MEREDITH CORP
Form DEFA14A
October 01, 2008

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, DC 20549

SCHEDULE 14A

Proxy Statement Pursuant to Section 14(a) of the Securities

Exchange Act of 1934 (Amendment No.)

Filed by the Registrant [X]

Filed by a Party other than the Registrant [_]

Check the appropriate box:

[_] Preliminary Proxy Statement

[_] Confidential, for Use of the Commission Only (as permitted by Rule 14A-6(E)(2))

[_] Definitive Proxy Statement

[X] Definitive Additional Materials

[_] Soliciting Material Pursuant to Section 240.14a-11(c) or Section 240.14a-12

MEREDITH CORPORATION

(Name of Registrant as Specified In Its Charter)

(Name of Person(s) Filing Proxy Statement, if other than the Registrant)

Payment of Filing Fee (Check the appropriate box):

[X] No fee required

[_] Fee computed on table below per Exchange Act Rules 14a-6(i)(4) and 0-11.

(1) Title of each class of securities to which transaction applies:

(2) Aggregate number of securities to which transaction applies:

(3) Per unit price or other underlying value of transaction computed pursuant to Exchange Act Rule 0-11 (set forth the amount on which the filing fee is calculated and state how it was determined):

(4) Proposed maximum aggregate value of transaction:

(5) Total fee paid:

[_] Fee paid previously with preliminary materials.

[_] Check box if any part of the fee is offset as provided by Exchange Act Rule 0-11(a)(2) and identify the filing for which the offsetting fee was paid previously. Identify the previous filing by registration statement number, or the Form or Schedule and the date of its filing.

(1) Amount Previously Paid:

(2) Form, Schedule or Registration Statement No.:

(3) Filing Party:

(4) Date Filed:

October 1, 2008

Dear Shareholder:

It has come to our attention that, due to a clerical error, we incorrectly reported in the Proxy Statement the number of shares of common stock of Meredith Corporation (the Company) outstanding as of the record date of September 11, 2008.

On the record date, there were issued and outstanding 36,015,155 shares of common stock, not 39,015,155 as set forth in the Proxy Statement. Each share of common stock is entitled to one vote at the Annual Meeting of the Company to be held on November 5, 2008. On the record date, there were also issued and outstanding 9,167,935 shares of class B common stock, each entitled to ten votes at the Annual Meeting of the Company, for a total of 127,694,505 eligible votes.

If you have already returned your proxy card and wish to change your vote because of this information, please follow the instructions for revoking your proxy as set forth on page 2 of the Proxy Statement.

Your vote is important. We encourage you to vote promptly so that your shares are represented at the Annual Meeting. We appreciate your continued support of the Company.

Sincerely,

JOHN S. ZIESER

Chief Development Officer

General Counsel and Secretary

font-size:10pt;">
Consumer loans

8

12

11

47

5

Total repossessions

5,156

4,262

63

6,792

5,670

Operating leases

6

—

—

29

236

Total nonperforming assets

$
42,480

$
46,746

$
45,267

$
72,476

$
88,712

Nonperforming loans and leases to loans and leases, net of unearned discount

0.96
%

1.04
%

1.11
%

1.84
%

2.45
%
Nonperforming assets to loans and leases and operating leases, net of unearned discount

1.13
%

1.29
%

1.25
%

2.28
%

2.81

%

Potential Problem Loans — Potential problem loans consist of loans that are performing but for which management has concerns about the ability of a borrower to continue to comply with repayment terms because of the borrower's potential operating or financial difficulties. Management monitors these loans closely and reviews their performance on a regular basis. As of December 31, 2014 and 2013, we had $16.18 million and $4.33 million, respectively, in loans of this type which are not included in either of the non-accrual or 90 days past due loan categories. At December 31, 2014, potential problem loans consisted of three foreign aircraft credit relationships. Weakness in these companies' operating performance and payment patterns has caused us to heighten attention given to these credits.

Foreign Outstandings — Our foreign loan and lease outstandings, all denominated in U.S. dollars except for one loan denominated in Euros at December 31, 2013, which was not significant, were $224.51 million and $270.30 million as of December 31, 2014 and 2013, respectively. Foreign loans and leases are in aircraft financing. Loan and lease outstandings to borrowers in Brazil and Mexico were $105.39 million and $100.76 million as of December 31, 2014, respectively, compared to $142.79 million and $77.96 million as of December 31, 2013, respectively. Outstanding balances to borrowers in other countries were insignificant.

INVESTMENT PORTFOLIO

The amortized cost of securities at year-end 2014 decreased from 2013, following a decrease from year-end 2012 to year-end 2013. The amortized cost of securities at December 31, 2014 was $776.06 million or 16.07% of total assets, compared to $822.16 million or 17.41% of total assets at December 31, 2013.

Table of Contents

The following table shows the amortized cost of securities available-for-sale as of December 31.

(Dollars in thousands)	2014	2013	2012
U.S. Treasury and Federal agencies securities	$371,878	$394,558	$410,983
U.S. States and political subdivisions securities	121,510	120,416	100,055
Mortgage-backed securities — Federal agencies	248,299	273,495	301,136
Corporate debt securities	31,677	30,828	30,897
Foreign government and other securities	800	700	3,700
Marketable equity securities	1,893	2,166	2,368
Total investment securities available-for-sale	$776,057	$822,163	$849,139

Yields on tax-exempt obligations are calculated on a fully tax equivalent basis assuming a 35% tax rate. The following table shows the maturities of securities available-for-sale at December 31, 2014, at the amortized costs and weighted average yields of such securities.

(Dollars in thousands)	Amount	Yield	
U.S. Treasury and Federal agencies securities			
Under 1 year	$15,501	2.27	%
1 – 5 years	356,377	1.53	
5 – 10 years	—	—	
Over 10 years	—	—	
Total U.S. Treasury and Federal agencies securities	371,878	1.56	
U.S. States and political subdivisions securities			
Under 1 year	8,287	5.15	
1 – 5 years	66,872	3.92	
5 – 10 years	44,139	3.36	
Over 10 years	2,212	5.48	
Total U.S. States and political subdivisions securities	121,510	3.83	
Corporate debt securities			
Under 1 year	4,525	1.49	
1 – 5 years	27,152	1.70	
5 – 10 years	—	—	
Over 10 years	—	—	
Total Corporate debt securities	31,677	1.67	
Foreign government and other securities			
Under 1 year	200	1.27	
1 – 5 years	600	1.98	
5 – 10 years	—	—	
Over 10 years	—	—	
Total Foreign government and other securities	800	1.80	
Mortgage-backed securities — Federal agencies	248,299	2.43	
Marketable equity securities	1,893	6.74	
Total investment securities available-for-sale	$776,057	2.21	%

At December 31, 2014, the residential mortgage-backed securities we held consisted primarily of GNMA, FNMA and FHLMC pass-through certificates (Government Sponsored Enterprise, GSEs). The type of loans underlying the securities were all conforming loans at the time of issuance. The underlying GSE backing these mortgage-backed securities are rated Aaa or AA+ from the rating agencies. At December 31, 2014, the vintage of the underlying loans comprising our securities are: 24% in the years 2013 and 2014; 40% in the years 2011 and 2012; 25% in the years 2009 and 2010; and 11% in years 2008 and prior.

Table of Contents

DEPOSITS

The following table shows the average daily amounts of deposits and rates paid on such deposits.

	2014		2013		2012	
(Dollars in thousands)	Amount	Rate	Amount	Rate	Amount	Rate
Noninterest bearing demand deposits	$762,050	— %	$690,326	— %	$616,426	— %
Interest bearing demand deposits	1,296,929	0.12	1,234,145	0.13	1,151,617	0.16
Savings deposits	710,216	0.08	691,942	0.09	656,245	0.14
Time deposits	1,008,548	0.91	1,084,096	1.33	1,149,923	1.66
Total deposits	$3,777,743		$3,700,509		$3,574,211	

See Part II, Item 8, Financial Statements and Supplementary Data — Note 10 of the Notes to Consolidated Financial Statements for additional information on deposits.

SHORT-TERM BORROWINGS

The following table shows the distribution of our short-term borrowings and the weighted average interest rates thereon at the end of each of the last three years. Also provided are the maximum amount of borrowings and the average amount of borrowings, as well as weighted average interest rates for the last three years.

(Dollars in thousands)	Federal Funds Purchased and Securities Repurchase Agreements	Commercial Paper	Other Short-Term Borrowings	Total Borrowings
2014				
Balance at December 31, 2014	$138,843	$11,778	$95,201	$245,822
Maximum amount outstanding at any month-end	230,075	17,245	155,573	402,893
Average amount outstanding	143,270	13,137	106,970	263,377
Weighted average interest rate during the year	0.15 %	0.26 %	0.27 %	0.21 %
Weighted average interest rate for outstanding amounts at December 31, 2014	0.13 %	0.27 %	0.29 %	0.20 %
2013				
Balance at December 31, 2013	$181,120	$10,814	$122,197	$314,131
Maximum amount outstanding at any month-end	181,120	16,552	122,197	319,869
Average amount outstanding	121,294	9,035	24,475	154,804
Weighted average interest rate during the year	0.11 %	0.22 %	0.22 %	0.14 %
Weighted average interest rate for outstanding amounts at December 31, 2013	0.17 %	0.24 %	0.28 %	0.22 %
2012				
Balance at December 31, 2012	$158,680	$3,469	$7,039	$169,188
Maximum amount outstanding at any month-end	189,150	10,114	11,531	210,795
Average amount outstanding	121,495	6,739	9,703	137,937
Weighted average interest rate during the year	0.13 %	0.21 %	— %	0.12 %
Weighted average interest rate for outstanding amounts at December 31, 2012	0.20 %	0.22 %	— %	0.19 %

LIQUIDITY

Core Deposits — Our major source of investable funds is provided by stable core deposits consisting of all interest bearing and noninterest bearing deposits, excluding brokered certificates of deposit and certain certificates of deposit over $250,000 based on established FDIC insured deposits. In 2014, average core deposits equaled 74.85% of average total assets, compared to 78.35% in 2013 and 77.32% in 2012. The effective rate of core deposits in 2014 was 0.28%, compared to 0.43% in 2013 and 0.58% in 2012.

Average noninterest bearing core deposits increased 10.39% in 2014 compared to an increase of 11.99% in 2013. These represented 21.18% of total core deposits in 2014, compared to 19.12% in 2013, and 17.82% in 2012.

31

Table of Contents

Purchased Funds — We use purchased funds to supplement core deposits, which include certain certificates of deposit over $250,000, brokered certificates of deposit, over-night borrowings, securities sold under agreements to repurchase, commercial paper, and other short-term borrowings. Purchased funds are raised from customers seeking short-term investments and are used to manage the Bank's interest rate sensitivity. During 2014, our reliance on purchased funds increased to 9.23% of average total assets from 5.31% in 2013.

Shareholders' Equity — Average shareholders' equity equated to 12.52% of average total assets in 2014, compared to 12.49% in 2013. Shareholders' equity was 12.72% of total assets at year-end 2014, compared to 12.39% at year-end 2013. We include unrealized gains (losses) on available-for-sale securities, net of income taxes, in accumulated other comprehensive income (loss) which is a component of shareholders' equity. While regulatory capital adequacy ratios exclude unrealized gains (losses), it does impact our equity as reported in the audited financial statements. The unrealized gains (losses) on available-for-sale securities, net of income taxes, were $9.41 million and $6.58 million at December 31, 2014 and 2013, respectively.

Other Liquidity — Under Indiana law governing the collateralization of public fund deposits, the Indiana Board of Depositories determines which financial institutions are required to pledge collateral based on the strength of their financial ratings. We have been informed that no collateral is required for our public fund deposits. However, the Board of Depositories could alter this requirement in the future and adversely impact our liquidity. Our potential liquidity exposure if we must pledge collateral is approximately $548 million.

Liquidity Risk Management — The Bank's liquidity is monitored and closely managed by the Asset/Liability Management Committee (ALCO), whose members are comprised of the Bank's senior management. Asset and liability management includes the management of interest rate sensitivity and the maintenance of an adequate liquidity position. The purpose of interest rate sensitivity management is to stabilize net interest income during periods of changing interest rates.

Liquidity management is the process by which the Bank ensures that adequate liquid funds are available to meet financial commitments on a timely basis. Financial institutions must maintain liquidity to meet day-to-day requirements of depositors and borrowers, take advantage of market opportunities and provide a cushion against unforeseen needs.

Liquidity of the Bank is derived primarily from core deposits, principal payments received on loans, the sale and maturity of investment securities, net cash provided by operating activities, and access to other funding sources. The most stable source of liability-funded liquidity is deposit growth and retention of the core deposit base. The principal source of asset-funded liquidity is available-for-sale investment securities, cash and due from banks, overnight investments, securities purchased under agreements to resell, and loans and interest bearing deposits with other banks maturing within one year. Additionally, liquidity is provided by repurchase agreements, and the ability to borrow from the Federal Reserve Bank (FRB) and the Federal Home Loan Bank (FHLB).

The Bank's liquidity strategy is guided by internal policies and the Interagency Policy Statement on Funding and Liquidity Risk Management. Internal guidelines consist of:

(i) Available Liquidity (sum of short term borrowing capacity) greater than $500 million;

(ii) Liquidity Ratio (total of net cash, short term investments and unpledged marketable assets divided by the sum of net deposits and short term liabilities) greater than 15%;

(iii) Dependency Ratio (net potentially volatile liabilities minus short term investments divided by total earning assets minus short term investments) less than 15%; and

(iv) Loans to Deposits Ratio less than 100%

At December 31, 2014, we were in compliance with the foregoing internal policies and regulatory guidelines.

The Bank also maintains a contingency funding plan that assesses the liquidity needs under various scenarios of market conditions, asset growth and credit rating downgrades. The plan includes liquidity stress testing which measures various sources and uses of funds under the different scenarios. The contingency plan provides for ongoing monitoring of unused borrowing capacity and available sources of contingent liquidity to prepare for unexpected liquidity needs and to cover unanticipated events that could affect liquidity.

We have borrowing sources available to supplement deposits and meet our funding needs. 1st Source Bank has established relationships with several banks to provide short term borrowings in the form of federal funds purchased.

While at December 31, 2014 there was $10.50 million outstanding, we could borrow approximately $254.50 million in additional funds for a short time from these banks on a collective basis. As of December 31, 2014, we had $128.58 million outstanding in FHLB advances and could borrow an additional $79.34 million. We also had $377.16 million available to borrow from the FRB with no amounts outstanding as of December 31, 2014.

32

Table of Contents

Interest Rate Risk Management — ALCO monitors and manages the relationship of earning assets to interest bearing liabilities and the responsiveness of asset yields, interest expense, and interest margins to changes in market interest rates. In the normal course of business, we face ongoing interest rate risks and uncertainties. We may utilize interest rate swaps to partially manage the primary market exposures associated with the interest rate risk related to underlying assets, liabilities, and anticipated transactions.

A hypothetical change in net interest income was modeled by calculating an immediate 200 basis point (2.00%) and 100 basis point (1.00%) increase and a 100 basis point (1.00%) decrease in interest rates across all maturities. The following table shows the aggregate hypothetical impact to pre-tax net interest income.

	Percentage Change in Net Interest Income			
	December 31, 2014		December 31, 2013	
Basis Point Interest Rate Change	12 Months	24 Months	12 Months	24 Months
Up 200	1.12%	8.15%	(0.81)%	3.36%
Up 100	(0.23)%	3.50%	(1.36)%	0.73%
Down 100	(1.94)%	(6.11)%	(1.18)%	(4.45)%

The earnings simulation model excludes the earnings dynamics related to how fee income and noninterest expense may be affected by changes in interest rates. Actual results may differ materially from those projected. The use of this methodology to quantify the market risk of the balance sheet should not be construed as an endorsement of its accuracy or the accuracy of the related assumptions.

At December 31, 2014 and 2013, the impact of these hypothetical fluctuations in interest rates on our derivative holdings was not significant, and, as such, separate disclosure is not presented. We manage the interest rate risk related to mortgage loan commitments by entering into contracts for future delivery of loans with outside parties. See Part II, Item 8, Financial Statements and Supplementary Data — Note 18 of the Notes to Consolidated Financial Statements.

OFF-BALANCE SHEET ARRANGEMENTS AND CONTRACTUAL OBLIGATIONS

In the ordinary course of operations, we enter into certain contractual obligations. Such obligations include the funding of operations through debt issuances as well as leases for premises and equipment. The following table summarizes our significant fixed, determinable, and estimated contractual obligations, by payment date, at December 31, 2014, except for obligations associated with short-term borrowing arrangements. Payments for borrowings do not include interest. Further discussion of the nature of each obligation is included in the referenced note to the consolidated financial statements.

The following table shows contractual obligation payments by period.

(Dollars in thousands)	Note	0 – 1 Year	1 – 3 Years	3 – 5 Years	Over 5 Years	Indeterminate maturity	Total
Deposits without stated maturity	—	$2,824,935	$—	$—	$—	$—	$2,824,935
Certificates of deposit	10	437,478	356,422	164,156	19,869	—	977,925
Long-term debt	11	1,068	32,467	1,526	5,493	15,678	56,232
Subordinated notes	12	—	—	—	58,764	—	58,764
Operating leases	18	3,162	5,335	4,450	3,123	—	16,070
Purchase obligations	—	22,793	2,563	1,584	1,080	—	28,020
Total contractual obligations		$3,289,436	$396,787	$171,716	$88,329	$15,678	$3,961,946

We routinely enter into contracts for services. These contracts may require payment for services to be provided in the future and may also contain penalty clauses for early termination of the contract. We have made a diligent effort to estimate such payments and penalties, where applicable. Additionally, where necessary, we have made reasonable estimates as to certain purchase obligations as of December 31, 2014. Our management has used the best information available to make the estimations necessary to value the related purchase obligations. Our management is not aware of any additional commitments or contingent liabilities which may have a material adverse impact on our liquidity or capital resources at year-end 2014.

We also enter into derivative contracts under which we are required to either receive cash from, or pay cash to, counterparties depending on changes in interest rates. Derivative contracts are carried at fair value on the consolidated balance sheet with the fair value representing the net present value of expected future cash receipts or payments based on market interest rates as of the balance sheet date. The fair value of the contracts changes daily as market interest rates change. Because the derivative assets and liabilities recorded on the balance sheet at December 31, 2014 do not necessarily represent the amounts that may ultimately be paid under these contracts, these assets and liabilities are not included in the table of contractual obligations presented above.

33

Table of Contents

Assets under management and assets under custody are held in fiduciary or custodial capacity for our clients. In accordance with U.S. generally accepted accounting principles, these assets are not included on our balance sheet. We are also party to financial instruments with off-balance sheet risk in the normal course of business to meet the financing needs of our clients. These financial instruments include commitments to extend credit and standby letters of credit. Further discussion of these commitments is included in Part II, Item 8, Financial Statements and Supplementary Data — Note 18 of the Notes to Consolidated Financial Statements.

QUARTERLY RESULTS OF OPERATIONS

The following table sets forth unaudited consolidated selected quarterly statement of operations data for the years ended December 31, 2014 and 2013.

Three Months Ended (Dollars in thousands, except per share amounts)	March 31	June 30	September 30	December 31
2014				
Interest income	$43,355	$44,850	$45,152	$45,196
Interest expense	4,737	4,688	4,442	4,357
Net interest income	38,618	40,162	40,710	40,839
Provision for (recovery of) loan and lease losses	804	2,543	1,206	(820)
Gains on investment securities available-for-sale	963	—	—	—
Income before income taxes	21,239	22,416	21,243	19,544
Net income	13,632	14,494	14,947	14,996
Diluted net income per common share	0.55	0.59	0.62	0.62
2013				
Interest income	$43,878	$44,611	$46,966	$44,130
Interest expense	6,124	5,740	5,808	5,096
Net interest income	37,754	38,871	41,158	39,034
Provision for (recovery of) loan and lease losses	757	1,293	(419)	(859)
Losses on investment securities available-for-sale	—	—	(28)	(140)
Income before income taxes	19,395	21,955	23,305	19,288
Net income	12,404	13,942	14,896	13,716
Diluted net income per common share	0.50	0.56	0.60	0.56

Net income was $15.00 million for the fourth quarter of 2014, compared to the $13.72 million of net income reported for the fourth quarter of 2013. Diluted net income per common share for the fourth quarter of 2014 amounted to $0.62, compared to $0.56 per common share reported in the fourth quarter of 2013.

