COMMUNITY TRUST BANCORP INC /KY/
Form 10-Q
November 06, 2015

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 September 30, 2015

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, or a smaller reporting company. See definition of "accelerated filer, large accelerated filer, and smaller reporting 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

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 – 17,519,343 shares outstanding at October 31, 2015

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. CTBI's 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," and 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; the adoption by CTBI of a Federal Financial Institutions Examination Council (FFIEC) policy that provides guidance on the reporting of delinquent consumer loans and the timing of associated credit charge-offs for financial institution subsidiaries; and the resolution of legal proceedings and related matters. In addition, the banking industry in general is subject to various monetary and fiscal policies and regulations, which include those determined by the Federal Reserve Board, the Federal Deposit Insurance Corporation, and state regulators, whose policies and regulations 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, 2014 for further information in this regard.

Community Trust Bancorp, Inc.
Condensed Consolidated Balance Sheets

(dollars in thousands)	(unaudited) September 30 2015	December 31 2014
Assets:		
Cash and due from banks	$54,041	$56,299
Interest bearing deposits	106,628	44,285
Federal funds sold	2,523	4,933
Cash and cash equivalents	163,192	105,517
Certificates of deposit in other banks	5,759	8,197
Securities available-for-sale at fair value (amortized cost of $571,539 and $638,395, respectively)	576,713	640,186
Securities held-to-maturity at amortized cost (fair value of $1,651 and $1,644, respectively)	1,661	1,662
Loans held for sale	1,983	2,264
Loans	2,820,460	2,733,824
Allowance for loan and lease losses	(35,540)	(34,447)
Net loans	2,784,920	2,699,377
Premises and equipment, net	48,541	49,980
Federal Home Loan Bank stock	17,927	17,927
Federal Reserve Bank stock	4,887	4,869
Goodwill	65,490	65,490
Core deposit intangible (net of accumulated amortization of $8,285 and $8,138, respectively)	331	477
Bank owned life insurance	61,942	60,697
Mortgage servicing rights	3,030	2,968
Other real estate owned	34,654	36,776
Other assets	37,118	27,378
Total assets	$3,808,148	$3,723,765
Liabilities and shareholders' equity:		
Deposits:		
Noninterest bearing	$737,657	$677,626
Interest bearing	2,237,572	2,196,631
Total deposits	2,975,229	2,874,257
Repurchase agreements	256,153	235,186
Federal funds purchased and other short-term borrowings	9,215	11,041
Advances from Federal Home Loan Bank	1,084	61,170
Long-term debt	61,341	61,341
Other liabilities	34,541	32,893
Total liabilities	3,337,563	3,275,888
Shareholders' equity:		
Preferred stock, 300,000 shares authorized and unissued	-	-

Common stock, $5 par value, shares authorized 25,000,000; shares outstanding 2015 – 17,513,449; 2014 – 17,466,375	87,568	87,332
Capital surplus	216,253	214,684
Retained earnings	163,401	144,697
Accumulated other comprehensive income, net of tax	3,363	1,164
Total shareholders' equity	470,585	447,877
Total liabilities and shareholders' equity	$3,808,148	$3,723,765

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 September 30 2015	2014	Nine Months Ended September 30 2015	2014
Interest income:				
Interest and fees on loans, including loans held for sale	$32,847	$32,191	$97,691	$95,741
Interest and dividends on securities				
Taxable	2,044	2,763	7,007	8,616
Tax exempt	679	664	2,032	1,912
Interest and dividends on Federal Reserve Bank and Federal Home Loan Bank stock	252	252	756	882
Other, including interest on federal funds sold	90	87	234	310
Total interest income	35,912	35,957	107,720	107,461
Interest expense:				
Interest on deposits	2,412	2,475	7,077	7,409
Interest on repurchase agreements and other short-term borrowings	231	205	689	614
Interest on advances from Federal Home Loan Bank	9	6	33	17
Interest on long-term debt	295	283	869	850
Total interest expense	2,947	2,969	8,668	8,890
Net interest income	32,965	32,988	99,052	98,571
Provision for loan losses	2,520	3,300	6,740	5,380
Net interest income after provision for loan losses	30,445	29,688	92,312	93,191
Noninterest income:				
Service charges on deposit accounts	6,348	6,321	17,976	17,739
Gains on sales of loans, net	462	303	1,575	781
Trust and wealth management income	2,297	2,395	6,902	6,703
Loan related fees	641	1,128	2,747	2,573
Bank owned life insurance	581	523	1,623	1,473
Brokerage revenue	395	505	1,058	1,709
Securities gains (losses)	12	(34)	142	(145)
Other noninterest income	1,299	865	2,976	2,210
Total noninterest income	12,035	12,006	34,999	33,043
Noninterest expense:				
Officer salaries and employee benefits	3,288	2,584	9,179	8,206
Other salaries and employee benefits	10,687	10,881	32,063	31,950
Occupancy, net	1,942	2,007	5,937	6,108
Equipment	746	831	2,295	2,669
Data processing	1,577	2,017	5,204	5,875
Bank franchise tax	1,272	1,208	3,816	3,625
Legal fees	505	558	1,604	1,912
Professional fees	524	491	1,497	1,331
FDIC insurance	606	575	1,798	1,782

