COMMUNITY TRUST BANCORP INC /KY/
Form 10-Q
August 08, 2018

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

[X] QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended June 30, 2018

or

[ ] TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from _____________ to _____________

Commission file number 0-11129

COMMUNITY TRUST BANCORP, INC.
(Exact name of registrant as specified in its charter)

Kentucky (State or other jurisdiction of incorporation or organization)	61-0979818 IRS Employer Identification No.
346 North Mayo Trail Pikeville, Kentucky (Address of principal executive offices)	41501 (Zip code)

(606) 432-1414
(Registrant’s telephone number)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports) and (2) has been subject to such filing requirements for the past 90 days.

Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files.)

Yes No

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

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

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes No

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practical date.

Common stock – 17,729,210 shares outstanding at July 31, 2018

CAUTIONARY STATEMENT
REGARDING FORWARD LOOKING STATEMENTS

Certain of the statements contained herein that are not historical facts are forward-looking statements within the meaning of the Private Securities Litigation Reform Act. Community Trust Bancorp, Inc.'s ("CTBI") actual results may differ materially from those included in the forward-looking statements. Forward-looking statements are typically identified by words or phrases such as "believe," "expect," "anticipate," "intend," "estimate," "may increase," "may fluctuate," similar expressions or future or conditional verbs such as "will," "should," "would," and "could." These forward-looking statements involve risks and uncertainties including, but not limited to, economic conditions, portfolio growth, the credit performance of the portfolios, including bankruptcies, and seasonal factors; changes in general economic conditions including the performance of financial markets, prevailing inflation and interest rates, realized gains from sales of investments, gains from asset sales, and losses on commercial lending activities; results of various investment activities; the effects of competitors' pricing policies, changes in laws and regulations, competition, and demographic changes on target market populations' savings and financial planning needs; industry changes in information technology systems on which we are highly dependent; failure of acquisitions to produce revenue enhancements or cost savings at levels or within the time frames originally anticipated or unforeseen integration difficulties; and the resolution of legal proceedings and related matters. In addition, the banking industry in general is subject to various monetary, operational, and fiscal policies and regulations, which include, but are not limited to, those determined by the Federal Reserve Board, the Federal Deposit Insurance Corporation, the Consumer Financial Protection Bureau, and state regulators, whose policies, regulations, and enforcement actions could affect CTBI's results. These statements are representative only on the date hereof, and CTBI undertakes no obligation to update any forward-looking statements made.

PART I - FINANCIAL INFORMATION

Item 1. Condensed Consolidated Financial Statements

The accompanying information has not been audited by our independent registered public accountants; however, in the opinion of management such information reflects all adjustments necessary for a fair presentation of the results for the interim period. All such adjustments are of a normal and recurring nature.

The accompanying condensed consolidated financial statements are presented in accordance with the requirements of Form 10-Q and consequently do not include all of the disclosures normally required by accounting principles generally accepted in the United States of America or those normally made in the Registrant's annual report on Form 10-K. Accordingly, the reader of the Form 10-Q should refer to the Registrant's Form 10-K for the year ended December 31, 2017 for further information in this regard.

Community Trust Bancorp, Inc.
Condensed Consolidated Balance Sheets

(dollars in thousands)	(unaudited) June 30 2018	December 31 2017
Assets:		
Cash and due from banks	$54,987	$47,528
Interest bearing deposits	143,398	127,746
Cash and cash equivalents	198,385	175,274
Certificates of deposit in other banks	5,635	9,800
Securities available-for-sale at fair value (amortized cost of $597,020 and $590,199, respectively)	585,764	585,761
Securities held-to-maturity at amortized cost (fair value of $660 and $660, respectively)	659	659
Loans held for sale	1,093	1,033
Loans	3,169,042	3,122,940
Allowance for loan and lease losses	(35,771)	(36,151)
Net loans	3,133,271	3,086,789
Premises and equipment, net	46,483	46,318
Federal Home Loan Bank stock	17,927	17,927
Federal Reserve Bank stock	4,887	4,887
Goodwill	65,490	65,490
Bank owned life insurance	63,867	65,354
Mortgage servicing rights	3,772	3,484
Other real estate owned	30,262	31,996
Other assets	47,691	41,459
Total assets	$4,205,186	$4,136,231
Liabilities and shareholders’ equity:		
Deposits:		
Noninterest bearing	$819,525	$790,930
Interest bearing	2,489,883	2,472,933
Total deposits	3,309,408	3,263,863
Repurchase agreements	248,781	243,814
Federal funds purchased	7,978	7,312
Advances from Federal Home Loan Bank	802	845
Long-term debt	59,341	59,341
Deferred taxes	3,030	4,434
Other liabilities	33,671	25,923
Total liabilities	3,663,011	3,605,532
Shareholders’ equity:		
Preferred stock, 300,000 shares authorized and unissued	-	-
Common stock, $5 par value, shares authorized 25,000,000; shares outstanding 2018 – 17,725,313; 2017 – 17,692,912	88,626	88,465
Capital surplus	222,486	221,472

Retained earnings	239,955	224,268
Accumulated other comprehensive loss, net of tax	(8,892)	(3,506)
Total shareholders’ equity	542,175	530,699
Total liabilities and shareholders’ equity	$4,205,186	$4,136,231

See notes to condensed consolidated financial statements.

