	\$.52	\$.58
DILUTED	.18	.30	.51	.58
DIVIDENDS PER SHARE – COMMON	.0375	.0375	.075	.075

THE FIRST BANCSHARES, INC.

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(\$ amounts in thousands)

	(Unaudited) Three Months Ended June 30,		(Unaudited) Six Months Ended June 30,	
	2013	2012	2013	2012
Net income per consolidated statements of income	\$ 812	\$ 1,037	\$ 2,037	\$ 2,008
Other comprehensive income:				
Unrealized holding gains (losses) arising during the period on available-for-sale securities	(6,174)	1,167	(6,068)	1,723
Unrealized holding gains (losses) on loans held for sale	(123)	64	(105)	36
Income tax benefit (expense)	2,140	(419)	2,099	(598)
Other Comprehensive Income (Loss)	(4,157)	812	(4,074)	1,161
Comprehensive Income (Loss)	\$ (3,345)	\$ 1,849	\$ (2,037)	\$ 3,169

THE FIRST BANCSHARES, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY

(unaudited)

(\$ in thousands)

	Accumulated							Total
	Common Stock	Preferred Stock	Stock Warrants	Additional Paid-in Capital	Retained Earnings	Other Compre- hensive Income(Loss)	Treasury Stock	
Balance, January 1, 2012	\$ 3,093	\$ 16,939	\$ 284	\$ 23,220	\$ 16,791	\$ 562	\$ (464)	\$ 60,425
Net income	-	-	-	-	2,008	-	-	2,008
Other compre- hensive income	-	-	-	-	-	1,161	-	1,161
Accretion and dividends on preferred stock	-	41	-	-	(212)	-	-	(171)
Dividends on common stock, \$.075 per share	-	-	-	-	(231)	-	-	(231)
Restricted stock grant	42	-	-	(42)	-	-	-	-
Compensation expense	-	-	-	108	-	-	-	108
Balance, June 30, 2012	\$ 3,135	\$ 16,980	\$ 284	\$ 23,286	\$ 18,356	\$ 1,723	\$ (464)	\$ 63,300
Balance, January 1, 2013	\$ 3,134	\$ 17,021	\$ 284	\$ 23,427	\$ 19,951	\$ 2,533	\$ (464)	\$ 65,886
Net income	-	-	-	-	2,037	-	-	2,037
Other compre- hensive income(loss)	-	-	-	-	-	(4,074)	-	(4,074)
Accretion and dividends on preferred stock	-	41	-	-	(212)	-	-	(171)
Dividends on common stock, \$.075 per share	-	-	-	-	(235)	-	-	(235)
Issuance of 1,951,220 common shares	1,951	-	-	18,049	(1,003)	-	-	18,997
Restricted stock grant	35	-	-	(35)	-	-	-	-
Compensation expense	-	-	-	177	-	-	-	177
Balance, June 30, 2013	\$ 5,120	\$ 17,062	\$ 284	\$ 41,618	\$ 20,538	\$ (1,541)	\$ (464)	\$ 82,617

THE FIRST BANCSHARES, INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS

(\$ Amounts in Thousands)

	(Unaudited)	
	Six Months Ended	
	June 30,	
	2013	2012
CASH FLOWS FROM OPERATING ACTIVITIES:		
NET INCOME	\$2,037	\$2,008
Adjustments to reconcile net income to net cash provided by operating activities: Depreciation, amortization and accretion	1,038	1,259
Provision for loan losses	660	373
Loss on sale/writedown of ORE	122	309
Restricted stock expense	177	108
Increase in cash value of life insurance	(72)	(88)
Federal Home Loan Bank stock dividends	(2)	(2)
Changes in:		
Interest receivable	(26)	(238)
Loans held for sale, net	3,584	(268)
Interest payable	(83)	(49)
Other, net	1,900	1,891
NET CASH PROVIDED BY OPERATING ACTIVITIES	9,335	5,303
CASH FLOWS FROM INVESTING ACTIVITIES:		
Cash received in excess of cash paid for acquisition	43,150	-
Maturities and calls of securities available- for-sale	38,146	24,455
Purchases of securities available-for-sale and held-to-maturity	(73,521)	(42,876)
Net purchases of other securities	(208)	(443)
Net increase in loans	(24,662)	(1,725)
Net additions in premises and equipment	(432)	(200)
NET CASH USED IN INVESTING ACTIVITIES	(17,527)	(20,789)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Increase in deposits	60,827	14,573
Net increase (decrease) in borrowed funds	(20,271)	1,259
Dividends paid on common stock	(226)	(226)
Dividends paid on preferred stock	(171)	(171)
Issuance of 1,951,220 common shares, net	18,997	-

NET CASH PROVIDED BY FINANCING ACTIVITIES	59,156	15,435
NET INCREASE (DECREASE) IN CASH	50,964	(51)
CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD	30,877	23,181
CASH AND CASH EQUIVALENTS AT END OF PERIOD	\$81,841	\$23,130

SUPPLEMENTAL DISCLOSURES:

CASH PAYMENTS FOR INTEREST	\$1,324	\$2,331
CASH PAYMENTS FOR INCOME TAXES	980	768
LOANS TRANSFERRED TO OTHER REAL ESTATE	1,437	4,142
ISSUANCE OF RESTRICTED STOCK GRANTS	35	42

THE FIRST BANCSHARES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

NOTE A — BASIS OF PRESENTATION

The accompanying unaudited consolidated financial statements have been prepared in accordance with generally accepted accounting principles for interim financial statements and with the instructions to Form 10-Q of the Securities and Exchange Commission. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. However, in the opinion of management, all adjustments (consisting of normal recurring adjustments) considered necessary for a fair presentation have been included. Operating results for the six months ended June 30, 2013, are not necessarily indicative of the results that may be expected for the year ending December 31, 2013. For further information, please refer to the consolidated financial statements and footnotes thereto included in the Company's Form 10-K for the year ended December 31, 2012.

NOTE B — SUMMARY OF ORGANIZATION

The First Bancshares, Inc., Hattiesburg, Mississippi (the "Company"), was incorporated June 23, 1995, under the laws of the State of Mississippi for the purpose of operating as a bank holding company. The Company's primary asset is its interest in its wholly-owned subsidiary, The First, A National Banking Association (the "Bank").

At June 30, 2013, the Company had approximately \$965.4 million in assets, \$552.4 million in loans, \$843.3 million in deposits, and \$82.6 million in stockholders' equity. For the six months ended June 30, 2013, the Company reported net income of \$2.0 million (\$1.8 million applicable to common stockholders).

In the first and second quarters of 2013, the Company declared and paid a dividend of \$.0375 per common share.

NOTE C – BUSINESS COMBINATION

The Company entered into an Acquisition Agreement dated January 31, 2013, as amended (the "Agreement") with First Baldwin Bancshares, Inc., an Alabama corporation ("Baldwin"). The Agreement provided that, based upon the terms and subject to the conditions set forth in the Agreement, the Company would acquire all of the outstanding shares (the "Acquisition") of Baldwin's wholly-owned subsidiary, First National Bank of Baldwin County, A National Banking Association ("FNB"). Subject to the terms and conditions of the Agreement, as amended, which was approved by both the Company's Board of Directors and the Board of Directors of Baldwin, on February 21, 2013, Baldwin filed a voluntary bankruptcy petition under Chapter 11 of the Bankruptcy Code in the United States Bankruptcy Court for the Southern District of Alabama ("Bankruptcy Court") and sought Bankruptcy Court approval of the Agreement and the Acquisition through a Chapter 11 plan. Upon approval by the Bankruptcy Court and consummation of the Acquisition, all outstanding FNB common stock would be sold to the Company for cash consideration of \$3,300,000 (the "Purchase Price"). Each outstanding share of FNB common stock will remain outstanding and be unaffected by the Acquisition.