Other real estate owned provision and expense	1,289	707	2,525	2,948
Repossession expense	347	322	947	863
Other noninterest expense	4,751	3,682	12,800	10,711
Total noninterest expense	27,534	25,863	79,665	77,980
Income before income taxes	14,946	15,831	47,646	48,254
Income taxes	3,724	4,907	13,084	14,995
Net income	11,222	10,924	34,562	33,259
Other comprehensive income:				
Unrealized holding gains (losses) on securities available-for-sale:				
Unrealized holding gains (losses) arising during the period	3,463	(2,009)	3,525	10,642
Less: Reclassification adjustments for realized gains (losses) included in net income	12	(34)	142	(145)
Tax (benefit) expense	1,208	(691)	1,184	3,776
Other comprehensive income (loss), net of tax	2,243	(1,284)	2,199	7,011
Comprehensive income	$13,465	$9,640	$36,761	$40,270
Basic earnings per share	$0.64	$0.63	$1.98	$1.92
Diluted earnings per share	$0.64	$0.63	$1.98	$1.91
Weighted average shares outstanding-basic	17,440	17,326	17,420	17,317
Weighted average shares outstanding-diluted	17,491	17,402	17,472	17,395
Dividends declared per share	$0.310	$0.300	$0.910	$0.881

See notes to condensed consolidated financial statements.

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

(in thousands)	Nine Months Ended September 30 2015	2014
Cash flows from operating activities:		
Net income	$34,562	$33,259
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	2,977	3,307
Deferred taxes	1,711	1,421
Stock-based compensation	518	548
Excess tax benefits of stock-based compensation	190	22
Provision for loan losses	6,740	5,380
Write-downs of other real estate owned and other repossessed assets	1,146	1,402
Gains on sale of mortgage loans held for sale	(1,575)	(781)
Securities (gains) losses	(142)	145
Losses on sale of assets, net	(115)	(3)
Proceeds from sale of mortgage loans held for sale	63,580	33,240
Funding of mortgage loans held for sale	(61,724)	(31,998)
Amortization of securities premiums and discounts, net	2,552	2,011
Change in cash surrender value of bank owned life insurance	(1,245)	(1,113)
Mortgage servicing rights:		
Fair value adjustments	381	546
New servicing assets created	(443)	(234)
Changes in:		
Other assets	(9,612)	297
Other liabilities	(1,068)	(943)
Net cash provided by operating activities	38,433	46,506
Cash flows from investing activities:		
Certificates of deposit in other banks:		
Maturity of certificates of deposit	2,438	389
Securities available-for-sale (AFS):		
Purchase of AFS securities	(36,561)	(177,579)
Proceeds from the sales of AFS securities	44,198	112,949
Proceeds from prepayments and maturities of AFS securities	56,809	49,094
Securities held-to-maturity (HTM):		
Proceeds from maturities of HTM securities	1	0
Change in loans, net	(98,730)	(73,376)
Purchase of premises and equipment	(1,685)	(1,750)
Proceeds from sale of premises and equipment	232	22
Redemption of stock by Federal Home Loan Bank	0	7,746
Additional investment in Federal Reserve Bank stock	(18)	(1)
Proceeds from sale of other real estate and other repossessed assets	7,563	4,551
Additional investment in other real estate and other repossessed assets	(85)	0
Net cash used in investing activities	(25,838)	(77,955)
Cash flows from financing activities:		

Change in deposits, net	100,972	47,107
Change in repurchase agreements, federal funds purchased, and other short-term borrowings, net	19,141	10,677
Advances from Federal Home Loan Bank	70,000	0
Payments on advances from Federal Home Loan Bank	(130,086)	(87)
Issuance of common stock	1,345	930
Repurchase of common stock	(189)	0
Excess tax benefits of stock-based compensation	(190)	(22)
Dividends paid	(15,913)	(15,339)
Net cash provided by financing activities	45,080	43,266
Net increase in cash and cash equivalents	57,675	11,817
Cash and cash equivalents at beginning of period	105,517	106,641
Cash and cash equivalents at end of period	$163,192	$118,458
Supplemental disclosures:		
Income taxes paid	$15,199	$10,170
Interest paid	7,935	8,058
Non-cash activities:		
Loans to facilitate the sale of other real estate and repossessed assets	3,548	5,745
Common stock dividends accrued, paid in subsequent quarter	220	207
Real estate acquired in settlement of loans	9,694	5,267

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 September 30, 2015, the results of operations for the three and nine months ended September 30, 2015 and 2014, and the cash flows for the nine months ended September 30, 2015 and 2014. 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 nine months ended September 30, 2015 and 2014, and the cash flows for the nine months ended September 30, 2015 and 2014, are not necessarily indicative of the results to be expected for the full year. The condensed consolidated balance sheet as of December 31, 2014 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, 2014, 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. (the "Bank") 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.

