

CITY HOLDING CO
Form 10-Q
May 05, 2016
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

(Mark One)

QUARTERLY REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For The Quarterly Period Ended March 31, 2016

OR

TRANSITION REPORT PURSANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For The Transition Period From _____ To _____.

Commission File Number 0-11733

CITY HOLDING COMPANY

(Exact name of registrant as specified in its charter)

West Virginia

55-0619957

(State or other jurisdiction of incorporation or organization) (I.R.S. Employer Identification No.)

25 Gatewater Road

Charleston, West Virginia

25313

(Address of principal executive offices)

(Zip Code)

(304) 769-1100

(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant has (1) 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.

YesNo

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

YesNo

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

Large accelerated filer Accelerated filer

Non-accelerated filer Smaller reporting company

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

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

Common stock, \$2.50 Par Value – 14,992,321 shares as of May 3, 2016.

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FORWARD-LOOKING STATEMENTS

All statements other than statements of historical fact included in this Quarterly Report on Form 10-Q, including statements in Management's Discussion and Analysis of Financial Condition and Result of Operations are, or may be deemed to be, forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. Such information involves risks and uncertainties that could result in the Company's actual results differing materially from those projected in the forward-looking statements. Important factors that could cause actual results to differ materially from those discussed in such forward-looking statements include, but are not limited to, (1) the Company may incur additional loan loss provision due to negative credit quality trends in the future that may lead to a deterioration of asset quality; (2) the Company may incur increased charge-offs in the future; (3) the Company could have adverse legal actions of a material nature; (4) the Company may face competitive loss of customers; (5) the Company may be unable to manage its expense levels; (6) the Company may have difficulty retaining key employees; (7) changes in the interest rate environment may have results on the Company's operations materially different from those anticipated by the Company's market risk management functions; (8) changes in general economic conditions and increased competition could adversely affect the Company's operating results; (9) changes in other regulations and government policies affecting bank holding companies and their subsidiaries, including changes in monetary policies, could negatively impact the Company's operating results; (10) the Company may experience difficulties growing loan and deposit balances; (11) the current economic environment poses significant challenges for us and could adversely affect our financial condition and results of operations; (12) deterioration in the financial condition of the U.S. banking system may impact the valuations of investments the Company has made in the securities of other financial institutions resulting in either actual losses or other than temporary impairments on such investments; (13) the effects of the Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act") and the regulations promulgated and to be promulgated thereunder, which may subject the Company and its subsidiaries to a variety of new and more stringent legal and regulatory requirements which adversely affect their respective businesses; (14) the impact of new minimum capital thresholds established as a part of the implementation of Basel III; and (15) other risk factors relating to the banking industry or the Company as detailed from time to time in the Company's reports filed with the Securities and Exchange Commission, including those risk factors included in the disclosures under the heading "ITEM 1A Risk Factors" of the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2015. Forward-looking statements made herein reflect management's expectations as of the date such statements are made. Such information is provided to assist stockholders and potential investors in understanding current and anticipated financial operations of the Company and is included pursuant to the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. The Company undertakes no obligation to update any forward-looking statement to reflect events or circumstances that arise after the date such statements are made.

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City Holding Company and Subsidiaries

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Part I - FINANCIAL INFORMATION

Item 1 - Financial Statements

Consolidated Balance Sheets

City Holding Company and Subsidiaries

(in thousands)

	(Unaudited)	
	March 31, 2016	December 31, 2015
Assets		
Cash and due from banks	\$ 165,134	\$ 58,829
Interest-bearing deposits in depository institutions	10,031	11,284
Cash and Cash Equivalents	175,165	70,113
Investment securities available for sale, at fair value	362,282	369,466
Investment securities held-to-maturity, at amortized cost (approximate fair value at March 31, 2016 and December 31, 2015 - \$89,600 and \$90,810, respectively)	86,518	88,937
Other securities	9,960	12,915
Total Investment Securities	458,760	471,318
Gross loans	2,877,117	2,862,534
Allowance for loan losses	(19,315)	(19,251)
Net Loans	2,857,802	2,843,283
Bank owned life insurance	98,679	97,919
Premises and equipment, net	75,965	77,271
Accrued interest receivable	8,517	7,432
Net deferred tax asset	27,541	29,974
Goodwill and other intangible assets, net	79,581	79,792
Other assets	47,656	36,957
Total Assets	\$3,829,666	\$ 3,714,059
Liabilities		
Deposits:		
Noninterest-bearing	\$ 666,523	\$ 621,073
Interest-bearing:		
Demand deposits	711,366	679,735
Savings deposits	780,982	765,611
Time deposits	1,028,400	1,017,556
Total Deposits	3,187,271	3,083,975
Short term borrowings:		
Federal funds purchased	—	13,000
Customer repurchase agreements	156,714	141,869
Long-term debt	16,495	16,495
Other liabilities	51,068	39,448
Total Liabilities	3,411,548	3,294,787

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Shareholders' Equity

Preferred stock, par value \$25 per share: 500,000 shares authorized; none issued	—	—
Common stock, par value \$2.50 per share: 50,000,000 shares authorized; 18,499,282 shares issued at March 31, 2016 and December 31, 2015, less 3,528,111 and 3,319,067 shares in treasury, respectively	46,249	46,249
Capital surplus	106,137	106,269
Retained earnings	395,963	390,690
Cost of common stock in treasury	(129,142)	(120,104)
Accumulated other comprehensive income (loss):		
Unrealized gain on securities available-for-sale	3,670	927
Underfunded pension liability	(4,759)	(4,759)
Total Accumulated Other Comprehensive Loss	(1,089)	(3,832)
Total Shareholders' Equity	418,118	419,272
Total Liabilities and Shareholders' Equity	\$3,829,666	\$3,714,059

See notes to consolidated financial statements.

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Consolidated Statements of Income (Unaudited)
City Holding Company and Subsidiaries
(in thousands, except earnings per share data)

	Three months ended March 31,	
	2016	2015
Interest Income		
Interest and fees on loans	\$28,927	\$29,388
Interest and dividends on investment securities:		
Taxable	3,005	2,712
Tax-exempt	357	264
Total Interest Income	32,289	32,364
Interest Expense		
Interest on deposits	2,898	2,741
Interest on short-term borrowings	107	82
Interest on long-term debt	164	150
Total Interest Expense	3,169	2,973
Net Interest Income	29,120	29,391
Provision for loan losses	539	888
Net Interest Income After Provision for Loan Losses	28,581	28,503
Non-Interest Income		
Gains on sale of investment securities	—	14
Service charges	6,303	5,927
Bankcard revenue	3,967	4,074
Trust and investment management fee income	1,276	1,200
Bank owned life insurance	760	764
Gain on sale of insurance division	—	11,084
Other income	821	958
Total Non-Interest Income	13,127	24,021
Non-Interest Expense		
Salaries and employee benefits	12,673	12,179
Occupancy and equipment	2,836	2,590
Depreciation	1,567	1,511
FDIC insurance expense	465	450
Advertising	716	704
Bankcard expenses	833	870
Postage, delivery, and statement mailings	565	561
Office supplies	353	346
Legal and professional fees	471	567
Telecommunications	428	475
Repossessed asset losses, net of expenses	288	220
Other expenses	2,945	2,692
Total Non-Interest Expense	24,140	23,165
Income Before Income Taxes	17,568	29,359
Income tax expense	5,866	11,367
Net Income Available to Common Shareholders	\$11,702	\$17,992

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Total Comprehensive Income	\$ 14,445	\$ 18,898
Average common shares outstanding	14,916	15,067
Effect of dilutive securities:		
Employee stock awards and warrant outstanding	11	82
Shares for diluted earnings per share	14,927	15,149
Basic earnings per common share	\$0.78	\$1.18
Diluted earnings per common share	\$0.78	\$1.17
Dividends declared per common share	\$0.43	\$0.42

See notes to consolidated financial statements.