Community Trust Bancorp, Inc.
Condensed Consolidated Statements of Income and Comprehensive Income
(unaudited)

(in thousands except per share data)	Three Months Ended June 30 2018	2017	Six Months Ended June 30 2018	2017
Interest income:				
Interest and fees on loans, including loans held for sale	$37,791	$34,880	$74,368	$68,355
Interest and dividends on securities				
Taxable	2,422	2,230	4,892	4,260
Tax exempt	706	721	1,403	1,470
Interest and dividends on Federal Reserve Bank and Federal Home Loan Bank stock	328	283	661	559
Interest on Federal Reserve Bank deposits	713	239	1,152	455
Other, including interest on federal funds sold	65	58	129	80
Total interest income	42,025	38,411	82,605	75,179
Interest expense:				
Interest on deposits	5,585	3,181	10,457	6,122
Interest on repurchase agreements	723	411	1,358	749
Interest on advances from Federal Home Loan Bank	2	165	4	168
Interest on long-term debt	567	414	1,047	810
Total interest expense	6,877	4,171	12,866	7,849
Net interest income	35,148	34,240	69,739	67,330
Provision for loan losses	1,929	2,764	2,875	3,993
Net interest income after provision for loan losses	33,219	31,476	66,864	63,337
Noninterest income:				
Service charges on deposit accounts	6,480	6,199	12,701	12,159
Gains on sales of loans, net	304	251	583	507
Trust and wealth management income	2,856	2,649	5,814	5,235
Loan related fees	919	773	2,063	1,778
Bank owned life insurance	793	526	2,557	1,050
Brokerage revenue	440	423	723	735
Securities gains (losses)	2	18	(286)	10
Other noninterest income	1,946	1,472	2,895	2,416
Total noninterest income	13,740	12,311	27,050	23,890
Noninterest expense:				
Officer salaries and employee benefits	3,220	2,663	6,434	5,927
Other salaries and employee benefits	12,202	11,381	24,607	23,041
Occupancy, net	2,043	1,972	4,159	3,999
Equipment	727	748	1,444	1,534
Data processing	1,634	1,757	3,270	3,546
Bank franchise tax	1,577	1,521	3,278	3,041
Legal fees	428	385	902	827
Professional fees	495	551	997	1,047

Advertising and marketing	876	708	1,608	1,393
FDIC insurance	279	315	593	607
Other real estate owned provision and expense	1,315	1,827	2,254	2,743
Repossession expense	304	227	713	428
Amortization of limited partnership investments	716	604	1,216	1,209
Other noninterest expense	6,623	2,907	9,645	5,868
Total noninterest expense	32,439	27,566	61,120	55,210
Income before income taxes	14,520	16,221	32,794	32,017
Income taxes	2,921	4,680	5,381	9,199
Net income	11,599	11,541	27,413	22,818
Other comprehensive income (loss):				
Unrealized holding gains (losses) on securities available-for-sale:				
Unrealized holding gains (losses) arising during the period	(1,811)	1,630	(7,309)	2,745
Less: Reclassification adjustments for realized gains included in net income	2	18	151	10
Tax expense (benefit)	(381)	564	(1,567)	957
Unrealized holding gains (losses) on securities available-for-sale, net of tax	(1,432)	1,048	(5,893)	1,778
Implementation of ASU 2016-01	0	0	507	0
Other comprehensive income (loss), net of tax	(1,432)	1,048	(5,386)	1,778
Comprehensive income	$10,167	$12,589	$22,027	$24,596
Basic earnings per share	$0.66	$0.65	$1.55	$1.29
Diluted earnings per share	$0.66	$0.65	$1.55	$1.29
Weighted average shares outstanding-basic	17,687	17,626	17,679	17,621
Weighted average shares outstanding-diluted	17,703	17,645	17,695	17,641
Dividends declared per share	$0.33	$0.32	$0.66	$0.64

See notes to condensed consolidated financial statements.

Community Trust Bancorp, Inc.
Condensed Consolidated Statements of Cash Flows
(unaudited)

	Six Months Ended June 30	
(in thousands)	2018	2017
Cash flows from operating activities:		
Net income	$27,413	$22,818
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	1,918	2,023
Deferred taxes	163	123
Stock-based compensation	400	302
Provision for loan losses	2,875	3,993
Write-downs of other real estate owned and other repossessed assets	1,320	1,987
Gains on sale of mortgage loans held for sale	(583)	(507)
Securities (gains) losses	286	(10)
Gain on debt repurchase	0	(560)
(Gains) losses on sale of assets, net	(69)	10
Proceeds from sale of mortgage loans held for sale	26,254	22,859
Funding of mortgage loans held for sale	(25,731)	(25,732)
Amortization of securities premiums and discounts, net	2,407	1,551
Change in cash surrender value of bank owned life insurance	(2,191)	(708)
Mortgage servicing rights:		
Fair value adjustments	(77)	301
New servicing assets created	(211)	(172)
Changes in:		
Other assets	(6,288)	(1,966)
Other liabilities	8,179	2,756
Net cash provided by operating activities	36,065	29,068
Cash flows from investing activities:		
Certificates of deposit in other banks:		
Purchase of certificates of deposit	0	(11,515)
Maturity of certificates of deposit	4,165	235
Securities available-for-sale (AFS):		
Purchase of AFS securities	(131,770)	(77,344)
Proceeds from the sales of AFS securities	57,079	3,261
Proceeds from prepayments and maturities of AFS securities	64,535	70,304
Securities held-to-maturity (HTM):		
Proceeds from maturities of HTM securities	0	8
Change in loans, net	(49,769)	(151,624)
Purchase of premises and equipment	(2,083)	(1,187)
Proceeds from sale and retirement of premises and equipment	23	25
Proceeds from sale of other real estate and repossessed assets	928	1,128
Proceeds from settlement of bank owned life insurance	3,678	0
Net cash used in investing activities	(53,214)	(166,709)
Cash flows from financing activities:		
Change in deposits, net	45,545	24,302