All share data has been adjusted for the 10% stock dividend issued on June 2, 2014.

New Accounting Standards –

Ø Accounting for Investments in Qualified Affordable Housing Projects – In January 2014, the FASB issued ASU No. 2014-01, Investments—Equity Method and Joint Ventures (Topic 323): Accounting for Investments in Qualified Affordable Housing Projects, which enables companies that invest in affordable housing projects that qualify for the low-income housing tax credit (LIHTC) to elect to use the proportional amortization method if certain conditions are met. Under the proportional amortization method, the initial investment cost of the project is amortized in proportion to the amount of tax credits and benefits received, with the results of the investment presented on a net basis as a component of income tax expense (benefit). ASU 2014-01 is effective for interim and annual periods beginning after December 15, 2014. The adoption of this ASU did not have a material impact on CTBI's consolidated financial statements.

Ø Reclassification of Residential Real Estate Collateralized Consumer Mortgage Loans upon Foreclosure – In January 2014, the FASB also issued ASU No. 2014-04, Receivables—Troubled Debt Restructurings by Creditors (Subtopic 310-40): Reclassification of Residential Real Estate Collateralized Consumer Mortgage Loans upon Foreclosure, which clarifies when an in-substance foreclosure or repossession of residential real estate property occurs, requiring a creditor to reclassify the loan to other real estate. According to ASU 2014-04, a consumer mortgage loan should be reclassified to other real estate either upon the creditor obtaining legal title to the real estate collateral or when the borrower voluntarily conveys all interest in the real estate property to the creditor through a deed in lieu of foreclosure or similar legal agreement. ASU 2014-04 also clarifies that a creditor should not delay reclassification when a borrower has a legal right of redemption. ASU 2014-04 is effective for interim and annual periods beginning after December 15, 2014. The adoption of this ASU did not have a material impact on CTBI's consolidated financial statements as our practice was already consistent with the new guidance.

Ø Elimination of Extraordinary Reporting – In January 2015, the FASB issued ASU No. 2015-01, Income Statement – Extraordinary and Unusual Items (Subtopic 225-20): Simplifying Income Statement Presentation by Eliminating the Concept of Extraordinary Items. ASU No. 2015-01 eliminates from U.S. GAAP the concept of an extraordinary item. The FASB issued this ASU as part of its initiative to reduce complexity in accounting standards. The objective of the simplification initiative is to identify, evaluate, and improve areas of U.S. GAAP for which cost and complexity can be reduced while maintaining or improving the usefulness of the information provided to the users of financial statements. The amendments in this ASU are effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2015. A reporting entity may apply the amendments prospectively. A reporting entity also may apply the amendments retrospectively to all prior periods presented in the financial statements. Early adoption is permitted provided that the guidance is applied from the beginning of the fiscal year of adoption. The effective date is the same for both public business entities and all other entities. For an entity that prospectively applies the guidance, the only required transition disclosure will be to disclose, if applicable, both the nature and the amount of an item included in income from continuing operations after adoption that adjusts an extraordinary item previously classified and presented before the date of adoption. An entity retrospectively applying the guidance should provide the disclosures in paragraphs 250-10-50-1 through 50-2. The adoption of this ASU is not expected to have a material impact on CTBI's consolidated financial statements.

Ø Intangibles – Goodwill and Other – Internal-Use Software – In April 2015, the FASB issued ASU No. 2015-05, Intangibles – Goodwill and Other – Internal-Use Software (Subtopic 350-40). The amendments in this update provide guidance to customers about whether a cloud computing arrangement includes a software license. If a cloud computing arrangement includes a software license, then the customer should account for the software license element of the arrangement consistent with the acquisition of other software licenses. If a cloud computing arrangement does not include a software license, the customer should account for the arrangement as a service contract. The guidance will not change GAAP for a customer's accounting for service contracts. In addition, the guidance in this update supersedes paragraph 350-40-25-16. Consequently, all software licenses within the scope of Subtopic 350-40 will be accounted for consistent with other licenses of intangible assets. For public business entities, the amendments will be effective for annual periods, including interim periods within those annual periods, beginning after December 15, 2015. Early adoption is permitted. An entity can elect to adopt the amendments either (1) prospectively to all arrangements entered into or materially modified after the effective date or (2) retrospectively. For prospective transition, the only disclosure requirements at transition are the nature of and reason for the change in accounting principle, the transition method, and a qualitative description of the financial statement line items affected by the change. For retrospective transition, the disclosure requirements at transition include the requirements for prospective transition and quantitative information about the effects of the accounting change. We are currently evaluating the impact of adopting ASU 2015-05, but we do not expect the adoption to have a material effect on CTBI's consolidated financial statements.