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Consolidated Statements of Comprehensive Income (Unaudited)
 City Holding Company and Subsidiaries
 (in thousands)

	Three Months Ended March 31, 2016 2015	
Net income	\$11,702	\$17,992
Unrealized gains (losses) on available-for-sale securities arising during the period	4,348	1,450
Reclassification adjustment for gains	—	(14)
Other comprehensive income (loss) before income taxes	4,348	1,436
Tax effect	(1,605)	(530)
Other comprehensive income (loss), net of tax	2,743	906
 Comprehensive Income, Net of Tax	 \$14,445	 \$18,898

See notes to consolidated financial statements.

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Consolidated Statements of Changes in Shareholders' Equity (Unaudited)
City Holding Company and Subsidiaries
Three Months Ended March 31, 2016 and 2015
(in thousands)

	Common Stock	Capital Surplus	Retained Earnings	Treasury Stock	Accumulated Other Comprehensive Income (Loss)	Total Shareholders' Equity
Balance at December 31, 2014	\$ 46,249	\$ 107,370	\$ 362,211	\$(120,818)	\$ (4,159)	\$ 390,853
Net income	—	—	17,992	—	—	17,992
Other comprehensive loss	—	—	—	—	906	906
Cash dividends declared (\$0.42 per share)	—	—	(6,391)	—	—	(6,391)
Stock-based compensation expense, net	—	(679)	—	1,419	—	740
Exercise of 28,500 stock options	—	(294)	—	1,269	—	975
Balance at March 31, 2015	\$ 46,249	\$ 106,397	\$ 373,812	\$(118,130)	\$ (3,253)	\$ 405,075

	Common Stock	Capital Surplus	Retained Earnings	Treasury Stock	Accumulated Other Comprehensive Income (Loss)	Total Shareholders' Equity
Balance at December 31, 2015	\$ 46,249	\$ 106,269	\$ 390,690	\$(120,104)	\$ (3,832)	\$ 419,272
Net income	—	—	11,702	—	—	11,702
Other comprehensive income	—	—	—	—	2,743	2,743
Cash dividends declared (\$0.43 per share)	—	—	(6,429)	—	—	(6,429)
Stock-based compensation expense, net	—	(132)	—	887	—	755
Purchase of 229,132 treasury shares	—	—	—	(9,925)	—	(9,925)
Balance at March 31, 2016	\$ 46,249	\$ 106,137	\$ 395,963	\$(129,142)	\$ (1,089)	\$ 418,118

See notes to consolidated financial statements.

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Consolidated Statements of Cash Flows (Unaudited)
City Holding Company and Subsidiaries
(in thousands)

	Three months ended March 31,	
	2016	2015
Net income	\$11,702	\$17,992
Adjustments to reconcile net income to net cash provided by operating activities:		
Accretion and amortization	117	(1,922)
Provision for loan losses	539	888
Depreciation of premises and equipment	1,567	1,511
Deferred income tax expense	830	964
Net periodic employee benefit cost	129	200
Realized investment securities gains	—	(14)
Stock-compensation expense	755	740
Increase in value of bank-owned life insurance	(760)	(764)
Loans originated for sale	(2,809)	(4,184)
Proceeds from the sale of loans originated for sale	3,107	3,637
Gain on sale of loans	(58)	(58)
Gain on sale of insurance division	—	(11,084)
Change in accrued interest receivable	(1,085)	(926)
Change in other assets	(10,630)	(1,824)
Change in other liabilities	11,432	8,343
Net Cash Provided by Operating Activities	14,836	13,499
Proceeds from sales of securities available-for-sale	35	—
Proceeds from maturities and calls of securities available-for-sale	18,078	16,172
Proceeds from maturities and calls of securities held-to-maturity	2,332	3,336
Purchases of securities available-for-sale	(4,289)	(34,857)
Net (increase) decrease in loans	(14,668)	21,622
Purchases of premises and equipment	(610)	(472)
Disposals of premises and equipment	341	—
Proceeds from sale of insurance division	—	15,250
Net Cash Provided by Investing Activities	1,219	21,051
Net increase in non-interest-bearing deposits	45,450	6,131
Net increase in interest-bearing deposits	57,994	63,633
Net increase (decrease) in short-term borrowings	1,845	(2,343)
Purchases of treasury stock	(9,925)	—
Proceeds from exercise of stock options, net of tax benefit	—	975
Dividends paid	(6,367)	(6,064)
Net Cash Provided by Financing Activities	88,997	62,332
Increase in Cash and Cash Equivalents	105,052	96,882
Cash and cash equivalents at beginning of period	70,113	148,228
Cash and Cash Equivalents at End of Period	\$175,165	\$245,110

See notes to consolidated financial statements.

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Notes to Consolidated Financial Statements (Unaudited)
March 31, 2016

Note A –Background and Basis of Presentation

City Holding Company ("City Holding"), a West Virginia corporation headquartered in Charleston, West Virginia, is a registered financial holding company under the Bank Holding Company Act and conducts its principal activities through its wholly-owned subsidiary, City National Bank of West Virginia ("City National"). City National is a retail and consumer-oriented community bank with 85 banking offices in West Virginia (57), Virginia (14), Kentucky (11) and Ohio (3). City National provides credit, deposit, and trust and investment management services to its customers. In addition to its branch network, City National's delivery channels include ATMs, mobile banking, debit cards, interactive voice response systems, and Internet technology. The Company's business activities are currently limited to one reportable business segment, which is community banking.

On January 9, 2015 the Company sold its insurance operations, CityInsurance, to The Hilb Group effective January 1, 2015. As a result of this sale, the Company recognized a one-time after tax gain of \$5.8 million from this transaction in the first quarter of 2015.

On November 6, 2015, the Company consummated the acquisition of three branch locations from American Founders Bank, Inc. ("AFB") located in Lexington, Kentucky. The Company acquired approximately \$119 million in performing loans and assumed deposit liabilities of approximately \$145 million. The Company paid AFB a deposit premium of 5.5% on non-time deposits, and 1.0% on premium loan balances acquired.

The accompanying consolidated financial statements, which are unaudited, include all of the accounts of the City Holding Company and its wholly-owned subsidiaries (collectively, the "Company"). All material intercompany transactions have been eliminated. The consolidated financial statements include all adjustments that, in the opinion of management, are necessary for a fair presentation of the results of operations and financial condition for each of the periods presented. Such adjustments are of a normal recurring nature. The results of operations for the three months ended March 31, 2016 are not necessarily indicative of the results of operations that can be expected for the year ending December 31, 2016. The Company's accounting and reporting policies conform with generally accepted accounting principles for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Such policies require management to make estimates and develop assumptions that affect the amounts reported in the consolidated financial statements and related footnotes. Actual results could differ from management's estimates.