The net interest margin was 3.61% for the fourth quarter of 2014 versus 3.59% for the same period in 2013.

Tax-equivalent net interest income was $41.29 million for the fourth quarter of 2014, up 4.53% from 2013's fourth quarter.

Our recovery of provision for loan and lease losses was $(0.82) million in the fourth quarter of 2014 compared to a recovery of provision for loan and lease losses of $(0.86) million in the fourth quarter of 2013. Net charge-offs were $1.51 million for the fourth quarter 2014, compared to net charge-offs of $0.14 million a year ago.

Noninterest income for the fourth quarter of 2014 was $19.88 million, compared to $17.99 million for the fourth quarter of 2013. Noninterest expense for the fourth quarter of 2014 was $41.99 million and was $38.59 million in the fourth quarter 2013.

The provision for income taxes included a one-time benefit of $2.12 million for the fourth quarter of 2014 which resulted in a lower effective tax rate. This benefit was the result of a reduction in uncertain tax positions due to settlements with taxing authorities and the lapse of the applicable statute of limitations.

Item 7A. Quantitative and Qualitative Disclosures about Market Risk.

For information regarding Quantitative and Qualitative Disclosures about Market Risk, see Part II, Item 7, Management's Discussion and Analysis of Financial Condition and Results of Operations, Interest Rate Risk Management.

Table of Contents

Item 8. Financial Statements and Supplementary Data.

Report of Independent Registered Public Accounting Firm

The Board of Directors and Shareholders of 1st Source Corporation

We have audited 1st Source Corporation's (the "Company's") internal control over financial reporting as of December 31, 2014, based on criteria established in Internal Control — Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (2013 framework) (the COSO criteria). 1st Source Corporation's management is responsible for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting included in the accompanying Management Report on Internal Control over Financial Reporting. Our responsibility is to express an opinion on the company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, 1st Source Corporation maintained, in all material respects, effective internal control over financial reporting as of December 31, 2014 based on the COSO criteria.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated statements of financial condition of 1st Source Corporation as of December 31, 2014 and 2013, and the related consolidated statements of income, comprehensive income, shareholders' equity and cash flows for each of the three years in the period ended December 31, 2014 and our report dated February 20, 2015 expressed an unqualified opinion thereon.

/s/ Ernst & Young LLP

Chicago, Illinois
February 20, 2015

Report of Independent Registered Public Accounting Firm

The Board of Directors and Shareholders of 1st Source Corporation

We have audited the accompanying consolidated statements of financial condition of 1st Source Corporation ("the Company") as of December 31, 2014 and 2013, and the related consolidated statements of income, comprehensive income, shareholders' equity, and cash flows for each of the three years in the period ended December 31, 2014. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion

on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of 1st Source Corporation at December 31, 2014 and 2013, and the consolidated results of its operations and its cash flows for each of the three years in the period ended December 31, 2014, in conformity with U.S. generally accepted accounting principles.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), 1st Source Corporation’s internal control over financial reporting as of December 31, 2014, based on criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (2013 framework) (the COSO criteria) and our report dated February 20, 2015 expressed an unqualified opinion thereon.

/s/ Ernst & Young LLP

Chicago, Illinois
February 20, 2015

Table of Contents

CONSOLIDATED STATEMENTS OF FINANCIAL CONDITION

December 31 (Dollars in thousands)	2014	2013
ASSETS		
Cash and due from banks	$64,834	$77,568
Federal funds sold and interest bearing deposits with other banks	1,356	2,484
Investment securities available-for-sale		
(amortized cost of $776,057 and $822,163 at December 31, 2014, and December 31, 2013, respectively)	791,118	832,700
Other investments	20,801	22,400
Trading account securities	205	192
Mortgages held for sale	13,604	6,079
Loans and leases, net of unearned discount:		
Commercial and agricultural loans	710,758	679,492
Auto and light truck	397,902	391,649
Medium and heavy duty truck	247,153	237,854
Aircraft financing	727,665	738,133
Construction equipment financing	399,940	333,088
Commercial real estate	616,587	583,997
Residential real estate	445,759	460,981
Consumer loans	142,810	124,130
Total loans and leases	3,688,574	3,549,324
Reserve for loan and lease losses	(85,068)	(83,505)
Net loans and leases	3,603,506	3,465,819
Equipment owned under operating leases, net	74,143	60,967
Net premises and equipment	50,328	46,630
Goodwill and intangible assets	85,371	86,343
Accrued income and other assets	124,692	121,644
Total assets	$4,829,958	$4,722,826
LIABILITIES		
Deposits:		
Noninterest bearing	$796,241	$735,212
Interest bearing	3,006,619	2,918,438
Total deposits	3,802,860	3,653,650
Short-term borrowings:		
Federal funds purchased and securities sold under agreements to repurchase	138,843	181,120
Other short-term borrowings	106,979	133,011
Total short-term borrowings	245,822	314,131
Long-term debt and mandatorily redeemable securities	56,232	58,335
Subordinated notes	58,764	58,764
Accrued expenses and other liabilities	51,807	52,568
Total liabilities	4,215,485	4,137,448
SHAREHOLDERS’ EQUITY		
Preferred stock; no par value Authorized 10,000,000 shares; none issued or outstanding	—	—
Common Stock; no par value Authorized 40,000,000 shares; issued 25,641,887 shares at December 31, 2014 and 2013	346,535	346,535
Retained earnings	302,242	261,626
	(43,711)	(29,364)

Cost of common stock in treasury (1,779,442 shares at December 31, 2014 and 1,319,377 shares at December 31, 2013)		
Accumulated other comprehensive income	9,407	6,581
Total shareholders’ equity	614,473	585,378
Total liabilities and shareholders’ equity	$4,829,958	$4,722,826

The accompanying notes are a part of the consolidated financial statements.

36

Table of Contents

CONSOLIDATED STATEMENTS OF INCOME

Year Ended December 31 (Dollars in thousands, except per share amounts)	2014	2013	2012
Interest income:			
Loans and leases	$161,215	$161,137	$161,376
Investment securities, taxable	13,054	14,414	16,426
Investment securities, tax-exempt	3,269	3,094	3,340
Other	1,016	940	943
Total interest income	178,554	179,585	182,085
Interest expense:			
Deposits	11,356	16,604	21,877
Short-term borrowings	541	211	169
Subordinated notes	4,220	4,220	6,484
Long-term debt and mandatorily redeemable securities	2,108	1,733	1,779
Total interest expense	18,225	22,768	30,309
Net interest income	160,329	156,817	151,776
Provision for loan and lease losses	3,733	772	5,752
Net interest income after provision for loan and lease losses	156,596	156,045	146,024
Noninterest income:			
Trust fees	18,511	17,383	16,498
Service charges on deposit accounts	8,684	9,177	10,418
Debit card income	9,585	8,882	8,389
Mortgage banking income	5,381	5,944	8,357
Insurance commissions	5,556	5,492	5,494
Equipment rental income	17,156	16,229	18,796
Gains (losses) on investment securities available-for-sale	963	(168)	282
Other income	12,051	14,273	12,958
Total noninterest income	77,887	77,212	81,192
Noninterest expense:			
Salaries and employee benefits	80,488	79,783	82,599
Net occupancy expense	9,311	8,700	7,819
Furniture and equipment expense	17,657	16,895	15,406
Depreciation — leased equipment	13,893	13,055	15,202
Professional fees	5,046	5,321	6,083
Supplies and communications	5,589	5,690	5,701
FDIC and other insurance	3,384	3,462	3,602
Business development and marketing expense	6,049	4,938	4,232
Loan and lease collection and repossession expense	1,102	4,030	5,772
Other expense	7,521	7,440	5,120
Total noninterest expense	150,040	149,314	151,536
Income before income taxes	84,443	83,943	75,680
Income tax expense	26,374	28,985	26,047
Net income	$58,069	$54,958	$49,633
Basic net income per common share	$2.39	$2.23	$2.02
Diluted net income per common share	$2.39	$2.23	$2.02

The accompanying notes are a part of the consolidated financial statements.

Table of Contents

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

Year Ended December 31 (Dollars in thousands)	2014	2013	2012
Net income	$58,069	$54,958	$49,633
Other comprehensive income (loss):			
Change in unrealized appreciation (depreciation) of available-for-sale securities	5,488	(20,915)	1,946
Reclassification adjustment for realized (gains) losses included in net income	(963)	168	(282)
Income tax effect	(1,699)	7,789	(636)
Other comprehensive income (loss), net of tax	2,826	(12,958)	1,028
Comprehensive income	$60,895	$42,000	$50,661

The accompanying notes are a part of the consolidated financial statements.

CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY

(Dollars in thousands, except per share amounts)	Preferred Stock	Common Stock	Retained Earnings	Cost of Common Stock in Treasury	Accumulated Other Comprehensive Income (Loss), Net	Total
Balance at January 1, 2012	$—	$346,535	$190,261	$(31,389)	$ 18,511	$523,918
Net income	—	—	49,633	—	—	49,633
Other comprehensive income	—	—	—	—	1,028	1,028
Issuance of 184,220 common shares under stock based compensation awards, including related tax effects	—	—	(21)	3,956	—	3,935
Cost of 154,637 shares of common stock acquired for treasury	—	—	—	(3,701)	—	(3,701)
Common stock dividend ($0.66 per share)	—	—	(16,158)	—	—	(16,158)
Balance at December 31, 2012	$—	$346,535	$223,715	$(31,134)	$ 19,539	$558,655
Net income	—	—	54,958	—	—	54,958
Other comprehensive loss	—	—	—	—	(12,958)	(12,958)
Issuance of 169,942 common shares under stock based compensation awards, including related tax effects	—	—	(388)	4,043	—	3,655
Cost of 90,058 shares of common stock acquired for treasury	—	—	—	(2,273)	—	(2,273)
Common stock dividend ($0.68 per share)	—	—	(16,659)	—	—	(16,659)
Balance at December 31, 2013	$—	$346,535	$261,626	$(29,364)	$ 6,581	$585,378
Net income	—	—	58,069	—	—	58,069
Other comprehensive income	—	—	—	—	2,826	2,826
Issuance of 83,341 common shares under stock based compensation awards, including related tax effects	—	—	(243)	1,995	—	1,752
Cost of 543,406 shares of common stock acquired for treasury	—	—	—	(16,342)	—	(16,342)
Common stock dividend ($0.71 per share)	—	—	(17,210)	—	—	(17,210)
Balance at December 31, 2014	$—	$346,535	$302,242	$(43,711)	$ 9,407	$614,473

The accompanying notes are a part of the consolidated financial statements.

Table of Contents

CONSOLIDATED STATEMENTS OF CASH FLOWS

Year Ended December 31 (Dollars in thousands)	2014	2013	2012
Operating activities:			
Net income	$58,069	$54,958	$49,633
Adjustments to reconcile net income to net cash provided by operating activities:			
Provision for loan and lease losses	3,733	772	5,752
Depreciation of premises and equipment	4,748	4,727	4,241
Depreciation of equipment owned and leased to others	13,893	13,055	15,202
Amortization of investment security premiums and accretion of discounts, net	4,351	3,499	4,214
Amortization of mortgage servicing rights	1,278	1,571	2,921
Mortgage servicing asset recoveries	—	—	(238)
Deferred income taxes	4,341	(1,947)	(7,641)
(Gains) losses on investment securities available-for-sale	(963)	168	(282)
Originations of loans held for sale, net of principal collected	(121,440)	(102,195)	(210,276)
Proceeds from the sales of loans held for sale	117,447	110,390	219,269
Net gain on sale of loans held for sale	(3,532)	(3,395)	(7,228)
Change in trading account securities	(13)	(46)	(14)
Change in interest receivable	(603)	160	928
Change in interest payable	(917)	(1,883)	(1,001)
Change in other assets	(484)	10,654	15,571
Change in other liabilities	(857)	(4,360)	1,254
Other	2,733	738	888
Net change in operating activities	81,784	86,866	93,193
Investing activities:			
Proceeds from sales of investment securities	1,236	48,888	61,001
Proceeds from maturities of investment securities	190,323	175,875	295,241
Purchases of investment securities	(148,841)	(201,029)	(355,811)
Net change in other investments	1,599	209	(3,635)
Loans sold or participated to others	16,889	25,054	28,919
Net change in loans and leases	(165,463)	(255,345)	(273,439)
Net change in equipment owned under operating leases	(27,069)	(21,849)	2,176
Purchases of premises and equipment	(8,489)	(6,508)	(9,478)
Net change in investing activities	(139,815)	(234,705)	(255,026)
Financing activities:			
Net change in demand deposits and savings accounts	102,130	166,683	223,037
Net change in time deposits	47,080	(137,380)	(118,831)
Net change in short-term borrowings	(68,309)	144,943	43,954
Proceeds from issuance of long-term debt	7,161	6,502	36,169
Payments on subordinated notes	—	—	(30,928)
Payments on long-term debt	(11,660)	(21,119)	(5,673)
Net proceeds from issuance of treasury stock	1,752	3,655	3,935
Acquisition of treasury stock	(16,342)	(2,273)	(3,701)
Cash dividends paid on common stock	(17,643)	(17,054)	(16,522)
Net change in financing activities	44,169	143,957	131,440
Net change in cash and cash equivalents	(13,862)	(3,882)	(30,393)
Cash and cash equivalents, beginning of year	80,052	83,934	114,327
Cash and cash equivalents, end of year	$66,190	$80,052	$83,934
Supplemental Information:			

Non-cash transactions:			
Loans transferred to other real estate and repossessed assets	$7,154	$7,942	$3,425
Common stock matching contribution to Employee Stock Ownership and Profit Sharing Plan	—	2,801	2,643
Cash paid for:			
Interest	$19,143	$24,651	$31,309
Income taxes	29,211	33,831	33,833

The accompanying notes are a part of the consolidated financial statements.

39

Table of Contents

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 1 — Accounting Policies

1st Source Corporation is a bank holding company headquartered in South Bend, Indiana that provides, through its subsidiaries (collectively referred to as “1st Source” or “the Company”), a broad array of financial products and services. 1st Source Bank (“Bank”), its banking subsidiary, offers commercial and consumer banking services, trust and investment management services, and insurance to individual and business clients in Indiana and Michigan. The following is a summary of significant accounting policies followed in the preparation of the consolidated financial statements.

Basis of Presentation — The financial statements consolidate 1st Source and its subsidiaries (principally the Bank). All significant intercompany balances and transactions have been eliminated. For purposes of the parent company only financial information presented in Note 22, investments in subsidiaries are carried at equity in the underlying net assets.

Use of Estimates in the Preparation of Financial Statements — Financial statements prepared in accordance with U.S. generally accepted accounting principles (GAAP) require the Company to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of income and expenses during the reporting period. Actual results could differ from those estimates.

Business Combinations — Business combinations are accounted for under the purchase method of accounting. Under the purchase method, assets and liabilities of the business acquired are recorded at their estimated fair values as of the date of acquisition with any excess of the cost of the acquisition over the fair value of the net tangible and intangible assets acquired recorded as goodwill. Results of operations of the acquired business are included in the income statement from the date of acquisition.

Cash Flows — For purposes of the consolidated and parent company only statements of cash flows, the Company considers cash and due from banks, federal funds sold and interest bearing deposits with other banks with original maturities of three months or less as cash and cash equivalents.

Securities — Securities that the Company has the ability and positive intent to hold to maturity are classified as investment securities held-to-maturity. Held-to-maturity investment securities, when present, are carried at amortized cost. As of December 31, 2014 and 2013, the Company held no securities classified as held-to-maturity. Securities that may be sold in response to, or in anticipation of, changes in interest rates and resulting prepayment risk, or for other factors, are classified as available-for-sale and are carried at fair value. Unrealized gains and losses on these securities are reported, net of applicable taxes, as a separate component of accumulated other comprehensive income (loss) in shareholders’ equity.

The initial indication of other-than-temporary impairment (OTTI) for both debt and equity securities is a decline in fair value below amortized cost. Quarterly, any impaired securities are analyzed on a qualitative and quantitative basis in determining OTTI. Declines in the fair value of available-for-sale debt securities below their cost that are deemed to be other-than-temporary are reflected in earnings as realized losses to the extent the impairment is related to credit losses. The amount of impairment related to other factors is recognized in other comprehensive income. In estimating OTTI impairment losses, the Company considers among other things, (i) the length of time and the extent to which fair value has been less than cost, (ii) the financial condition and near-term prospects of the issuer, and (iii) whether it is more likely than not that the Company will not have to sell any such securities before an anticipated recovery of cost.

Debt and equity securities that are purchased and held principally for the purpose of selling them in the near term are classified as trading account securities and are carried at fair value with unrealized gains and losses reported in earnings. Realized gains and losses on the sales of all securities are reported in earnings and computed using the specific identification cost basis.

Other investments consist of shares of Federal Home Loan Bank of Indianapolis (FHLBI) and Federal Reserve Bank stock. As restricted member stocks, these investments are carried at cost. Both cash and stock dividends received on the stocks are reported as income. Quarterly, the Company reviews its investment in FHLBI for impairment. Factors considered in determining impairment are: history of dividend payments; determination of cause for any net loss;

adequacy of capital; and review of the most recent financial statements. As of December 31, 2014 and 2013, it was determined that the Company's investment in FHLBI stock is appropriately valued at cost, which equates to par value. In addition, other investments include interest bearing deposits with other banks with original maturities of greater than three months. These investments are in denominations, including accrued interest, that are fully insured by the FDIC.

Loans and Leases — Loans are stated at the principal amount outstanding, net of unamortized deferred loan origination fees and costs and net of unearned income. Interest income is accrued as earned based on unpaid principal balances. Origination fees and direct loan and lease origination costs are deferred and the net amount amortized to interest income over the estimated life of the related loan or lease. Loan commitment fees are deferred and amortized into other income over the commitment period.

Direct financing leases are carried at the aggregate of lease payments plus estimated residual value of the leased property, net of unamortized deferred lease origination fees and costs and unearned income. Interest income on direct financing leases is recognized over the term of the lease to achieve a constant periodic rate of return on the outstanding investment.

Table of Contents

The accrual of interest on loans and leases is discontinued when a loan or lease becomes contractually delinquent for 90 days, or when an individual analysis of a borrower's credit worthiness indicates a credit should be placed on nonperforming status, except for residential mortgage loans and consumer loans that are well secured and in the process of collection. Residential mortgage loans are placed on nonaccrual at the time the loan is placed in foreclosure. When interest accruals are discontinued, interest credited to income in the current year is reversed and interest accrued in the prior year is charged to the reserve for loan and lease losses. However, in some cases, the Company may elect to continue the accrual of interest when the net realizable value of collateral is sufficient to cover the principal and accrued interest. When a loan or lease is classified as nonaccrual and the future collectibility of the recorded loan or lease balance is doubtful, collections on interest and principal are applied as a reduction to principal outstanding. Loans are returned to accrual status when all principal and interest amounts contractually due are brought current and future payments are reasonably assured, which is typically evidenced by a sustained repayment performance of at least six months.

A loan or lease is considered impaired, based on current information and events, if 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 or lease agreement. Interest on impaired loans and leases, which are not classified as nonaccrual, is recognized on the accrual basis. The Company evaluates loans and leases exceeding $100,000 for impairment and establishes a specific reserve as a component of the reserve for loan and lease losses when it is probable all amounts due will not be collected pursuant to the contractual terms of the loan or lease and the recorded investment in the loan or lease exceeds its fair value.