Change in repurchase agreements and federal funds purchased, net	5,633	8,547
Proceeds from Federal Home Loan Bank advances	0	100,000
Payments on advances from Federal Home Loan Bank	(43)	(50)
Repurchase of long-term debt	0	(1,440)
Issuance of common stock	800	708
Dividends paid	(11,675)	(11,312)
Net cash provided by financing activities	40,260	120,755
Net increase (decrease) in cash and cash equivalents	23,111	(16,886)
Cash and cash equivalents at beginning of period	175,274	144,716
Cash and cash equivalents at end of period	$198,385	127,830
Supplemental disclosures:		
Income taxes paid	$5,100	$6,400
Interest paid	10,898	6,912
Non-cash activities:		
Loans to facilitate the sale of other real estate owned and repossessed assets	2,406	1,574
Common stock dividends accrued, paid in subsequent quarter	202	204
Real estate acquired in settlement of loans	2,843	1,434

See notes to condensed consolidated financial statements.

Community Trust Bancorp, Inc.
Notes to Condensed Consolidated Financial Statements (unaudited)

Note 1 - Summary of Significant Accounting Policies

In the opinion of management, the unaudited condensed consolidated financial statements include all adjustments (which consist of normal recurring adjustments) necessary, to present fairly the condensed consolidated financial position as of June 30, 2018, the results of operations for the three and six months ended June 30, 2018 and 2017 and the cash flows for the six months ended June 30, 2018 and 2017. In accordance with accounting principles generally accepted in the United States of America for interim financial information, these statements do not include certain information and footnote disclosures required by accounting principles generally accepted in the United States of America for complete annual financial statements. The results of operations for the three and six months ended June 30, 2018 and 2017 and the cash flows for the six months ended June 30, 2018 and 2017 are not necessarily indicative of the results to be expected for the full year. The condensed consolidated balance sheet as of December 31, 2017 has been derived from the audited consolidated financial statements of Community Trust Bancorp, Inc. ("CTBI") for that period. For further information, refer to the consolidated financial statements and footnotes thereto for the year ended December 31, 2017, included in our annual report on Form 10-K.

Principles of Consolidation – The unaudited condensed consolidated financial statements include the accounts of CTBI and its separate and distinct, wholly owned subsidiaries Community Trust Bank, Inc. ("CTB") and Community Trust and Investment Company. All significant intercompany transactions have been eliminated in consolidation.

Reclassifications – Certain reclassifications considered to be immaterial have been made in the prior year condensed consolidated financial statements to conform to current year classifications. These reclassifications had no effect on net income.

New Accounting Standards –

Ø Financial Instruments – Overall – In January 2016, the Financial Accounting Standards Board ("FASB") issued Accounting Standard Update ("ASU") No. 2016-01, Financial Instruments – Overall (Subtopic 825-10). The amendments in this Update require all equity investments to be measured at fair value with changes in the fair value recognized through net income (other than those accounted for under equity method of accounting or those that result in consolidation of the investee). The amendments in this Update also require an entity to present separately in other comprehensive income the portion of the total change in the fair value of a liability resulting from a change in the instrument-specific credit risk when the entity has elected to measure the liability at fair value in accordance with the fair value option for financial instruments. In addition, the amendments in this Update eliminate the requirement to disclose the method(s) and significant assumptions used to estimate the fair value that is required to be disclosed for financial instruments measured at amortized cost on the balance sheet for public business entities. Public business entities will be required to use the exit price notion when measuring the fair value of financial instruments for disclosure purposes. This Update is the final version of Proposed ASU 2013-220—Financial Instruments—Overall (Subtopic 825-10) and Proposed ASU 2013-221—Financial Instruments—Overall (Subtopic 825-10). For public business entities, the amendments in this Update are effective for fiscal years beginning after December 15, 2017, including interim periods within those fiscal years. The amendments should be applied by means of a cumulative-effect adjustment to the balance sheet as of the beginning of the year of adoption. The amendments related to equity securities without readily determinable fair values (including disclosure requirements) should be applied prospectively to equity investments that exist as of the date of adoption. At December 31, 2017, we had $25 million in equity securities with a net unrealized loss of $0.6 million. Accordingly, an adjustment has been made as a cumulative effect adjustment to our consolidated balance sheet effective January 1, 2018. Note 8 below has been modified to reflect the changes in disclosure and the use of a notional exit price.
Ø Leases – In February 2016, the FASB issued ASU No. 2016-02, Leases (Topic 842). ASU 2016-02 establishes a right of use model that requires a lessee to record a right of use asset and a lease liability for all leases with terms

longer than 12 months. Leases will be classified as either finance or operating, with classification affecting the pattern of expense recognition in the income statement. For lessors, the guidance modifies the classification criteria and the accounting for sales-type and direct financing leases. A lease will be treated as a sale if it transfers all of the risks and rewards, as well as control of the underlying asset, to the lessee. If risks and rewards are conveyed without the transfer of control, the lease is treated as a financing. If the lessor does not convey risks and rewards or control, an operating lease results. The amendments are effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years for public business entities. Entities are required to use a modified retrospective approach for leases that exist or are entered into after the beginning of the earliest comparative period in the financial statements, with certain practical expedients available. Early adoption is permitted. CTBI has an implementation team working through the provisions of ASU 2016-02 including reviewing all leases to assess the impact on its accounting and disclosures. CTBI does not anticipate a significant increase in leasing activity between now and the date of adoption. We have calculated the minimum and maximum net present value of all potential lease payments to be between $10.1 million and $20.3 million. We have determined the renewal periods reasonably expected to be exercised. We are now in the process of determining the amount to recognize as right of use assets and the corresponding lease liabilities.