The consolidated balance sheet as of December 31, 2015 has been derived from audited financial statements included in the Company's 2015 Annual Report to Shareholders. Certain information and footnote disclosures normally included in annual financial statements prepared in accordance with U.S. generally accepted accounting principles have been omitted. These financial statements should be read in conjunction with the financial statements and notes thereto included in the 2015 Annual Report of the Company.

Certain amounts in the financial statements have been reclassified. Such reclassifications had no impact on shareholders' equity or net income for any period.

Note B - Recent Accounting Pronouncements

In February 2015, the FASB issued ASU No. 2015-02, "Consolidation (Topic 810) - Amendments to the Consolidation Analysis". ASU 2015-02 eliminates the deferral of FAS 167 and makes changes to both the variable

interest model and the voting model. This ASU became effective for the Company on January 1, 2016. The adoption of ASU 2015-02 did not have a material impact on the Company's financial statements.

In April 2015, the FASB issued ASU No. 2015-03, "Interest - Imputation of Interest (Subtopic 835-30): Simplifying the Presentation of Debt Issuance Costs." ASU 2015-03 requires that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability, consistent with debt discounts. This ASU became effective for the Company on January 1, 2016. The adoption of ASU 2015-03 did not have a material impact on the Company's financial statements.

In April 2015, the FASB issued ASU No. 2015-05, "Intangibles - Goodwill and Other - Internal-Use Software (Subtopic 350-40): Customer's Accounting for Fees Paid in a Cloud Computing Arrangement." ASU 2015-05 provides guidance to clarify the customer's accounting for fees paid in a cloud computing arrangement. This ASU became effective for

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the Company on January 1, 2016. The adoption of ASU 2015-05 did not have a material impact on the Company's financial statements.

In May 2015, the FASB issued ASU No. 2015-07, "Fair Value Measurement (Topic 820): Disclosures for Investments in Certain Entities That Calculate Net Asset Value per Share (or Its Equivalent)." ASU 2015-07 removes the requirement to categorize within the fair value hierarchy all investments for which fair value is measured using the net asset value per share practical expedient. The ASU also removes the requirement to make certain disclosures for all investments that are eligible to be measured at fair value using the net asset value per share practical expedient. This ASU became effective for the Company on January 1, 2016. The adoption of ASU 2015-07 did not have a material impact on the Company's financial statements.

In September 2015, the FASB issued ASU No. 2015-16, "Business Combinations (Topic 85): Simplifying the Accounting for Measurement-Period Adjustments." The amendments in ASU 2015-16 require that an acquirer recognize adjustments to provisional amounts that are identified during the measurement period in the reporting period in which the adjustment amounts are determined. The effect on earnings of the adjustments as a result of the change to the provisional amounts will be calculated as if the accounting had been completed at the acquisition date. The amount that would've been recorded in the previous reporting periods will be presented separately on the face of the income statement or disclosed in the notes to the financial statements. This ASU became effective for the Company on January 1, 2016. The adoption of ASU 2015-16 did not have a material impact on the Company's financial statements.

In November 2015, the FASB issued ASU No. 2015-17, "Income Taxes (Topic 740): Balance Sheet Classification of Deferred Taxes." This standard requires that deferred tax liabilities and assets be classified as non-current on the balance sheet. This ASU will become effective for the Company for interim and annual periods on January 1, 2017 and early adoption is permitted. The adoption of ASU No. 2015-17 is not expected to have a material impact on the Company's financial statements.

In January 2016, the FASB issued ASU No. 2016-01, "Financial Instruments—Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities." This standard makes several modifications to Subtopic 825-10 including the elimination of the available-for-sale classification of equity investments, and requires equity investments with readily determinable fair values to be measured at fair value with changes in fair value recognized in net income. This ASU will become effective for the Company for interim and annual periods on January 1, 2018. The adoption of ASU No. 2016-01 is not expected to have a material impact on the Company's financial statements.

In February 2016, the FASB issued ASU No. 2016-02, "Leases (Topic 842)." This standard requires organizations to recognizing lease assets and lease liabilities on the balance sheet and disclose key information about leasing requirements for leases that were historically classified as operating leases under previous generally accepted accounting principals. This ASU will become effective for the Company for interim and annual periods on January 1, 2019. The adoption of ASU No. 2016-02 is not expected to have a material impact on the Company's financial statements.

In March 2016, the FASB issued ASU No. 2016-09, "Compensation-Stock Compensation (Topic 718)." This standard makes several modifications to the accounting for share-based payment transactions, including the income tax consequences, classification of awards as either equity or liabilities, and classification on the statement of cash flows. This ASU will become effective for the Company for interim and annual periods on January 1, 2017. The adoption of ASU No. 2016-09 is not expected to have a material impact on the Company's financial statements.

In April 2016, the FASB issued ASU No. 2016-10, "Revenue from Contracts with Customers (Topic 606)." The amendments in this standard clarify identifying performance obligations and the licensing implementation guidance under Topic 606. This ASU will become effective for the Company for interim and annual periods on January 1, 2018. The adoption of ASU No. 2016-10 is not expected to have a material impact on the Company's financial statements.

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Note C –Investments

The amortized cost and estimated fair values of the Company's securities are shown in the following table (in thousands):

	March 31, 2016				December 31, 2015			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
Securities available-for-sale:								
U.S. Treasuries and U.S. government agencies								
Obligations of states and political subdivisions	\$4	\$ —	\$ —	\$4	\$5	\$ —	\$ —	\$5
Mortgage-backed securities:	48,632	1,293	—	49,925	49,725	979	7	50,697
U.S. government agencies	276,666	4,920	380	281,206	287,933	2,285	2,021	288,197
Private label	1,155	2	1	1,156	1,222	9	—	1,231
Trust preferred securities	6,454	579	1,544	5,489	6,550	463	1,155	5,858
Corporate securities	19,788	352	443	19,697	18,793	221	321	18,693
Total Debt Securities	352,699	7,146	2,368	357,477	364,228	3,957	3,504	364,681
Marketable equity securities	2,136	1,136	—	3,272	2,131	1,142	—	3,273
Investment funds	1,525	8	—	1,533	1,525	—	13	1,512
Total Securities Available-for-Sale	\$356,360	\$ 8,290	\$ 2,368	\$362,282	\$367,884	\$ 5,099	\$ 3,517	\$369,466
Securities held-to-maturity:								
Mortgage-backed securities								
US government agencies	\$82,518	\$ 3,082	\$ —	—\$ 85,600	\$84,937	\$ 1,949	\$ 76	\$ 86,810
Trust preferred securities	4,000	—	—	4,000	4,000	—	—	4,000
Total Securities Held-to-Maturity	\$86,518	\$ 3,082	\$ —	—\$ 89,600	\$88,937	\$ 1,949	\$ 76	\$ 90,810
Other investment securities:								
Non-marketable equity securities	\$9,960	\$ —	\$ —	—\$ 9,960	\$12,915	\$ —	\$ —	\$ 12,915
Total Other Investment Securities	\$9,960	\$ —	\$ —	—\$ 9,960	\$12,915	\$ —	\$ —	\$ 12,915

Marketable equity securities consist of investments made by the Company in equity positions of various regional community banks. Included within this portfolio are ownership positions in the following community bank holding companies: First National Corporation (FXNC) (4%) and Eagle Financial Services, Inc. (EFSI) (1.5%). Securities with limited marketability, such as stock in the Federal Reserve Bank ("Federal Reserve") or the Federal Home Loan Bank ("FHLB"), are carried at cost and are reported as non-marketable equity securities in the table above.