The Company has recently completed its Acquisition of FNB. On April 23, 2013, the Bankruptcy Court confirmed the Chapter 11 Plan of Reorganization for Baldwin pursuant to which Baldwin had agreed to sell all of the outstanding voting stock of its subsidiary, FNB, under the Agreement. The Bankruptcy Court's approval received was the last required regulatory approval regarding the Acquisition. Previously, both the Board of Governors of the Federal Reserve System and the Office of the Comptroller of the Currency had granted the requisite approvals for the Acquisition by the Company of all of the outstanding voting stock of FNB on March 28, 2013, and April 4, 2013, respectively. The Acquisition closed and was completed on April 30, 2013. There was no vote required of shareholders of FNB to approve the Acquisition.

No further additional action or regulatory approval is required with respect to the Acquisition. As of the closing on April 30, 2013, FNB became a wholly-owned subsidiary of the Company and subsequently was merged with and into the Company's bank subsidiary, The First, A National Banking Association.

In connection with the acquisition, the Company recorded \$1.4 million of goodwill and \$.7 million of core deposit intangible. The core deposit intangible will be expensed over 10 years.

The Company acquired the \$124.2 million loan portfolio at a fair value discount of \$.5 million. The discount represents expected credit losses, adjustments to market interest rates and liquidity adjustments.

The amounts of the acquired identifiable assets and liabilities as of the acquisition date were as follows (dollars in thousands):

Purchase price:	
Cash	\$3,300
Total purchase price	3,300
Identifiable assets:	
Cash and due from banks	46,450
Investments	2,508
Loans and leases	124,165
Core deposit intangible	680
Personal and real property	10,655
Deferred tax asset	2,969
Other assets	1,029
Total assets	188,456
Liabilities and equity:	
Deposits	185,771
Other liabilities	736
Total liabilities	186,507

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Net assets acquired	1,949
Goodwill resulting from acquisition	\$1,351

In the second quarter interest income of \$978,000 was recorded on loans acquired. The outstanding principal balance and the carrying amount of these loans included in the consolidated balance sheet at June 30, 2013, are as follows (dollars in thousands):

7

Outstanding principal balance	\$120,246
Carrying amount	119,788

All loans obtained in the acquisition reflect no specific evidence of credit deterioration and very low probability that the Company would be unable to collect all contractually required principal and interest payments.

The amount of the revenue and earnings included in the Company's consolidated income statement for the six months ended June 30, 2013, reflect only amounts from the acquisition date of April 30, 2013, through the quarter end June 30, 2013. Historical financial information related to each loan and deposit acquired was impractical to determine due to retrospective application requiring significant estimates of amounts that cannot be independently substantiated. Further, we believe it is impossible to distinguish objectively information about those estimates that provides evidence of circumstances that existed on the dates at which those amounts would be recognized and measured under retrospective application.

Expenses associated with the acquisition were \$635,500 and \$976,500 for the three and six month periods ended June 30, 2013, respectively. These costs included system conversion and integrating operations charges as well as legal and consulting expenses, which have been expensed as incurred.

NOTE D – PREFERRED STOCK AND WARRANT

On February 6, 2009, as part of the U.S. Department of Treasury's ("Treasury") Capital Purchase Program ("CPP"), the Company received a \$5.0 million equity investment by issuing 5 thousand shares of Series A, no par value preferred stock to the Treasury pursuant to a Letter Agreement and Securities Purchase Agreement that was previously disclosed by the Company. The Company also issued a warrant to the Treasury allowing it to purchase 54,705 shares of the Company's common stock at an exercise price of \$13.71. The warrant can be exercised immediately and has a term of 10 years.

The Company allocated the proceeds received from the Treasury, net of transaction costs, on a pro rata basis to the Series A preferred stock and the warrant based on their relative fair values. The Company assigned \$.3 million and \$4.7 million to the warrant and the Series A preferred stock, respectively. The resulting discount on the Series A preferred stock is being accreted up to the \$5.0 million liquidation amount at the time of the exchange that is described in the following paragraphs.

On September 29, 2010, and pursuant to the terms of the letter agreement between the Company and the United States Department of the Treasury ("Treasury"), the Company closed a transaction whereby Treasury exchanged its 5,000

shares of Fixed Rate Cumulative Perpetual Preferred Stock, Series UST, (the “CPP Preferred Shares”) for 5,000 shares of a new series of preferred stock designated Fixed Rate Cumulative Perpetual Preferred Stock, Series CD (the “CDCI Preferred Shares”). On the same day, and pursuant to the terms of the letter agreement between the Company and Treasury, the Company issued an additional 12,123 CDCI Preferred Shares to Treasury for a purchase price of \$12,123,000. As a result of the CDCI Transactions, the Company is no longer participating in the TARP Capital Purchase Program being administered by Treasury and is now participating in Treasury’s TARP Community Development Capital Initiative (the “CDCI”). The terms of the CDCI Transactions are more fully set forth in the Exchange Letter Agreement and the Purchase Letter Agreement.

The Letter Agreement, pursuant to which the Preferred Shares were exchanged, contains limitations on the payment of dividends on the common stock to no more than 100% of the aggregate per share dividend and distributions for the immediate prior fiscal year (dividends of \$0.15 per share were declared and paid in 2010, 2011, and 2012) and on the Company’s ability to repurchase its common stock, and continues to subject the Company to certain of the executive compensation limitations included in the Emergency Economic Stabilization Act of 2008 (EESA), as previously disclosed by the Company.

The most significant difference in terms between the CDCI Preferred Shares and the CPP Preferred Shares is the dividend rate applicable to each. The CPP Preferred Shares entitled the holder to an annual dividend of 5% increasing to 9% after 5 years of the liquidation value of the shares, payable quarterly in arrears; by contrast, the CDCI Preferred Shares entitle the holder to an annual dividend of 2% for 8 years of the liquidation value of the shares, payable quarterly in arrears. Other differences in terms between the CDCI Preferred Shares and the CPP Preferred Shares, including, without limitation, the restrictions on common stock dividends and on redemption of common stock and other securities exist. The terms of the CDCI Preferred Shares are more fully set forth in the Articles of Amendment creating the CDCI Preferred Shares, which Articles of Amendment were filed with the Mississippi Secretary of State on September 27, 2010.

As a condition to participate in the CDCI, the Company was required to obtain certification as a Community Development Financial Institution (a "CDFI") from the Treasury's Community Development Financial Fund. On September 28, 2010, the Company was notified that its application for CDFI certification had been approved. In order to become certified and maintain its certification as a CDFI, the Company is required to meet the CDFI eligibility requirements set forth in 12 C.F.R. 1805.201(b).

On March 22, 2013, the Company raised \$20,000,005 in a private placement of 1,951,220 shares of newly authorized Series D Nonvoting Convertible Preferred Stock ("Convertible Preferred Stock") at a purchase price of \$10.25 per share. The terms of the Convertible Preferred Stock provide for mandatory conversion into the Company's common stock upon approval, which occurred at the annual meeting, May 23, 2013. The Company paid \$921,487.43 in fees to its financial advisors who acted as placement agents in the private placement.

The Company intends to use the net proceeds from the private placement to increase its equity capital and for general corporate purposes, which includes, among other things, support for organic and acquisition-based growth. The private placement was exempt from Securities and Exchange Commission registration pursuant to Section 4(2) of the Securities Act of 1933, as amended, and Rule 506 of Regulation D promulgated thereunder.

Upon conversion of the Convertible Preferred Stock, the Company issued 1,951,220 shares of common stock. On June 30, 2013, the Company had 5,093,455 shares of common stock outstanding, excluding treasury shares.

NOTE E — EARNINGS APPLICABLE TO COMMON STOCKHOLDERS

Basic per share data is calculated based on the weighted-average number of common shares outstanding during the reporting period. Diluted per share data includes any dilution from potential common stock outstanding, such as stock options.