Loans and leases that have been modified and economic concessions have been granted to borrowers who have experienced financial difficulties are considered a troubled debt restructuring (TDR) and, by definition, are deemed an impaired loan. These concessions typically result from the Company's loss mitigation activities and may include reductions in the interest rate, payment extensions, forgiveness of principal, forbearance or other actions. Certain TDRs are classified as nonperforming at the time of restructuring and typically are returned to performing status after considering the borrower's sustained repayment performance for a reasonable period of at least six months.

When the Company modifies loans and leases in a TDR, it evaluates any possible impairment similar to other impaired loans based on the present value of expected future cash flows, discounted at the contractual interest rate of the original loan or lease agreement, or uses the current fair value of the collateral, less selling costs for collateral dependent loans. If the Company determines that the value of the modified loan is less than the recorded investment in the loan (net of previous charge-offs, deferred loan fees or costs and unamortized premium or discount), impairment is recognized through a reserve for loan and lease losses estimate or a charge-off to the reserve for loan and lease losses. In periods subsequent to modification, the Company evaluates all TDRs, including those that have payment defaults, for possible impairment and recognizes impairment through the reserve for loan and lease losses.

The Company sells mortgage loans to the Government National Mortgage Association (GNMA) in the normal course of business and retains the servicing rights. The GNMA programs under which the loans are sold allow the Company to repurchase individual delinquent loans that meet certain criteria from the securitized loan pool. At its option, and without GNMA's prior authorization, the Company may repurchase a delinquent loan for an amount equal to 100% of the remaining principal balance on the loan. Once the Company has the unconditional ability to repurchase a delinquent loan, the Company is deemed to have regained effective control over the loan and the Company is required to recognize the loan on its balance sheet and record an offsetting liability, regardless of its intent to repurchase the loan. At December 31, 2014 and 2013, residential real estate portfolio loans included $5.20 million and $6.73 million, respectively, of loans available for repurchase under the GNMA optional repurchase programs with the offsetting liability recorded within other short-term borrowings.

Mortgage Banking Activities — Loans held for sale are composed of performing one-to-four family residential mortgage loans originated for resale. Mortgage loans originated with the intent to sell are carried at fair value.

The Company recognizes the rights to service mortgage loans for others as separate assets, whether the servicing rights are acquired through a separate purchase or through the sale of originated loans with servicing rights retained. The Company allocates a portion of the total proceeds of a mortgage loan to servicing rights based on the relative fair value. These assets are amortized as reductions of mortgage servicing fee income over the estimated servicing period

in proportion to the estimated servicing income to be received. Gains and losses on the sale of MSRs are recognized in Noninterest Income on the Statements of Income in the period in which such rights are sold.
MSRs are evaluated for impairment at each reporting date. For purposes of impairment measurement, MSRs are stratified based on the predominant risk characteristics of the underlying servicing, principally by loan type. If temporary impairment exists within a tranche, a valuation allowance is established through a charge to income equal to the amount by which the carrying value exceeds the fair value. If it is later determined all or a portion of the temporary impairment no longer exists for a particular tranche, the valuation allowance is reduced through a recovery of income.

41

Table of Contents

MSRs are also reviewed for other-than-temporary impairment. Other-than-temporary impairment exists when recoverability of a recorded valuation allowance is determined to be remote considering historical and projected interest rates, prepayments, and loan pay-off activity. When this situation occurs, the unrecoverable portion of the valuation allowance is applied as a direct write-down to the carrying value of the MSRs. Unlike a valuation allowance, a direct write-down permanently reduces the carrying value of the MSRs and the valuation allowance, precluding subsequent recoveries.

As part of mortgage banking operations, the Company enters into commitments to originate loans whereby the interest rate on these loans is determined prior to funding (“rate lock commitments”). Similar to loans held for sale, the fair value of rate lock commitments is subject to change primarily due to changes in interest rates. Under the Company’s risk management policy, these fair values are hedged primarily by selling forward contracts on agency securities. The rate lock commitments on mortgage loans intended to be sold and the related hedging instruments are recorded at fair value with changes in fair value recorded in current earnings.

Reserve for Loan and Lease Losses — The reserve for loan and lease losses is maintained at a level believed to be appropriate by the Company to absorb probable losses inherent in the loan and lease portfolio. The determination of the reserve requires significant judgment reflecting the Company’s best estimate of probable loan and lease losses related to specifically identified impaired loans and leases as well as probable losses in the remainder of the various loan and lease portfolios. For purposes of determining the reserve, the Company has segmented loans and leases into classes based on the associated risk within these segments. The Company has determined that eight classes exist within the loan and lease portfolio. The methodology for assessing the appropriateness of the reserve consists of several key elements, which include: specific reserves for impaired loans, formula reserves for each business lending division portfolio including percentage allocations for special attention loans and leases not deemed impaired, and reserves for pooled homogenous loans and leases. The Company’s evaluation is based upon a continuing review of these portfolios, estimates of customer performance, collateral values and dispositions, and assessments of economic and geopolitical events, all of which are subject to judgment and will change.

Specific reserves are established for certain business and specialty finance credits based on a regular analysis of special attention loans and leases. This analysis is performed by the Credit Policy Committee (CPC), the Loan Review Department, Credit Administration, and the Loan Workout Departments. The specific reserves are based on an analysis of underlying collateral values, cash flow considerations and, if applicable, guarantor capacity. Sources for determining collateral values include appraisals, evaluations, auction values and industry guides. Generally, for loans secured by commercial real estate and dependent on cash flows from the underlying collateral to service the debt, a new appraisal is obtained at the time the credit is deemed to be impaired. For non-income producing commercial real estate, an appraisal or evaluation is ordered depending on an analysis of the underlying factors, including an assessment of the overall credit worthiness of the borrower, the value of non-real estate collateral supporting the transaction and the date of the most recent existing appraisal or evaluation. An evaluation may be performed in lieu of obtaining a new appraisal for less complex transactions secured by local market properties. Values based on evaluations are discounted more heavily than those determined by appraisals when calculating loan impairment. Appraisals, evaluations and industry guides are used to determine aircraft values. Appraisals, industry guides and auction values are used to determine construction equipment, truck and auto values.

The formula reserves determined for each business lending division portfolio are calculated quarterly by applying loss factors to outstanding loans and leases based upon a review of historical loss experience and qualitative factors, which include but are not limited to, economic trends, current market risk assessment by industry, recent loss experience in particular segments of the portfolios, movement in equipment values collateralizing specialized industry portfolios, concentrations of credit, delinquencies, trends in volume, experience and depth of relationship managers and division management, and the effects of changes in lending policies and practices, including changes in quality of the loan and lease origination, servicing and risk management processes. Special attention loans and leases without specific reserves receive a higher percentage allocation ratio than credits not considered special attention.

Pooled loans and leases are smaller credits and are homogenous in nature, such as consumer credits and residential mortgages. Pooled loan and lease loss reserves are based on historical net charge-offs, adjusted for delinquencies, the effects of lending practices and programs and current economic conditions, and current trends in the geographic

markets which the Company serves.

A comprehensive analysis of the reserve is performed on a quarterly basis by reviewing all loans and leases over a fixed dollar amount ($100,000) where the internal credit quality grade is at or below a predetermined classification. Although the Company determines the amount of each element of the reserve separately and relies on this process as an important credit management tool, the entire reserve is available for the entire loan and lease portfolio. The actual amount of losses incurred can vary significantly from the estimated amounts both positively and negatively. The Company's methodology includes several factors intended to minimize the difference between estimated and actual losses. These factors allow the Company to adjust its estimate of losses based on the most recent information available.

Table of Contents

Impaired loans are reviewed quarterly to assess the probability of being able to collect the portion considered impaired. When a review and analysis of the underlying credit and collateral indicates ultimate collection is improbable, the deficiency is charged-off and deducted from the reserve. Loans and leases, which are deemed uncollectible or have a low likelihood of collection, are charged-off and deducted from the reserve, while recoveries of amounts previously charged-off are credited to the reserve. A (recovery of) provision for loan and lease losses is credited or charged to operations based on the Company’s periodic evaluation of the factors previously mentioned, as well as other pertinent factors.

Equipment Owned Under Operating Leases — The Company finances various types of construction equipment, medium and heavy duty trucks, automobiles and other equipment under leases classified as operating leases. The equipment underlying the operating leases is reported at cost, net of accumulated depreciation, in the Statements of Financial Condition. These operating lease arrangements require the lessee to make a fixed monthly rental payment over a specified lease term generally ranging from three to seven years. Revenue consists of the contractual lease payments and is recognized on a straight-line basis over the lease term and reported as noninterest income. Leased assets are being depreciated on a straight-line method over the lease term to the estimate of the equipment’s fair market value at lease termination, also referred to as “residual” value. The depreciation of these operating lease assets is reported as Noninterest Expense on the Statements of Income. For automobile leases, fair value is based upon published industry market guides. For other equipment leases, fair value may be based upon observable market prices, third-party valuations, or prices received on sales of similar assets at the end of the lease term. These residual values are reviewed periodically to ensure the recorded amount does not exceed the fair market value at the lease termination. At the end of the lease, the operating lease asset is either purchased by the lessee or returned to the Company.

Other Real Estate — Other real estate acquired through partial or total satisfaction of nonperforming loans is included in Other Assets and recorded at fair value less anticipated selling costs based upon the property’s appraised value at the date of transfer, with any difference between the fair value of the property less cost to sell, and the carrying value of the loan charged to the reserve for loan losses or other income, if a positive adjustment. Other real estate also includes bank premises qualifying as held for sale. Bank premises are transferred at fair value less anticipated selling costs. Subsequent fair value write-downs or write-ups, to the extent of previous write-downs, property maintenance costs, and gains or losses recognized upon the sale of other real estate are recognized in Noninterest Expense on the Statements of Income. Gains or losses resulting from the sale of other real estate are recognized on the date of sale. As of December 31, 2014 and 2013, other real estate had carrying values of $1.74 million and $5.49 million, respectively, and is included in Other Assets in the Statements of Financial Condition.

Repossessed Assets — Repossessed assets may include fixtures and equipment, inventory and receivables, aircraft, construction equipment, and vehicles acquired from business banking and specialty finance activities. Repossessed assets are included in Other Assets at fair value of the equipment or vehicle less estimated selling costs. At the time of repossession, the recorded amount of the loan or lease is written down to the fair value of the equipment or vehicle by a charge to the reserve for loan and lease losses or other income, if a positive adjustment. Subsequent fair value write-downs or write-ups, to the extent of previous write-downs, equipment maintenance costs, and gains or losses recognized upon the sale of repossessions are recognized in Noninterest Expense on the Statements of Income. Gains or losses resulting from the sale of repossessed assets are recognized on the date of sale. Repossessed assets totaled $5.16 million and $4.26 million, as of December 31, 2014 and 2013, respectively, and are included in Other Assets in the Statements of Financial Condition.

Premises and Equipment — Premises and equipment are stated at cost, less accumulated depreciation and amortization. The provision for depreciation is computed by the straight-line method, primarily with useful lives ranging from three to 31.5 years. Maintenance and repairs are charged to expense as incurred, while improvements, which extend the useful life, are capitalized and depreciated over the estimated remaining life.

Goodwill and Intangibles — Goodwill represents the excess of the cost of businesses acquired over the fair value of the net assets acquired. Other intangible assets represent purchased assets that also lack physical substance but can be distinguished from goodwill because of contractual or other legal rights or because the asset is capable of being sold or exchanged either on its own or in combination with a related contract, asset, or liability. Goodwill is reviewed for impairment at least annually or on an interim basis if an event occurs or circumstances change that would more likely

than not reduce the carrying amount. Goodwill is allocated into two reporting units. Fair value for each reporting unit is estimated using stock price multiples or revenue multiples. Intangible assets that have finite lives are amortized over their estimated useful lives and are subject to impairment testing. All of the Company's other intangible assets have finite lives and are amortized on a straight-line basis over varying periods not exceeding eleven years. The Company performed the required annual impairment test of goodwill during the fourth quarter of 2014 and determined that no impairment exists.

Partnership Investment — The Company accounts for its investments in partnerships for which it owns three percent or more of the partnership on the equity method. The partnerships in which the Company has investments account for their investments at fair value. As a result, the Company's investments in these partnerships reflect the underlying fair value of the partnerships' investments. The Company accounts for its investments in partnerships of which it owns less than three percent at the lower of cost or fair value. Investments in partnerships are included in Other Assets in the Statements of Financial Condition. The balances as of December 31, 2014 and 2013 were $2.78 million and $4.28 million, respectively.

Table of Contents

Short-Term Borrowings — Short-term borrowings consist of Federal funds purchased, securities sold under agreements to repurchase, commercial paper, Federal Home Loan Bank notes, and borrowings from non-affiliated banks. Federal funds purchased, securities sold under agreements to repurchase, and other short-term borrowings mature within one to 365 days of the transaction date. Commercial paper matures within seven to 270 days. Other short-term borrowings in the Statements of Financial Condition include the Company's liability related to mortgage loans available for repurchase under GNMA optional repurchase programs.
Securities purchased under agreements to resell and securities sold under agreements to repurchase are treated as collateralized financing transactions and are recorded at the amounts at which the securities were acquired or sold plus accrued interest. The fair value of collateral either received from or provided to a third party is continually monitored and additional collateral obtained or requested to be returned to the Company as deemed appropriate.
Trust Fees — Trust fees are recognized on the accrual basis.
Income Taxes — 1st Source and its subsidiaries file a consolidated Federal income tax return. The provision for incomes taxes is based upon income in the consolidated financial statements, rather than amounts reported on the income tax return. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized as income or expense in the period that includes the enactment date. A valuation allowance, if needed, reduces deferred tax assets to the expected amount most likely to be realized. Realization of deferred tax assets is dependent upon the generation of a sufficient level of future taxable income and recoverable taxes paid in prior years. Although realization is not assured, the Company believes it is more likely than not that all of the deferred tax assets will be realized.
Positions taken in the tax returns may be subject to challenge by the taxing authorities upon examination. Uncertain tax positions are initially recognized in the financial statements when it is more likely than not the position will be sustained upon examination by the tax authorities. Such tax positions are both initially and subsequently measured as the largest amount of tax benefit that is greater than 50% likely of being realized upon settlement with the tax authority, assuming full knowledge of the position and all relevant facts. The Company provides for interest and, in some cases, penalties on tax positions that may be challenged by the taxing authorities. Interest expense is recognized beginning in the first period that such interest would begin accruing. Penalties are recognized in the period that the Company claims the position in the tax return. Interest and penalties on income tax uncertainties are classified within Income Tax Expense in the Statements of Income.
Net Income Per Common Share — Basic earnings per common share is computed by dividing net income available to common shareholders by the weighted-average number of shares of common stock outstanding. Diluted earnings per common share is computed by dividing net income available to common shareholders by the weighted-average number of shares of common stock outstanding, plus the dilutive effect of outstanding stock options, stock warrants and nonvested stock-based compensation awards.
Stock-Based Employee Compensation — The Company recognizes stock-based compensation as compensation cost in the Statements of Income based on their fair values on the measurement date, which, for its purposes, is the date of grant. The Company accounts for stock-based compensation using the modified prospective transition method.
Segment Information — 1st Source has one principal business segment, commercial banking. While our chief decision makers monitor the revenue streams of various products and services, the identifiable segments' operations are managed and financial performance is evaluated on a company-wide basis. Accordingly, all of the Company's financial service operations are considered to be aggregated in one reportable operating segment.
Derivative Financial Instruments — The Company occasionally enters into derivative financial instruments as part of its interest rate risk and foreign currency risk management strategies. These derivative financial instruments consist primarily of interest rate swaps and foreign currency forward contracts. All derivative instruments are recorded on the Statements of Financial Condition, as either an asset or liability, at their fair value. The accounting for the gain or loss resulting from the change in fair value depends on the intended use of the derivative. For a derivative used to hedge changes in fair value of a recognized asset or liability, or an unrecognized firm commitment, the gain or loss on the

derivative will be recognized in earnings together with the offsetting loss or gain on the hedged item. This results in an earnings impact only to the extent that the hedge is ineffective in achieving offsetting changes in fair value. If it is determined that the derivative instrument is not highly effective as a hedge, hedge accounting is discontinued and the adjustment to fair value of the derivative instrument is recorded in earnings. For a derivative used to hedge changes in cash flows associated with forecasted transactions, the gain or loss on the effective portion of the derivative will be deferred, and reported as accumulated other comprehensive income, a component of shareholders' equity, until such time the hedged transaction affects earnings. For derivative instruments not accounted for as hedges, changes in fair value are recognized in noninterest income/expense. Deferred gains and losses from derivatives that are terminated and were in a cash flow hedge are amortized over the shorter of the original remaining term of the derivative or the remaining life of the underlying asset or liability.

Table of Contents

Fair Value Measurements — The Company records certain assets and liabilities at fair value. Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Securities available for sale, trading securities, mortgage loans held for sale, and derivative instruments are carried at fair value on a recurring basis. Fair value measurements are also utilized to determine the initial value of certain assets and liabilities, to perform impairment assessments, and for disclosure purposes. The Company uses quoted market prices and observable inputs to the maximum extent possible when measuring fair value. In the absence of quoted market prices, various valuation techniques are utilized to measure fair value. When possible, observable market data for identical or similar financial instruments are used in the valuation. When market data is not available, fair value is determined using valuation models that incorporate management's estimates of the assumptions a market participant would use in pricing the asset or liability.

Fair value measurements are classified within one of three levels based on the observability of the inputs used to determine fair value, as follows:

Level 1 — The valuation is based on quoted prices in active markets for identical instruments.

Level 2 — The valuation is based on observable inputs such as quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-based valuation techniques for which all significant assumptions are observable in the market.

Level 3 — The valuation is based on unobservable inputs that are supported by minimal or no market activity and that are significant to the fair value of the instrument. Level 3 valuations are typically performed using pricing models, discounted cash flow methodologies, or similar techniques that incorporate management's own estimates of assumptions that market participants would use in pricing the instrument, or valuations that require significant management judgment or estimation.

Reclassifications — Certain amounts in the prior periods consolidated financial statements have been reclassified to conform with the current year presentation. These reclassifications had no effect on total assets, shareholders' equity or net income as previously reported.

Note 2 — Recent Accounting Pronouncements

Troubled Debt Restructurings by Creditors: In August 2014, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2014-14 "Receivables - Troubled Debt Restructurings by Creditors (Subtopic 310-40) - Classification of Certain Government Guaranteed Mortgage Loans upon Foreclosure." ASU 2014-14 requires that a mortgage loan be derecognized and a separate other receivable be recognized upon foreclosure if certain conditions are met. Upon foreclosure, the separate other receivable should be measured based on the amount of the loan balance (principal and interest) expected to be recovered from the guarantor. ASU 2014-14 is effective for annual periods and interim periods within those annual periods, beginning after December 15, 2014. The amendments can be applied using either a prospective transition method or a modified retrospective transition method. Early adoption is permitted. The Company adopted ASU 2014-14 on January 1, 2015 and it did not have an impact on its accounting and disclosures.

Share Based Payments: In June 2014, the FASB issued ASU No. 2014-12 "Compensation - Stock Compensation (Topic 718) - Accounting for Share Based Payments When the Terms of an Award Provide That a Performance Target Could Be Achieved after the Requisite Service Period." ASU 2014-12 requires that a performance target that affects vesting and that could be achieved after the requisite service period be treated as a performance condition. ASU 2014-12 is effective for interim and annual periods beginning after December 15, 2015. The amendments can be applied prospectively to all awards granted or modified after the effective date or retrospectively to all awards with performance targets that are outstanding as of the beginning of the earliest annual period presented and to all new or modified awards thereafter. Early adoption is permitted. The Company has determined that ASU 2014-12 will not have an impact on its accounting and disclosures.