Certain investment securities owned by the Company were in an unrealized loss position (i.e., amortized cost basis exceeded the estimated fair value of the securities). The following table shows the gross unrealized losses and fair

value of the Company's investments aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position (in thousands):

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	March 31, 2016					
	Less Than Twelve Months		Twelve Months or Greater		Total	
	Estimated Fair Value	Unrealized Loss	Estimated Fair Value	Unrealized Loss	Estimated Fair Value	Unrealized Loss
Securities available-for-sale:						
Obligations of states and political subdivisions	\$—	\$ —	\$—	\$ —	\$—	\$ —
Mortgage-backed securities:						
U.S. Government agencies	18	1	33,433	379	33,451	380
Private label	955	1	—	—	955	1
Trust preferred securities	—	—	4,383	1,544	4,383	1,544
Corporate securities	4,148	262	2,197	181	6,345	443
Investment funds	—	—	—	—	—	—
Total	\$5,121	\$ 264	\$40,013	\$ 2,104	\$45,134	\$ 2,368

	December 31, 2015					
	Less Than Twelve Months		Twelve Months or Greater		Total	
	Estimated Fair Value	Unrealized Loss	Estimated Fair Value	Unrealized Loss	Estimated Fair Value	Unrealized Loss
Securities available-for-sale:						
Obligations of states and political subdivisions	\$2,406	\$ 5	\$128	\$ 2	\$2,534	\$ 7
Mortgage-backed securities:						
U.S. Government agencies	129,612	688	34,044	1,333	163,656	2,021
Private label	—	—	—	—	—	—
Trust preferred securities	—	—	4,769	1,155	4,769	1,155
Corporate securities	10,856	174	2,231	147	13,087	321
Investment funds	—	—	1,488	13	1,488	13
Total	\$142,874	\$ 867	\$42,660	\$ 2,650	\$185,534	\$ 3,517

During the three months ended March 31, 2016 and 2015, the Company had no credit-related net investment impairment losses. Also, for the year ended December 31, 2015, the Company had no credit-related net investment impairment losses. At March 31, 2016 and December 31, 2015, the cumulative amount of credit-related investment impairment losses that have been recognized by the Company on investments that remain in the Company's investment portfolio as of those dates was \$18.2 million (\$16.6 million related to the Company's debt securities and \$1.6 million related to the Company's equity securities).

Declines in the fair value of held-to-maturity and available-for-sale securities below their cost that are deemed to be other-than-temporary would be reflected in earnings as realized losses. In estimating other-than-temporary impairment losses, management considers, among other things (i) the length of time and the extent to which the fair value has been less than cost; (ii) the financial condition, capital strength, and near-term (within 12 months) prospects of the issuer, including any specific events which may influence the operations of the issuer such as changes in technology that may impair the earnings potential of the investment or the discontinuance of a segment of the business that may affect the future earnings potential; (iii) the historical volatility in the market value of the investment and/or the liquidity or illiquidity of the investment; (iv) adverse conditions specifically related to the security, an industry, or a

geographic area; or (v) the intent to sell the investment security and if it's more likely than not that the Company will not have to sell the security before recovery of its cost basis. In addition, management also employs a continuous monitoring process in regards to its marketable equity securities, specifically its portfolio of regional community bank holdings. Although the regional community bank stocks that are owned by the Company are publicly traded, the trading activity for these stocks is minimal, with trading volumes of less than 0.2% of each respective company being traded on a daily basis. As part of management's review process for these securities, management reviews the financial condition of each respective regional community bank for any indications of financial weakness.

Management has the ability and intent to hold the securities classified as held-to-maturity until they mature, at which time the Company expects to receive full value for the securities. Furthermore, as of March 31, 2016, management does not intend to sell an impaired security and it is not more than likely that it will be required to sell the security before the recovery of its amortized cost basis. The unrealized losses on debt securities are primarily the result of interest rate changes, credit spread fluctuations on agency-issued mortgage related securities, general financial market uncertainty and unprecedented market volatility.

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These conditions will not prohibit the Company from receiving its contractual principal and interest payments on its debt securities. The fair value is expected to recover as the securities approach their maturity date or repricing date. As of March 31, 2016, management believes the unrealized losses detailed in the table above are temporary and no additional impairment loss has been recognized in the Company's consolidated income statement. Should the impairment of any of these securities become other-than-temporary, the cost basis of the investment will be reduced and the resulting loss will be recognized in net income in the period the other-than-temporary impairment is identified, while any noncredit loss will be recognized in other comprehensive income.

The amortized cost and estimated fair value of debt securities at March 31, 2016, by contractual maturity, are shown in the following table (in thousands). Expected maturities will differ from contractual maturities because the issuers of the securities may have the right to prepay obligations without prepayment penalties. Mortgage-backed securities have been allocated to their respective maturity groupings based on their contractual maturity.

	Amortized Cost	Estimated Fair Value
Securities Available-for-Sale		
Due in one year or less	\$ 1,240	\$ 1,258
Due after one year through five years	25,979	18,326
Due after five years through ten years	31,778	40,690
Due after ten years	293,702	297,203
	\$ 352,699	\$ 357,477
Securities Held-to-Maturity		
Due in one year or less	\$ —	\$ —
Due after one year through five years	—	—
Due after five years through ten years	—	—
Due after ten years	86,518	89,600
	\$ 86,518	\$ 89,600

Gross gains and gross losses realized by the Company from investment security transactions are summarized in the table below (in thousands).

	Three months ended March 31, 2015
Gross realized gains	\$ \$-14
Gross realized losses	—
Net investment security gains	\$ \$-14

The carrying value of securities pledged to secure public deposits and for other purposes as required or permitted by law approximated \$274 million and \$273 million at March 31, 2016 and December 31, 2015, respectively.

Note D –Loans

The following summarizes the Company's major classifications for loans (in thousands):

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	March 31, 2016	December 31, 2015
Residential real estate	\$1,395,670	\$1,383,133
Home equity	142,694	147,036
Commercial and industrial	165,549	165,340
Commercial real estate	1,135,625	1,127,581
Consumer	34,754	36,083
DDA overdrafts	2,825	3,361
Gross loans	2,877,117	2,862,534
Allowance for loan losses	(19,315)	(19,251)
Net loans	\$2,857,802	\$2,843,283

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Construction loans of \$14.0 million and \$13.1 million are included within residential real estate loans at March 31, 2016 and December 31, 2015, respectively. Construction loans of \$15.2 million and \$12.6 million are included within commercial real estate loans at March 31, 2016 and December 31, 2015, respectively. The Company's commercial and residential real estate construction loans are primarily secured by real estate within the Company's principal markets. These loans were originated under the Company's loan policy, which is focused on the risk characteristics of residential and commercial real estate lending, including specific risks related to construction lending. Adequate consideration has been given to these loans in establishing the Company's allowance for loan losses.