For the Three Months Ended
June 30, 2013

	Net Income (Numerator)	Shares (Denominator)	Per Share Data
Basic per share	\$ 706,000	3,955,243	\$.18
Effect of dilutive shares: Restricted stock grants		46,238	
Diluted per share	\$ 706,000	4,001,481	\$.18

For the Six Months Ended
June 30, 2013

	Net Income (Numerator)	Shares (Denominator)	Per Share Data
Basic per share	\$ 1,825,000	3,536,362	\$.52
Effect of dilutive shares: Restricted stock grants		46,238	
Diluted per share	\$ 1,825,000	3,582,600	\$.51

For the Three Months Ended
June 30, 2012

	Net Income (Numerator)	Shares (Denominator)	Per Share Data
Basic per share	\$ 931,000	3,108,867	\$.30
Effect of dilutive shares: Restricted stock grants		21,557	
Diluted per share	\$ 931,000	3,130,424	\$.30

For the Six Months Ended
June 30, 2012

	Net Income (Numerator)	Shares (Denominator)	Per Share Data
--	------------------------------	-------------------------	-------------------

Basic per share	\$ 1,796,000	3,094,102	\$.58
Effect of dilutive shares:			
Restricted stock grants		21,557	
Diluted per share	\$ 1,796,000	3,115,659	\$.58

The Company granted 35,133 shares of restricted stock in the first quarter of 2013 and 42,795 shares of restricted stock in the first quarter of 2012.

NOTE F — FAIR VALUE OF ASSETS AND LIABILITIES

The Company groups its financial assets measured at fair value in three levels, based on the markets in which the assets are traded and the reliability of the assumptions used to determine fair value. These levels are:

Level 1: Valuations for assets and liabilities traded in active exchange markets, such as the New York Stock Exchange. Valuations are obtained from readily available pricing sources for market transactions involving identical assets or liabilities.

Level 2: Valuations for assets and liabilities traded in less active dealer or broker markets. Valuations are obtained from third party pricing services for identical or comparable assets or liabilities which use observable inputs other than Level 1 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 for substantially the full term of the assets and liabilities

Level 3: Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities.

Following is a description of the valuation methodologies used for instruments measured at fair value on a recurring basis and recognized in the accompanying balance sheets.

Available-for-Sale Securities

The fair value of available-for-sale securities is determined by various valuation methodologies. Where quoted market prices are available in an active market, securities are classified within Level 1. If quoted market prices are not available, then fair values are estimated by using pricing models or quoted prices of securities with similar characteristics. Level 2 securities include U.S. Treasury securities, obligations of U.S. government corporations and agencies, obligations of states and political subdivisions, mortgage-backed securities and collateralized mortgage obligations. In certain cases where Level 1 or Level 2 inputs are not available, securities are classified within Level 3 of the hierarchy.

The following table presents the Company's assets that are measured at fair value on a recurring basis and the level within the hierarchy in which the fair value measurements fell as of June 30, 2013 and December 31, 2012 (in thousands):

June 30, 2013

(Dollars in thousands)

		Fair Value Measurements Using		
		Quoted	Significant	
		Prices	Other	Significant
		in	Observable	Unobservable
		Active	Inputs	Inputs
		Markets		
		For		
		Identical		
		Assets		
	Fair Value	(Level	(Level 2)	(Level 3)
		1)		
Obligations of U. S. Government Agencies	\$ 27,671	\$ -	\$ 27,671	\$ -
Municipal securities	113,068	-	113,068	-
Mortgage-backed securities	79,654	-	79,654	-
Corporate obligations	26,677	-	24,040	2,637
Other	960	960	-	-
Total	\$ 248,030	\$ 960	\$ 244,433	\$ 2,637

11

December 31, 2012

		Fair Value Measurements Using		
		Quoted Prices in Active Markets For Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
	Fair Value			
Obligations of U. S. Government Agencies	\$ 36,359	\$ -	\$ 36,359	\$ -
Municipal securities	98,910	-	98,910	-
Mortgage-backed securities	61,967	-	61,967	-
Corporate obligations	16,187	-	13,519	2,668
Other	970	970	-	-
Total	\$ 214,393	\$ 970	\$ 210,755	\$ 2,668

The following is a reconciliation of activity for assets measured at fair value based on significant unobservable (non-market) information.

	Bank-Issued Trust Preferred Securities	
	2013	2012
<i>(Dollars in thousands)</i>		
Balance, January 1	\$2,668	\$2,252
Transfers into Level 3	-	-
Transfers out of Level 3	-	-
Other-than-temporary impairment loss included in earnings	-	-
Unrealized gain (loss) included in comprehensive income	(31)	416
Balance at June 30, 2013 and December 31, 2012	\$2,637	\$2,668

Following is a description of the valuation methodologies used for assets measured at fair value on a non-recurring basis and recognized in the accompanying balance sheets, as well as the general classification of such assets pursuant to the valuation hierarchy.

Impaired Loans

Loans for which it is probable that the Company will not collect all principal and interest due according to contractual terms are measured for impairment. Allowable methods for estimating fair value include using the fair value of the collateral for collateral dependent loans or, where a loan is determined not to be collateral dependent, using the discounted cash flow method.

If the impaired loan is identified as collateral dependent, then the fair value method of measuring the amount of impairment is utilized. This method requires obtaining a current independent appraisal of the collateral and applying a discount factor to the value. If the impaired loan is determined not to be collateral dependent, then the discounted cash flow method is used. This method requires the impaired loan to be recorded at the present value of expected future cash flows discounted at the loan's effective interest rate. The effective interest rate of a loan is the contractual interest rate adjusted for any net deferred loan fees or costs, or premium or discount existing at origination or acquisition of the loan. Impaired loans are classified within Level 2 of the fair value hierarchy.

Other Real Estate Owned

Other real estate owned acquired through loan foreclosure is initially recorded at fair value less estimated costs to sell, establishing a new cost basis. The adjustment at the time of foreclosure is recorded through the allowance for loan losses. Due to the subjective nature of establishing the fair value, the actual fair value of the other real estate owned or foreclosed asset could differ from the original estimate. If it is determined the fair value declines subsequent to foreclosure, a valuation allowance is recorded through non-interest expense. Operating costs associated with the assets are also recorded as non-interest expense. Gains and losses on the disposition of other real estate owned and foreclosed assets are netted and posted to other non-interest expense. Other real estate owned measured at fair value on a non-recurring basis at June 30, 2013, amounted to \$5.7 million. Other real estate owned is classified within Level 2 of the fair value hierarchy.

The following table presents the fair value measurement of assets measured at fair value on a nonrecurring basis and the level within the fair value hierarchy in which the fair value measurements fell at June 30, 2013 and December 31, 2012.

(\$ in thousands)

June 30, 2013

		Fair Value Measurements Using		
		Quoted		
		Prices		
		in	Significant	Significant
		Active	Other	Unobservable
		Markets	Observable	Inputs
		For	Inputs	
		Identical		
		Assets		
	Fair Value	(Level	(Level 2)	(Level 3)
		1)		
Impaired loans	\$ 4,063	\$ -	\$ 4,063	\$ -
Other real estate owned	5,687	-	5,687	-

December 31, 2012

	Fair Value	Fair Value Measurements Using		
		Quoted Prices in Active Markets For Identical Assets	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Impaired loans	\$ 3,589	\$ -	\$ 3,589	\$ -
Other real estate owned	6,782	-	6,782	-

The following methods and assumptions were used to estimate the fair value of each class of financial instrument for which it is practicable to estimate that value:

Cash and Cash Equivalents – For such short-term instruments, the carrying amount is a reasonable estimate of fair value.

Investment in securities available-for-sale and held-to-maturity – The fair value measurement for securities available-for-sale was discussed earlier. The same measurement approach was used for securities held-to-maturity.

Loans – The fair value of loans is estimated by discounting the future cash flows using the current rates at which similar loans would be made to borrowers with similar credit ratings and for the same remaining maturities.

Deposits – The fair values of demand deposits are, as required by ASC Topic 825, equal to the carrying value of such deposits. Demand deposits include noninterest-bearing demand deposits, savings accounts, NOW accounts, and money market demand accounts. The fair value of variable rate term deposits, those repricing within six months or less, approximates the carrying value of these deposits. Discounted cash flows have been used to value fixed rate term deposits and variable rate term deposits repricing after six months. The discount rate used is based on interest rates currently being offered on comparable deposits as to amount and term.

Short-Term Borrowings – The carrying value of any federal funds purchased and other short-term borrowings approximates their fair values.

FHLB and Other Borrowings – The fair value of the fixed rate borrowings are estimated using discounted cash flows, based on current incremental borrowing rates for similar types of borrowing arrangements. The carrying amount of any variable rate borrowing approximates its fair value.