Ø Revenue from Contracts with Customers – In May 2014, the FASB issued ASU No. 2014-09, Revenue from Contracts with Customers. The core principle of ASU 2014-09 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 or services. The guidance also specifies the accounting for some costs to obtain or fulfill a contract with a customer, as well as enhanced disclosure requirements. In August 2015, the FASB issued ASU 2015-14 which deferred the effective date of ASU 2014-09 to fiscal years, and interim reporting periods within those fiscal years, beginning after December 15, 2017. In March 2016, the FASB issued ASU 2016-08 which clarified the revenue recognition implementation guidance on principal versus agent considerations and is effective during the same period as ASU 2014-09. In April 2016, the FASB issued ASU 2016-10 which clarified the revenue recognition guidance regarding the identification of performance obligations and the licensing implementation and is effective during the same period as ASU 2014-09. In May 2016, the FASB issued ASU 2016-12 which narrowly amended the revenue recognition guidance regarding collectability, noncash consideration, presentation of sales tax, and transition. ASU 2016-12 is effective during the same period as ASU 2014-09. We adopted these Updates effective January 1, 2018 with no material change to the timing or amounts of income recognized, as the majority of the revenues earned by CTBI are not within the scope of ASU 2014-09.

Accounting Standards Codification 606, Revenue from Contracts with Customers ("ASC 606"), establishes principles for reporting information about the nature, amount, timing and uncertainty of revenue and cash flows arising from the entity's contracts to provide goods or services to customers. The core principle requires an entity to recognize revenue to depict the transfer of goods or services to customers in an amount that reflects the consideration that it expects to be entitled to receive in exchange for those goods or services recognized as performance obligations are satisfied.

The majority of our revenue-generating transactions are not subject to ASC 606, including revenue generated from financial instruments, such as our loans, letters of credit, derivatives and investment securities, as well as revenue related to our mortgage servicing activities, as these activities are subject to other generally accepted accounting principles ("GAAP") discussed elsewhere within our disclosures. Descriptions of our revenue-generating activities that are within the scope of ASC 606, which are presented in our income statements as components of noninterest income are as follows:

- Service charges on deposit accounts represents general service fees for monthly account maintenance and activity- or transaction-based fees and consist of transaction-based revenue, time-based revenue (service period), item-based revenue or some other individual attribute-based revenue. Revenue is recognized when our performance obligation is completed which is generally monthly for account maintenance services or when a transaction has been completed. Payment for such performance obligations is generally received at the time the performance obligations are satisfied.

- Trust and wealth management income represents monthly or quarterly fees due from wealth management customers as consideration for managing the customers' assets. Wealth management and trust services include custody of assets, investment management, escrow services, fees for trust services, and similar fiduciary activities. Revenue is recognized when our performance obligation is completed each month or quarter, which is generally the time that payment is received.

- Brokerage revenue is transaction based and collected upon the settlement of the transaction. Other sales, such as life insurance, generate commissions from other third parties. These fees are generally collected monthly.

- Other noninterest income primarily includes items such as letter of credit fees, gains on sale of loans held for sale and servicing fees related to mortgage and commercial loans, none of which are subject to the requirements of ASC 606.

Ø Accounting for Credit Losses – In June 2016, the FASB issued ASU No. 2016-13, Financial Instruments—Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments. The provisions of ASU 2016-13 were issued to provide financial statement users with more decision-useful information about the expected credit losses on financial instruments that are not accounted for at fair value through net income, including loans held for investment, held-to-maturity debt securities, trade and other receivables, net investment in leases and other commitments to extend credit held by a reporting entity at each reporting date. This ASU requires that financial assets measured at amortized cost be presented at the net amount expected to be collected, through an allowance for credit losses that is deducted from the amortized cost basis. The amendments in ASU 2016-13 eliminate the probable incurred loss recognition in current GAAP and reflect an entity's current estimate of all expected credit losses. The measurement of expected credit losses is based upon historical experience, current conditions, and reasonable and supportable forecasts that affect the collectability of the financial assets.

For purchased financial assets with a more-than-insignificant amount of credit deterioration since origination ("PCD assets") that are measured at amortized cost, the initial allowance for credit losses is added to the purchase price rather than being reported as a credit loss expense. Subsequent changes in the allowance for credit losses on PCD assets are recognized through the statement of income as a credit loss expense.

Credit losses relating to available-for-sale debt securities will be recorded through an allowance for credit losses rather than as a direct write-down to the security.

ASU 2016-13 is effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2019. Early adoption is permitted for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2018. CTBI has an implementation team working through the provisions of ASU 2016-13 including assessing the impact on its accounting and disclosures. The team has established the historical data that will be available and has identified the potential loan segments to be analyzed. We are continuing data analysis, including the analysis of historical charge-off and recovery data.