The following table details the loans acquired in conjunction with the Virginia Savings Bancorp, Inc. ("Virginia Savings"), Community Financial Corporation ("Community") and American Founders Bank ("AFB") acquisitions (in thousands):

	Virginia			Total
	Savings	Community	AFB	
March 31, 2016				
Outstanding loan balance	\$27,763	\$ 172,173	\$ 108,584	\$308,520
Credit-impaired loans:				
Carrying value	1,715	11,219	—	12,934
Contractual principal and interest	1,942	14,415	—	16,357
December 31, 2015				
Outstanding loan balance	\$28,914	\$ 181,545	\$ 112,862	\$323,321
Credit-impaired loans:				
Carrying value	1,707	12,899	—	14,606
Contractual principal and interest	1,965	16,362	—	18,327

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Changes in the accretable yield of the credit-impaired loans for the three months ended March 31, 2016 is as follows (in thousands):

	Virginia Savings		Community		Total	
	Carrying Amount		Carrying Amount		Carrying Amount	
	Yield of Loans		Yield of Loans		Yield of Loans	
Balance at the beginning of the period	\$374	\$1,707	\$6,266	\$12,899	\$6,640	\$14,606
Accretion	(50)	50	(285)	285	(335)	335
Net reclassifications to accretable yield from non-accretable yield	—	—	—	—	—	—
Payments received, net	—	(42)	—	(1,707)	—	(1,749)
Disposals	—	—	—	(258)	—	(258)
Balance at the end of period	\$324	\$1,715	\$5,981	\$11,219	\$6,305	\$12,934

Increases in expected cash flow subsequent to the acquisition are recognized first as a reduction of any previous impairment, then prospectively through adjustment of the yield on the loans or pools over its remaining life, while decreases in expected cash flows are recognized as impairment through a provision for loan loss and an increase in the allowance for purchased credit-impaired loans.

Note E – Allowance For Loan Losses

Management systematically monitors the loan portfolio and the adequacy of the allowance for loan losses on a quarterly basis to provide for probable losses inherent in the portfolio. Management assesses the risk in each loan type based on historical trends, the general economic environment of its local markets, individual loan performance and other relevant factors.

Individual credits are selected throughout the year for detailed loan reviews, which are utilized by management to assess the risk in the portfolio and the adequacy of the allowance. Due to the nature of commercial lending, evaluation of the adequacy of the allowance as it relates to these loan types is often based more upon specific credit reviews, with consideration given to the potential impairment of certain credits and historical loss rates, adjusted for economic conditions and other inherent risk factors.

The following table summarizes the activity in the allowance for loan loss, by portfolio segment, for the three months ended March 31, 2016 and 2015 (in thousands). The allocation of a portion of the allowance in one portfolio segment does not preclude its availability to absorb losses in other portfolio segments. The following table also presents the balance in the allowance for loan loss disaggregated on the basis of the Company's impairment measurement method and the related recorded investment in loans, by portfolio segment, as of March 31, 2016 and December 31, 2015 (in thousands).

	Commercial & Industrial	Commercial Real Estate	Residential Real Estate	Home equity	DDA Consumer	Overdrafts	Total
Three months ended March 31, 2016							
Allowance for loan loss							
Beginning balance	\$ 3,271	\$ 6,985	\$ 6,778	\$1,463	\$ 97	\$ 657	\$19,251
Charge-offs	(1)	(302)	(405)	(106)	(38)	(318)	(1,170)
Recoveries	1	384	39	—	29	242	695

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Provision for acquired loans	—	40	—	—	—	—	40
Provision	632	(703) 347	45	5	173	499
Ending balance	\$ 3,903	\$ 6,404	\$ 6,759	\$1,402	\$ 93	\$ 754	\$19,315

Three months ended March 31, 2015

Allowance for loan loss							
Beginning balance	\$ 1,582	\$ 8,845	\$ 7,208	\$1,495	\$ 85	\$ 859	\$20,074
Charge-offs	(94) (337) (257) (91) (74) (311) (1,164)
Recoveries	18	8	10	—	28	241	305

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Provision for acquired loans	—	246	—	—	—	—	246
Provision	(378))827	(60))180	140	(67))642
Ending balance	\$1,128	\$9,589	\$6,901	\$1,584	\$179	\$722	\$20,103

As of March 31, 2016

Allowance for loan loss

Evaluated for impairment:

Individually	\$—	\$—	\$—	\$—	\$—	\$—	\$—
Collectively	3,899	5,850	6,758	1,390	93	754	18,744
Acquired with deteriorated credit quality	4	554	1	12	—	—	571
Total	\$3,903	\$6,404	\$6,759	\$1,402	\$93	\$754	\$19,315

Loans

Evaluated for impairment:

Individually	\$2,349	\$4,886	\$—	\$—	\$—	\$—	\$7,235
Collectively	162,878	1,120,311	1,395,301	140,985	34,647	2,825	2,856,947
Acquired with deteriorated credit quality	322	10,428	369	1,709	107	—	12,935
Total	\$165,549	\$1,135,625	\$1,395,670	\$142,694	\$34,754	\$2,825	\$2,877,117

As of December 31, 2015

Allowance for loan loss

Evaluated for impairment:

Individually	\$—	\$—	\$—	\$—	\$—	\$—	\$—
Collectively	3,267	6,173	6,777	1,451	97	657	18,422
Acquired with deteriorated credit quality	4	812	1	12	—	—	829
Total	\$3,271	\$6,985	\$6,778	\$1,463	\$97	\$657	\$19,251

Loans

Evaluated for impairment:

Individually	\$2,349	\$6,133	\$—	\$—	\$—	\$—	\$8,482
Collectively	162,662	1,109,327	1,382,762	145,338	35,997	3,361	2,839,447
Acquired with deteriorated credit quality	329	12,121	371	1,698	86	—	14,605
Total	\$165,340	\$1,127,581	\$1,383,133	\$147,036	\$36,083	\$3,361	\$2,862,534

Credit Quality Indicators

All commercial loans within the portfolio are subject to internal risk grading. All non-commercial loans are evaluated based on payment history. The Company's internal risk ratings for commercial loans are: Pass, Special Mention, Substandard and Doubtful. Each internal risk rating is defined in the loan policy using the following criteria: balance sheet yields, ratios and leverage, cash flow spread and coverage, prior history, capability of management, market position/industry, potential impact of changing economic, legal, regulatory or environmental conditions, purpose, structure, collateral support, and guarantor support. Risk grades are generally assigned by the primary lending officer and are periodically evaluated by the Company's internal loan review process. Based on an individual loan's risk grade, estimated loss percentages are applied to the outstanding balance of the loan to determine the amount of

probable loss.

The Company categorizes loans into risk categories based on relevant information regarding the customer's debt service ability, capacity, overall collateral position along with other economic trends, and historical payment performance. The risk grades for each credit are updated when the Company receives current financial information, the loan is reviewed by the Company's internal loan review/credit administration departments, or the loan becomes delinquent or impaired. The risk grades are updated

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a minimum of annually for loans rated exceptional, good, acceptable, or pass/watch. Loans rated special mention, substandard or doubtful are reviewed at least quarterly. The Company uses the following definitions for its risk ratings:

Risk Rating	Description
Pass ratings:	
(a) Exceptional	Loans classified as exceptional are secured with liquid collateral conforming to the internal loan policy. Loans rated within this category pose minimal risk of loss to the bank.
(b) Good	Loans classified as good have similar characteristics that include a strong balance sheet, satisfactory debt service coverage ratios, strong management and/or guarantors, and little exposure to economic cycles. Loans in this category generally have a low chance of loss to the bank.
(c) Acceptable	Loans classified as acceptable have acceptable liquidity levels, adequate debt service coverage ratios, experienced management, and have average exposure to economic cycles. Loans within this category generally have a low risk of loss to the bank.
(d) Pass/watch	Loans classified as pass/watch have erratic levels of leverage and/or liquidity, cash flow is volatile and the borrower is subject to moderate economic risk. A borrower in this category poses a low to moderate risk of loss to the bank.
Special mention	Loans classified as special mention have a potential weakness(es) that deserves management's close attention. The potential weakness could result in deterioration of the loan repayment or the bank's credit position at some future date. A loan rated in this category poses a moderate loss risk to the bank.
Substandard	Loans classified as substandard reflect a customer with a well defined weakness that jeopardizes the liquidation of the debt. Loans in this category have the possibility that the bank will sustain some loss if the deficiencies are not corrected and the bank's collateral value is weakened by the financial deterioration of the borrower.
Doubtful	Loans classified as doubtful have all the weaknesses inherent in those classified as substandard, with the added characteristics that make collection of the full contract amount highly improbable. Loans rated in this category are most likely to cause the bank to have a loss due to a collateral shortfall or a negative capital position.