Ø Business Combinations: Simplifying the Accounting Measurement-Period Adjustments – In September 2015, the FASB issued ASU No. 2015-16 – Business Combinations (Topic 805): Simplifying the Accounting for Measurement-Period Adjustments. Topic 805 requires that an acquirer retrospectively adjust provisional amounts recognized in a business combination, during the measurement period. To simplify the accounting for adjustments made to provisional amounts, the amendments in the Update require that the acquirer recognize adjustments to provisional amounts that are identified during the measurement period in the reporting period in which the adjustment amount is determined. The acquirer is required to also record, in the same period's financial statements, the effect on earnings of changes in depreciation, amortization, or other income effects, if any, as a result of the change to the provisional amounts, calculated as if the accounting had been completed at the acquisition date. In addition an entity is required to present separately on the face of the income statement or disclose in the notes to the financial statements the portion of the amount recorded in current-period earnings by line item that would have been recorded in previous reporting periods if the adjustment to the provisional amounts had been recognized as of the acquisition date. For public business entities, the amendments in this Update are effective for fiscal years beginning after December 15, 2015, including interim periods within those fiscal years. The amendments in this Update should be applied prospectively to adjustments to provisional amounts that occur after the effective date of this Update with earlier application permitted for financial statements that have not been issued. The adoption of this ASU is not expected to have a material impact on CTBI's consolidated financial statements.

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 (FASB) 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.

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. Since arriving at an appropriate ALLL involves a high degree of management judgment, we use an ongoing quarterly analysis to develop a range of estimated losses. In accordance with accounting principles generally accepted in the United States, we use our best estimate within the range of potential credit loss to determine the appropriate ALLL. 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 non-accrual 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, a charge off is taken, if necessary, in order that the remaining balance reflects the fair value estimated less costs to sell of the collateral then transferred to other real estate owned or other repossessed assets. 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. Based upon management's judgment, "best case," "worst case," and "most likely" scenarios are determined. The total of each of these weighted factors is then applied against the applicable portion of the portfolio and the ALLL is adjusted accordingly to approximate the most likely scenario. 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 market value less expected sales costs. Additionally, periodic updated appraisals are obtained on unsold foreclosed properties. When an updated appraisal reflects a market value below the current book value, a charge is booked to current earnings to reduce the property to its new 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 by a charge to income.

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 nine months ended September 30, 2015 and 2014, CTBI did not recognize a significant amount of interest expense or penalties in connection with income taxes.

CTBI is currently under IRS examination of its 2013 corporate income tax return. Management does not expect that the results of the examination will have a material effect on our financial condition. While management believes our tax positions are appropriate, the IRS could challenge our positions as a part of this examination.

Note 2 – Stock-Based Compensation

CTBI's compensation expense related to stock option grants was $10 thousand and $3 thousand, respectively, for the three months ended September 30, 2015 and 2014, and $29 thousand and $8 thousand, respectively, for the nine months ended September 30, 2015 and 2014. Restricted stock expense for the three months ended September 30, 2015 and 2014 was $186 thousand and $202 thousand, respectively, including $20 thousand and $30 thousand in dividends paid for each period. Restricted stock expense for the nine months ended September 30, 2015 and 2014 was $554 thousand and $540 thousand, respectively, including $59 thousand and $90 thousand in dividends. As of September 30, 2015, there was a total of $0.2 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 4.1 years and a total of $0.5 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 2.0 years.

There were no shares of restricted stock granted during the three months ended September 30, 2015 and 2014. There were 10,582 and 4,561 shares of restricted stock granted during the nine months ended September 30, 2015 and 2014, respectively. The restrictions on the restricted stock lapse ratably over four years or in the event of a change in control of CTBI or the death of the participant. In the event of the disability of the participant, the restrictions will lapse on a pro rata basis. The Compensation Committee of the Board of Directors will have discretion to review and revise restrictions applicable to a participant's restricted stock in the event of the participant's retirement. There were no options granted to purchase shares of CTBI common stock during the three months ended September 30, 2015. There were 20,000 options granted during the nine months ended September 30, 2015. There were 10,000 options granted during the three and nine months ended September 30, 2014.

The fair value of options granted during the nine months ended September 30, 2015, were established at the date of grant using a Black-Scholes option pricing model with the weighted average assumptions as follows:

	Nine Months Ended September 30	
	2015	2014
Expected dividend yield	3.72 %	3.40 %
Risk-free interest rate	1.54 %	2.01 %
Expected volatility	30.77 %	30.77 %
Expected term (in years)	7.0	7.0
Weighted average fair value of options	$ 6.60	$ 7.76

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 September 30, 2015 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	$ 201,461	$ 990	$ (401)	$ 202,050
State and political subdivisions	132,249	3,718	(508)	135,459

U.S. government sponsored agency mortgage-backed securities	212,829	2,473	(1,126)	214,176
Total debt securities	546,539	7,181	(2,035)	551,685
CRA investment funds	25,000	28	0	25,028
Total available-for-sale securities	$571,539	$ 7,209	$ (2,035)	$576,713