Repurchase to Maturity Transactions, Repurchase Financings and Disclosures: In June 2014, the FASB issued ASU No. 2014-11 "Transfers and Servicing (Topic 860) - Repurchase to Maturity Transactions, Repurchase Financings, and Disclosures." ASU 2014-11 aligns the accounting for repurchase to maturity transactions and repurchase agreements executed as a repurchase financing with the accounting for other typical repurchase agreements. Going forward, these transactions would all be accounted for as secured borrowings. ASU 2014-11 is effective for the first

interim or annual period beginning after December 15, 2014. In addition the disclosure of certain transactions accounted for as a sale is effective for the first interim or annual period beginning on or after December 15, 2014, and the disclosure for transactions accounted for as secured borrowings is required for annual periods beginning after December 15, 2014, and interim periods beginning after March 15, 2015. Early adoption is prohibited. The Company adopted ASU 2014-11 on January 1, 2015 and it did not have a material impact on its accounting and disclosures.

Table of Contents

Revenue from Contracts with Customers: In May 2014, the FASB issued ASU No. 2014-09 "Revenue from Contracts with Customers (Topic 606)." The core principle of the guidance is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods and services. ASU 2014-09 is effective for annual reporting periods beginning after December 15, 2016, including interim periods within that reporting period. The amendments can be applied retrospectively to each prior reporting period or retrospectively with the cumulative effect of initially applying this Update recognized at the date of initial application. Early application is not permitted. The Company is assessing the impact of ASU 2014-09 on its accounting and disclosures.

Reclassification of Residential Real Estate Collateralized Consumer Mortgage Loans Upon Foreclosure: In January 2014, the FASB issued ASU No. 2014-04 "Receivables - Troubled Debt Restructurings by Creditors (Subtopic 310-40) - Reclassification of Residential Real Estate Collateralized Consumer Mortgage Loans Upon Foreclosure." ASU 2014-04 clarifies when an in substance repossession or foreclosure occurs and requires interim and annual disclosures of the amount of foreclosed residential real estate property and the recorded investment in consumer mortgage loans collateralized by residential real estate property that are in the process of foreclosure. ASU 2014-04 is effective either on a modified retrospective transition method or a prospective transition method for interim and annual periods beginning after December 15, 2014. Early adoption is permitted. The Company adopted ASU 2014-04 on January 1, 2015 and it did not have a material impact on its disclosures.

Accounting for Investments in Qualified Affordable Housing Projects: In January 2014, the FASB issued ASU No. 2014-01 "Investments - Equity method and Joint Ventures (Topic 323) - Accounting for Investments in Qualified Affordable Housing Projects." ASU 2014-01 allows investors to use the proportional amortization method to account for investments in limited liability entities that manage or invest in affordable housing projects that qualify for low-income housing tax credits if certain conditions are met. ASU 2014-01 is effective retrospectively for interim and annual periods in fiscal years that begin after December 15, 2014. Early adoption is permitted. The Company adopted ASU 2014-01 on January 1, 2015 and it did not have a material impact on its accounting and disclosures for affordable housing projects.

Note 3 — Investment Securities

The following table shows investment securities available-for-sale.

(Dollars in thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
December 31, 2014				
U.S. Treasury and Federal agencies securities	$371,878	$ 3,593	$ (1,968)	$373,503
U.S. States and political subdivisions securities	121,510	3,392	(214)	124,688
Mortgage-backed securities - Federal agencies	248,299	5,490	(781)	253,008
Corporate debt securities	31,677	281	(26)	31,932
Foreign government and other securities	800	11	—	811
Total debt securities	774,164	12,767	(2,989)	783,942
Marketable equity securities	1,893	5,285	(2)	7,176
Total investment securities available-for-sale	$776,057	$ 18,052	$ (2,991)	$791,118
December 31, 2013				
U.S. Treasury and Federal agencies securities	$394,558	$ 5,008	$ (4,527)	$395,039
U.S. States and political subdivisions securities	120,416	3,670	(847)	123,239
Mortgage-backed securities - Federal agencies	273,495	5,148	(3,563)	275,080
Corporate debt securities	30,828	241	(4)	31,065
Foreign government and other securities	700	9	—	709
Total debt securities	819,997	14,076	(8,941)	825,132
Marketable equity securities	2,166	5,404	(2)	7,568
Total investment securities available-for-sale	$822,163	$ 19,480	$ (8,943)	$832,700

At December 31, 2014, the residential mortgage-backed securities held by the Company consisted primarily of GNMA, FNMA and FHLMC pass-through certificates which are guaranteed by those respective agencies of the

United States government (Government Sponsored Enterprise, GSEs).

46

Table of Contents

The following table shows the contractual maturities of investments in securities available-for-sale at December 31, 2014. Expected maturities will differ from contractual maturities, because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

(Dollars in thousands)	Amortized Cost	Fair Value
Due in one year or less	$28,513	$28,892
Due after one year through five years	451,001	455,126
Due after five years through ten years	44,139	44,644
Due after ten years	2,212	2,272
Mortgage-backed securities	248,299	253,008
Total debt securities available-for-sale	$774,164	$783,942

The following table shows the gross realized gains and losses on sale of securities from the securities available-for-sale portfolio, including marketable equity securities.

(Dollars in thousands)	2014	2013	2012
Gross realized gains	$963	$903	$282
Gross realized losses	—	(1,071)	—
Net realized gains (losses)	$963	$(168)	$282

The following table summarizes gross unrealized losses and fair value by investment category and age.

	Less than 12 Months		12 months or Longer		Total	
(Dollars in thousands)	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
December 31, 2014						
U.S. Treasury and Federal agencies securities	$54,944	$(148)	$115,195	$(1,820)	$170,139	$(1,968)
U.S. States and political subdivisions securities	16,805	(112)	8,333	(102)	25,138	(214)
Mortgage-backed securities - Federal agencies	21,754	(62)	32,781	(719)	54,535	(781)
Corporate debt securities	3,072	(26)	—	—	3,072	(26)
Foreign government and other securities	—	—	—	—	—	—
Total debt securities	96,575	(348)	156,309	(2,641)	252,884	(2,989)
Marketable equity securities	—	—	3	(2)	3	(2)
Total temporarily impaired available-for-sale securities	$96,575	$(348)	$156,312	$(2,643)	$252,887	$(2,991)
December 31, 2013						
U.S. Treasury and Federal agencies securities	$153,868	$(4,404)	$15,085	$(123)	$168,953	$(4,527)
U.S. States and political subdivisions securities	37,115	(814)	1,419	(33)	38,534	(847)
Mortgage-backed securities - Federal agencies	99,488	(3,099)	5,352	(464)	104,840	(3,563)
Corporate debt securities	6,332	(4)	—	—	6,332	(4)
Foreign government and other securities	—	—	—	—	—	—
Total debt securities	296,803	(8,321)	21,856	(620)	318,659	(8,941)
Marketable equity securities	—	—	4	(2)	4	(2)
Total temporarily impaired available-for-sale securities	$296,803	$(8,321)	$21,860	$(622)	$318,663	$(8,943)

There were no OTTI write-downs in 2014, 2013 or 2012.

At December 31, 2014, the Company does not have the intent to sell any of the available-for-sale securities in the table above and believes that it is more likely than not that it will not have to sell any such securities before an anticipated recovery of cost. The unrealized losses on debt securities are due to market volatility. The fair value is expected to recover on all debt securities as they approach their maturity date or repricing date or if market yields for such investments decline. The Company does not believe any of the securities are impaired due to reasons of credit

quality.
At December 31, 2014 and 2013, investment securities with carrying values of $231.50 million and $237.42 million, respectively, were pledged as collateral for security repurchase agreements and for other purposes.

Table of Contents

Note 4 — Loan and Lease Financings

Total loans and leases outstanding were recorded net of unearned income and deferred loan fees and costs at December 31, 2014 and 2013, and totaled $3.69 billion and $3.55 billion, respectively. At December 31, 2014 and 2013, net deferred loan and lease costs were $4.00 million and $3.81 million, respectively.

The loan and lease portfolio includes direct financing leases, which are included in auto and light truck, medium and heavy duty truck, aircraft financing, and construction equipment financing on the Statements of Financial Condition. The following table shows the summary of the gross investment in lease financing and the components of the investment in lease financing at December 31, 2014 and 2013.

(Dollars in thousands)	2014	2013
Direct finance leases:		
Rentals receivable	$234,772	$245,207
Estimated residual value of leased assets	13,458	12,537
Gross investment in lease financing	248,230	257,744
Unearned income	(37,356)	(38,946)
Net investment in lease financing	$210,874	$218,798

At December 31, 2014, the direct financing minimum future lease payments receivable for each of the years 2015 through 2019 were $48.18 million, $41.22 million, $38.29 million, $32.85 million, and $25.14 million, respectively.

In the ordinary course of business, the Company has extended loans to certain directors, executive officers, and principal shareholders of equity securities of 1st Source and to their affiliates. In the opinion of management, these loans are made on substantially the same terms, including interest rates and collateral, as those prevailing at the time for comparable transactions with persons not related to the Company and did not involve more than the normal risk of collectability, or present other unfavorable features. The loans are consistent with sound banking practices and within applicable regulatory and lending limitations. The aggregate dollar amounts of these loans were $27.93 million and $17.96 million at December 31, 2014 and 2013, respectively. During 2014, $12.36 million of new loans and other additions were made and repayments and other reductions totaled $2.39 million.

The Company evaluates loans and leases for credit quality at least annually but more frequently if certain circumstances occur (such as material new information which becomes available and indicates a potential change in credit risk). The Company uses two methods to assess credit risk: loan or lease credit quality grades and credit risk classifications. The purpose of the loan or lease credit quality grade is to document the degree of risk associated with individual credits as well as inform management of the degree of risk in the portfolio taken as a whole. Credit risk classifications are used to categorize loans by degree of risk and to designate individual or committee approval authorities for higher risk credits at the time of origination. Credit risk classifications include categories for: Acceptable, Marginal, Special Attention, Special Risk, Restricted by Policy, Regulated and Prohibited by Law.

All loans and leases, except residential real estate loans and consumer loans, are assigned credit quality grades on a scale from 1 to 12 with grade 1 representing superior credit quality. The criteria used to assign grades to extensions of credit that exhibit potential problems or well-defined weaknesses are primarily based upon the degree of risk and the likelihood of orderly repayment, and their effect on our safety and soundness. Loans or leases graded 7 or weaker are considered “special attention” credits and, as such, relationships in excess of $100,000 are reviewed quarterly as part of management’s evaluation of the appropriateness of the reserve for loan and lease losses. Grade 7 credits are defined as “watch” and contain greater than average credit risk and are monitored to limit our exposure to increased risk; grade 8 credits are “special mention” and, following regulatory guidelines, are defined as having potential weaknesses that deserve management’s close attention. Credits that exhibit well-defined weaknesses and a distinct possibility of loss are considered ‘‘classified’’ and are graded 9 through 12 corresponding to the regulatory definitions of “substandard” (grades 9 and 10) and the more severe ‘‘doubtful’’ (grade 11) and ‘‘loss’’ (grade 12).

Table of Contents

The following table shows the credit quality grades of the recorded investment in loans and leases, segregated by class.

	Credit Quality Grades		
(Dollars in thousands)	1-6	7-12	Total
December 31, 2014			
Commercial and agricultural loans	$683,169	$27,589	$710,758
Auto and light truck	380,425	17,477	397,902
Medium and heavy duty truck	243,798	3,355	247,153
Aircraft financing	691,018	36,647	727,665
Construction equipment financing	393,965	5,975	399,940
Commercial real estate	592,787	23,800	616,587
Total	$2,985,162	$114,843	$3,100,005
December 31, 2013			
Commercial and agricultural loans	$652,620	$26,872	$679,492
Auto and light truck	378,392	13,257	391,649
Medium and heavy duty truck	235,465	2,389	237,854
Aircraft financing	704,997	33,136	738,133
Construction equipment financing	325,849	7,239	333,088
Commercial real estate	557,692	26,305	583,997
Total	$2,855,015	$109,198	$2,964,213

For residential real estate and consumer loans, credit quality is based on the aging status of the loan and by payment activity. The following table shows the recorded investment in residential real estate and consumer loans by performing or nonperforming status. Nonperforming loans are those loans which are on nonaccrual status or are 90 days or more past due.

(Dollars in thousands)	Performing	Nonperforming	Total
December 31, 2014			
Residential real estate	$442,918	$2,841	$445,759
Consumer	142,476	334	142,810
Total	$585,394	$3,175	$588,569
December 31, 2013			
Residential real estate	$458,385	$2,596	$460,981
Consumer	123,663	467	124,130
Total	$582,048	$3,063	$585,111

Table of Contents

The following table shows the recorded investment of loans and leases, segregated by class, with delinquency aging and nonaccrual status.

(Dollars in thousands)	Current	30-59 Days Past Due	60-89 Days Past Due	90 Days or More Past Due and Accruing	Total Accruing Loans	Nonaccrual	Total Financing Receivables
December 31, 2014							
Commercial and agricultural loans	$696,351	$—	$123	$ —	$ 696,474	$ 14,284	$710,758
Auto and light truck	397,815	48	1	—	397,864	38	397,902
Medium and heavy duty truck	247,097	—	—	—	247,097	56	247,153
Aircraft financing	699,054	541	15,597	—	715,192	12,473	727,665
Construction equipment financing	396,821	999	1,369	—	399,189	751	399,940
Commercial real estate	611,780	—	—	—	611,780	4,807	616,587
Residential real estate	441,508	1,099	311	873	443,791	1,968	445,759
Consumer	141,577	676	223	109	142,585	225	142,810
Total	$3,632,003	$3,363	$17,624	$ 982	$ 3,653,972	$ 34,602	$3,688,574
December 31, 2013							
Commercial and agricultural loans	$667,462	$263	$2	$ —	$ 667,727	$ 11,765	$679,492
Auto and light truck	387,881	222	36	—	388,139	3,510	391,649
Medium and heavy duty truck	237,645	20	—	—	237,665	189	237,854
Aircraft financing	713,832	10,309	3,627	—	727,768	10,365	738,133
Construction equipment financing	331,083	973	—	—	332,056	1,032	333,088
Commercial real estate	576,933	—	—	—	576,933	7,064	583,997
Residential real estate	456,782	1,334	269	197	458,582	2,399	460,981
Consumer	122,657	786	220	84	123,747	383	124,130
Total	$3,494,275	$13,907	$4,154	$ 281	$ 3,512,617	$ 36,707	$3,549,324

Interest income for the years ended December 31, 2014, 2013, and 2012, would have increased by approximately $3.03 million, $2.93 million, and $3.58 million, respectively, if the nonaccrual loans and leases had earned interest at their full contract rate.

Table of Contents

The following table shows impaired loans and leases, segregated by class, and the corresponding reserve for impaired loan and lease losses.

(Dollars in thousands)	Recorded Investment	Unpaid Principal Balance	Related Reserve
December 31, 2014			
With no related reserve recorded:			
Commercial and agricultural loans	$14,468	$14,467	$—
Auto and light truck	—	—	—
Medium and heavy duty truck	—	—	—
Aircraft financing	12,740	12,741	—
Construction equipment financing	746	746	—
Commercial real estate	11,707	11,707	—
Residential real estate	—	—	—
Consumer	—	—	—
Total with no related reserve recorded	39,661	39,661	—
With a reserve recorded:			
Commercial and agricultural loans	74	74	5
Auto and light truck	—	—	—
Medium and heavy duty truck	—	—	—
Aircraft financing	—	—	—
Construction equipment financing	—	—	—
Commercial real estate	798	798	80
Residential real estate	373	376	156
Consumer	—	—	—
Total with a reserve recorded	1,245	1,248	241
Total impaired loans	$40,906	$40,909	$241
December 31, 2013			
With no related reserve recorded:			
Commercial and agricultural loans	$11,231	$11,230	$—
Auto and light truck	3,499	3,499	—
Medium and heavy duty truck	—	—	—
Aircraft financing	9,764	9,764	—
Construction equipment financing	938	938	—
Commercial real estate	14,897	14,897	—
Residential real estate	—	—	—
Consumer	—	—	—
Total with no related reserve recorded	40,329	40,328	—
With a reserve recorded:			
Commercial and agricultural loans	—	—	—
Auto and light truck	—	—	—
Medium and heavy duty truck	—	—	—
Aircraft financing	563	563	113
Construction equipment financing	—	—	—
Commercial real estate	—	—	—
Residential real estate	381	381	161
Consumer	—	—	—
Total with a reserve recorded	944	944	274
Total impaired loans	$41,273	$41,272	$274

51

Table of Contents

The following table shows average recorded investment and interest income recognized on impaired loans and leases, segregated by class, for years ending December 31, 2014, 2013 and 2012.

(Dollars in thousands)	2014 Average Recorded Investment	2014 Interest Income	2013 Average Recorded Investment	2013 Interest Income	2012 Average Recorded Investment	2012 Interest Income
Commercial and agricultural loans	$16,325	$48	$10,077	$143	$9,322	$16
Auto and light truck	407	—	488	—	1,590	7
Medium and heavy duty truck	—	—	431	—	1,219	2
Aircraft financing	4,088	28	9,254	79	7,976	—
Construction equipment financing	938	—	2,799	5	4,409	6
Commercial real estate	13,162	588	17,655	610	22,126	441
Residential real estate	376	16	32	—	87	6
Consumer loans	—	—	—	—	—	—
Total	$35,296	$680	$40,736	$837	$46,729	$478

The following table shows the number of loans and leases classified as troubled debt restructuring (TDR) during 2014, 2013 and 2012, segregated by class, as well as the recorded investment as of December 31. The classification between nonperforming and performing is shown at the time of modification. Modification programs focused on extending maturity dates or modifying payment patterns with most TDRs experiencing a combination of concessions. The modifications did not result in the contractual forgiveness of principal or interest. There were three modifications during 2014, two modifications during 2013, and no modifications during 2012 that resulted in an interest rate reduction below market rate. Consequently, the financial impact of the modifications was immaterial.

(Dollars in thousands)	2014 Number of Modifications	2014 Recorded Investment	2013 Number of Modifications	2013 Recorded Investment	2012 Number of Modifications	2012 Recorded Investment
Performing TDRs:						
Commercial and agricultural loans	2	$273	1	$750	1	$127
Auto and light truck	—	—	—	—	—	—
Medium and heavy duty truck	—	—	—	—	—	—
Aircraft financing	2	337	—	—	—	—
Construction equipment financing	—	—	—	—	—	—
Commercial real estate	—	—	—	—	1	7,014
Residential real estate	—	—	1	381	1	101
Consumer	—	—	—	—	—	—
Total performing TDR modifications	4	610	2	1,131	3	7,242
Nonperforming TDRs:						
Commercial and agricultural loans	4	7,315	1	158	—	—
Auto and light truck	—	—	—	—	—	—
Medium and heavy duty truck	—	—	—	—	—	—
Aircraft financing	—	—	1	4,157	—	—
Construction equipment financing	—	—	—	—	3	1,316
Commercial real estate	1	798	—	—	1	1,141

Residential real estate	—	—	—	—	—	—
Consumer	—	—	—	—	—	—
Total nonperforming TDR modifications	5	8,113	2	4,315	4	2,457
Total TDR modifications	9	$8,723	4	$5,446	7	$9,699

52

Table of Contents

The following table shows the number of troubled debt restructured loans and leases which had payment defaults within twelve months following modification during the years ended December 31, 2014, 2013 and 2012, segregated by class, as well as the recorded investment as of December 31. The classification between nonperforming and performing is shown at the time of modification. Default occurs when a loan or lease is 90 days or more past due under the modified terms or transferred to nonaccrual.