Ø Statement of Cash Flows – In August 2016, the FASB issued ASU No. 2016-15, Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments. Stakeholders indicated that there is diversity in practice in how certain cash receipts and cash payments are presented and classified in the statement of cash flows under Topic 230, Statement of Cash Flows, and other Topics. This ASU addresses the following eight specific cash flow issues: Debt prepayment or debt extinguishment costs; settlement of zero-coupon debt instruments or other debt instruments with coupon interest rates that are insignificant in relation to the effective interest rate of the borrowing; contingent consideration payments made after a business combination; proceeds from the settlement of insurance claims; proceeds from the settlement of corporate-owned life insurance policies (including bank-owned life insurance policies); distributions received from equity method investees; beneficial interests in securitization transactions; and separately identifiable cash flows and application of the predominance principle. The amendments in this Update apply to all entities that are required to present a statement of cash flows under Topic 230. This Update is the final version of Proposed Accounting Standards Update EITF-15F—Statement of Cash Flows—Classification of Certain Cash

Receipts and Cash Payments (Topic 230), which has been deleted. The amendments in this Update are effective for public business entities for fiscal years beginning after December 15, 2017, and interim periods within those fiscal years. The amendments in this Update should be applied using a retrospective transition method to each period presented. If it is impracticable to apply the amendments retrospectively for some of the issues, the amendments for those issues would be applied prospectively as of the earliest date practicable. We adopted this ASU effective January 1, 2018 with no material impact on CTBI's consolidated financial statements.

Ø Simplifying the Test for Goodwill Impairment – In January 2017, the FASB issued ASU No. 2017-04, Intangibles – Goodwill and Other (Topic 350) – Simplifying the Test for Goodwill Impairment. These amendments eliminate Step 2 from the goodwill impairment test. The amendments also eliminate the requirements from any reporting unit with a zero or negative carrying amount to perform a qualitative assessment and, if it fails that qualitative test, to perform Step 2 of the goodwill impairment test. An entity still has the option to perform the qualitative assessment for a reporting unit to determine if the quantitative impairment test is necessary. The guidance is effective for fiscal years beginning after December 15, 2019, and interim periods with those fiscal years. ASU 2017-04 should be implemented on a prospective basis. Management does not expect ASU 2017-04 to have an impact on CTBI's consolidated financial statements.

Ø Receivables – Nonrefundable Fees and Other Costs: Premium Amortization on Purchased Callable Debt Securities – In April 2017, the FASB issued ASU No. 2017-08, Receivables—Nonrefundable Fees and Other Costs (Subtopic 310-20), Premium Amortization on Purchased Callable Debt Securities. The ASU shortens the amortization period for certain callable debt securities held at a premium to the earliest call date. However, the amendments do not require an accounting change for securities held at a discount; the discount continues to be amortized to maturity. The amendments are effective for public business entities for fiscal periods beginning after December 15, 2018, including interim periods within those fiscal periods. Entities are required to apply the amendments on a modified retrospective basis through a cumulative-effect adjustment directly to retained earnings as of the beginning of the period of adoption. We adopted this ASU effective January 1, 2018 with no material impact on CTBI's consolidated financial statements.

Ø Income Statement—Reporting Comprehensive Income – In February 2018, the FASB issued ASU No. 2018-02, Income Statement—Reporting Comprehensive Income (Topic 220). On December 22, 2017, the U.S. federal government enacted a tax bill, the Tax Cuts and Jobs Act of 2017. The guidance in GAAP requires deferred tax liabilities and assets to be adjusted for the effect of a change in tax laws or rates with the effect included in income from continuing operations in the reporting period that includes the enactment date. That guidance was applicable even in situations in which the related income tax effects of items in accumulated other comprehensive income were originally recognized in other comprehensive income (rather than in net income). Because the adjustment of deferred taxes due to the reduction of the historical corporate income tax rate to the newly enacted corporate income tax rate of 21 percent was required to be included in income from continuing operations, the tax effects of items within accumulated other comprehensive income (referred to as stranded tax effects for purposes of this Update) did not reflect the appropriate tax rate. The amendments in this ASU requires a reclassification from accumulated other comprehensive income to retained earnings for stranded tax effects resulting from the newly enacted federal corporate income tax rate. The amount of the reclassification is the difference between the historical corporate income tax rate and the newly enacted 21 percent corporate income tax rate. Consequently, the amendments in this Update eliminate the stranded tax effects associated with the change in the federal corporate income tax rate in the Tax Cuts and Jobs Act of 2017 and improve the usefulness of information reported to financial statement users. The amendments in this Update are effective for all entities for fiscal years beginning after December 15, 2018, and interim periods within those fiscal years. Early adoption is permitted for public business entities for reporting periods for which financial statements have not yet been issued by applying retrospectively to each period in which the effect of the change in the U.S. federal corporate income tax rate in the Tax Cuts and Jobs Act of 2017 is recognized. We elected to early adopt this ASU, and therefore, have adjusted our consolidated financial statements effective December 31, 2017 with minimal effect to our financial position.