Held-to-Maturity

(in thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
U.S. Treasury and government agencies	$ 480	$ 0	$ (11)	$469
State and political subdivisions	1,181	1	0	1,182
Total held-to-maturity securities	$ 1,661	$ 1	$ (11)	$1,651

The amortized cost and fair value of securities at December 31, 2014 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	$190,563	$ 509	$ (2,140)	$188,932
State and political subdivisions	133,951	3,973	(466)	137,458
U.S. government sponsored agency mortgage-backed securities	288,881	2,876	(2,850)	288,907
Total debt securities	613,395	7,358	(5,456)	615,297
CRA investment funds	25,000	0	(111)	24,889
Total available-for-sale securities	$638,395	$ 7,358	$ (5,567)	$640,186

Held-to-Maturity

(in thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
U.S. Treasury and government agencies	$ 480	$ 0	$ (19)	$461
State and political subdivisions	1,182	1	0	1,183
Total held-to-maturity securities	$ 1,662	$ 1	$ (19)	$1,644

The amortized cost and fair value of securities at September 30, 2015 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	$30,015	$30,092	$0	$0
Due after one through five years	128,605	129,937	1,181	1,182
Due after five through ten years	124,654	126,142	480	469
Due after ten years	50,436	51,338	0	0
U.S. government sponsored agency mortgage-backed securities	212,829	214,176	0	0
Total debt securities	546,539	551,685	1,661	1,651
CRA investment funds	25,000	25,028	0	0

Total securities	$571,539	$576,713	$1,661	$1,651

As of September 30, 2015, there was a net gain of $142 thousand realized on sales and calls of AFS securities, consisting of a pre-tax gain of $840 thousand and a pre-tax loss of $698 thousand. As of September 30, 2014, there was a net loss of $145 thousand.

The amortized cost of securities pledged as collateral, to secure public deposits and for other purposes, was $217.6 million at September 30, 2015 and $267.1 million at December 31, 2014.

The amortized cost of securities sold under agreements to repurchase amounted to $286.4 million at September 30, 2015 and $280.9 million at December 31, 2014.

CTBI evaluates its investment portfolio on a quarterly basis for impairment. The analysis performed as of September 30, 2015 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 September 30, 2015 was 34.8% compared to 44.1% as of December 31, 2014. 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 September 30, 2015 that are not deemed to be other-than-temporarily impaired.

Available-for-Sale

(in thousands)	Amortized Cost	Gross Unrealized Losses	Fair Value
Less Than 12 Months			
U.S. Treasury and government agencies	$22,178	$ (13)	$22,165
State and political subdivisions	17,068	(179)	16,889
U.S. government sponsored agency mortgage-backed securities	50,213	(207)	50,006
Total debt securities	89,459	(399)	89,060
CRA investment funds	0	(0)	0
Total <12 months temporarily impaired AFS securities	89,459	(399)	89,060
12 Months or More			
U.S. Treasury and government agencies	54,773	(388)	54,385
State and political subdivisions	7,297	(329)	6,968
U.S. government sponsored agency mortgage-backed securities	51,291	(919)	50,372
Total debt securities	113,361	(1,636)	111,725
CRA investment funds	0	0	0
Total ≥12 months temporarily impaired AFS securities	113,361	(1,636)	111,725
Total			
U.S. Treasury and government agencies	76,951	(401)	76,550
State and political subdivisions	24,365	(508)	23,857
U.S. government sponsored agency mortgage-backed securities	101,504	(1,126)	100,378
Total debt securities	202,820	(2,035)	200,785
CRA investment funds	0	(0)	0
Total temporarily impaired AFS securities	$202,820	$ (2,035)	$200,785

Held-to-Maturity

(in thousands)

	Amortized Cost	Gross Unrealized Losses	Fair Value
12 Months or More			
U.S. Treasury and government agencies	$ 480	$ (11)	$ 469
Total temporarily impaired HTM securities	$ 480	$ (11)	$ 469

U.S. Treasury and Government Agencies

The unrealized losses in U.S. Treasury and government agencies were caused by interest rate increases. The contractual terms of those investments do not permit the issuer to settle the securities at a price less than amortized cost. CTBI does not consider those investments to be other-than-temporarily impaired at September 30, 2015, because CTBI does not intend to sell the investments and it is not more likely than not that we will be required to sell the investments before recovery of their amortized cost, which may be at maturity.

State and Political Subdivisions

The unrealized losses in securities of state and political subdivisions were caused by interest rate increases. The contractual terms of those investments do not permit the issuer to settle the securities at a price less than amortized cost. CTBI does not consider those investments to be other-than-temporarily impaired at September 30, 2015, because CTBI does not intend to sell the investments before recovery of their amortized cost, which may be at maturity.

U.S. Government Sponsored Agency Mortgage-Backed Securities

The unrealized losses in U.S. government sponsored agency mortgage-backed securities were caused by interest rate increases. CTBI expects to recover the amortized cost basis over the term of the securities. CTBI does not consider those investments to be other-than-temporarily impaired at September 30, 2015, because (i) the decline in market value is attributable to changes in interest rates and not credit quality, (ii) CTBI does not intend to sell the investments, and (iii) it is not more likely than not we will be required to sell the investments before recovery of their amortized cost, which may be at maturity.