(Dollars in thousands)	2014 Number of Defaults	Recorded Investment	2013 Number of Defaults	Recorded Investment	2012 Number of Defaults	Recorded Investment
Performing TDRs:						
Commercial and agricultural loans	—	$ —	1	$ 750	—	$ —
Auto and light truck	—	—	—	—	—	—
Medium and heavy duty truck	—	—	—	—	—	—
Aircraft financing	—	—	—	—	—	—
Construction equipment financing	—	—	—	—	—	—
Commercial real estate	—	—	—	—	—	—
Residential real estate	—	—	—	—	—	—
Consumer	—	—	—	—	—	—
Total performing TDR defaults	—	—	1	750	—	—
Nonperforming TDRs:						
Commercial and agricultural loans	1	255	—	—	3	113
Auto and light truck	—	—	—	—	—	—
Medium and heavy duty truck	—	—	—	—	—	—
Aircraft financing	—	—	—	—	—	—
Construction equipment financing	—	—	—	—	1	—
Commercial real estate	—	—	1	—	2	171
Residential real estate	—	—	—	—	—	—
Consumer	—	—	—	—	—	—
Total nonperforming TDR defaults	1	255	1	—	6	284
Total TDR defaults	1	$ 255	2	$ 750	6	$ 284

The following table shows the recorded investment of loans and leases classified as troubled debt restructurings as of December 31.

Year Ended December 31 (Dollars in thousands)	2014	2013
Performing TDRs	$9,118	$8,786
Nonperforming TDRs	14,507	11,824
Total TDRs	$23,625	$20,610

53

Table of Contents

Note 5 — Reserve for Loan and Lease Losses

The following table shows the changes in the reserve for loan and lease losses, segregated by class, for each of the three years ended December 31.

(Dollars in thousands)	Commercial and agricultural	Auto and light truck loans	Medium and heavy duty truck	Aircraft financing	Construction equipment financing	Commercial real estate	Residential real estate	Consumer loans	Total
December 31, 2014									
Reserve for loan and lease losses									
Balance, beginning of year	$11,515	$9,657	$4,212	$34,037	$5,972	$12,406	$4,093	$1,613	$83,505
Charge-offs	5,007	42	—	—	4	99	46	833	6,031
Recoveries	929	1,283	142	240	525	347	97	298	3,861
Net charge-offs (recoveries)	4,078	(1,241)	(142)	(240)	(521)	(248)	(51)	535	2,170
Provision (recovery of provision)	4,323	(572)	146	(2,043)	515	616	(42)	790	3,733
Balance, end of year	$11,760	$10,326	$4,500	$32,234	$7,008	$13,270	$4,102	$1,868	$85,068
Ending balance, individually evaluated for impairment	$5	$—	$—	$—	$—	$80	$156	$—	$241
Ending balance, collectively evaluated for impairment	11,755	10,326	4,500	32,234	7,008	13,190	3,946	1,868	84,827
Total reserve for loan and lease losses	$11,760	$10,326	$4,500	$32,234	$7,008	$13,270	$4,102	$1,868	$85,068
Recorded investment in loans									
Ending balance, individually evaluated for impairment	$14,542	$—	$—	$12,740	$746	$12,505	$373	$—	$40,906
Ending balance, collectively evaluated for impairment	696,216	397,902	247,153	714,925	399,194	604,082	445,386	142,810	3,647,668
Total recorded investment in loans	$710,758	$397,902	$247,153	$727,665	$399,940	$616,587	$445,759	$142,810	$3,688,57
December 31, 2013									
Reserve for loan and lease losses									
Balance, beginning of year	$12,326	$8,864	$3,721	$34,205	$5,390	$13,778	$3,652	$1,375	$83,311
Charge-offs	538	226	57	1,308	88	170	316	1,125	3,828
Recoveries	468	139	462	884	323	627	14	333	3,250
Net charge-offs (recoveries)	70	87	(405)	424	(235)	(457)	302	792	578
Provision (recovery of provision)	(741)	880	86	256	347	(1,829)	743	1,030	772

Balance, end of year	$11,515	$9,657	$4,212	$34,037	$5,972	$12,406	$4,093	$1,613	$83,505
Ending balance, individually evaluated for impairment	$—	$—	$—	$113	$—	$—	$161	$—	$274
Ending balance, collectively evaluated for impairment	11,515	9,657	4,212	33,924	5,972	12,406	3,932	1,613	83,231
Total reserve for loan and lease losses	$11,515	$9,657	$4,212	$34,037	$5,972	$12,406	$4,093	$1,613	$83,505
Recorded investment in loans									
Ending balance, individually evaluated for impairment	$11,231	$3,499	$—	$10,327	$938	$14,897	$381	$—	$41,273
Ending balance, collectively evaluated for impairment	668,261	388,150	237,854	727,806	332,150	569,100	460,600	124,130	3,508,051
Total recorded investment in loans	$679,492	$391,649	$237,854	$738,133	$333,088	$583,997	$460,981	$124,130	$3,549,32
December 31, 2012									
Reserve for loan and lease losses									
Balance, beginning of year	$13,091	$7,037	$5,174	$28,626	$6,295	$16,772	$3,362	$1,287	$81,644
Charge-offs	524	3,754	41	600	120	471	594	1,532	7,636
Recoveries	484	230	1,185	711	268	223	43	407	3,551
Net charge-offs (recoveries)	40	3,524	(1,144)	(111)	(148)	248	551	1,125	4,085
Provision (recovery of provision)	(725)	5,351	(2,597)	5,468	(1,053)	(2,746)	841	1,213	5,752
Balance, end of year	$12,326	$8,864	$3,721	$34,205	$5,390	$13,778	$3,652	$1,375	$83,311
Ending balance, individually evaluated for impairment	$729	$—	$—	$852	$—	$42	$—	$—	$1,623
Ending balance, collectively evaluated for impairment	11,597	8,864	3,721	33,353	5,390	13,736	3,652	1,375	81,688
Total reserve for loan and lease losses	$12,326	$8,864	$3,721	$34,205	$5,390	$13,778	$3,652	$1,375	$83,311
Recorded investment in loans									
Ending balance, individually evaluated for impairment	$8,647	$—	$474	$5,201	$5,109	$21,185	$101	$—	$40,717
Ending balance, collectively evaluated for impairment	630,422	396,602	213,073	691,278	273,865	533,783	438,540	109,273	3,286,836
	$639,069	$396,602	$213,547	$696,479	$278,974	$554,968	$438,641	$109,273	$3,327,55

Total recorded investment in loans

54

Table of Contents

Note 6 — Operating Leases

Operating lease equipment at December 31, 2014 and 2013 was $74.14 million and $60.97 million, respectively, net of accumulated depreciation of $29.62 million and $26.99 million, respectively.

The minimum future lease rental payments due from clients on operating lease equipment at December 31, 2014, totaled $54.87 million, of which $17.24 million is due in 2015, $14.62 million in 2016, $10.93 million in 2017, $7.35 million in 2018, $3.82 million in 2019, and $0.91 million thereafter. Depreciation expense related to operating lease equipment for the years ended December 31, 2014, 2013 and 2012 was $13.89 million, $13.06 million and $15.20 million, respectively.

Note 7 — Premises and Equipment

The following table shows premises and equipment as of December 31.

(Dollars in thousands)	2014	2013
Land	$15,785	$14,029
Buildings and improvements	51,412	48,149
Furniture and equipment	36,737	37,564
Total premises and equipment	103,934	99,742
Accumulated depreciation and amortization	(53,606)	(53,112)
Net premises and equipment	$50,328	$46,630

Depreciation and amortization of properties and equipment totaled $4.75 million in 2014, $4.73 million in 2013, and $4.24 million in 2012.

During 2014, the Company recorded long-lived asset impairment charges totaling $275,000. The impairment was recorded as a result of an appraisal on a building and was recognized in Other Expense on the Statements of Income.

Note 8 — Mortgage Servicing Rights

The unpaid principal balance of residential mortgage loans serviced for third parties was $825.17 million at December 31, 2014, compared to $839.26 million at December 31, 2013, and $921.20 million at December 31, 2012. Amortization expense on MSRs is expected to total $0.84 million, $0.70 million, $0.57 million, $0.47 million, and $0.39 million in 2015, 2016, 2017, 2018 and 2019, respectively. Projected amortization excludes the impact of future asset additions or disposals.

The following table shows changes in the carrying value of MSRs and the associated valuation allowance.

(Dollars in thousands)	2014	2013
Mortgage servicing rights:		
Balance at beginning of year	$4,844	$4,645
Additions	1,167	1,770
Amortization	(1,278)	(1,571)
Sales	—	—
Carrying value before valuation allowance at end of year	4,733	4,844
Valuation allowance:		
Balance at beginning of year	—	—
Impairment recoveries	—	—
Balance at end of year	$—	$—
Net carrying value of mortgage servicing rights at end of year	$4,733	$4,844
Fair value of mortgage servicing rights at end of year	$6,979	$8,127

At December 31, 2014, the fair value of MSRs exceeded the carrying value reported in the Statements of Financial Condition by $2.25 million. This difference represents increases in the fair value of certain MSRs that could not be recorded above cost basis.

Funds held in trust at 1st Source for the payment of principal, interest, taxes and insurance premiums applicable to mortgage loans being serviced for others, were approximately $14.74 million and $12.27 million at December 31, 2014 and December 31, 2013, respectively. Mortgage loan contractual servicing fees, including late fees and ancillary income, were $3.01 million, $3.21 million, and $3.63 million for 2014, 2013, and 2012, respectively. Mortgage loan contractual servicing fees are included in Mortgage Banking Income on the Statements of Income.

Table of Contents

Note 9 — Intangible Assets and Goodwill

At December 31, 2014, intangible assets consisted of goodwill of $83.68 million and other intangible assets of $1.69 million, which was net of accumulated amortization of $8.13 million. At December 31, 2013, intangible assets consisted of goodwill of $83.68 million and other intangible assets of $2.66 million, which was net of accumulated amortization of $7.16 million. Intangible asset amortization was $0.97 million, $1.16 million, and $1.32 million for 2014, 2013, and 2012, respectively. Amortization on other intangible assets is expected to total $0.70 million, $0.58 million, $0.36 million, and $0.05 million in 2015, 2016, 2017, and 2018, respectively.

The following table shows a summary of core deposit intangible and other intangible assets as of December 31.

(Dollars in thousands)	2014	2013
Core deposit intangibles:		
Gross carrying amount	$9,566	$9,566
Less: accumulated amortization	(7,888)	(6,947)
Net carrying amount	$1,678	$2,619
Other intangibles:		
Gross carrying amount	$254	$254
Less: accumulated amortization	(241)	(209)
Net carrying amount	$13	$45

Note 10 — Deposits

The aggregate amount of certificates of deposit of $250,000 or more and other time deposits of $250,000 or more outstanding at December 31, 2014 and 2013 was $295.42 million and $178.39 million, respectively.

The following table shows the amount of certificates of deposit of $250,000 or more and other time deposits of $250,000 or more outstanding at December 31, 2014, by time remaining until maturity.

(Dollars in thousands)	
Under 3 months	$111,366
4 – 6 months	54,745
7 – 12 months	16,760
Over 12 months	112,552
Total	$295,423

The following table shows scheduled maturities of time deposits, including both private and public funds, at December 31, 2014.

(Dollars in thousands)	
2015	$437,478
2016	169,782
2017	186,640
2018	137,284
2019	26,872
Thereafter	19,869
Total	$977,925

Note 11 — Borrowed Funds and Mandatorily Redeemable Securities

The following table shows the details of long-term debt and mandatorily redeemable securities as of December 31, 2014 and 2013.

(Dollars in thousands)	2014	2013
Federal Home Loan Bank borrowings (1.10% – 6.54%)	$38,582	$42,512
Mandatorily redeemable securities	15,678	14,072
Other long-term debt	1,972	1,751
Total long-term debt and mandatorily redeemable securities	$56,232	$58,335

Annual maturities of long-term debt outstanding at December 31, 2014, for the next five years and thereafter beginning in 2015, are as follows (in thousands): $1,068; $6,224; $26,243; $808; $718; and $21,171.

56

Table of Contents

At December 31, 2014, the Federal Home Loan Bank borrowings represented a source of funding for community economic development activities, agricultural loans and general funding for the bank and consisted of 18 fixed rate notes with maturities ranging from 2016 to 2024. These notes were collateralized by $48.23 million of certain real estate loans.

Mandatorily redeemable securities as of December 31, 2014 and 2013, of $15.68 million and $14.07 million, respectively reflected the "book value" shares under the 1st Source Executive Incentive Plan. See Note 16 - Employee Stock Benefit Plans for additional information. Dividends paid on these shares and changes in book value per share are recorded as other interest expense. Total interest expense recorded for 2014, 2013, and 2012 was $1.47 million, $1.00 million, and $1.11 million, respectively.

The following table shows the details of short-term borrowings as of December 31, 2014 and 2013.

	2014		2013	
(Dollars in thousands)	Amount	Weighted Average Rate	Amount	Weighted Average Rate
Federal funds purchased	$10,500	0.50 %	$63,500	0.34 %
Security repurchase agreements	128,343	0.10	117,620	0.08
Commercial paper	11,778	0.27	10,814	0.24
Other short-term borrowings	95,201	0.29	122,197	0.28
Total short-term borrowings	$245,822		$314,131	

Note 12 — Subordinated Notes

The Company sponsors one trust, 1st Source Master Trust (Capital Trust) of which 100% of the common equity is owned by the Company. The Capital Trust was formed in 2007 for the purpose of issuing corporation-obligated mandatorily redeemable capital securities (the capital securities) to third-party investors and investing the proceeds from the sale of the capital securities solely in junior subordinated debenture securities of the Company (the subordinated notes). The subordinated notes held by the Capital Trust are the sole assets of the Capital Trust. The Capital Trust qualifies as a variable interest entity for which the Company is not the primary beneficiary and therefore reported in the financial statements as an unconsolidated subsidiary. The junior subordinated debentures are reflected as subordinated notes in the Statements of Financial Condition with the corresponding interest distributions reflected as Interest Expense in the Statements of Income. The common shares issued by the Capital Trust are included in Other Assets in the Statements of Financial Condition.

Distributions on the capital securities issued by the Capital Trust are payable quarterly at a rate per annum equal to the interest rate being earned by the Capital Trust on the subordinated notes held by the Capital Trust. The capital securities are subject to mandatory redemption, in whole or in part, upon repayment of the subordinated notes. The Company has entered into agreements which, taken collectively, fully and unconditionally guarantee the capital securities subject to the terms of each of the guarantees. The capital securities held by the Capital Trust qualify as Tier 1 capital under Federal Reserve Board guidelines.

The following table shows subordinated notes at December 31, 2014.

(Dollars in thousands)	Amount of Subordinated Notes	Interest Rate	Maturity Date
June 2007 issuance (1)	$41,238	7.22 %	6/15/2037
August 2007 issuance (2)	17,526	7.10 %	9/15/2037
Total	$58,764		

(1) Fixed rate through life of debt.

(2) Fixed rate through September 15, 2017 then LIBOR +1.48% through remaining life of debt.

Note 13 — Earnings Per Share

Earnings per common share is computed using the two-class method. Basic earnings per common share is computed by dividing net income available to common shareholders by the weighted-average number of common shares outstanding during the applicable period, excluding outstanding participating securities. Participating securities

include non-vested restricted stock awards. Non-vested restricted stock awards are considered participating securities to the extent the holders of these securities receive non-forfeitable dividends at the same rate as holders of common stock. Diluted earnings per common share is computed using the weighted-average number of shares determined for the basic earnings per common share computation plus the dilutive effect of stock compensation using the treasury stock method.

57

Table of Contents

Stock options, where the exercise price was greater than the average market price of the common shares, were excluded from the computation of diluted earnings per common share because the result would have been antidilutive. No stock options were considered antidilutive as of December 31, 2014, 2013 and 2012.
The following table presents a reconciliation of the number of shares used in the calculation of basic and diluted earnings per common share for the three years ending December 31.

(Dollars in thousands - except per share amounts)	2014	2013	2012
Distributed earnings allocated to common stock	$17,091	$16,563	$16,027
Undistributed earnings allocated to common stock	40,249	37,673	32,923
Net earnings allocated to common stock	57,340	54,236	48,950
Net earnings allocated to participating securities	729	722	683
Net income allocated to common stock and participating securities	$58,069	$54,958	$49,633
Weighted average shares outstanding for basic earnings per common share	24,031,608	24,344,623	24,267,471
Dilutive effect of stock compensation	—	586	9,857
Weighted average shares outstanding for diluted earnings per common share	24,031,608	24,345,209	24,277,328
Basic earnings per common share	$2.39	$2.23	$2.02
Diluted earnings per common share	$2.39	$2.23	$2.02

Note 14 — Accumulated Other Comprehensive Income

The following table presents reclassifications out of accumulated other comprehensive income related to unrealized gains and losses on available-for-sale securities for the two years ending December 31.

(Dollars in thousands)	2014	2013	Affected Line Item in the Statements of Income
Realized gains (losses) included in net income	$963	$(168)	Gains (losses) on investment securities available-for-sale
	963	(168)	Income before income taxes
Tax effect	(361)	63	Income tax expense
Net of tax	$602	$(105)	Net income

Note 15 — Employee Benefit Plans

The 1st Source Corporation Employee Stock Ownership and Profit Sharing Plan (as amended, the "Plan") includes an employee stock ownership component, which is designed to invest in and hold 1st Source common stock, and a 401(k) plan component, which holds all Plan assets not invested in 1st Source common stock. The Plan encourages diversification of investments with opportunities to change investment elections and contribution levels.
Employees are eligible to participate in the Plan the first of the month following 90 days of employment. The Company matches dollar for dollar on the first 4% of deferred compensation, plus 50 cents on the dollar of the next 2% deferrals. The Company will also contribute to the Plan an amount designated as a fixed 2% employer contribution. The amount of fixed contribution is equal to two percent of the participant's eligible compensation. Additionally, each year the Company may, in its sole discretion, make a discretionary profit sharing contribution. As of December 31, 2014 and 2013, there were 1,308,041 and 1,399,533 shares, respectively, of 1st Source Corporation common stock held in relation to employee benefit plans.
The Company contributions are allocated among the participants on the basis of compensation. Each participant's account is credited with cash and/or shares of 1st Source common stock based on that participant's compensation earned during the year. After completing 5 years of service in which they worked at least 1,000 hours per year, a participant will be completely vested in the Company's contribution. An employee is always 100% vested in their deferral. Plan participants are entitled to receive distributions from their Plan accounts upon termination of service, retirement, or death.

Contribution expense for the years ended December 31, 2014, 2013, and 2012, amounted to $4.32 million, $4.38 million, and $4.52 million, respectively.

In addition to the 1st Source Corporation Employee Stock Ownership and Profit Sharing Plan, the Company provides a limited health care and life insurance benefit for some of its retired employees. Effective March 31, 2009, the Company amended the plan so that no new retirees would be covered by the plan. The amendment will have no effect on the coverage for retirees covered at the time of the amendment. Prior to amendment, all full-time employees became eligible for these retiree benefits upon reaching age 55 with 20 years of credited service. The retiree medical plan pays a stated percentage of eligible medical expenses reduced by any deductibles and payments made by government programs and other group coverage. The lifetime maximum benefit payable under the medical plan is $15,000 and for life insurance is $3,000.

Table of Contents

The Company's net periodic post retirement benefit cost (recovery) recognized in the Statements of Income for the years ended December 31, 2014, 2013 and 2012, amounted to $(0.05) million, $(0.04) million, and $(0.01) million, respectively. The accrued post retirement benefit cost was not material at December 31, 2014, 2013, and 2012.