Subordinated Debentures – The subordinated debentures bear interest at a variable rate and the carrying value approximates the fair value.

Off-Balance Sheet Instruments – Fair values of off-balance sheet financial instruments are based on fees charged to enter into similar agreements. However, commitments to extend credit do not represent a significant value until such commitments are funded or closed. Management has determined that these instruments do not have a distinguishable fair value and no fair value has been assigned.

	As of June 30, 2013		As of December 31, 2012	
	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
(In thousands)				
Financial Instruments:				
Assets:				
Cash and cash equivalents	\$81,841	\$81,841	\$30,877	\$30,877
Securities available-for-sale	248,030	248,030	214,393	214,393
Securities held-to-maturity	8,455	9,430	8,470	7,055
Other securities	4,101	4,101	3,438	3,438
Loans, net	552,378	567,780	408,971	422,029
Liabilities:				
Noninterest-bearing deposits	\$182,324	\$182,324	\$109,625	\$109,625
Interest-bearing deposits	661,015	660,894	487,002	487,599
Subordinated debentures	10,310	10,310	10,310	10,310
FHLB and other borrowings	16,500	16,500	36,771	36,771

NOTE G — LOANS

Loans typically provide higher yields than the other types of earning assets, and, thus, one of the Company's goals is for loans to be the largest category of the Company's earning assets. At June 30, 2013 and December 31, 2012, loans accounted for 63.9% and 63.6% of earning assets, respectively. The Company controls and mitigates the inherent credit and liquidity risks through the composition of its loan portfolio.

The following table shows the composition of the loan portfolio by category:

Composition of Loan Portfolio

June 30, 2013		December 31, 2012	
Amount	Percent	Amount	Percent
	of		of
	Total		Total
(Dollars in thousands)			

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Mortgage loans held for sale	\$2,933	0.5	%	\$ 5,586	1.4	%
Commercial, financial and agricultural	69,376	12.4		53,234	12.9	
Real Estate:						
Mortgage-commercial	186,219	33.4		142,046	34.3	
Mortgage-residential	210,543	37.7		140,703	34.0	
Construction	72,349	12.9		57,529	13.9	
Consumer and other	16,351	3.1		14,600	3.5	
Total loans	557,771	100	%	413,698	100	%
Allowance for loan losses	(5,393)			(4,727)		
Net loans	\$552,378			\$ 408,971		

In the context of this discussion, a "real estate mortgage loan" is defined as any loan, other than a loan for construction purposes, secured by real estate, regardless of the purpose of the loan. The Company follows the common practice of financial institutions in the Company's market area of obtaining a security interest in real estate whenever possible, in addition to any other available collateral. This collateral is taken to reinforce the likelihood of the ultimate repayment of the loan and tends to increase the magnitude of the real estate loan portfolio component. Generally, the Company limits its loan-to-value ratio to 80%. Management attempts to maintain a conservative philosophy regarding its underwriting guidelines and believes it will reduce the risk elements of its loan portfolio through strategies that diversify the lending mix.

Loans held for sale consists of mortgage loans originated by the Bank and sold into the secondary market. Commitments from investors to purchase the loans are obtained upon origination.

Activity in the allowance for loan losses for the period is as follows:

(In thousands)

	Three Months Ended June 30, 2013	Six Months Ended June 30, 2013
Balance at beginning of period	\$ 4,918	\$ 4,727
Loans charged-off:		
Real Estate	(276)	(306)
Installment and Other	(75)	(130)
Commercial, Financial and Agriculture	(4)	(70)
Total	(355)	(506)
Recoveries on loans previously charged-off:		
Real Estate	461	465
Installment and Other	18	39
Commercial, Financial and Agriculture	2	8
Total	481	512
Net recoveries	126	6
Provision for Loan Losses	349	660
Balance at end of period	\$ 5,393	\$ 5,393

The following tables represent how the allowance for loan losses is allocated to a particular loan type, as well as the percentage of the category to total loans at June 30, 2013 and December 31, 2012.

Allocation of the Allowance for Loan Losses

June 30, 2013 (Dollars in thousands)			
	Amount	% of loans in each category to total loans	
Commercial Non Real Estate	\$ 457	12.7	%
Commercial Real Estate	3,328	57.7	
Consumer Real Estate	1,228	26.4	
Consumer	195	3.2	
Unallocated	185	-	
Total	\$ 5,393	100	%

December 31, 2012 (Dollars in thousands)			
	Amount	% of loans in each category to total loans	
Commercial Non Real Estate	\$ 420	13.3	%
Commercial Real Estate	3,338	63.7	
Consumer Real Estate	810	19.0	
Consumer	151	4.0	
Unallocated	8	-	
Total	\$ 4,727	100	%

The following table represents the Company's impaired loans at June 30, 2013, and December 31, 2012.

	June 30, December 31, 2013 2012 (In thousands)	
Impaired Loans:		
Impaired loans without a valuation allowance	\$2,031	\$ 1,445
Impaired loans with a valuation allowance	2,032	2,144

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Total impaired loans	\$4,063	\$ 3,589
Allowance for loan losses on impaired loans at period end	757	936
Total nonaccrual loans	1,886	3,401
Past due 90 days or more and still accruing	352	158
Average investment in impaired loans	6,612	2,979

The following table is a summary of interest recognized and cash-basis interest earned on impaired loans:

	Three Months Ended June 30, 2013	Six Months Ended June 30, 2013
Average of individually impaired loans during period	5,900	6,086
Interest income recognized during impairment	13	29
Cash-basis interest income recognized	15	65

The gross interest income that would have been recorded in the period that ended if the nonaccrual loans had been current in accordance with their original terms and had been outstanding throughout the period or since origination, if held for part of the three and six months ended June 30, 2013, was \$23,300 and \$90,900, respectively. The Company had no loan commitments to borrowers in non-accrual status at June 30, 2013 and 2012.

The following tables provide the ending balances in the Company's loans (excluding mortgage loans held for sale) and allowance for loan losses, broken down by portfolio segment as of June 30, 2013 and December 31, 2012. The tables also provide additional detail as to the amount of our loans and allowance that correspond to individual versus collective impairment evaluation. The impairment evaluation corresponds to the Company's systematic methodology for estimating its Allowance for Loan Losses.

June 30, 2013

	Real Estate (In thousands)	Installment and Other	Commercial, Financial and Agriculture	Total
Loans				
Individually evaluated	\$3,238	\$ 44	\$ 1,241	\$4,523
Collectively evaluated	462,720	19,460	68,135	550,315
Total	\$465,958	\$ 19,504	\$ 69,376	\$554,838
Allowance for Loan Losses				
Individually evaluated	\$681	\$ 38	\$ 38	\$757
Collectively evaluated	3,875	342	419	4,636
Total	\$4,556	\$ 380	\$ 457	\$5,393

December 31, 2012

	Real Estate (In thousands)	Installment and Other	Commercial, Financial and Agriculture	Total
Loans				
Individually evaluated	\$4,111	\$ 55	\$ 221	\$4,387
Collectively evaluated	333,299	16,401	54,025	403,725
Total	\$337,410	\$ 16,456	\$ 54,246	\$408,112

Allowance for Loan Losses

Individually evaluated	\$917	\$ 110	\$ 76	\$1,103
Collectively evaluated	3,231	49	344	3,624
Total	\$4,148	\$ 159	\$ 420	\$4,727

The following tables provide additional detail of impaired loans broken out according to class as of June 30, 2013 and December 31, 2012. The recorded investment included in the following table represents customer balances net of any partial charge-offs recognized on the loans, net of any deferred fees and costs. As nearly all of our impaired loans at June 30, 2013, are on nonaccrual status, recorded investment excludes any insignificant amount of accrued interest receivable on loans 90-days or more past due and still accruing. The unpaid balance represents the recorded balance prior to any partial charge-offs.