The analysis performed as of December 31, 2014 indicated that all impairment was considered temporary, market and interest rate driven, and not credit-related. 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 December 31, 2014 that are not deemed to be other-than-temporarily impaired.

Available-for-Sale

(in thousands)	Amortized Cost	Gross Unrealized Losses	Fair Value
Less Than 12 Months			
U.S. Treasury and government agencies	$ 31,185	$ (87)	$ 31,098
State and political subdivisions	8,800	(23)	8,777
U.S. government sponsored agency mortgage-backed securities	50,115	(442)	49,673
Total debt securities	90,100	(552)	89,548
CRA investment funds	25,000	(111)	24,889
Total <12 months temporarily impaired AFS securities	115,100	(663)	114,437

12 Months or More			
U.S. Treasury and government agencies	65,209	(2,053)	63,156
State and political subdivisions	21,308	(443)	20,865
U.S. government sponsored agency mortgage-backed securities	86,389	(2,408)	83,981
Total debt securities	172,906	(4,904)	168,002
CRA investment funds	0	0	0
Total ≥12 months temporarily impaired AFS securities	172,906	(4,904)	168,002
Total			
U.S. Treasury and government agencies	96,394	(2,140)	94,254
State and political subdivisions	30,108	(466)	29,642
U.S. government sponsored agency mortgage-backed securities	136,504	(2,850)	133,654
Total debt securities	263,006	(5,456)	257,550
CRA investment funds	25,000	(111)	24,889
Total temporarily impaired AFS securities	$ 288,006	$ (5,567)	$ 282,439

Held-to-Maturity

(in thousands)	Amortized Cost	Gross Unrealized Losses	Fair Value
12 Months or More			
U.S. Treasury and government agencies	$ 480	$ (19)	$ 461
Total temporarily impaired HTM securities	$ 480	$ (19)	$ 461

Note 4 – Loans

Major classifications of loans, net of unearned income, deferred loan origination costs, and net premiums on acquired loans, are summarized as follows:

(in thousands)	September 30 2015	December 31 2014
Commercial construction	$ 106,855	$ 121,942
Commercial secured by real estate	997,654	948,626
Equipment lease financing	9,146	10,344
Commercial other	346,318	352,048
Real estate construction	62,226	62,412
Real estate mortgage	706,187	712,465
Home equity	88,624	88,335
Consumer direct	125,847	122,136
Consumer indirect	377,603	315,516
Total loans	$ 2,820,460	$ 2,733,824

CTBI has segregated and evaluates its loan portfolio through nine portfolio segments. CTBI serves customers in small and mid-sized communities in eastern, northeastern, central, and south central Kentucky, southern West Virginia, and northeastern Tennessee. Therefore, CTBI's exposure to credit risk is significantly affected by changes in these communities.

Commercial construction loans are for the purpose of erecting or rehabilitating buildings or other structures for commercial purposes, including any infrastructure necessary for development. Included in this category are improved property, land development, and tract development loans. The terms of these loans are generally short-term with permanent financing upon completion.

Commercial real estate loans include loans secured by nonfarm, nonresidential properties, 1-4 family/multi-family properties, farmland, and other commercial real estate. These loans are originated based on the borrower's ability to service the debt and secondarily based on the fair value of the underlying collateral.

Equipment lease financing loans are fixed, variable, and tax exempt leases for commercial purposes.

Commercial other loans consist of commercial check loans, agricultural loans, receivable financing, floorplans, loans to financial institutions, loans for purchasing or carrying securities, and other commercial purpose loans. Commercial loans are underwritten based on the borrower's ability to service debt from the business's underlying cash flows. As a general practice, we obtain collateral such as real estate, equipment, or other assets, although such loans may be uncollateralized but guaranteed.

Real estate construction loans are typically for owner-occupied properties. The terms of these loans are generally short-term with permanent financing upon completion.

Residential real estate loans are a mixture of fixed rate and adjustable rate first and second lien residential mortgage loans. As a policy, CTBI holds adjustable rate loans and sells the majority of its fixed rate first lien mortgage loans into the secondary market. Changes in interest rates or market conditions may impact a borrower's ability to meet contractual principal and interest payments. Residential real estate loans are secured by real property.

Home equity lines are revolving adjustable rate credit lines secured by real property.

Consumer direct loans are primarily fixed rate products comprised of unsecured loans, consumer revolving credit lines, deposit secured loans, and all other consumer purpose loans.

Consumer indirect loans are fixed rate loans secured by automobiles, trucks, vans, and recreational vehicles originated at the selling dealership underwritten and purchased by CTBI's indirect lending department. Both new and used products are financed. Only dealers who have executed dealer agreements with CTBI participate in the indirect lending program.

Not included in the loan balances above were loans held for sale in the amount of $2.0 million at September 30, 2015 and $2.3 million at December 31, 2014, respectively.