Note 16 — Stock Based Compensation

As of December 31, 2014, the Company had four active stock-based employee compensation plans. These plans include three executive stock award plans, the Executive Incentive Plan (EIP), the Restricted Stock Award Plan (RSAP), the 1998 Performance Compensation Plan (PCP); and the Employee Stock Purchase Plan (ESPP). The 2011 Stock Option Plan was approved by the shareholders on April 21, 2011 but the Company had not made any grants through December 31, 2014. These stock-based employee compensation plans were established to help retain and motivate key employees. All of the plans have been approved by the shareholders of 1st Source Corporation. The Executive Compensation and Human Resources Committee (the "Committee") of the 1st Source Corporation Board of Directors has sole authority to select the employees, establish the awards to be issued, and approve the terms and conditions of each award under the stock-based compensation plans.

Stock-based compensation to employees is recognized as compensation cost in the Statements of Income based on their fair values on the measurement date, which, for 1st Source, is the date of grant. Stock-based compensation expense is recognized ratably over the requisite service period for all awards. The total fair value of share awards vested was $3.66 million during 2014, $1.97 million in 2013, and $4.30 million in 2012.

The following table shows the combined summary of activity regarding active stock option and stock award plans.

		Non-Vested Stock Awards Outstanding		Stock Options Outstanding	
	Shares Available for Grant	Number of Shares	Weighted-Average Grant-Date Fair Value	Number of Shares	Weighted-Average Exercise Price
Balance, January 1, 2012	2,320,492	530,848	$ 18.76	22,000	$ 12.04
Shares authorized - 2012 EIP	76,815	—	—	—	—
Shares authorized - 1998 Performance Compensation Plan	2,302	—	—	—	—
Granted	(98,617)	98,617	21.95	—	—
Stock options exercised	—	—	—	(14,500)	12.04
Stock awards vested	—	(190,674)	17.24	—	—
Forfeited	4,124	(5,587)	19.71	—	—
Canceled	—	—	—	—	—
Balance, December 31, 2012	2,305,116	433,204	20.15	7,500	12.04
Shares authorized - 2013 EIP	61,970	—	—	—	—
Shares authorized - 1998 Performance Compensation Plan	2,010	—	—	—	—
Granted	(88,980)	88,980	24.19	—	—
Stock options exercised	—	—	—	(7,500)	12.04
Stock awards vested	—	(85,985)	19.58	—	—
Forfeited	5,642	(10,754)	20.71	—	—
Canceled	—	—	—	—	—
Balance, December 31, 2013	2,285,758	425,445	21.09	—	—
Shares authorized - 2014 EIP	69,300	—	—	—	—
Granted	(110,851)	110,851	25.86	—	—
Stock awards vested	—	(130,657)	20.33	—	—
Forfeited	3,057	(5,607)	20.87	—	—
Canceled	—	—	—	—	—

Balance, December 31, 2014	2,247,264	400,032	$ 22.66	—	$ —

Stock Option Plans — Incentive stock option plans include the 2001 Stock Option Plan (the “2001 Plan”) and the 2011 Stock Option Plan (the “2011 Plan”). The 2001 Plan was terminated, except for outstanding options, after the 2011 Plan was approved by the shareholders. During 2013, all remaining shares available for issuance upon exercise from previous grants under the 2001 Plan were exercised. No additional grants will be made under the 2001 Plan. There were 2,000,000 shares available for issuance under the 2011 Plan.

Table of Contents

Each award from all plans is evidenced by an award agreement that specifies the option price, the duration of the option, the number of shares to which the option pertains, and such other provisions as the Committee determines. The option price is equal to the fair market value of a share of 1st Source Corporation's common stock on the date of grant. Options granted expire at such time as the Committee determines at the date of grant and in no event does the exercise period exceed a maximum of ten years. Upon merger, consolidation, or other corporate consolidation in which 1st Source Corporation is not the surviving corporation, as defined in the plans, all outstanding options immediately vest. There were zero, 7,500 and 14,500 stock options exercised during 2014, 2013 and 2012, respectively. All shares issued in connection with stock option exercises and non-vested stock awards are issued from available treasury stock. No stock-based compensation expense related to stock options was recognized in 2014, 2013 or 2012.
The fair value of each option on the date of grant is estimated using the Black-Scholes option pricing model. Expected volatility is based on the historical volatility estimated over a period equal to the expected life of the options. In estimating the fair value of stock options under the Black-Scholes valuation model, separate groups of employees that have similar historical exercise behavior are considered separately. The expected life of the options granted is derived based on past experience and represents the period of time that options granted are expected to be outstanding.
Stock Award Plans — Incentive stock award plans include the EIP, the PCP and the RSAP. The EIP is administered by the Committee. Awards under the EIP and PCP include "book value" shares and "market value" shares of common stock. These shares are awarded annually based on weighted performance criteria and generally vest over a period of five years. The EIP book value shares may only be sold to 1st Source and such sale is mandatory in the event of death, retirement, disability, or termination of employment. The RSAP is designed for key employees. Awards under the RSAP are made to employees recommended by the Chief Executive Officer and approved by the Committee. Shares granted under the RSAP vest over two to ten years and vesting is based upon meeting certain various criteria, including continued employment with 1st Source.
Stock-based compensation expense relating to the EIP, PCP and RSAP totaled $3.18 million in 2014, $2.90 million in 2013, and $2.07 million in 2012. The total income tax benefit recognized in the accompanying Statements of Income related to stock-based compensation was $1.20 million in 2014, $1.10 million in 2013, and $0.78 million in 2012. Unrecognized stock-based compensation expense related to non-vested stock awards (EIP/PCP/RSAP) was $6.37 million at December 31, 2014. At such date, the weighted-average period over which this unrecognized expense was expected to be recognized was 3.12 years.
The fair value of non-vested stock awards for the purposes of recognizing stock-based compensation expense is market price of the stock on the measurement date, which, for the Company's purposes is the date of the award.
Employee Stock Purchase Plan — The Company offers an ESPP for substantially all employees with at least two years of service on the effective date of an offering under the plan. Eligible employees may elect to purchase any dollar amount of stock, so long as such amount does not exceed 25% of their base rate of pay and the aggregate stock accrual rate for all offerings does not exceed $25,000 in any calendar year. The purchase price for shares offered is the lower of the closing market bid price for the offering date or the average market bid price for the five business days preceding the offering date. The purchase price and discount to the actual market closing price on the offering date for the 2014, 2013, and 2012 offerings were $30.39 (0.88%), $24.32 (1.82%), and $20.54 (0.15%), respectively. Payment for the stock is made through payroll deductions over the offering period, and employees may discontinue the deductions at any time and exercise the option or take the funds out of the program. The most recent offering began June 2, 2014 and runs through May 31, 2016, with $148,228 in stock value to be purchased at $30.39 per share.
Note 17 — Income Taxes
The following table shows the composition of income tax expense.

Year Ended December 31 (Dollars in thousands)	2014	2013	2012
Current:			
Federal	$20,999	$28,634	$30,041
State	1,034	2,298	3,647
Total current	22,033	30,932	33,688
Deferred:			
Federal	4,022	(2,337)	(7,087)

State	319	390	(554)
Total deferred	4,341	(1,947)	(7,641)
Total provision	$26,374	$28,985	$26,047

Table of Contents

The following table shows the reasons for the difference between income tax expense and the amount computed by applying the statutory federal income tax rate (35%) to income before income taxes.

	2014		2013		2012	
Year Ended December 31 (Dollars in thousands)	Amount	Percent of Pretax Income	Amount	Percent of Pretax Income	Amount	Percent of Pretax Income
Statutory federal income tax	$29,555	35.0 %	$29,380	35.0 %	$26,488	35.0 %
(Decrease) increase in income taxes resulting from:						
Tax-exempt interest income	(1,236)	(1.5)	(1,219)	(1.5)	(1,370)	(1.8)
State taxes, net of federal income tax benefit	2,300	2.7	1,747	2.1	2,010	2.7
Reduction in uncertain tax positions	(3,300)	(3.9)	—	—	—	—
Other	(945)	(1.1)	(923)	(1.1)	(1,081)	(1.5)
Total	$26,374	31.2 %	$28,985	34.5 %	$26,047	34.4 %

The tax expense (benefit) related to gains (losses) on investment securities available-for-sale for the years 2014, 2013, and 2012 was approximately $361,000, $(63,000), and $108,000, respectively.

The following table shows the composition of deferred tax assets and liabilities as of December 31, 2014 and 2013.

(Dollars in thousands)	2014	2013
Deferred tax assets:		
Reserve for loan and lease losses	$33,088	$32,545
Accruals for employee benefits	3,346	4,153
Other	1,079	2,243
Total deferred tax assets	37,513	38,941
Deferred tax liabilities:		
Differing depreciable bases in premises and leased equipment	24,506	22,296
Net unrealized gains on securities available-for-sale	5,654	3,956
Differing bases in assets related to acquisitions	5,160	4,725
Mortgage servicing	1,644	1,588
Capitalized loan costs	1,437	816
Prepaid expenses	1,035	931
Other	443	956
Total deferred tax liabilities	39,879	35,268
Net deferred tax (liability) asset	$(2,366)	$3,673

No valuation allowance for deferred tax assets was recorded at December 31, 2014 and 2013 as the Company believes it is more likely than not that all of the deferred tax assets will be realized.

The following table shows a reconciliation of the beginning and ending amounts of unrecognized tax benefits.

(Dollars in thousands)	2014	2013	2012
Balance, beginning of year	$4,611	$4,068	$3,387
Additions based on tax positions related to the current year	66	484	704
Additions for tax positions of prior years	592	1,118	1,471
Reductions for tax positions of prior years	(553)	—	(49)
Reductions due to lapse in statute of limitations	(1,650)	(1,059)	(1,445)
Settlements	(3,066)	—	—
Balance, end of year	$—	$4,611	$4,068

There were no unrecognized tax benefits that would affect the effective tax rate if recognized at December 31, 2014 and the total amount of unrecognized tax benefits that would affect the effective tax rate if recognized was $2.62 million at December 31, 2013 and $2.02 million at December 31, 2012. Interest and penalties are recognized through the income tax provision. For the years 2014, 2013 and 2012, the Company recognized approximately $(0.69) million, $0.14 million and $(0.02) million in interest, net of tax effect, and penalties, respectively. There were no accrued

interest and penalties at December 31, 2014 and interest and penalties of approximately $0.69 million and $0.55 million were accrued at December 31, 2013 and 2012, respectively.

Table of Contents

Tax years that remain open and subject to audit include the federal 2011-2014 years and the Indiana 2013-2014 years. Additionally, during 2014 the Company reached a state tax settlement for the 2010-2013 years and as a result recorded a reduction of unrecognized tax benefits in the amount of $2.93 million that affected the effective tax rate and increased earnings in the amount of $2.12 million. The Company does not anticipate a significant change in the amount of uncertain tax positions within the next 12 months.

Note 18 — Contingent Liabilities, Commitments, and Financial Instruments with Off-Balance-Sheet Risk

Contingent Liabilities —1st Source and its subsidiaries are defendants in various legal proceedings arising in the normal course of business. In the opinion of management, based upon present information including the advice of legal counsel, the ultimate resolution of these proceedings will not have a material effect on the Company's consolidated financial position or results of operations.

1st Source Bank sells residential mortgage loans to Fannie Mae as well as FHA-insured and VA-guaranteed loans in Ginnie Mae mortgage-backed securities. Additionally, the Bank has sold loans on a service released basis to various other financial institutions in recent years. The agreements under which the Bank sells these mortgage loans contain various representations and warranties regarding the acceptability of loans for purchase. On occasion, the Bank may be required to indemnify the loan purchaser for credit losses on loans that were later deemed ineligible for purchase or may be required to repurchase a loan. Both circumstances are collectively referred to as "repurchases."

The Company's liability for repurchases, included in accrued expenses and other liabilities on the Statements of Financial Condition, was $1.72 million and $2.46 million as of December 31, 2014 and 2013, respectively. The mortgage repurchase liability represents the Company's best estimate of the loss that it may incur. The estimate is based on specific loan repurchase requests and a historical loss ratio with respect to origination dollar volume. Because the level of mortgage loan repurchase losses are dependent on economic factors, investor demand strategies and other external conditions that may change over the life of the underlying loans, the level of liability for mortgage loan repurchase losses is difficult to estimate and requires considerable management judgment.

Commitments — 1st Source and its subsidiaries are obligated under operating leases for certain office premises and equipment. Future minimum rental commitments for all noncancellable operating leases total approximately, $3.16 million in 2015, $2.82 million in 2016, $2.52 million in 2017, $2.27 million in 2018, $2.18 million in 2019, and $3.12 million, thereafter. As of December 31, 2014, future minimum rentals to be received under noncancellable subleases totaled $2.25 million.

The following table shows rental expense of office premises and equipment and related sublease income.

Year Ended December 31 (Dollars in thousands)	2014	2013	2012
Gross rental expense	$3,799	$3,875	$3,787
Sublease rental income	(878)	(910)	(878)
Net rental expense	$2,921	$2,965	$2,909

Financial Instruments with Off-Balance-Sheet Risk —To meet the financing needs of our clients, 1st Source and its subsidiaries are parties to financial instruments with off-balance-sheet risk in the normal course of business. These off-balance-sheet financial instruments include commitments to originate and sell loans, and standby letters of credit. The instruments involve, to varying degrees, elements of credit and interest rate risk in excess of the amount recognized in the consolidated statements of financial condition.

The Company's exposure to credit loss in the event of nonperformance by the other party to the financial instruments for loan commitments and standby letters of credit is represented by the dollar amount of those instruments. The Company uses the same credit policies and collateral requirements in making commitments and conditional obligations as it does for on-balance-sheet instruments.

Loan commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The Company grants mortgage loan commitments to borrowers, subject to normal loan underwriting standards. The interest rate risk associated with these loan commitments is managed by entering into contracts for future deliveries of loans.

Standby letters of credit are conditional commitments issued to guarantee the performance of a client to a third party. The credit risk involved in and collateral obtained when issuing standby letters of credit are essentially the same as

those involved in extending loan commitments to clients. Standby letters of credit totaled $26.94 million and $19.27 million at December 31, 2014 and 2013, respectively. Standby letters of credit generally have terms ranging from six months to one year.

Note 19 — Derivative Financial Instruments

Commitments to originate residential mortgage loans held for sale and forward commitments to sell residential mortgage loans are considered derivative instruments. See Note 18 for further information.

Table of Contents

The Company has certain interest rate derivative positions that are not designated as hedging instruments. These derivative positions relate to transactions in which the Company enters into an interest rate swap with a client while at the same time entering into an offsetting interest rate swap with another financial institution. In connection with each transaction, the Company agrees to pay interest to the client on a notional amount at a variable interest rate and receive interest from the client on the same notional amount at a fixed interest rate. At the same time, the Company agrees to pay another financial institution the same fixed interest rate on the same notional amount and receive the same variable interest rate on the same notional amount. The transaction allows the client to effectively convert a variable rate loan to a fixed rate. Because the terms of the swaps with the customers and the other financial institution offset each other, with the only difference being counterparty credit risk, changes in the fair value of the underlying derivative contracts are not materially different and do not significantly impact the Company's results of operations. The following table shows the amounts of non-hedging derivative financial instruments at December 31, 2014 and 2013.

		Asset derivatives		Liability derivatives	
(Dollars in thousands)	Notional or contractual amount	Statement of Financial Condition classification	Fair value	Statement of Financial Condition classification	Fair value
Interest rate swap contracts	$459,508	Other assets	$9,125	Other liabilities	$9,302
Loan commitments	11,109	Mortgages held for sale	2	N/A	—
Forward contracts - mortgage loan	19,800	N/A	—	Mortgages held for sale	142
Total - December 31, 2014	$490,417		$9,127		$9,444
Interest rate swap contracts	$462,790	Other assets	$9,894	Other liabilities	$10,087
Loan commitments	7,878	Mortgages held for sale	12	N/A	—
Forward contracts - mortgage loan	10,600	Mortgages held for sale	121	N/A	—
Forward contracts - foreign exchange	1,308	N/A	—	Other assets	7
Total - December 31, 2013	$482,576		$10,027		$10,094

The following table shows the amounts included in the Statements of Income for non-hedging derivative financial instruments at December 31, 2014, 2013 and 2012.

		Gain (loss)		
(Dollars in thousands)	Statement of Income classification	2014	2013	2012
Interest rate swap contracts	Other expense	$16	$124	$131
Interest rate swap contracts	Other income	357	716	721
Loan commitments	Mortgage banking income	(10)	(208)	31
Forward contracts - mortgage loan	Mortgage banking income	(263)	154	185
Forward contracts - foreign exchange	Other income	79	(7)	—
Total		$179	$779	$1,068

The following table shows the offsetting of financial assets and derivative assets at December 31, 2014 and 2013.

Gross Amounts Not Offset in the Statement of

(Dollars in thousands)	Gross Amounts of Recognized Assets	Gross Amounts Offset in the Statement of Financial Condition	Net Amounts of Assets Presented in the Statement of Financial Condition	Financial Condition		Net Amount
				Financial Instruments	Cash Collateral Received	
December 31, 2014						
Interest rate swaps	$9,492	$367	$9,125	$—	$—	$9,125
December 31, 2013						
Interest rate swaps	$10,511	$617	$9,894	$—	$—	$9,894

63

Table of Contents

The following table shows the offsetting of financial liabilities and derivative liabilities at December 31, 2014 and 2013.

(Dollars in thousands)	Gross Amounts of Recognized Liabilities	Gross Amounts Offset in the Statement of Financial Condition	Net Amounts of Liabilities Presented in the Statement of Financial Condition	Gross Amounts Not Offset in the Statement of Financial Condition		
				Financial Instruments	Cash Collateral Pledged	Net Amount
December 31, 2014						
Interest rate swaps	$ 9,669	$ 367	$ 9,302	$—	$ 9,018	$ 284
Repurchase agreements	128,343	—	128,343	128,343	—	—
Total	$ 138,012	$ 367	$ 137,645	$ 128,343	$ 9,018	$ 284
December 31, 2013						
Interest rate swaps	$ 10,704	$ 617	$ 10,087	$—	$ 8,409	$ 1,678
Repurchase agreements	117,620	—	117,620	117,620	—	—
Total	$ 128,324	$ 617	$ 127,707	$ 117,620	$ 8,409	$ 1,678

If a default in performance of any obligation of a repurchase agreement occurs, each party will set-off property held in respect of transactions against obligations owing in respect of any other transactions.

Note 20 — Regulatory Matters

The Company is subject to various regulatory capital requirements administered by the Federal banking agencies. Failure to meet minimum capital requirements can result in certain mandatory and possible additional discretionary actions by regulators that, if undertaken, could have a material effect on the Company's financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Company must meet specific capital guidelines that involve quantitative measures of assets, liabilities, and certain off-balance-sheet items as calculated under regulatory accounting practices. Capital amounts and classification are subject to qualitative judgments by the regulators about components, risk weightings, and other factors.

Quantitative measures established by regulation to ensure capital adequacy require the Company to maintain minimum amounts and ratios of total capital and Tier I capital to risk-weighted assets and of Tier I capital to average assets. The Company believes that it meets all capital adequacy requirements to which it is subject.

The most recent notification from the Federal bank regulators categorized 1st Source Bank, the largest of its subsidiaries, as "well capitalized" under the regulatory framework for prompt corrective action. To be categorized as "well capitalized" the Bank must maintain minimum total risk-based, Tier I risk-based, and Tier I leverage ratios as set forth in the table below. There are no conditions or events since that notification that the Company believes will have changed the institution's category.

Table of Contents

As discussed in Note 12, the capital securities held by the Capital Trusts qualify as Tier 1 capital under Federal Reserve Board guidelines. The following table shows the actual and required capital amounts and ratios for 1st Source Corporation and 1st Source Bank as of December 31, 2014 and 2013.