June 30, 2013

	Recorded Investment (In thousands)	Unpaid Balance	Related Allowance	Average Recorded Investment YTD	Interest Income Recognized YTD
Impaired loans with no related allowance:					
Commercial installment	\$12	\$12	\$ -	\$ 13	\$ -
Commercial real estate	908	1,036	-	3,139	17
Consumer real estate	1,105	1,105	-	1,167	21
Consumer installment	6	6	-	3	-
Total	\$2,031	\$2,159	\$ -	\$ 4,322	\$ 38
Impaired loans with a related allowance:					
Commercial installment	\$115	\$115	\$ 38	\$ 124	\$ 3
Commercial real estate	1,005	1,005	370	1,383	14
Consumer real estate	873	873	311	660	9
Consumer installment	39	39	38	44	1
Total	\$2,032	\$2,032	\$ 757	\$ 2,211	\$ 27
Total Impaired Loans:					
Commercial installment	\$127	\$127	\$ 38	\$ 137	\$ 3
Commercial real estate	1,913	2,041	370	4,522	31
Consumer real estate	1,978	1,978	311	1,827	30
Consumer installment	45	45	38	47	1
Total Impaired Loans	\$4,063	\$4,191	\$ 757	\$ 6,533	\$ 65

December 31, 2012

	Recorded Investment (In thousands)	Unpaid Balance	Related Allowance	Average Recorded Investment YTD	Interest Income Recognized YTD
Impaired loans with no related allowance:					
Commercial installment	\$ 15	\$ 15	\$ -	\$ 46	\$ -
Commercial real estate	1,013	1,529	-	1,004	39
Consumer real estate	106	969	-	168	8
Consumer installment	311	311	-	156	1
Total	\$ 1,445	\$ 2,824	\$ -	\$ 1,374	\$ 48
Impaired loans with a related allowance:					
Commercial installment	\$ 203	\$ 203	\$ 73	\$ 173	\$ 8
Commercial real estate	1,549	1,549	747	1,546	38
Consumer real estate	44	44	44	72	4
Consumer installment	348	348	72	197	2
Total	\$ 2,144	\$ 2,144	\$ 936	\$ 1,988	\$ 52
Total Impaired Loans:					
Commercial installment	\$ 218	\$ 218	\$ 73	\$ 219	\$ 8
Commercial real estate	2,562	3,078	747	2,550	77
Consumer real estate	150	1,013	44	240	12
Consumer installment	659	659	72	353	3
Total Impaired Loans	\$ 3,589	\$ 4,968	\$ 936	\$ 3,362	\$ 100

The following tables provide additional detail of troubled debt restructurings at June 30, 2013.

For the Three Months Ending June 30, 2013

	Outstanding Recorded Investment Pre-Modification	Outstanding Recorded Investment Post- Modification	Number of Loans	Interest Income Recognized
Commercial installment	\$ -	\$ -	-	\$ -
Commercial real estate	-	-	-	-
Consumer real estate	72	72	2	-
Consumer installment	-	-	-	-
Total	\$ 72	\$ 72	2	\$ -

For the Six Months Ending June 30, 2013

	Outstanding Recorded Investment Pre-Modification	Outstanding Recorded Investment Post- Modification	Number of Loans	Interest Income Recognized
Commercial installment	\$ -	\$ -	-	\$ -
Commercial real estate	-	-	-	-
Consumer real estate	249	249	3	-
Consumer installment	-	-	-	-
Total	\$ 249	\$ 249	3	\$ -

The recorded investment in receivables for which the allowance for credit losses was previously measured under a general allowance for credit losses methodology and are now impaired under Section 310-10-35 was \$249,000. The allowance for credit losses associated with those receivables on the basis of a current evaluation of loss was \$29,000. All loans were performing as agreed with modified terms.

During the three and six month periods ending June 30, 2013, there were 2 loans and 3 loans, respectively, modified as TDR, and are considered non-performing.

The following tables summarize by class our loans classified as past due in excess of 30 days or more in addition to those loans classified as non-accrual:

	June 30, 2013 (In thousands)		Non- Accrual	Total	
	Past Due 90 Days or More Days and Still Accruing	Past Due 30 to 89 Days		Past Due and Non- Accrual	Total Loans
Real Estate-construction	\$ 106	\$ -	\$ 56	\$ 162	\$72,349
Real Estate-mortgage	3,939	352	1,199	5,490	210,543

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Real Estate-non farm non residential	180	-	585	765	186,219
Commercial	133	-	44	177	69,376
Consumer	88	-	2	90	16,351
Total	\$4,446	\$ 352	\$ 1,886	\$ 6,684	\$554,838

21

	December 31, 2012 (In thousands)				
	Past Due 30 to 89 Days	Past Due 90 Days or More and Still Accruing	Non- Accrual	Total Past Due and Non- Accrual	Total Loans
Real Estate-construction	\$990	\$ -	\$ 1,667	\$ 2,657	\$57,529
Real Estate-mortgage	3,045	147	986	4,178	140,703
Real Estate-non farm non residential	389	-	608	997	142,046
Commercial	88	-	135	223	53,234
Consumer	132	11	5	148	14,600
Total	\$4,644	\$ 158	\$ 3,401	\$ 8,203	\$408,112

The Company 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 Company uses the following definitions for risk ratings, which are consistent with the definitions used in supervisory guidance:

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 Company's credit position at some future date.

Substandard. Loans classified as substandard are inadequately protected by the current net worth and paying capacity of the obligor or of the collateral pledged, if any. Loans so classified have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt. They are characterized by the distinct possibility that the institution will sustain some loss if the deficiencies are not corrected.

Doubtful. Loans classified as doubtful have all the weaknesses inherent in those classified as substandard, with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently existing facts, conditions, and values, highly questionable and improbable.

Loans not meeting the criteria above that are analyzed individually as part of the above described process are considered to be pass rated loans.

As of June 30, 2013 and December 31, 2012, and based on the most recent analysis performed, the risk category of loans by class of loans (excluding mortgage loans held for sale) was as follows:

(\$ in thousands)

June 30, 2013

	Real Estate Commercial	Real Estate Mortgage	Installment and Other	Commercial, Financial and Agriculture	Total
Pass	\$ 301,612	\$ 144,708	\$ 19,459	\$ 68,008	\$ 533,787
Special Mention	6,993	32	-	1,113	8,138
Substandard	11,017	1,950	45	273	13,285
Doubtful	-	-	-	-	-
Subtotal	319,622	146,690	19,504	69,394	555,210
Less:					
Unearned discount	213	141	-	18	372
Loans, net of unearned discount	\$ 319,409	\$ 146,549	\$ 19,504	\$ 69,376	\$ 554,838

December 31, 2012

	Real Estate Commercial	Real Estate Mortgage	Installment and Other	Commercial, Financial and Agriculture	Total
Pass	\$ 241,927	\$ 76,206	\$ 16,426	\$ 53,880	\$ 388,439
Special Mention	5,653	144	17	-	5,814
Substandard	12,606	1,059	15	320	14,000
Doubtful	-	-	-	60	60
Subtotal	260,186	77,409	16,458	54,260	408,313
Less:					
Unearned discount	91	94	2	14	201
Loans, net of unearned discount	\$ 260,095	\$ 77,315	\$ 16,456	\$ 54,246	\$ 408,112

NOTE H — SECURITIES

The following disclosure of the estimated fair value of financial instruments is made in accordance with authoritative guidance. The estimated fair value amounts have been determined using available market information and appropriate valuation methodologies. However, considerable judgment is necessarily required to interpret market data to develop the estimates of fair value. Accordingly, the estimates presented herein are not necessarily indicative of the amounts that could be realized in a current market exchange. The use of different market assumptions and/or estimation methodologies may have a material effect on the estimated fair value amounts.

A summary of the amortized cost and estimated fair value of available-for-sale securities and held-to-maturity securities at June 30, 2013, follows:

(\$ in thousands)

	June 30, 2013			Estimated Fair Value
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	
Available-for-sale securities:				
Obligations of U.S. Government Agencies	\$27,717	\$ 63	\$ 109	\$ 27,671
Tax-exempt and taxable obligations of states and municipal subdivisions	112,510	1,997	1,439	113,068
Mortgage-backed securities	80,220	775	1,341	79,654
Corporate obligations	28,514	410	2,247	26,677
Other	1,255	-	295	960
Total	\$250,216	\$ 3,245	\$ 5,431	\$ 248,030
Held-to-maturity securities:				
Mortgage-backed securities	\$2,455	\$ -	\$ 60	\$ 2,395
Taxable obligations of states and municipal subdivisions	6,000	1,035	-	7,035
Total	\$8,455	\$ 1,035	\$ 60	\$ 9,430

NOTE I — ALLOWANCE FOR LOAN LOSSES

The Company has developed policies and procedures for evaluating the overall quality of its credit portfolio and the timely identification of potential problem loans. Management's judgment as to the adequacy of the allowance is based upon a number of assumptions which it believes to be reasonable, but which may not prove to be accurate, particularly given the Company's growth and the economy. Thus, there can be no assurance that charge-offs in future periods will not exceed the allowance for loan losses or that additional increases in the loan loss allowance will not be required.