Refer to note 1 to the condensed consolidated financial statements for further information regarding our nonaccrual policy. Nonaccrual loans segregated by class of loans were as follows:

(in thousands)	September 30 2015	December 31 2014
Commercial:		
Commercial construction	$ 3,443	$ 4,339
Commercial secured by real estate	4,134	6,725
Commercial other	1,412	2,423
Residential:		
Real estate construction	311	602
Real estate mortgage	5,108	6,513
Home equity	200	369

Consumer:		
Consumer direct	114	0
Total nonaccrual loans	$ 14,722	$ 20,971

The following tables present CTBI's loan portfolio aging analysis, segregated by class, as of September 30, 2015 and December 31, 2014:

	September 30, 2015						
(in thousands)	30-59 Days Past Due	60-89 Days Past Due	90+ Days Past Due	Total Past Due	Current	Total Loans	90+ and Accruing*
Commercial:							
Commercial construction	$251	$7	$5,133	$5,391	$101,464	$106,855	$ 1,690
Commercial secured by real estate	5,348	1,401	6,574	13,323	984,331	997,654	4,766
Equipment lease financing	0	0	0	0	9,146	9,146	0
Commercial other	870	417	4,152	5,439	340,879	346,318	2,904
Residential:							
Real estate construction	609	129	717	1,455	60,771	62,226	420
Real estate mortgage	1,517	4,637	10,906	17,060	689,127	706,187	7,111
Home equity	516	122	749	1,387	87,237	88,624	602
Consumer:							
Consumer direct	1,055	260	89	1,404	124,443	125,847	89
Consumer indirect	2,503	404	419	3,326	374,277	377,603	419
Total	$12,669	$7,377	$28,739	$48,785	$2,771,675	$2,820,460	$ 18,001

	December 31, 2014						
(in thousands)	30-59 Days Past Due	60-89 Days Past Due	90+ Days Past Due	Total Past Due	Current	Total Loans	90+ and Accruing*
Commercial:							
Commercial construction	$40	$31	$6,171	$6,242	$115,700	$121,942	$ 1,863
Commercial secured by real estate	2,471	1,595	10,763	14,829	933,797	948,626	4,682
Equipment lease financing	0	0	0	0	10,344	10,344	0
Commercial other	826	55	4,205	5,086	346,962	352,048	2,367
Residential:							
Real estate construction	92	144	985	1,221	61,191	62,412	383
Real estate mortgage	1,005	5,171	13,049	19,225	693,240	712,465	7,742
Home equity	779	197	703	1,679	86,656	88,335	422
Consumer:							
Consumer direct	1,307	295	141	1,743	120,393	122,136	141
Consumer indirect	2,304	586	385	3,275	312,241	315,516	385
Total	$8,824	$8,074	$36,402	$53,300	$2,680,524	$2,733,824	$ 17,985

*90+ and Accruing are also included in 90+ Days Past Due column.

The risk characteristics of CTBI's material portfolio segments are as follows:

Commercial construction loans generally are made to customers for the purpose of building income-producing properties. Personal guarantees of the principals are generally required. Such loans are made on a projected cash flow basis and are secured by the project being constructed. Construction loan draw procedures are included in each specific loan agreement, including required documentation items and inspection requirements. Construction loans may convert to term loans at the end of the construction period, or may be repaid by the take-out commitment from another financing source. If the loan is to convert to a term loan, the repayment ability is based on the borrower's projected cash flow. Risk is mitigated during the construction phase by requiring proper documentation and inspections whenever a draw is requested. Loans in amounts greater than $500,000 generally require a performance bond to be posted by the general contractor to assure completion of the project.

Commercial real estate loans are viewed primarily as cash flow loans and secondarily as loans secured by real estate. Commercial real estate lending typically involves higher loan principal amounts and the repayment of these loans is generally dependent on the successful operation of the property securing the loan or the business conducted on the property securing the loan. Commercial real estate loans may be more adversely affected by conditions in the real estate markets or in the general economy. Management monitors and evaluates commercial real estate loans based on collateral and risk grade criteria.

Equipment lease financing is underwritten by our commercial lenders using the same underwriting standards as would be applied to a secured commercial loan requesting 100% financing. The pricing for equipment lease financing is comparable to that of borrowers with similar quality commercial credits with similar collateral. Maximum terms of equipment leasing are determined by the type and expected life of the equipment to be leased. Residual values are determined by appraisals or opinion letters from industry experts. Leases must be in conformity with our consolidated annual tax plan. As we underwrite our equipment lease financing in a manner similar to our commercial loan portfolio described below, the risk characteristics for this portfolio mirror that of the commercial loan portfolio.

Commercial loans are primarily based on the identified cash flows of the borrower and secondarily on the underlying collateral provided by the borrower. The cash flows of borrowers, however, may not be as expected and the collateral securing these loans may fluctuate in value. Most commercial loans are secured by the assets being financed or other business assets such as accounts receivable or inventory and may incorporate a personal guarantee; however, some short-term loans may be made on an unsecured basis. In the case of loans secured by accounts receivable, the availability of funds for the repayment of these loans may be substantially dependent on the ability of the borrower to collect amounts due from its customers.