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The following table presents the Company's commercial loans by credit quality indicators, by class (in thousands):

	Commercial and industrial	Commercial real estate	Total
March 31, 2016			
Pass	\$ 157,275	\$ 1,079,256	\$ 1,236,531
Special mention	1,995	21,247	23,242
Substandard	6,279	34,892	41,171
Doubtful	—	230	230
Total	\$ 165,549	\$ 1,135,625	\$ 1,301,174
December 31, 2015			
Pass	\$ 156,664	\$ 1,070,506	\$ 1,227,170
Special mention	4,099	20,942	25,041
Substandard	4,539	36,133	40,672
Doubtful	38	—	38
Total	\$ 165,340	\$ 1,127,581	\$ 1,292,921

The following table presents the Company's non-commercial loans by payment performance, by class (in thousands):

	Performing	Non-Performing	Total
March 31, 2016			
Residential real estate	\$ 1,392,531	\$ 3,139	\$ 1,395,670
Home equity	142,523	171	142,694
Consumer	34,754	—	34,754
DDA overdrafts	2,825	—	2,825
Total	\$ 1,572,633	\$ 3,310	\$ 1,575,943
December 31, 2015			
Residential real estate	\$ 1,379,797	\$ 3,336	\$ 1,383,133
Home equity	146,877	159	147,036
Consumer	36,049	34	36,083
DDA overdrafts	3,361	—	3,361
Total	\$ 1,566,084	\$ 3,529	\$ 1,569,613

Aging Analysis of Accruing and Non-Accruing Loans

Interest income on loans is accrued and credited to operations based upon the principal amount outstanding, using methods that generally result in level rates of return. Loan origination fees, and certain direct costs, are deferred and amortized as an adjustment to the yield over the term of the loan. The accrual of interest generally is discontinued when a loan becomes 90 days past due as to principal or interest for all loan types. However, any loan may be placed on non-accrual if the Company receives information that indicates a borrower is unable to meet the contractual terms of their respective loan agreement. Other indicators considered for placing a loan on non-accrual status include the borrower's involvement in bankruptcies, foreclosures, repossessions, litigation and any other situation resulting in doubt as to whether full collection of contractual principal and interest is attainable. When interest accruals are discontinued, unpaid interest recognized in income in the current year is reversed, and interest accrued in prior years is charged to the allowance for loan losses. Management may elect to continue the accrual of interest when the net realizable value of collateral exceeds the principal balance and related accrued interest, and the loan is in the process

of collection.

Generally for all loan classes, interest income during the period the loan is non-performing is recorded on a cash basis after recovery of principal is reasonably assured. Cash payments received on nonperforming loans are typically applied directly against the outstanding principal balance until the loan is fully repaid. Generally, loans are restored to accrual status when the obligation is brought current, has performed in accordance with the contractual terms for a reasonable period of time, and the ultimate collectability of the total contractual principal and interest is no longer in doubt.

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Generally, all loan types are considered past due when the contractual terms of a loan are not met and the borrower is 30 days or more past due on a payment. Furthermore, residential and home equity loans are generally subject to charge-off when the loan becomes 120 days past due, depending on the estimated fair value of the collateral less cost to dispose, versus the outstanding loan balance. Commercial loans are generally charged off when the loan becomes 120 days past due. Open-end consumer loans are generally charged off when the loan becomes 180 days past due.

A loan acquired and accounted for under ASC Topic 310-30 is reported as an accruing loan and a performing asset provided that the loan is performing in accordance with the initial expectations. The loan would be considered non-performing if the loan's performance deteriorates below the initial expectations.

The following table presents an aging analysis of the Company's accruing and non-accruing loans, by class (in thousands):

	March 31, 2016						
	Accruing						
	Current	30-59 days	60-89 days	Over 90 days	Purchased-Credit Impaired	Non-accrual	Total
Residential real estate	\$1,387,649	\$4,330	\$553	\$161	\$ —	\$ 2,977	\$1,395,670
Home equity	141,947	535	41	19	—	152	142,694
Commercial and industrial	162,239	145	198	—	—	2,967	165,549
Commercial real estate	1,123,769	1,094	380	45	619	9,718	1,135,625
Consumer	34,672	51	31	—	—	—	34,754
DDA overdrafts	2,312	172	341	—	—	—	2,825
Total	\$2,852,588	\$6,327	\$1,544	\$225	\$ 619	\$ 15,814	\$2,877,117

	December 31, 2015						
	Accruing						
	Current	30-59 days	60-89 days	Over 90 days	Purchased-Credit Impaired	Non-accrual	Total
Residential real estate	\$1,373,604	\$5,261	\$932	\$418	\$ —	\$ 2,918	\$1,383,133
Home equity	146,493	318	65	24	—	136	147,036
Commercial and industrial	162,435	141	—	19	—	2,745	165,340
Commercial real estate	1,114,953	762	211	—	506	11,149	1,127,581
Consumer	35,886	154	9	34	—	—	36,083
DDA overdrafts	3,048	310	3	—	—	—	3,361
Total	\$2,836,419	\$6,946	\$1,220	\$495	\$ 506	\$ 16,948	\$2,862,534

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The following table presents the Company's impaired loans, by class (in thousands). The difference between the unpaid principal balance and the recorded investment generally reflects amounts that have been previously charged-off.

	March 31, 2016			December 31, 2015		
	Recorded Investment	Unpaid Principal Balance	Related Allowance	Recorded Investment	Unpaid Principal Balance	Related Allowance
With no related allowance recorded:						
Residential real estate	\$—	\$—	\$—	—	\$—	\$—
Home equity	—	—	—	—	—	—
Commercial and industrial	2,349	7,547	—	2,349	7,547	—
Commercial real estate	4,886	7,125	—	6,133	9,502	—
Consumer	—	—	—	—	—	—
Total	\$7,235	\$14,672	\$—	—\$8,482	\$17,049	\$—
With an allowance recorded:						
Residential real estate	\$—	\$—	\$—	—	\$—	\$—
Home equity	—	—	—	—	—	—
Commercial and industrial	—	—	—	—	—	—
Commercial real estate	—	—	—	—	—	—
Consumer	—	—	—	—	—	—
Total	\$—	\$—	\$—	—	\$—	\$—

The following table presents information related to the average recorded investment and interest income recognized on the Company's impaired loans, by class (in thousands):

	Three months ended March 31, 2016		2015	
	Average Recorded Investment	Interest Income Recognized	Average Recorded Investment	Interest Income Recognized
With no related allowance recorded:				
Residential real estate	\$—	\$—	\$—	\$—
Home equity	—	—	—	—
Commercial and industrial	2,349	—	—	—
Commercial real estate	5,358	4	5,354	5
Consumer	—	—	—	—
Total	\$7,707	\$4	\$5,354	\$5
With an allowance recorded:				
Residential real estate	\$—	\$—	\$—	\$—
Home equity	—	—	—	—
Commercial and industrial	—	—	2,859	—
Commercial real estate	—	—	1,383	10
Consumer	—	—	—	—
Total	\$—	\$—	\$4,242	\$10

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Approximately \$0.2 million and \$0.2 million of interest income would have been recognized during the three months ended March 31, 2016 and 2015, respectively, if such loans had been current in accordance with their original terms. There were no commitments to provide additional funds on non-accrual, impaired or other potential problem loans at March 31, 2016.