Ø Income Taxes—Amendments to SEC Paragraphs – The FASB issued ASU 2018-05, Income Taxes (Topic 740) - Amendments to SEC Paragraphs Pursuant to SEC Staff Accounting Bulletin (SAB) No. 118 in March 2018. ASU 2018-05 amends the Accounting Standards Codification to incorporate various SEC paragraphs pursuant to the issuance of SAB 118. SAB 118 addresses the application of generally accepted accounting principles in situations when a registrant does not have the necessary information available, prepared, or analyzed (including computations) in reasonable detail to complete the accounting for certain income tax effects of the Tax Cuts and Jobs Act. We do not, nor do we expect to have, any situations where we do not have the necessary information available, prepared, and analyzed in reasonable detail to complete the accounting for the tax effects of the Tax Cuts and Jobs Act.

Critical Accounting Policies and Estimates

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires the appropriate application of certain accounting policies, many of which require us to make estimates and assumptions about future events and their impact on amounts reported in our consolidated financial statements and related notes. Since future events and their impact cannot be determined with certainty, the actual results will inevitably differ from our estimates. Such differences could be material to the consolidated financial statements.

We believe the application of accounting policies and the estimates required therein are reasonable. These accounting policies and estimates are constantly reevaluated, and adjustments are made when facts and circumstances dictate a change. Historically, we have found our application of accounting policies to be appropriate, and actual results have not differed materially from those determined using necessary estimates.

We have identified the following critical accounting policies:

Investments – Management determines the classification of securities at purchase. We classify securities into held-to-maturity, trading, or available-for-sale categories. Held-to-maturity securities are those which we have the positive intent and ability to hold to maturity and are reported at amortized cost. In accordance with Financial Accounting Standards Board Accounting Standards Codification ("ASC") 320, Investment Securities, investments in debt securities that are not classified as held-to-maturity and equity securities that have readily determinable fair values shall be classified in one of the following categories and measured at fair value in the statement of financial position:
a. Trading securities. Securities that are bought and held principally for the purpose of selling them in the near term (thus held for only a short period of time) shall be classified as trading securities. Trading generally reflects active and frequent buying and selling, and trading securities are generally used with the objective of generating profits on short-term differences in price.
b. Available-for-sale securities. Investments not classified as trading securities (nor as held-to-maturity securities) shall be classified as available-for-sale securities.
We do not have any securities that are classified as trading securities. Available-for-sale securities are reported at fair value, with unrealized gains and losses included as a separate component of shareholders' equity, net of tax. If declines in fair value are other than temporary, the carrying value of the securities is written down to fair value as a realized loss with a charge to income for the portion attributable to credit losses and a charge to other comprehensive income for the portion that is not credit related.

Beginning in January 1, 2018, upon adoption of ASU 2016-01, equity securities with readily determinable fair values are stated at fair value with realized and unrealized gains and losses reported in net income. For periods prior to January 1, 2018, equity securities were classified as available-for-sale and stated at fair value with unrealized gains and losses reported as a separate component of accumulated other comprehensive income, net of tax. Equity securities without a readily determinable fair value are recorded at cost less impairment, if any, adjusted for subsequent observable price changes.

Gains or losses on disposition of securities are computed by specific identification for all securities except for shares in mutual funds, which are computed by average cost. Interest and dividend income, adjusted by amortization of purchase premium or discount, is included in earnings.

When the fair value of a security is below its amortized cost, and depending on the length of time the condition exists and the extent the fair market value is below amortized cost, additional analysis is performed to determine whether an other than temporary impairment condition exists. Available-for-sale and held-to-maturity securities are analyzed quarterly for possible other than temporary impairment. The analysis considers (i) whether we have the intent to sell our securities prior to recovery and/or maturity and (ii) whether it is more likely than not that we will not have to sell our securities prior to recovery and/or maturity. Often, the information available to conduct these assessments is limited and rapidly changing, making estimates of fair value subject to judgment. If actual information or conditions are different than estimated, the extent of the impairment of the security may be different than previously estimated, which could have a material effect on the CTBI's results of operations and financial condition.

Loans – Loans with the ability and the intent to be held until maturity and/or payoff are reported at the carrying value of unpaid principal reduced by unearned interest, an allowance for loan and lease losses, and unamortized deferred fees or costs. Income is recorded on the level yield basis. Interest accrual is discontinued when management believes, after considering economic and business conditions, collateral value, and collection efforts, that the borrower's financial condition is such that collection of interest is doubtful. Any loan greater than 90 days past due must be well secured and in the process of collection to continue accruing interest. Cash payments received on nonaccrual loans generally are applied against principal, and interest income is only recorded once principal recovery is reasonably assured. Loans are not reclassified as accruing until principal and interest payments remain current for a period of time, generally six months, and future payments appear reasonably certain. Included in certain loan categories of impaired loans are troubled debt restructurings that were classified as impaired. A restructuring of a debt constitutes a troubled debt restructuring if the creditor for economic or legal reasons related to the debtor's financial difficulties grants a concession to the debtor that it would not otherwise consider.

Loan origination and commitment fees and certain direct loan origination costs are deferred and the net amount amortized over the estimated life of the related loans, leases, or commitments as a yield adjustment.

Allowance for Loan and Lease Losses – We maintain an allowance for loan and lease losses ("ALLL") at a level that is appropriate to cover estimated credit losses on individually evaluated loans determined to be impaired, as well as estimated credit losses inherent in the remainder of the loan and lease portfolio. Credit losses are charged and recoveries are credited to the ALLL.