	Actual			Minimum Capital Adequacy			To Be Well Capitalized Under Prompt Corrective Action Provisions		
(Dollars in thousands)	Amount	Ratio		Amount	Ratio		Amount	Ratio	
2014									
Total Capital (to Risk-Weighted Assets):									
1st Source Corporation	$629,023	15.89	%	$316,704	8.00	%	$395,880	10.00	%
1st Source Bank	598,038	15.15	%	315,886	8.00	%	394,857	10.00	%
Tier I Capital (to Risk-Weighted Assets):									
1st Source Corporation	576,692	14.57	%	158,352	4.00	%	237,528	6.00	%
1st Source Bank	548,094	13.88	%	157,943	4.00	%	236,914	6.00	%
Tier I Capital (to Average Assets):									
1st Source Corporation	576,692	12.16	%	189,718	4.00	%	237,147	5.00	%
1st Source Bank	548,094	11.57	%	189,412	4.00	%	236,765	5.00	%
2013									
Total Capital (to Risk-Weighted Assets):									
1st Source Corporation	$599,603	15.86	%	$302,409	8.00	%	$378,011	10.00	%
1st Source Bank	566,307	15.01	%	301,783	8.00	%	377,229	10.00	%
Tier I Capital (to Risk-Weighted Assets):									
1st Source Corporation	549,441	14.54	%	151,205	4.00	%	226,807	6.00	%
1st Source Bank	518,230	13.74	%	150,892	4.00	%	226,338	6.00	%
Tier I Capital (to Average Assets):									
1st Source Corporation	549,441	12.08	%	182,008	4.00	%	227,510	5.00	%
1st Source Bank	518,230	11.41	%	181,726	4.00	%	227,157	5.00	%

The Bank was not required to maintain noninterest bearing cash balances with the Federal Reserve Bank as of December 31, 2014 and 2013.

Dividends that may be paid by a subsidiary bank to the parent company are subject to certain legal and regulatory limitations and also may be affected by capital needs, as well as other factors.

Due to the Company’s mortgage activities, 1st Source Bank is required to maintain minimum net worth capital requirements established by various governmental agencies. 1st Source Bank’s net worth requirements are governed by the Department of Housing and Urban Development and GNMA. As of December 31, 2014, 1st Source Bank met its minimum net worth capital requirements.

Note 21 — Fair Value Measurements

The Company determines the fair values of its financial instruments based on the fair value hierarchy, which requires an entity to maximize the use of quoted prices and observable inputs and to minimize the use of unobservable inputs when measuring fair value. The Company elected fair value accounting for mortgages held for sale. The Company believes the election for mortgages held for sale (which are economically hedged with free-standing derivatives) will reduce certain timing differences and better match changes in the value of these assets with changes in the value of derivatives used as economic hedges for these assets. At December 31, 2014 and 2013, all mortgages held for sale are carried at fair value.

Table of Contents

The following table shows the differences between fair value carrying amount of mortgages held for sale measured at fair value and the aggregate unpaid principal amount the Company is contractually entitled to receive at maturity on December 31, 2014 and 2013.

(Dollars in thousands)	Fair value carrying amount	Aggregate unpaid principal	Excess of fair value carrying amount over (under) unpaid principal	
December 31, 2014				
Mortgages held for sale reported at fair value:				
Total Loans	$13,604	$13,526	$78	(1)
December 31, 2013				
Mortgages held for sale reported at fair value:				
Total Loans	$6,079	$5,974	$105	(1)

(1)The excess of fair value carrying amount over (under) unpaid principal is included in mortgage banking income and includes changes in fair value at and subsequent to funding and gains and losses on the related loan commitment prior to funding.

Financial Instruments on Recurring Basis:

The following is a description of the valuation methodologies used for financial instruments measured at fair value on a recurring basis:

Investment securities available for sale are valued primarily by a third party pricing agent. Prices supplied by the independent pricing agent, as well as their pricing methodologies and assumptions, are reviewed by the Company for reasonableness and to ensure such prices are aligned with market levels. In general, the Company’s investment securities do not possess a complex structure that could introduce greater valuation risk. The portfolio mainly consists of traditional investments including U.S. Treasury and Federal agencies securities, federal agency mortgage pass-through securities, and general obligation and revenue municipal bonds. Pricing for such instruments is fairly generic and is easily obtained. On a quarterly basis, prices supplied by the pricing agent are validated by comparison to prices obtained from other third party sources for a material portion of the portfolio.

The valuation policy and procedures for Level 3 fair value measurements of available for sale debt securities are decided through collaboration between management of the Corporate Accounting and Funds Management departments. The changes in fair value measurement for Level 3 securities are analyzed on a periodic basis under a collaborative framework with the aforementioned departments. The methodology and variables used for input are derived from the combination of observable and unobservable inputs. The unobservable inputs are determined through internal assumptions that may vary from period to period due to external factors, such as market movement and credit rating adjustments.

Both the market and income valuation approaches are implemented using the following types of inputs:

- U.S. treasuries are priced using the market approach and utilizing live data feeds from active market exchanges for identical securities.
- Government-sponsored agency debt securities and corporate bonds are primarily priced using available market information through processes such as benchmark curves, market valuations of like securities, sector groupings and matrix pricing.
- Other government-sponsored agency securities, mortgage-backed securities and some of the actively traded REMICs and CMOs, are primarily priced using available market information including benchmark yields, prepayment speeds, spreads and volatility of similar securities.
- Other inactive government-sponsored agency securities are primarily priced using consensus pricing and dealer quotes.
- State and political subdivisions are largely grouped by characteristics, i.e., geographical data and source of revenue in trade dissemination systems. Since some securities are not traded daily and due to other grouping limitations, active

market quotes are often obtained using benchmarking for like securities. Local direct placement municipal securities, with very little market activity, are priced using an appropriate market yield curve which incorporates a credit spread assumption.

- Marketable equity (common) securities are primarily priced using the market approach and utilizing live data feeds from active market exchanges for identical securities.

Trading account securities are priced using the market approach and utilizing live data feeds from active market exchanges for identical securities.

Table of Contents

Mortgages held for sale and the related loan commitments and forward contracts (hedges) are valued using a market value approach and utilizing an appropriate current market yield and a loan commitment closing rate based on historical analysis.

Interest rate swap positions, both assets and liabilities, are valued by a third party pricing agent using an income approach and utilizing models that use as their basis readily observable market parameters. This valuation process considers various factors including interest rate yield curves, time value and volatility factors. Validation of third party agent valuations is accomplished by comparing those values to the Company's swap counterparty valuations.

Management believes an adjustment is required to "mid-market" valuations for derivatives tied to its performing loan portfolio to recognize the imprecision and related exposure inherent in the process of estimating expected credit losses as well as velocity of deterioration evident with systemic risks imbedded in these portfolios.

The following table shows the balance of assets and liabilities measured at fair value on a recurring basis.

(Dollars in thousands)	Level 1	Level 2	Level 3	Total
December 31, 2014				
Assets:				
Investment securities available-for-sale:				
U.S. Treasury and Federal agencies securities	$19,808	$353,695	$—	$373,503
U.S. States and political subdivisions securities	—	118,222	6,466	124,688
Mortgage-backed securities - Federal agencies	—	253,008	—	253,008
Corporate debt securities	—	31,932	—	31,932
Foreign government and other securities	—	—	811	811
Total debt securities	19,808	756,857	7,277	783,942
Marketable equity securities	7,176	—	—	7,176
Total investment securities available-for-sale	26,984	756,857	7,277	791,118
Trading account securities	205	—	—	205
Mortgages held for sale	—	13,604	—	13,604
Accrued income and other assets (interest rate swap agreements)	—	9,125	—	9,125
Total	$27,189	$779,586	$7,277	$814,052
Liabilities:				
Accrued expenses and other liabilities (interest rate swap agreements)	$—	$9,302	$—	$9,302
Total	$—	$9,302	$—	$9,302
December 31, 2013				
Assets:				
Investment securities available-for-sale:				
U.S. Treasury and Federal agencies securities	$19,631	$375,408	$—	$395,039
U.S. States and political subdivisions securities	—	117,741	5,498	123,239
Mortgage-backed securities - Federal agencies	—	275,080	—	275,080
Corporate debt securities	—	31,065	—	31,065
Foreign government and other securities	—	709	—	709
Total debt securities	19,631	800,003	5,498	825,132
Marketable equity securities	7,568	—	—	7,568
Total investment securities available-for-sale	27,199	800,003	5,498	832,700
Trading account securities	192	—	—	192
Mortgages held for sale	—	6,079	—	6,079
Accrued income and other assets (interest rate swap agreements)	—	9,894	—	9,894

Total	$27,391	$815,976	$5,498	$848,865
Liabilities:				
Accrued expenses and other liabilities (interest rate swap agreements)	$—	$10,087	$—	$10,087
Total	$—	$10,087	$—	$10,087

67

Table of Contents

The following table shows the changes in Level 3 assets and liabilities measured at fair value on a recurring basis.

(Dollars in thousands)	U.S. States and political subdivisions securities	Foreign government and other securities	Investment securities available-for-sale
Beginning balance January 1, 2014	$5,498	$—	$5,498
Total gains or losses (realized/unrealized):			
Included in earnings	—	—	—
Included in other comprehensive income	(99)	6	(93)
Purchases	2,635	—	2,635
Issuances	—	—	—
Sales	—	—	—
Settlements	—	—	—
Maturities	(1,568)	(100)	(1,668)
Transfers into Level 3	—	905	905
Transfers out of Level 3	—	—	—
Ending balance December 31, 2014	$6,466	$811	$7,277
Beginning balance January 1, 2013	$7,701	$—	$7,701
Total gains or losses (realized/unrealized):			
Included in earnings	(140)	—	(140)
Included in other comprehensive income	566	—	566
Purchases	2,200	—	2,200
Issuances	—	—	—
Sales	(2,000)	—	(2,000)
Settlements	—	—	—
Maturities	(2,829)	—	(2,829)
Transfers into Level 3	—	—	—
Transfers out of Level 3	—	—	—
Ending balance December 31, 2013	$5,498	$—	$5,498

There were no gains or losses for the period included in earnings attributable to the change in unrealized gains or losses relating to assets and liabilities still held at December 31, 2014 or 2013. No transfers between Level 1 and 2 occurred during 2014 or 2013. One transfer between Level 2 and 3 occurred during 2014 and no transfers between Level 2 and 3 occurred during 2013. A foreign government debt security was transferred from Level 2 to Level 3 during 2014 due to the Company's periodic review of valuation methodologies and inputs. The Company determined that the observable inputs used in determining fair value warranted a transfer to Level 3 as the unobservable inputs were deemed to be significant to the overall fair value measurement.

The following table shows the valuation methodology and unobservable inputs for Level 3 assets and liabilities measured at fair value on a recurring basis.

(Dollars in thousands)	Fair value	Valuation Methodology	Unobservable Inputs	Range of Inputs
December 31, 2014				
Investment securities available-for-sale				
Direct placement municipal securities	$6,466	Discounted cash flows	Credit spread assumption	0.99% - 2.08%
Foreign government	$811	Discounted cash flows	Market yield assumption	0.25% - 1.31%

December 31, 2013				
Investment securities available-for-sale				
Direct placement municipal securities	$5,498	Discounted cash flows	Credit spread assumption	0.90% - 1.52%

Table of Contents

The sensitivity to changes in the unobservable inputs and their impact on the fair value measurement can be significant. The significant unobservable input for direct placement municipal securities are the credit spread assumptions used to determine the fair value measure. An increase (decrease) in the estimated spread assumption of the market will decrease (increase) the fair value measure of the securities. The significant unobservable input for foreign government securities are the market yield assumptions. The market yield assumption is negatively correlated to the fair value measure. An increase (decrease) in the determined market yield assumption will decrease (increase) the fair value measurement.

Financial Instruments on Non-recurring Basis:

The Company may be required, from time to time, to measure certain other financial assets at fair value on a non-recurring basis in accordance with GAAP. These adjustments to fair value usually result from application of lower of cost or market accounting or impairment charges of individual assets.

The Credit Policy Committee (CPC), a management committee, is responsible for overseeing the valuation processes and procedures for Level 3 measurements of impaired loans, other real estate and repossessions. The CPC reviews these assets on a quarterly basis to determine the accuracy of the observable inputs, generally third party appraisals, auction values, values derived from trade publications and data submitted by the borrower, and the appropriateness of the unobservable inputs, generally discounts due to current market conditions and collection issues. The CPC establishes discounts based on asset type and valuation source; deviations from the standard are documented. The discounts are reviewed periodically, annually at a minimum, to determine they remain appropriate. Consideration is given to current trends in market values for the asset categories and gain and losses on sales of similar assets. The Loan and Funds Management Committee of the Board of Directors is responsible for overseeing the CPC.

Discounts vary depending on the nature of the assets and the source of value. Aircraft are generally valued using quarterly trade publications adjusted for engine time, condition, maintenance programs, discounted by 10%. Likewise, autos are valued using current auction values, discounted by 10%; medium and heavy duty trucks are valued using trade publications and auction values, discounted by 15%. Construction equipment is generally valued using trade publications and auction values, discounted by 20%. Real estate is valued based on appraisals or evaluations, discounted by 20% at a minimum with higher discounts for property in poor condition or property with characteristics which may make it more difficult to market. Commercial loans subject to borrowing base certificates are generally discounted by 20% for receivables and 40-75% for inventory with higher discounts when monthly borrowing base certificates are not required or received.

Impaired loans and related write-downs are based on the fair value of the underlying collateral if repayment is expected solely from the collateral. Collateral values are reviewed quarterly and estimated using customized discounting criteria, appraisals and dealer and trade magazine quotes which are used in a market valuation approach. In accordance with fair value measurements, only impaired loans for which a reserve for loan loss has been established based on the fair value of collateral require classification in the fair value hierarchy. As a result, only a portion of the Company's impaired loans are classified in the fair value hierarchy.

Partnership investments and the adjustments to fair value primarily result from application of lower of cost or fair value accounting. The partnership investments are priced using financial statements provided by the partnerships. Quantitative unobservable inputs are not reasonably available for reporting purposes.

The Company has established MSRs valuation policies and procedures based on industry standards and to ensure valuation methodologies are consistent and verifiable. MSRs and related adjustments to fair value result from application of lower of cost or fair value accounting. For purposes of impairment, MSRs are stratified based on the predominant risk characteristics of the underlying servicing, principally by loan type. The fair value of each tranche of the servicing portfolio is estimated by calculating the present value of estimated future net servicing cash flows, taking into consideration actual and expected mortgage loan prepayment rates, discount rates, servicing costs, and other economic factors. Prepayment rates and discount rates are derived through a third party pricing agent. Changes in the most significant inputs, including prepayment rates and discount rates, are compared to the changes in the fair value measurements and appropriate resolution is made. A fair value analysis is also obtained from an independent third party agent and compared to the internal valuation for reasonableness. MSRs do not trade in an active, open market with readily observable prices and though sales of MSRs do occur, precise terms and conditions typically are not

readily available and the characteristics of the Company’s servicing portfolio may differ from those of any servicing portfolios that do trade.

Other real estate is based on the lower of cost or fair value of the underlying collateral less expected selling costs. Collateral values are estimated primarily using appraisals and reflect a market value approach. Fair values are reviewed quarterly and new appraisals are obtained annually. Repossessions are similarly valued.

For assets measured at fair value on a nonrecurring basis the following represents impairment charges (recoveries) recognized on these assets during the year ended December 31, 2014 and 2013, respectively: impaired loans - $4.49 million and $0.00 million; partnership investments - $0.29 million and $(0.42) million; MSRs - $0.00 million and $0.00 million; repossessions - $0.73 million and $0.02 million, and other real estate - $0.17 million and $0.34 million.

Table of Contents

The following table shows the carrying value of assets measured at fair value on a non-recurring basis.

(Dollars in thousands)	Level 1	Level 2	Level 3	Total
December 31, 2014				
Impaired loans - collateral based	$—	$—	$1,007	$1,007
Accrued income and other assets (partnership investments)	—	—	1,343	1,343
Accrued income and other assets (mortgage servicing rights)	—	—	4,733	4,733
Accrued income and other assets (repossessions)	—	—	5,156	5,156
Accrued income and other assets (other real estate)	—	—	1,735	1,735
Total	$—	$—	$13,974	$13,974
December 31, 2013				
Impaired loans - collateral based	$—	$—	$670	$670
Accrued income and other assets (partnership investments)	—	—	2,156	2,156
Accrued income and other assets (mortgage servicing rights)	—	—	4,844	4,844
Accrued income and other assets (repossessions)	—	—	4,262	4,262
Accrued income and other assets (other real estate)	—	—	5,490	5,490
Total	$—	$—	$17,422	$17,422

The following table shows the valuation methodology and unobservable inputs for Level 3 assets and liabilities measured at fair value on a non-recurring basis.

(Dollars in thousands)	Carrying Value	Fair value	Valuation Methodology	Unobservable Inputs	Range of Inputs
December 31, 2014					
Impaired loans	$ 1,007	$1,007	Collateral based measurements including appraisals, trade publications, and auction values	Discount for lack of marketability and current conditions	20% - 25%
Mortgage servicing rights	4,733	6,979	Discounted cash flows	Constant prepayment rate (CPR)	10.2% - 16.3%
				Discount rate	9.5% - 13.0%
Repossessions	5,156	5,307	Appraisals, trade publications and auction values	Discount for lack of marketability	0% - 3%
Other real estate	1,735	1,953	Appraisals	Discount for lack of marketability	5% - 38%
December 31, 2013					
Impaired loans	$ 670	$670	Collateral based measurements including appraisals, trade publications, and auction values	Discount for lack of marketability and current conditions	20% - 35%
Mortgage servicing rights	4,844	8,127	Discounted cash flows	Constant prepayment rate (CPR)	9.9% - 11.9%
				Discount rate	10.0% - 13.0%

Repossessions	4,262	4,435	Appraisals, trade publications and auction values	Discount for lack of marketability	0% - 16%
Other real estate	5,490	6,606	Appraisals	Discount for lack of marketability	0% - 48%

GAAP requires disclosure of the fair value of financial assets and financial liabilities, including those financial assets and financial liabilities that are not measured and reported at fair value on a recurring or non-recurring basis.

Table of Contents

The following table shows the fair values of the Company's financial instruments.

(Dollars in thousands)	Carrying or Contract Value	Fair Value	Level 1	Level 2	Level 3
December 31, 2014					
Assets:					
Cash and due from banks	$ 64,834	$64,834	$64,834	$—	$—
Federal funds sold and interest bearing deposits with other banks	1,356	1,356	1,356	—	—
Investment securities, available-for-sale	791,118	791,118	26,984	756,857	7,277
Other investments and trading account securities	21,006	21,006	21,006	—	—
Mortgages held for sale	13,604	13,604	—	13,604	—
Loans and leases, net of reserve for loan and lease losses	3,603,506	3,626,682	—	—	3,626,682
Cash surrender value of life insurance policies	60,371	60,371	60,371	—	—
Mortgage servicing rights	4,733	6,979	—	—	6,979
Interest rate swaps	9,125	9,125	—	9,125	—
Liabilities:					
Deposits	$ 3,802,860	$3,803,958	$2,824,935	$979,023	$—
Short-term borrowings	245,822	245,822	123,337	122,485	—
Long-term debt and mandatorily redeemable securities	56,232	56,044	—	56,044	—
Subordinated notes	58,764	59,427	—	59,427	—
Interest rate swaps	9,302	9,302	—	9,302	—
Off-balance-sheet instruments *	—	305	—	305	—
December 31, 2013					
Assets:					
Cash and due from banks	$ 77,568	$77,568	$77,568	$—	$—
Federal funds sold and interest bearing deposits with other banks	2,484	2,484	2,484	—	—
Investment securities, available-for-sale	832,700	832,700	27,199	800,003	5,498
Other investments and trading account securities	22,592	22,592	22,592	—	—
Mortgages held for sale	6,079	6,079	—	6,079	—
Loans and leases, net of reserve for loan and lease losses	3,465,819	3,491,718	—	—	3,491,718
Cash surrender value of life insurance policies	58,558	58,558	58,558	—	—
Mortgage servicing rights	4,844	8,127	—	—	8,127
Interest rate swaps	9,894	9,894	—	9,894	—
Liabilities:					
Deposits	$ 3,653,650	$3,657,586	$2,722,804	$934,782	$—
Short-term borrowings	314,131	314,131	184,304	129,827	—
Long-term debt and mandatorily redeemable securities	58,335	56,896	—	56,896	—
Subordinated notes	58,764	62,602	—	62,602	—
Interest rate swaps	10,087	10,087	—	10,087	—

Off-balance-sheet instruments *	—	177	—	177	—

* Represents estimated cash outflows required to currently settle the obligations at current market rates.