The Company's allowance consists of two parts. The first part is determined in accordance with authoritative guidance regarding contingencies. The Company's determination of this part of the allowance is based upon quantitative and qualitative factors. A loan loss history based upon the three year quarterly moving average is utilized in determining the appropriate allowance. Historical loss factors are determined by graded and ungraded loans by loan type. These historical loss factors are applied to the loans by loan type to determine an indicated allowance. The loss factors of peer groups are considered in the determination of the allowance and are used to assist in the establishment of a long-term loss history for areas in which this data is unavailable and incorporated into the qualitative factors to be considered. The historical loss factors may also be modified based upon other qualitative factors including but not limited to local and national economic conditions, trends of delinquent loans, changes in lending policies and underwriting standards, concentrations, and management's knowledge of the loan portfolio. These factors require judgment upon the part of management and are based upon state and national economic reports received from various

institutions and agencies including the Federal Reserve Bank, United States Bureau of Economic Analysis, Bureau of Labor Statistics, meetings with the Company's loan officers and loan committee, and data and guidance received or obtained from the Company's regulatory authorities.

The second part of the allowance is determined in accordance with authoritative guidance regarding loan impairment. Impaired loans are determined based upon a review by internal loan review and senior loan officers.

The sum of the two parts constitutes management's best estimate of an appropriate allowance for loan losses. When the estimated allowance is determined, it is presented to the Company's audit committee for review and approval on a quarterly basis.

A loan is considered impaired when, based on current information and events, it is probable that the Company will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. Factors considered by management in determining impairment include payment status, collateral value, and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower's prior payment record, and the amount of the shortfall in relation to the principal and interest owed.

Impairment is measured on a loan by loan basis, and a specific allowance is assigned to each loan determined to be impaired. Impaired loans not deemed collateral dependent are analyzed according to the ultimate repayment source, whether that is cash flow from the borrower, guarantor or some other source of repayment. Impaired loans are deemed collateral dependent if in the Company's opinion the ultimate source of repayment will be generated from the liquidation of collateral.

The Company discontinues accrual of interest on loans when management believes, after considering economic and business conditions and collection efforts, that a borrower's financial condition is such that the collection of interest is doubtful. Generally, the Company will place a delinquent loan in nonaccrual status when the loan becomes 90 days or more past due. At the time a loan is placed in nonaccrual status, all interest which has been accrued on the loan but remains unpaid is reversed and deducted from earnings as a reduction of reported interest income. No additional interest is accrued on the loan balance until the collection of both principal and interest becomes reasonably certain.

NOTE J – SUBSEQUENT EVENTS

Subsequent events have been evaluated by management through the date the financial statements were issued.

NOTE K – RECLASSIFICATION

Certain amounts in the 2012 financial statements have been reclassified for comparative purposes to conform to the current period financial statement presentation.

ITEM NO. 2 MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS
OF OPERATIONS

FINANCIAL CONDITION

The following discussion contains "forward-looking statements" relating to, without limitation, future economic performance, plans and objectives of management for future operations, and projections of revenues and other financial items that are based on the beliefs of the Company's management, as well as assumptions made by and information currently available to the Company's management. The words "expect," "estimate," "anticipate," and "believe," as well as similar expressions, are intended to identify forward-looking statements. The Company's actual results may differ materially from the results discussed in the forward-looking statements, and the Company's operating performance each quarter is subject to various risks and uncertainties that are discussed in detail in the Company's filings with the Securities and Exchange Commission, including the "Risk Factors" section in the Company's most recently filed Form 10-K.

The First represents the primary asset of the Company. The First reported total assets of \$964.4 million at June 30, 2013, compared to \$720.0 million at December 31, 2012. Loans increased \$144.1 million, or 34.8%, during the first six months of 2013. Deposits at June 30, 2013, totaled \$843.8 million compared to \$596.7 million at December 31, 2012. For the six month period ended June 30, 2013, The First reported net income of \$2.8 million compared to \$2.2 million for the six months ended June 30, 2012.

NONPERFORMING ASSETS AND RISK ELEMENTS. Diversification within the loan portfolio is an important means of reducing inherent lending risks. At June 30, 2013, The First had no concentrations of ten percent or more of total loans in any single industry or any geographical area outside its immediate market areas.

At June 30, 2013, The First had loans past due as follows:

	(\$ In Thousands)
Past due 30 through 89 days	\$ 4,446
Past due 90 days or more and still accruing	352

The accrual of interest is discontinued on loans which become ninety days past due (principal and/or interest), unless the loans are adequately secured and in the process of collection. Nonaccrual loans totaled \$1.9 million at June 30, 2013, a decrease of \$1.5 million from December 31, 2012. Any other real estate owned is carried at fair value, determined by an appraisal, less estimated costs to sell. Other real estate owned totaled \$5.7 million at June 30, 2013. A loan is classified as a restructured loan when the following two conditions are present: First, the borrower is experiencing financial difficulty and second, the creditor grants a concession it would not otherwise consider but for the borrower's financial difficulties. At June 30, 2013, the Bank had \$2,410,000 in loans that were modified as troubled debt restructurings, of which \$1,769,000 were performing as agreed with modified terms.

LIQUIDITY AND CAPITAL RESOURCES

Liquidity is adequate with cash and cash equivalents of \$81.8 million as of June 30, 2013. In addition, loans and investment securities repricing or maturing within one year or less exceeded \$218.5 million at June 30, 2013. Approximately \$103.3 million in loan commitments could fund within the next six months and other commitments, primarily standby letters of credit, totaled \$.6 million at June 30, 2013. There are no known trends or any known commitments or uncertainties that will result in The First's liquidity increasing or decreasing in a significant way.

Total consolidated equity capital at June 30, 2013, was \$82.6 million, or approximately 8.6% of total assets. The Company currently has adequate capital positions to meet the minimum capital requirements for all regulatory agencies. The Company's capital ratios as of June 30, 2013, were as follows:

Tier 1 leverage	8.97 %
Tier 1 risk-based	12.86 %
Total risk-based	13.72 %

On June 30, 2006, The Company issued \$4,124,000 of floating rate junior subordinated deferrable interest debentures to The First Bancshares Statutory Trust 2 in which the Company owns all of the common equity. The debentures are the sole asset of the Trust. The Trust issued \$4,000,000 of Trust Preferred Securities (TPSs) to investors. The Company's obligations under the debentures and related documents, taken together, constitute a full and unconditional guarantee by the Company of the Trust's obligations under the preferred securities. The preferred securities are redeemable by the Company at its option. The preferred securities must be redeemed upon maturity of the debentures in 2036. Interest on the preferred securities is the three month London Interbank Offer Rate (LIBOR) plus 1.65% and is payable quarterly. The terms of the subordinated debentures are identical to those of the preferred securities. On July 27, 2007, The Company issued \$6,186,000 of floating rate junior subordinated deferrable interest debentures to The First Bancshares Statutory Trust 3 in which the Company owns all of the common equity. The debentures are the sole asset of Trust 3. The Trust issued \$6,000,000 of Trust Preferred Securities (TPSs) to investors. The Company's obligations under the debentures and related documents, taken together, constitute a full and unconditional guarantee by the Company of the Trust's obligations under the preferred securities. The preferred securities are redeemable by the Company in 2013 or later, at its option. The preferred securities must be redeemed upon maturity of the debentures in 2037. Interest on the preferred securities is the three month LIBOR plus 1.40% and is payable quarterly. The terms of the subordinated debentures are identical to those of the preferred securities. In accordance with the authoritative guidance, the trusts are not included in the consolidated financial statements.