We utilize an internal risk grading system for commercial credits. Those larger commercial credits that exhibit probable or observed credit weaknesses are subject to individual review. The borrower's cash flow, adequacy of collateral coverage, and other options available to CTBI, including legal remedies, are evaluated. The review of individual loans includes those loans that are impaired as defined by ASC 310-10-35, Impairment of a Loan. We evaluate the collectability of both principal and interest when assessing the need for loss provision. Historical loss rates are analyzed and applied to other commercial loans not subject to specific allocations. The ALLL allocation for this pool of commercial loans is established based on the historical average, maximum, minimum, and median loss ratios.

A loan is considered impaired when, based on current information and events, it is probable that CTBI will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. Factors considered by management in determining impairment include payment status, collateral value, and the probability of collecting scheduled principal and interest payments when due. Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines the significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reasons for the delay, the borrower's prior payment record, and the amount of the shortfall in relation to the principal and interest owed. Impairment is measured on a loan-by-loan basis for commercial and construction loans by either the present value of expected future cash flows discounted at the loan's effective interest rate, the loan's obtainable market price, or the fair value of the collateral if the loan is collateral dependent.

Homogenous loans, such as consumer installment, residential mortgages, and home equity lines are not individually risk graded. The associated ALLL for these loans is measured under ASC 450, Contingencies.

When any secured commercial loan is considered uncollectable, whether past due or not, a current assessment of the value of the underlying collateral is made. If the balance of the loan exceeds the fair value of the collateral, the loan is placed on nonaccrual and the loan is charged down to the value of the collateral less estimated cost to sell or a specific reserve equal to the difference between book value of the loan and the fair value assigned to the collateral is created until such time as the loan is foreclosed. When the foreclosed collateral has been legally assigned to CTBI, the estimated fair value of the collateral less costs to sell is then transferred to other real estate owned or other repossessed assets, and a charge-off is taken for any remaining balance. When any unsecured commercial loan is considered uncollectable the loan is charged off no later than at 90 days past due.

All closed-end consumer loans (excluding conventional 1-4 family residential loans and installment and revolving loans secured by real estate) are charged off no later than 120 days (5 monthly payments) delinquent. If a loan is considered uncollectable, it is charged off earlier than 120 days delinquent. For conventional 1-4 family residential loans and installment and revolving loans secured by real estate, when a loan is 90 days past due, a current assessment of the value of the real estate is made. If the balance of the loan exceeds the fair value of the property, the loan is placed on nonaccrual. Foreclosure proceedings are normally initiated after 120 days. When the foreclosed property has been legally assigned to CTBI, the fair value less estimated costs to sell is transferred to other real estate owned and the remaining balance is taken as a charge-off.

Historical loss rates for loans are adjusted for significant factors that, in management's judgment, reflect the impact of any current conditions on loss recognition. We use twelve rolling quarters for our historical loss rate analysis. Factors that we consider include delinquency trends, current economic conditions and trends, strength of supervision and administration of the loan portfolio, levels of underperforming loans, level of recoveries to prior year's charge-offs, trends in loan losses, industry concentrations and their relative strengths, amount of unsecured loans, and underwriting exceptions. Management continually reevaluates the other subjective factors included in its ALLL analysis.

Other Real Estate Owned – When foreclosed properties are acquired, appraisals are obtained and the properties are booked at the current fair market value less expected sales costs. Additionally, periodic updated appraisals are obtained on unsold foreclosed properties. When an updated appraisal reflects a fair market value below the current book value, a charge is booked to current earnings to reduce the property to its new fair market value less expected sales costs. Our policy for determining the frequency of periodic reviews is based upon consideration of the specific properties and the known or perceived market fluctuations in a particular market and is typically between 12 and 18 months but generally not more than 24 months. All revenues and expenses related to the carrying of other real estate owned are recognized through the income statement.

Income Taxes – Income tax expense is based on the taxes due on the consolidated tax return plus deferred taxes based on the expected future tax benefits and consequences of temporary differences between carrying amounts and tax bases of assets and liabilities, using enacted tax rates. Any interest and penalties incurred in connection with income taxes are recorded as a component of income tax expense in the consolidated financial statements. During the six months ended June 30, 2018 and 2017, CTBI has not recognized a significant amount of interest expense or penalties in connection with income taxes.

Note 2 – Stock-Based Compensation

CTBI's compensation expense related to stock option grants was $10 thousand and $63 thousand, respectively, for the three and six months ended June 30, 2018, compared to $14 thousand and $28 thousand, respectively, for the three and six months ended June 30, 2017. Restricted stock expense for the three and six months ended June 30, 2018 was $154 thousand and $337 thousand, respectively, including $13 thousand and $25 thousand in dividends paid for each period. Restricted stock expense for the three and six months ended June 30, 2017 was $142 thousand and $274 thousand, respectively, including $13 thousand and $27 thousand in dividends paid for each period. As of June 30, 2018, there was a total of $0.1 million of unrecognized compensation expense related to unvested stock option awards that will be recognized as expense as the awards vest over a weighted average period of 1.4 years and a total of $1.4 million of unrecognized compensation expense related to restricted stock grants that will be recognized as expense as the awards vest over a weighted average period of 2.8 years.