Loan Modifications

The Company's policy on loan modifications typically does not allow for modifications that would be considered a concession from the Company. However, when there is a modification, the Company evaluates each modification to determine if the modification constitutes a troubled debt restructuring ("TDR") in accordance with ASU 2011-2, whereby a modification of a loan would be considered a TDR when both of the following conditions are met: (1) a borrower is experiencing financial difficulty and (2) the modification constitutes a concession. When determining whether the borrower is experiencing financial difficulties, the Company reviews whether the borrower is currently in payment default on any of its debt or whether it is probable that the borrower would be in payment default in the foreseeable future without the modification. Other indicators of financial difficulty include whether the borrower has declared or is in the process of declaring bankruptcy, the borrower's ability to continue as a going concern, and the borrower's projected cash flow to service its debt (including principal and interest) in accordance with the contractual terms for the foreseeable future, without a modification.

Regulatory guidance requires loans to be accounted for as collateral-dependent loans when borrowers have filed Chapter 7 bankruptcy, the debt has been discharged by the bankruptcy court, and the borrower has not reaffirmed the debt. The filing of bankruptcy is deemed to be evidence that the borrower is in financial difficulty and the discharge of the debt by the bankruptcy court is deemed to be a concession granted to the borrower.

The following tables set forth the Company's TDRs (in thousands):

	March 31, 2016			December 31, 2015		
	Accruing	Non-Accruing	Total	Accruing	Non-Accruing	Total
Commercial and industrial	\$54	\$ —	\$54	\$58	\$ —	\$58
Commercial real estate	523	—	523	1,746	—	1,746
Residential real estate	18,306	36	18,342	17,796	191	17,987
Home equity	2,878	—	2,878	2,659	34	2,693
Consumer	—	—	—	—	—	—
	\$21,761	\$ 36	\$21,797	\$22,259	\$ 225	\$22,484

New TDRs

	Three months ended March 31, 2016		2015	
	Pre Modification Outstanding	Post Modification Outstanding	Pre Modification Outstanding	Post Modification Outstanding
	Number of Contracts	Investment	Number of Contracts	Investment
Commercial and industrial	—	\$ —	—	\$ —
Commercial real estate	—	—	—	—
Residential real estate	8741	741	171,405	1,405

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Home equity	129	29	7 187	187
Consumer	<u> </u>	<u> </u>	<u> </u>	<u> </u>
	9\$ 770	\$ 770	24\$ 1,592	\$ 1,592

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Note F – Long-Term Debt

The components of long-term debt are summarized below (in thousands):

	March 31, 2016	December 31, 2015
Junior subordinated debentures owed to City Holding Capital Trust III, due 2038, interest at a rate of 4.13% and 4.01%, respectively	\$ 16,495	\$ 16,495

The Company formed a statutory business trust, City Holding Capital Trust III (“Capital Trust III”), under the laws of Delaware. Capital Trust III was created for the exclusive purpose of (i) issuing trust-preferred capital securities (“Capital Securities”), which represent preferred undivided beneficial interests in the assets of the trust, (ii) using the proceeds from the sale of the Capital Securities to acquire junior subordinated debentures (“Debentures”) issued by the Company, and (iii) engaging in only those activities necessary or incidental thereto. The trust is considered a variable interest entity for which the Company is not the primary beneficiary. Accordingly, the accounts of the trusts are not included in the Company’s consolidated financial statements.

Distributions on the Debentures are cumulative and will be payable quarterly at an interest rate of 3.50% over the three month LIBOR rate, reset quarterly. Interest payments are due in March, June, September and December. The Debentures are redeemable prior to maturity at the option of the Company (i) in whole at any time or in part from time-to-time, or (ii) in whole, but not in part, at any time within 90 days following the occurrence and during the continuation of certain predefined events.

Payments of distributions on the Capital Securities and payments on redemption of the Capital Securities are guaranteed by the Company. The Company also entered into an agreement as to expenses and liabilities with the trust pursuant to which it agreed, on a subordinated basis, to pay any cost, expenses or liabilities of the trust other than those arising under the Capital Securities. The obligations of the Company under the Debentures, the related indentures, the trust agreement establishing the trust, the guarantees and the agreements as to expenses and liabilities, in the aggregate, constitute a full and unconditional guarantee by the Company of the trust’s obligations under the Capital Securities. The Capital Securities issued by the statutory business trusts qualify as Tier 1 capital for the Company under current Federal Reserve Board guidelines.

Note G – Derivative Instruments

The Company enters into derivative transactions principally to protect against the risk of adverse price or interest rate movements on the value of certain assets and liabilities on future cash flows. As of March 31, 2016 and December 31, 2015, the Company has derivative financial instruments not included in hedge relationships. These derivatives consist of interest rate swaps and floors used for interest rate management purposes and derivatives executed with commercial banking customers to facilitate their interest rate management strategies. For the majority of these instruments the Company acts as an intermediary for its customers. Changes in the fair value of the underlying derivative contracts for the most part offset each other and do not significantly impact the Company's results of operations. The Company also has an interest rate swap for the purpose of hedging changes in LIBOR related to commercial real estate loans. Hedge ineffectiveness is assessed quarterly and any ineffectiveness is recorded as non-interest expense. For the three months ended March 31, 2016 hedge ineffectiveness was less than \$0.1 million.

The following table summarizes the notional and fair value of these derivative instruments (in thousands):

	March 31, 2016	December 31, 2015
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	Notional Fair Amount	Fair Value	Notional Fair Amount	Fair Value
Non-hedging interest rate derivatives:				
Other Assets	\$373,378	\$22,332	\$372,995	\$10,811
Other Liabilities	381,065	22,574	380,995	10,872
Derivatives designated as hedges of fair value:				
Other Liabilities	4,950	180	5,475	61

The following table summarizes the change in fair value of these derivative instruments (in thousands):

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	Three months ended March 31,	
	2016	2015
Change in Fair Value Non-Hedging Interest Rate Derivatives:		
Other income - derivative asset	\$11,346	\$2,882
Other income - derivative liability	(11,630)	(2,882)
Change in Fair Value Hedging Interest Rate Derivatives:		
Hedged item - derivative asset	121	66
Other income - derivative liability	(2)	(9)

Certain financial instruments, including derivatives, may be eligible for offset in the consolidated balance sheet and/or subject to master netting arrangements. The Company's derivative transactions with financial institution counterparties are generally executed under International Swaps and Derivative Association ("ISDA") master agreements which include "right of setoff" provisions. In such cases there is generally a legally enforceable right to offset recognized amounts and there may be an intention to settle such amounts on a net basis. Nonetheless, the Company does not generally offset financial instruments for financial reporting purposes. Information about financial instruments that are eligible for offset in the consolidated balance sheet as of March 31, 2016 is presented in the following tables (in thousands):