RESULTS OF OPERATIONS - QUARTERLY

The Company had a consolidated net income of \$812,000 for the three months ended June 30, 2013, compared with consolidated net income of \$1,037,000 for the same period last year.

Net interest income increased to \$6.8 million from \$5.5 million for the three months ended June 30, 2013, or an increase of 23.2% as compared to the same period in 2012. Earning assets through June 30, 2013, increased \$370.3 million, or 73.7% and interest-bearing liabilities also increased \$263.7 million or 62.2% when compared to June 30, 2012.

Noninterest income for the three months ended June 30, 2013, was \$1,890,000 compared to \$1,510,000 for the same period in 2012, reflecting an increase of \$380,000 or 25.2%. An increase in fee income associated with higher loan and deposit volumes attributed to this increase.

The provision for loan losses was \$349,000 for the three months ended June 30, 2013, compared with \$221,000 for the same period in 2012. The allowance for loan losses of \$5.4 million at June 30, 2013 (approximately .97% of total loans and 1.26% of loans excluding those booked at fair value due to the business combination) is considered by management to be adequate to cover losses inherent in the loan portfolio. The level of this allowance is dependent upon a number of factors, including the total amount of past due loans, general economic conditions, and management's assessment of potential losses. This evaluation is inherently subjective as it requires estimates that are susceptible to significant change. Ultimately, losses may vary from current estimates and future additions to the allowance may be necessary.

Thus, there can be no assurance that charge-offs in future periods will not exceed the allowance for loan losses or that additional increases in the loan loss allowance will not be required. Management evaluates the adequacy of the allowance for loan losses quarterly and makes provisions for loan losses based on this evaluation.

Noninterest expense increased by \$1,831,000 or 33.8% for the three months ended June 30, 2013, when compared with the same period in 2012. This increase is primarily related to costs associated with the acquisition of First National Bank of Baldwin County in the amount of \$635,500, as well as an increase in salaries and employee benefits associated with the start of our Private Banking Division.

RESULTS OF OPERATIONS – YEAR TO DATE

The Company had a consolidated net income of \$2,037,000 for the six months ended June 30, 2013, compared with consolidated net income of \$2,008,000 for the same period last year.

Net interest income increased to \$12.7 million from \$11.0 million for the six months ended June 30, 2013, or an increase of 15.3% as compared to the same period in 2012. This increase was primarily a result of increased loan volume in existing markets as well as loan growth associated with the acquisition of First national Bank of Baldwin County.

Noninterest income for the six months ended June 30, 2013, was \$3,820,000 compared to \$2,985,000 for the same period in 2012, reflecting an increase of \$835,000 or 28.0%. Included in noninterest income is service charges on deposit accounts, which for the six months ended June 30, 2013, totaled \$1,854,000 compared to \$1,727,000 for the same period in 2012. An increase in fee income associated with higher loan and deposit volumes attributed to this income.

The provision for loan losses was \$660,000 for the six months ended June 30, 2013, compared with \$373,000 for the same period in 2012. The allowance for loan losses of \$5.4 million at June 30, 2013 (approximately .97% of total loans and 1.26% of loans excluding those booked at fair value due to the business combination) is considered by management to be adequate to cover losses inherent in the loan portfolio. The level of this allowance is dependent upon a number of factors, including the total amount of past due loans, general economic conditions, and management's assessment of potential losses. This evaluation is inherently subjective as it requires estimates that are susceptible to significant change. Ultimately, losses may vary from current estimates and future additions to the allowance may be necessary.

Thus, there can be no assurance that charge-offs in future periods will not exceed the allowance for loan losses or that additional increases in the loan loss allowance will not be required. Management evaluates the adequacy of the allowance for loan losses quarterly and makes provisions for loan losses based on this evaluation.

Noninterest expense increased by \$2.3 million or 20.9% for the six months ended June 30, 2013, when compared with the same period in 2012. This increase is primarily related to an increase in operating costs associated with the acquisition of First National Bank of Baldwin County as well as an increase in salaries and employee benefits associated with the start of our Private Banking Division.

ITEM NO. 3. CONTROLS AND PROCEDURES

As of June 30, 2013, (the "Evaluation Date"), we carried out an evaluation, under the supervision of and with the participation of our Chief Executive Officer and our Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures, as such term is defined under Rule 13a-15(e) promulgated under the Securities Exchange Act of 1934, as amended. Based on this evaluation, our Chief Executive Officer and our Chief Financial Officer concluded that our disclosure controls and procedures are effective to ensure that information we are required to disclose in reports that we file or submit under the Exchange Act is recorded, processed, summarized, and reported within the time periods specified in SEC rules and forms.

There have been no changes, significant or otherwise, in our internal controls over financial reporting that occurred during the quarter ended June 30, 2013, that have materially affected, or are reasonably likely to affect, our internal control over financial reporting.

ITEM NO. 4. RECENT ACCOUNTING PRONOUNCEMENTS

In December 2011, the FASB issued ASU No. 2011-11, "Balance Sheet Disclosures about Offsetting Assets and Liabilities." The ASU amends ASC Topic 210 by requiring additional improved information to be disclosed regarding financial instruments and derivative instruments that are offset in accordance with the conditions under ASC 210-20-45 or ASC 815-10-45 or subject to an enforceable master netting arrangement or similar agreement. The amendment is effective for annual and interim reporting periods beginning on or after January 1, 2013. The disclosures required by the amendments should be applied retrospectively for all comparative periods presented. In January 2013, the FASB issued ASU No. 2013-01, "Clarifying the Scope of Disclosures about Offsetting Assets and Liabilities." The ASU clarifies that ordinary trade receivables and receivables are not in the scope of ASU 2011-11. Only derivatives, repurchase agreements and reverse purchase agreements, and securities borrowing and securities lending transactions that are either offset in accordance with specific criteria contained in the Codification or subject to a master netting arrangement or similar agreement are applicable. The amendments did not have a material impact on the Company's financial statements.

In February 2013, the FASB issued ASU No. 2013-02, "Comprehensive Income – Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income." The amendments do not change the current requirements for reporting net income or other comprehensive income in financial statements. These amendments require an entity to provide information about the amounts reclassified out of accumulated other comprehensive income by component. In addition, an entity is required to present either on the face of the statement where net income is presented or in the notes, significant amounts reclassified out of accumulated other comprehensive income by the respective line items of net income but only if the amount reclassified is required under U. S. GAAP to be reclassified to net income in its entirety in the same reporting period. For other amounts that are not required under U. S. GAAP to be reclassified in their entirety to net income, an entity is required to cross-reference to other disclosures required under U. S. GAAP that provide additional details about these amounts. ASU 2013-02 is effective for interim and annual periods beginning after December 15, 2012. The Company adopted this standard on January 1, 2013. The effect of adopting this standard increased the disclosures surrounding reclassification items, if any, out of accumulated other comprehensive income.

In February 2013, the FASB issued ASU No. 2013-04, "Liabilities – Obligations Resulting from Joint and Several Liability Arrangements for Which the Total Amount of the Obligation is Fixed at the Reporting Date." The ASU requires entities to measure obligations resulting from joint and several liability arrangements for which the total amount of the obligation within the scope of this guidance is fixed at the reporting date. The measurement is the sum of both the amount the reporting entity agreed to pay on the basis of its arrangement among its co-obligors and any additional amount the reporting entity expects to pay on behalf of its co-obligors. Required disclosures include a description of the joint-and-several arrangement and the total outstanding amount of the obligation for all joint parties.

ASI 2013-04 is effective for interim and annual periods beginning on or after December 15, 2013. The ASU should be applied retrospectively to obligations existing at the beginning of an entity's fiscal year of adoption. Early adoption is permitted. The Company is currently evaluating the possible effects of this guidance on its financial statement disclosures.

PART II — OTHER INFORMATION

ITEM 1.