The methodologies for estimating fair value of financial assets and financial liabilities that are measured at fair value on a recurring or non-recurring basis are discussed above. The estimated fair value approximates carrying value for cash and due from banks, federal funds sold and interest bearing deposits with other banks, other investments, and cash surrender value of life insurance policies. The methodologies for other financial assets and financial liabilities are discussed below:

Loans and Leases — For variable rate loans and leases that reprice frequently and with no significant change in credit risk, fair values are based on carrying values. The fair values of other loans and leases are estimated using discounted cash flow analyses which use interest rates currently being offered for loans and leases with similar terms to borrowers of similar credit quality.

Table of Contents

Deposits — The fair values for all deposits other than time deposits are equal to the amounts payable on demand (the carrying value). Fair values of variable rate time deposits are equal to their carrying values. Fair values for fixed rate time deposits are estimated using discounted cash flow analyses using interest rates currently being offered for deposits with similar remaining maturities.

Short-Term Borrowings — The carrying values of Federal funds purchased, securities sold under repurchase agreements, and other short-term borrowings, including the liability related to mortgage loans available for repurchase under GNMA optional repurchase programs, approximate their fair values.

Long-Term Debt and Mandatorily Redeemable Securities — The fair values of long-term debt are estimated using discounted cash flow analyses, based on our current estimated incremental borrowing rates for similar types of borrowing arrangements. The carrying values of mandatorily redeemable securities are based on our current estimated cost of redeeming these securities which approximate their fair values.

Subordinated Notes — Fair values are estimated based on calculated market prices of comparable securities.

Off-Balance-Sheet Instruments — Contract and fair values for certain of our off-balance-sheet financial instruments (guarantees) are estimated based on fees currently charged to enter into similar agreements, taking into account the remaining terms of the agreements and the counterparties' credit standing.

Limitations — Fair value estimates are made at a specific point in time based on relevant market information and information about the financial instruments. Because no market exists for a significant portion of our financial instruments, fair value estimates are based on judgments regarding future expected loss experience, current economic conditions, risk characteristics of various financial instruments, and other such factors.

These estimates do not reflect any premium or discount that could result from offering for sale at one time the Company's entire holdings of a particular financial instrument. These estimates are subjective in nature and require considerable judgment to interpret market data. Accordingly, the estimates presented herein are not necessarily indicative of the amounts the Company could realize in a current market exchange, nor are they intended to represent the fair value of the Company as a whole. The use of different market assumptions and/or estimation methodologies may have a material effect on the estimated fair value amounts. The fair value estimates presented herein are based on pertinent information available to management as of the respective balance sheet date. Although the Company is not aware of any factors that would significantly affect the estimated fair value amounts, such amounts have not been comprehensively revalued since the presentation dates, and therefore, estimates of fair value after the balance sheet date may differ significantly from the amounts presented herein.

Other significant assets, such as premises and equipment, other assets, and liabilities not defined as financial instruments, are not included in the above disclosures. Also, the fair value estimates for deposits do not include the benefit that results from the low-cost funding provided by the deposit liabilities compared to the cost of borrowing funds in the market.

Table of Contents

Note 22 — 1st Source Corporation (Parent Company Only) Financial Information

STATEMENTS OF FINANCIAL CONDITION

December 31 (Dollars in thousands)	2014	2013
ASSETS		
Cash and cash equivalents	$51,725	$54,348
Short-term investments with bank subsidiary	500	500
Investment securities, available-for-sale (amortized cost of $1,218 at December 31, 2014 and 2013)	6,240	5,636
Other investments	1,470	1,470
Trading account securities	205	192
Investments in:		
Bank subsidiaries	639,035	607,695
Non-bank subsidiaries	1,165	2,374
Other assets	6,356	5,475
Total assets	$706,696	$677,690
LIABILITIES AND SHAREHOLDERS' EQUITY		
Commercial paper borrowings	$12,168	$12,351
Other liabilities	3,641	5,373
Long-term debt and mandatorily redeemable securities	17,650	15,824
Subordinated notes	58,764	58,764
Total liabilities	92,223	92,312
Shareholders' equity	614,473	585,378
Total liabilities and shareholders' equity	$706,696	$677,690

STATEMENTS OF INCOME

Year Ended December 31 (Dollars in thousands)	2014	2013	2012
Income:			
Dividends from bank subsidiary	$33,810	$30,429	$58,739
Rental income from subsidiaries	2,314	2,165	1,873
Other	408	418	499
Investment securities and other investment (losses) gains	(370)	626	273
Total income	36,162	33,638	61,384
Expenses:			
Interest on subordinated notes	4,220	4,220	6,484
Interest on long-term debt and mandatorily redeemable securities	1,475	999	1,108
Interest on commercial paper and other short-term borrowings	36	23	17
Rent expense	1,713	1,698	1,635
Other	2,553	639	354
Total expenses	9,997	7,579	9,598
Income before income tax benefit and equity in undistributed (distributed in excess of) income of subsidiaries	26,165	26,059	51,786
Income tax benefit	2,722	1,650	2,274
Income before equity in undistributed (distributed in excess of) income of subsidiaries	28,887	27,709	54,060
Equity in (distributed in excess of) undistributed income of subsidiaries:			
Bank subsidiaries	28,891	26,995	(4,690)
Non-bank subsidiaries	291	254	263
Net income	$58,069	$54,958	$49,633

Table of Contents

STATEMENTS OF CASH FLOWS

Year Ended December 31 (Dollars in thousands)	2014	2013	2012
Operating activities:			
Net income	$58,069	$54,958	$49,633
Adjustments to reconcile net income to net cash provided by operating activities:			
Equity (undistributed) distributed in excess of income of subsidiaries	(29,182)	(27,249)	4,427
Depreciation of premises and equipment	21	30	39
Realized/unrealized investment securities and other investment losses (gains)	370	(626)	(273)
Change in trading account securities	(13)	(46)	(14)
Other	(1,759)	1,714	3,600
Net change in operating activities	27,506	28,781	57,412
Investing activities:			
Proceeds from sales and maturities of investment securities	—	9	500
Purchases of other investments	—	—	(1,470)
Net change in premises and equipment	—	—	(6)
Return of capital from subsidiaries	1,500	1	—
Net change in investing activities	1,500	10	(976)
Financing activities:			
Net change in commercial paper	(183)	7,692	(3,342)
Proceeds from issuance of long-term debt and mandatorily redeemable securities	1,356	1,331	2,627
Payments on subordinated notes	—	—	(30,928)
Payments on long-term debt and mandatorily redeemable securities	(569)	(397)	(317)
Net proceeds from issuance of treasury stock	1,752	3,655	3,935
Acquisition of treasury stock	(16,342)	(2,273)	(3,701)
Cash dividends paid on common stock	(17,643)	(17,054)	(16,522)
Net change in financing activities	(31,629)	(7,046)	(48,248)
Net change in cash and cash equivalents	(2,623)	21,745	8,188
Cash and cash equivalents, beginning of year	54,348	32,603	24,415
Cash and cash equivalents, end of year	$51,725	$54,348	$32,603

Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure.

None

Item 9A. Controls and Procedures.

1st Source carried out an evaluation, under the supervision and with the participation of our management, including the Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Rule 13a-15(e) under the Securities Exchange Act of 1934) pursuant to Exchange Act Rule 13a-14. Based upon that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that, at December 31, 2014, our disclosure controls and procedures were effective in ensuring that information required to be disclosed by 1st Source in reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms and are designed to ensure that information required to be disclosed in those reports is accumulated and communicated to management as appropriate to allow timely decisions regarding required disclosure.

In addition, there were no changes in our internal control over financial reporting (as defined in Exchange Act Rule 13a-15(f)) during the fourth fiscal quarter of 2014 that have materially affected, or are reasonably likely to materially affect, our internal controls over financial reporting.

MANAGEMENT REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING

Management of 1st Source Corporation ("1st Source") is responsible for establishing and maintaining adequate internal control over financial reporting. 1st Source's internal control over financial reporting includes policies and procedures pertaining to 1st Source's ability to record, process, and report reliable information. Actions are taken to correct any deficiencies as they are identified through internal and external audits, regular examinations by bank regulatory agencies, 1st Source's formal risk management process, and other means. 1st Source's internal control system is designed to provide reasonable assurance to 1st Source's management and Board of Directors regarding the preparation and fair presentation of 1st Source's published financial statements.

All internal control systems, no matter how well designed, have inherent limitations. Therefore, even those systems determined to be effective can provide only reasonable assurance with respect to financial statement preparation and presentation. Further, because of changes in conditions, the effectiveness of internal control may vary over time.

1st Source's management assessed the effectiveness of internal control over financial reporting as of December 31, 2014. In making this assessment, management used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) in Internal Control — Integrated Framework (2013 framework). Based on management's assessment, 1st Source believes that, as of December 31, 2014, 1st Source's internal control over financial reporting is effective based on those criteria.

Ernst & Young LLP, independent registered public accounting firm, has issued an attestation report on management's assessment of 1st Source's internal control over financial reporting. This report appears on page 36.

By /s/ CHRISTOPHER J. MURPHY III
Christopher J. Murphy III, Chief Executive Officer

By /s/ ANDREA G. SHORT
Andrea G. Short, Treasurer and Chief Financial Officer

South Bend, Indiana

Item 9B. Other Information.

None

Table of Contents

Part III

Item 10. Directors, Executive Officers and Corporate Governance.

The information under the caption “Proposal Number 1: Election of Directors,” “Board Committees and Other Corporate Governance Matters,” and “Section 16(a) Beneficial Ownership Reporting Compliance” of the 2015 Proxy Statement is incorporated herein by reference.

Item 11. Executive Compensation.

The information under the caption “Compensation Discussion & Analysis” of the 2015 Proxy Statement is incorporated herein by reference.

Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters.

The information under the caption “Voting Securities and Principal Holders Thereof” and “Proposal Number 1: Election of Directors” of the 2015 Proxy Statement is incorporated herein by reference.

The following table shows Equity Compensation Plan Information as of December 31, 2014.

	(A) Number of Securities to be Issued upon Exercise of Outstanding Options, Warrants and Rights	Weighted-average Exercise Price of Outstanding Options, Warrants and Rights	Number of Securities Remaining Available for Future Issuance Under Equity Compensation Plans [excluding securities reflected in column (A)]	
Equity compensation plans approved by shareholders				
2011 stock option plan	—	$ —	2,000,000	
1997 employee stock purchase plan	11,765	26.84	122,538	
1982 executive incentive plan	—	—	112,194	(1)(2)
1982 restricted stock award plan	—	—	45,393	(1)
1998 performance compensation plan	—	—	89,677	(1)(2)
Total plans approved by shareholders	11,765	$ 26.84	2,369,802	
Equity compensation plans not approved by shareholders				
Director retainer stock plan	—	—	82,248	
Total equity compensation plans	11,765	$ 26.84	2,452,050	

(1) Amount is to be awarded by grants administered by the Executive Compensation Committee of the 1st Source Board of Directors.

(2) Amount includes market value stock only. Book value shares used for annual awards may only be sold to 1st Source.

Item 13. Certain Relationships and Related Transactions, and Director Independence.

The information under the caption “Proposal Number 1: Election of Directors”, “Board Committees and Other Corporate Governance Matters, “ and “Transactions with Related Persons” of the 2015 Proxy Statement is incorporated herein by reference.

Item 14. Principal Accounting Fees and Services.

The information under the caption “Relationship with Independent Registered Public Accounting Firm” of the 2015 Proxy Statement is incorporated herein by reference.

Part IV

Item 15. Exhibits and Financial Statement Schedules.

(a) Financial Statements and Schedules:

The following Financial Statements and Supplementary Data are filed as part of this annual report:

Reports of Independent Registered Public Accounting Firm
Consolidated Statements of Financial Condition — December 31, 2014 and 2013
Consolidated Statements of Income — Years ended December 31, 2014, 2013, and 2012
Consolidated Statements of Comprehensive Income — Years ended December 31, 2014, 2013, and 2012
Consolidated Statements of Shareholders' Equity — Years ended December 31, 2014, 2013, and 2012
Consolidated Statements of Cash Flows — Years ended December 31, 2014, 2013, and 2012
Notes to Consolidated Financial Statements — December 31, 2014, 2013, and 2012

Financial statement schedules required by Article 9 of Regulation S-X are not required under the related instructions, or are inapplicable and, therefore, have been omitted.

(b) Exhibits (numbered in accordance with Item 601 of Regulation S-K):

3(a)	Articles of Incorporation of Registrant, amended April 30, 1996, filed as exhibit to Form 10-K, dated December 31, 1996, and incorporated herein by reference.
3(b)	By-Laws of Registrant, as amended October 23, 2014, filed as exhibit to Form 8-K, dated October 29, 2014, and incorporated herein by reference.
3(c)	Certificate of Designations for Series A Preferred Stock, dated January 23, 2009, filed as exhibit to Form 8-K, dated January 23, 2009, and incorporated herein by reference.
4(a)	Form of Common Stock Certificates of Registrant, filed as exhibit to Registration Statement 2-40481 and incorporated herein by reference.
4(b)	1st Source agrees to furnish to the Commission, upon request, a copy of each instrument defining the rights of holders of Senior and Subordinated debt of 1st Source.
10(a)(1)	Employment Agreement of Christopher J. Murphy III, dated January 1, 2008, filed as exhibit to Form 8-K, dated March 17, 2008, amended February 6, 2014, filed as exhibit to Form 8-K, dated March 12, 2014, and incorporated herein by reference.
10(a)(2)	Employment Agreement of Andrea G. Short dated January 1, 2013, filed as exhibit to Form 10-K, dated December 31, 2012, amended February 6, 2014, filed as exhibit to Form 8-K, dated March 12, 2014, and incorporated herein by reference.
10(a)(3)	Employment Agreement of John B. Griffith, dated January 1, 2008, filed as exhibit to Form 8-K, dated March 17, 2008, amended February 6, 2014, filed as exhibit to Form 8-K, dated March 12, 2014, and incorporated herein by reference.
10(a)(4)	Employment Agreement of Steven J. Wessell, dated June 1, 2011, filed as exhibit to Form 10-Q, dated March 31, 2012, amended February 6, 2014, filed as exhibit to Form 8-K, dated March 12, 2014, and incorporated herein by reference.
10(b)	1st Source Corporation Employee Stock Purchase Plan dated April 17, 1997, filed as exhibit to Form 10-K, dated December 31, 1997, and incorporated herein by reference.
10(c)	

	1st Source Corporation 1982 Executive Incentive Plan, amended February 3, 2011, filed as exhibit to Form 10-K, dated December 31, 2010, and incorporated herein by reference.
10(d)	1st Source Corporation 1982 Restricted Stock Award Plan, amended January 17, 2003, filed as exhibit to Form 10-K, dated December 31, 2003, and incorporated herein by reference.
10(e)	1st Source Corporation 1998 Performance Compensation Plan, amended January 20, 2011, filed as exhibit to Form 10-K, dated December 31, 2010, and incorporated herein by reference.
10(f)	Contract with Fiserv Solutions, Inc. dated November 23, 2005, filed as exhibit to Form 10-K, dated December 31, 2005, and incorporated herein by reference.
10 (g)	1st Source Corporation 2011 Stock Option Plan, dated January 20, 2011, filed as exhibit to Form 10-K, dated December 31, 2010, and incorporated herein by reference.
10 (h)	1st Source Corporation Director Retainer Stock Plan, amended July 24, 2014, filed as exhibit to Form 10-Q, dated September 30, 2014, and incorporated herein by reference.

Table of Contents

21	Subsidiaries of Registrant (unless otherwise indicated, each subsidiary does business under its own name):

Name	Jurisdiction
1st Source Bank	Indiana
SFG Aircraft, Inc. * (formerly known as SFG Equipment Leasing, Inc.)	Indiana
1st Source Insurance, Inc. *	Indiana
1st Source Specialty Finance, Inc. *	Indiana
1st Source Leasing, Inc.	Indiana
1st Source Capital Corporation *	Indiana
Trustcorp Mortgage Company (Inactive)	Indiana
1st Source Master Trust	Delaware
Michigan Transportation Finance Corporation *	Michigan
1st Source Intermediate Holding, LLC	Delaware
1st Source Funding, LLC (Inactive)	Delaware
1st Source Corporation Investment Advisors, Inc. *	Indiana
SFG Commercial Aircraft Leasing, Inc. *	Indiana
SFG Equipment Leasing Corporation I*	Indiana
Washington and Michigan Insurance, Inc.*	Arizona

*Wholly-owned subsidiaries of 1st Source Bank

23	Consent of Ernst & Young LLP, Independent Registered Public Accounting Firm.
31.1	Certification of Christopher J. Murphy III, Chief Executive Officer (Rule 13a-14(a)).
31.2	Certification of Andrea G. Short, Chief Financial Officer (Rule 13a-14(a)).
32.1	Certification of Christopher J. Murphy III, Chief Executive Officer.
32.2	Certification of Andrea G. Short, Chief Financial Officer.
101.INS	XBRL Instance Document
101.SCH	XBRL Taxonomy Extension Schema Document
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document
101.LAB	XBRL Taxonomy Extension Labels Linkbase Document
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document

(c) Financial Statement Schedules — None.

Table of Contents

Signatures

Pursuant to the requirements of Section 13 or 15(d) 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.

1st SOURCE CORPORATION

By /s/ CHRISTOPHER J. MURPHY III

Christopher J. Murphy III, Chairman of the Board
and Chief Executive Officer

Date: February 20, 2015

Table of Contents

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

Signature	Title	Date
/s/ CHRISTOPHER J. MURPHY III Christopher J. Murphy III	Chairman of the Board and Chief Executive Officer	February 20, 2015
/s/ JAMES R. SEITZ James R. Seitz	President	February 20, 2015
/s/ WELLINGTON D. JONES III Wellington D. Jones III	Vice Chairman of the Board and Director	February 20, 2015
/s/ ANDREA G. SHORT Andrea G. Short	Treasurer, Chief Financial Officer and Principal Accounting Officer	February 20, 2015
/s/ JOHN B. GRIFFITH John B. Griffith	Secretary and General Counsel	February 20, 2015
/s/ ALLISON N. EGIDI Allison N. Egidi	Director	February 20, 2015
/s/ DANIEL B. FITZPATRICK Daniel B. Fitzpatrick	Director	February 20, 2015
/s/ TRACY D. GRAHAM Tracy D. Graham	Director	February 20, 2015
/s/ CRAIG A. KAPSON Craig A. Kapson	Director	February 20, 2015
/s/ NAJEEB A. KHAN Najeeb A. Khan	Director	February 20, 2015
/s/ VINOD M. KHILNANI Vinod M. Khilnani	Director	February 20, 2015
/s/ REX MARTIN Rex Martin	Director	February 20, 2015
/s/ CHRISTOPHER J. MURPHY IV Christopher J. Murphy IV	Director	February 20, 2015
/s/ TIMOTHY K. OZARK Timothy K. Ozark	Director	February 20, 2015
/s/ JOHN T. PHAIR John T. Phair	Director	February 20, 2015

/s/ MARK D. SCHWABERO Mark D. Schwabero	Director	February 20, 2015

80