Description	Gross Amounts of Recognized Assets	Gross Amounts Offset in the Statement of Financial Position	Net Amounts of Assets Presented in the Statement of Financial Position	Netting Adjustment per Applicable Master Agreement of Collateral	Gross Amounts Not Offset in the Statement of Financial Position	Total of Gross Amounts Not Offset in the Statement of Financial Position Including Applicable Netting Agreement and Fair Value of	Net Amount (c)-(d) *

Non-hedging derivative assets:

Interest rate swap agreements	\$ 22,332	\$	—	\$ 22,332	\$	—	\$	—
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Description	Gross Amounts of Recognized Liabilities in the Statement of Financial Position (a)	Gross Amounts Offset in the Statement of Financial Position (b)	Net Amounts of Liabilities Presented in the Statement of Financial Position (c)=(a)-(b)	Gross Amounts Not Offset in the Statement of Financial Position	Netting Adjustment per Applicable Master Netting Arrangements Collateral (d)	Total of Gross Amounts Not Offset in the Statement of Financial Position Including Applicable Netting Agreement and Fair Value of Collateral (e)	Net Amount (c)-(d) *
Non-hedging derivative liabilities:							
Interest rate swap agreements	\$22,574	\$	-\$ 22,574	\$ \$-31,428	\$ 31,428	\$	—
Hedging derivative liabilities:							
Interest rate swap agreements	\$180	\$	-\$ 180	\$ \$-251	\$ 251	\$	—

* For instances where the fair value of financial collateral meets or exceeds the amounts presented in the Statement of Financial Position, a no value is displayed to represent full collateralization.

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Note H – Employee Benefit Plans

Pursuant to the terms of the City Holding Company 2003 Incentive Plan and the City Holding Company 2013 Incentive Plan (the "2003 Plan" and "2013 Plan", respectively), the Compensation Committee of the Board of Directors, or its delegate, may, from time-to-time, grant stock options, stock appreciation rights ("SARs"), or restricted stock awards to employees, directors and individuals who provide service to the Company (collectively, "Plan Participants"). The 2003 Plan expired in April of 2013 and the 2013 Plan was approved by the Company's shareholders in April 2013. A maximum of 750,000 shares of the Company's common stock may be issued upon the exercise of stock options, SARs and stock awards under the 2013 Plan. These limitations may be adjusted in the event of a change in the number of outstanding shares of common stock by reason of a stock dividend, stock split or other similar event. Specific terms of options and SARs awarded, including vesting periods, exercise prices (stock price at date of grant) and expiration dates are determined at the date of grant and are evidenced by agreements between the Company and the awardee. The exercise price of the option grants equals the market price of the Company's common stock on the date of grant. All incentive stock options and SARs will be exercisable up to 10 years from the date granted and all options and SARs are exercisable for the period specified in the individual agreement. As of March 31, 2016, under the 2003 Plan and 2013 Plan, 462,863 stock options had been awarded and 254,247 restricted stock awards had been awarded, respectively.

Each award from the 2003 Plan and 2013 Plan 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 Compensation Committee, or its delegate, determines. The option price for each grant is equal to the fair market value of a share of the Company's common stock on the date of the grant. Options granted expire at such time as the Compensation Committee, or its delegate, determines at the date of the grant and in no event does the exercise period exceed a maximum of ten years. Upon a change-in-control of the Company, as defined in the 2003 Plan and 2013 Plan, all outstanding options and awards shall immediately vest.

Certain stock options and restricted stock awards granted pursuant to the 2013 Plan have performance-based vesting requirements. These shares will vest in three separate annual installments of approximately 33.33% per installment on the third, fourth and fifth anniversaries of the grant date, subject further to performance-based vesting requirements. The performance-based vesting requirements are as follows:

* First Installment – the mean return on average assets of the Company (excluding merger and acquisition expenses and other nonrecurring items as determined by the Board of Directors of the Company) of the three years immediately prior to the vesting date is equal to or exceeds the median return on average assets over the 20 year period immediately preceding the vesting date of all FDIC insured depository institutions.

* Second Installment – the mean return on average assets of the Company (excluding merger and acquisition expenses and other nonrecurring items as determined by the Board of Directors of the Company) of the four years immediately prior to the vesting date is equal to or exceeds the median return on average assets over the 20 year period immediately preceding the vesting date of all FDIC insured depository institutions.

* Third Installment – the mean return on average assets of the Company (excluding merger and acquisition expenses and other nonrecurring items as determined by the Board of Directors of the Company) of the five years immediately prior to the vesting date is equal to or exceeds the median return on average assets over the 20 year period immediately preceding the vesting date of all FDIC insured depository institutions.

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Stock Options

A summary of the Company's stock option activity and related information is presented below:

	Three months ended March 31, 2016		2015	
	Options	Weighted-Average Exercise Price	Options	Weighted-Average Exercise Price
Outstanding at January 1	95,015	\$ 38.38	167,554	\$ 36.74
Granted	24,348	43.73	12,961	46.41
Exercised	—	—	(28,500)	34.40
Forfeited	—	—	—	—
Outstanding at March 31	119,363	\$ 39.49	152,015	\$ 38.01
Exercisable at March 31	35,750	\$ 34.79	76,750	\$ 36.65

Information regarding stock option exercises and stock-based compensation expense associated with stock options is provided in the following table (in thousands):

	Three months ended March 31, 2016		2015	
Proceeds from stock option exercises	\$—	\$1,312		
Intrinsic value of stock options exercised	—	330		
Stock-based compensation expense associated with stock options	\$60	\$51		
At period-end:		March 31, 2016		
Unrecognized stock-based compensation expense associated with stock options		\$560		
Weighted average period (in years) in which the above amount is expected to be recognized		2.9		

Shares issued in connection with stock option exercises are issued from available treasury shares. If no treasury shares are available, new shares would be issued from available authorized shares. During the three months ended March 31, 2016 and 2015, all shares issued in connection with stock option exercises and restricted stock awards were issued from available treasury stock.

Additional information regarding stock options outstanding and exercisable at March 31, 2016, is provided in the following table:

Ranges of Exercise Prices	No. of Options Outstanding	Weighted-Average Exercise Price	Weighted-Average Contractual Life (Years)	Remaining Value	Aggregate Intrinsic Value (in thousands)	No. of Options Currently Exercisable	Weighted-Average Exercise Price of Options Currently Exercisable	Weighted-Average Remaining Contractual Life (Years)	Aggregate Intrinsic Value of Options Currently Exercisable (in thousands)
25.00 - 29.99	1,250	\$ 28.15	3.0	\$ 24	1,250	\$ 28.15	3.0	\$ 24	

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30.00 - 34.99	11,500	31.38	3.4	189	11,500	31.38	3.4	189
35.00 - 39.99	48,351	36.04	6.0	567	16,000	35.09	5.0	203
40.00 - 44.99	45,301	43.51	8.1	194	7,000	40.88	2.0	48
45.00 - 50.00	12,961	46.61	8.9	15	—	—	—	—
	119,363			\$ 989	35,750			\$ 464

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The fair value of the options is estimated at the date of grant using a Black-Scholes option-pricing model. The following weighted average assumptions were used to estimate the fair value of options granted:

	Three months ended March 31, 2016 2015	
Risk-free interest rate	1.43%	1.95%
Expected dividend yield	3.86%	