LEGAL PROCEEDINGS

None

ITEM 1A. RISK FACTORS

There are no material changes in the Company's risk factors since December 31, 2012. Please refer to the Annual Report on Form 10-K of The First Bancshares, Inc., filed with the Securities and Exchange Commission on March 28, 2013.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITY AND USE OF PROCEEDS

On March 20, 2013, The First Bancshares, Inc., a Mississippi corporation (the "Company") entered into Securities Purchase Agreements with a limited number of institutional and other accredited investors, including certain directors and executive officers of the Company (collectively, the "Purchasers") to sell a total of 1,951,220 shares of mandatorily convertible non-cumulative, non-voting, perpetual Preferred Stock, Series D, \$1.00 par value (the "Series D Preferred Stock") at a price of \$10.25 per share, for an aggregate gross purchase price of \$20,000,005 (the "Private Placement"). The Private Placement closed on March 22, 2013, after the Company issued an aggregate of 1,951,220 shares of Series D Preferred Stock against receipt of \$20,000,005 in cash from the Purchasers. The Private Placement was not registered under the Securities Act of 1933, as amended (the "Act"), in reliance on Section 4(2) of the Act and Rule 506 of Regulation D promulgated thereunder.

The Series D Preferred Stock automatically converted into a like number of shares of the Company's common stock after the Company received shareholder approval of such conversion at a meeting of shareholders held on May 23, 2013. Upon conversion of the Series D Preferred Stock, each share of Series D Preferred Stock was automatically converted into one share of the Company's common stock par value of one U.S. dollar (\$1.00) per share ("Common Stock"). The holders of record of Series D Preferred Stock were entitled to receive as, when, and if declared by the Company's board of directors, dividends on each share of Series D Preferred Stock equal to the per share amount paid on a share of Common Stock (the "Preferred Dividend"), and no dividends were payable on the Common Stock or any other class or series of capital stock ranking with respect to dividends *pari passu* with the Common Stock unless a Preferred Dividend was payable at the same time on the Series D Preferred Stock; *provided, however*, in the event the shareholders of the Company did not approve the conversion of the Series D Preferred Stock to Common Stock within six (6) months of issuance, the holders of record of Series D Preferred Stock would have been entitled to receive as, when, and if declared by the board of directors of the Company, dividends on each share of Series D Preferred Stock equal to six (6) percent of liquidation value per annum or \$0.62 per share (the "Fixed Preferred Dividend") and no

dividends would have been payable on the Common Stock or any other class or series of capital stock ranking with respect to dividends pari passu with the Common Stock unless a Preferred Dividend was payable at the time on the Series D Preferred Stock. Such Fixed Preferred Dividends would have been payable semi-annually in arrears on June 30 and December 31, beginning on December 31, 2013, until the shareholders of the Company approved the conversion of the Series D Preferred Shares into the Common Stock. The Series D Preferred Stock was not redeemable by the Company or by the holders. Complete details concerning the Series D Preferred Stock are contained in the Certificate of Designation filed with the Mississippi Secretary of State on March 20, 2013, a copy of which was attached as Exhibit 4.1 to the Form 8-K filed by the Company on March 25, 2013 and incorporated herein by reference.

In accordance with Section 4.11 of the Securities Purchase Agreement, the Company called a meeting of the Company shareholders to vote on proposals to approve the conversion of shares of Series D Preferred Stock into shares of Common Stock for purposes of compliance with NASDAQ Stock Market Rule 5635. The board of directors of the Company unanimously recommended shareholder approval of this proposal.

Also on March 20, 2013, pursuant to the Securities Purchase Agreements, the Company entered into a Registration Rights Agreement with each of the Purchasers. Pursuant to the Registration Rights Agreement, the Company filed a registration statement with the Securities and Exchange Commission to register for resale the Common Stock to be issued upon conversion of the Series D Preferred Stock, within 90 calendar days after the closing of the Private Placement, and to use commercially reasonable efforts to cause such registration statement to be declared effective upon the earlier of (i) the 120th calendar day following March 22, 2013 (or the 150th calendar day following March 22, 2013 in the event that such registration statement is subject to review by the Securities and Exchange Commission) and (ii) the 5th trading day (as defined in the Registration Rights Agreement) after the date the Company is notified (orally or in writing, whichever is earlier) by the Securities and Exchange Commission that such registration statement will not be “reviewed” or will not be subject to further review. Failure to meet these deadlines and certain other events could have resulted in the Company's payment of liquidated damages to the holders of the rights, monthly in the amount of 0.5% of the aggregate purchase price of each holder of the converted Common Stock.

Copies of the form of Securities Purchase Agreements and the form of Registration Rights Agreements were attached to the Company's Form 8-K filed on March 25, 2013 as Exhibits 10.1 and 10.2, respectively, and are incorporated herein by reference. The foregoing descriptions of the Securities Purchase Agreements, the Registration Rights Agreements and the Certificate of Designation do not purport to be complete and are qualified in their entirety by reference to the full text of the Securities Purchase Agreements, the Registration Rights Agreements and the Certificate of Designation filed as exhibits to this report.

Pursuant to shareholder approval obtained at the Annual Meeting held on May 23, 2013, the Series D Nonvoting Convertible Preferred Stock has been converted to common stock.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

Not Applicable

ITEM 4. REMOVED AND RESERVED

ITEM 5. OTHER INFORMATION

Not Applicable

ITEM 6. EXHIBITS

(a) Exhibits

Exhibit
No.

- 2.1 Acquisition Agreement, dated as of January 31, 2013, between The First Bancshares, Inc. and First Baldwin Bancshares, Inc. (incorporated by reference to Exhibit 2.1 to the Company's Form 8-K filed on 2-1-13) and First Amendment to Acquisition Agreement, dated as of March 15, 2013, between First Bancshares, Inc. and First Baldwin Bancshares, Inc. (incorporated by reference to Exhibit 2.1 to the Company's Form 8-K filed on 3-20-13)
- 3.1 Articles of Amendment and Certificate of Designation, Preferences and Rights of Series D Nonvoting Convertible Preferred Stock dated as of March 18, 2013 (incorporated by reference to Exhibit 3.1 of the Company's Form 8-K filed on 3-21-13).
- 3.2 Restated Articles of Incorporation dated as of March 21, 2013 (incorporated by reference to Exhibit 3.2 of the Company's Form 8-K filed on 3-21-13).
- 4.1 Certificate of Designation of Series D Nonvoting Convertible Preferred Stock, as filed with the Mississippi Secretary of State on March 20, 2013 (incorporated by reference to Exhibit 4.1 to the Company's Form 8-K filed on March 25, 2013).
- 10.1 Form of Securities Purchase Agreement between the Company and each of the Purchasers, dated as of March 20, 2013 (incorporated by reference to Exhibit 10.1 to the Company's Form 8-K filed on March 25, 2013)
- 10.2

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Form of Registration Rights Agreement between the Company and each of the Purchasers, dated as of March 20, 2013 (incorporated by reference to Exhibit 10.2 to the Company's Form 8-K filed on March 25, 2013)

31.1 Certification of principal executive officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

32

- 31.2 Certification of principal financial officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 32.1 Certification of principal executive officer pursuant to 18 U. S. C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
- 32.2 Certification of principal financial officer pursuant to 18 U. S. C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
- 101.INS** XBRL Instance Document
- 101.SCH** XBRL Taxonomy Extension Schema
- 101.CAL** XBRL Taxonomy Extension Calculation Linkbase
- 101.DEF** XBRL Taxonomy Extension Definition Linkbase
- 101.LAB** XBRL Taxonomy Extension Label Linkbase
- 101.PRE** XBRL Taxonomy Extension Presentation Linkbase

**Pursuant to Rule 406T of Regulation S-T, these interactive data files are deemed not filed or part of a registration statement or prospectus for purposes of Sections 11 or 12 of the Securities Act of 1933 or Section 18 of the Securities Act of 1934 and otherwise are not subject to liability.

(b)The Company filed six reports on Form 8-K during the quarter ended June 30, 2013

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

THE FIRST BANCSHARES, INC.
(Registrant)

/s/M. RAY (HOPPY)COLE, JR.

August 14, 2013 M. Ray (Hoppy) Cole, Jr.
(Date) Chief Executive Officer

/s/DEEDEE LOWERY

August 14, 2013
(Date) DeeDee Lowery, Executive
 Vice President and Chief
 Financial Officer