There were no stock options granted in the first six months of 2018 and 2017, and there were no restricted stock grants made during the three months ended June 30, 2018 and 2017. There were 11,320 and 23,668 shares of restricted stock granted during six months ended June 30, 2018 and 2017, respectively. The restricted stock was issued pursuant to the terms of CTBI's 2015 Stock Ownership Incentive Plan. The restrictions on the restricted stock will lapse ratably over four years, except for a 5,000 management retention restricted stock award granted in 2017 which will cliff vest at the end of five years. However, in the event of certain participant employee termination events occurring within 24 months of a change in control of CTBI or the death of the participant, the restrictions will lapse, and in the event of the participant's disability, the restrictions will lapse on a pro rata basis. The Compensation Committee will have discretion to review and revise restrictions applicable to a participant's restricted stock in the event of the participant's retirement.

Note 3 – Securities

Securities are classified into held-to-maturity and available-for-sale categories. Held-to-maturity (HTM) securities are those that CTBI has the positive intent and ability to hold to maturity and are reported at amortized cost. Available-for-sale (AFS) securities are those that CTBI may decide to sell if needed for liquidity, asset-liability management or other reasons. Available-for-sale securities are reported at fair value, with unrealized gains or losses included as a separate component of equity, net of tax.

The amortized cost and fair value of securities at June 30, 2018 are summarized as follows:

Available-for-Sale

(in thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
U.S. Treasury and government agencies	$ 249,625	$ 29	$ (2,881)	$ 246,773
State and political subdivisions	129,628	875	(3,014)	127,489
U.S. government sponsored agency mortgage-backed securities	217,260	194	(6,454)	211,000
Other debt securities	507	0	(5)	502
Total debt securities	597,020	1,098	(12,354)	585,764
CRA investment funds	0	0	0	0
Total available-for-sale securities	$ 597,020	$ 1,098	$ (12,354)	$ 585,764

Held-to-Maturity

(in thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
State and political subdivisions	$ 659	$ 1	$ 0	$ 660
Total held-to-maturity securities	$ 659	$ 1	$ 0	$ 660

The amortized cost and fair value of securities at December 31, 2017 are summarized as follows:

Available-for-Sale

(in thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
U.S. Treasury and government agencies	$211,574	$ 170	$ (1,172)	$210,572
State and political subdivisions	144,159	2,017	(1,161)	145,015
U.S. government sponsored agency mortgage-backed securities	208,959	357	(4,007)	205,309
Other debt securities	507	0	0	507
Total debt securities	565,199	2,544	(6,340)	561,403
CRA investment funds	25,000	76	(718)	24,358
Total available-for-sale securities	$590,199	$ 2,620	$ (7,058)	$585,761

Held-to-Maturity

(in thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
State and political subdivisions	$ 659	$ 1	$ 0	$ 660
Total held-to-maturity securities	$ 659	$ 1	$ 0	$ 660

The amortized cost and fair value of securities at June 30, 2018 by contractual maturity are shown below. Expected maturities will differ from contractual maturities because issuers may have the right to call or prepay obligations with or without call or prepayment penalties.

	Available-for-Sale		Held-to-Maturity	
(in thousands)	Amortized Cost	Fair Value	Amortized Cost	Fair Value
Due in one year or less	$45,792	$45,586	$ 0	$ 0
Due after one through five years	133,474	131,738	659	660
Due after five through ten years	66,356	65,169	0	0
Due after ten years	133,631	131,769	0	0
U.S. government sponsored agency mortgage-backed securities	217,260	211,000	0	0
Other debt securities	507	502	0	0
Total securities	$597,020	$585,764	$ 659	$ 660

During the three months ended June 30, 2018, there was a net gain of $2 thousand realized on sales and calls of AFS securities, consisting of a pre-tax gain of $3 thousand and a pre-tax loss of $1 thousand. During the three months ended June 30, 2017, there was a net gain of $18 thousand realized on sales and calls of AFS securities, consisting of a pre-tax gain of $30 thousand and a pre-tax loss of $12 thousand.

During the six months ended June 30, 2018, there was a combined loss of $286 thousand realized on sales and calls of AFS securities, consisting of a pre-tax gain of $284 thousand and a pre-tax loss of $570 thousand. This combined loss included a loss of $436 thousand from the sale of CTBI’s CRA investment funds in the first quarter of 2018. During the six months ended June 30, 2017, there was a combined gain of $10 thousand realized on sales and calls of AFS securities, consisting of a pre-tax gain of $29 thousand and a pre-tax loss of $19 thousand.

The amortized cost of securities pledged as collateral, to secure public deposits and for other purposes, was $237.7 million at June 30, 2018 and $225.7 million at December 31, 2017.

The amortized cost of securities sold under agreements to repurchase amounted to $295.7 million at June 30, 2018 and $296.4 million at December 31, 2017.

CTBI evaluates its investment portfolio on a quarterly basis for impairment. The analysis performed as of June 30, 2018 indicates that all impairment is considered temporary, market and interest rate driven, and not credit-related. The percentage of total investments with unrealized losses as of June 30, 2018 was 81.2% compared to 69.5% as of December 31, 2017. The following tables provide the amortized cost, gross unrealized losses, and fair market value, aggregated by investment category and length of time the individual securities have been in a continuous unrealized loss position as of June 30, 2018 that are not deemed to be other-than-temporarily impaired. There were no held-to-maturity securities that were deemed to be impaired as of June 30, 2018.

Available-for-Sale

(in thousands)	Amortized Cost	Gross Unrealized Losses	Fair Value
Less Than 12 Months			
U.S. Treasury and government agencies	$ 170,250	$ (2,091)	$ 168,159
State and political subdivisions	55,441	(1,492)	53,949
U.S. government sponso			