With respect to residential loans that are secured by 1-4 family residences and are generally owner occupied, CTBI generally establishes a maximum loan-to-value ratio and requires private mortgage insurance if that ratio is exceeded. Home equity loans are typically secured by a subordinate interest in 1-4 family residences. Residential construction loans are handled through the home mortgage area of the bank. The repayment ability of the borrower and the maximum loan-to-value ratio are calculated using the normal mortgage lending criteria. Draws are processed based on percentage of completion stages including normal inspection procedures. Such loans generally convert to term loans after the completion of construction.

Consumer loans are secured by consumer assets such as automobiles or recreational vehicles. Some consumer loans are unsecured such as small installment loans and certain lines of credit. Our determination of a borrower's ability to repay these loans is primarily dependent on the personal income and credit rating of the borrowers, which can be impacted by economic conditions in their market areas such as unemployment levels. Repayment can also be impacted by changes in property values on residential properties. Risk is mitigated by the fact that the loans are of smaller individual amounts and spread over a large number of borrowers.

The indirect lending area of the bank generally deals with purchasing/funding consumer contracts with new and used automobile dealers. The dealers generate consumer loan applications which are forwarded to the indirect loan processing area for approval or denial. Loan approvals or denials are based on the creditworthiness and repayment ability of the borrower, and on the collateral value. The dealers may have recourse agreements with the Bank.

Credit Quality Indicators:

CTBI categorizes loans into risk categories based on relevant information about the ability of borrowers to service their debt such as: current financial information, historical payment experience, credit documentation, public information, and current economic trends, among other factors. CTBI also considers the fair value of the underlying collateral and the strength and willingness of the guarantor(s). CTBI analyzes commercial loans individually by classifying the loans as to credit risk. Loans classified as loss, doubtful, substandard, or special mention are reviewed quarterly by CTBI for further deterioration or improvement to determine if appropriately classified and valued if deemed impaired. All other commercial loan reviews are completed every 12 to 18 months. In addition, during the renewal process of any loan, as well as if a loan becomes past due or if other information becomes available, CTBI will evaluate the loan grade. CTBI uses the following definitions for risk ratings:

- Pass grades include investment grade, low risk, moderate risk, and acceptable risk loans. The loans range from loans that have no chance of resulting in a loss to loans that have a limited chance of resulting in a loss. Customers in this grade have excellent to fair credit ratings. The cash flows are adequate to meet required debt repayments.

- Watch graded loans are loans that warrant extra management attention but are not currently criticized. Loans on the watch list may be potential troubled credits or may warrant "watch" status for a reason not directly related to the asset quality of the credit. The watch grade is a management tool to identify credits which may be candidates for future classification or may temporarily warrant extra management monitoring.

- Other assets especially mentioned (OAEM) reflects loans that are currently protected but are potentially weak. These loans constitute an undue and unwarranted credit risk but not to the point of justifying a classification of substandard. The credit risk may be relatively minor yet constitute an unwarranted risk in light of circumstances surrounding a specific asset. Loans in this grade display potential weaknesses which may, if unchecked or uncorrected, inadequately protect CTBI's credit position at some future date. The loans may be adversely affected by economic or market conditions.

- Substandard grading indicates that the loan is inadequately protected by the current sound worth and paying capacity of the obligor or of the collateral pledged. These loans have a well-defined weakness or weaknesses that jeopardize the orderly liquidation of the debt with the distinct possibility that CTBI will sustain some loss if the deficiencies are not corrected.

- Doubtful graded loans have the weaknesses inherent in the substandard grading with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently existing facts, conditions, and values, highly questionable and improbable. The probability of loss is extremely high, but because of certain important and reasonably specific pending factors which may work to CTBI's advantage or strengthen the asset(s), its classification as an estimated loss is deferred until its more exact status may be determined. Pending factors include proposed merger, acquisition, or liquidation procedures, capital injection, perfecting liens on additional collateral, and refinancing plans.

The following table presents the credit risk profile of CTBI's commercial loan portfolio based on rating category and payment activity, segregated by class of loans, as of September 30, 2015 and December 31, 2014:

(in thousands)	Commercial Construction	Commercial Secured by Real Estate	Equipment Leases	Commercial Other	Total
September 30, 2015					
Pass	$ 85,878	$ 885,941	$ 9,146	$ 296,254	$1,277,219

Watch	6,615	69,393	0	41,547	117,555
OAEM	4,205	8,286	0	1,001	13,492
Substandard	8,999	33,162	0	6,451	48,612
Doubtful	1,158	872	0	1,065	3,095
Total	$ 106,855	$ 997,654	$ 9,146	$ 346,318	$ 1,459,973
December 31, 2014					
Pass	$ 101,314	$ 834,751	$ 10,344	$ 307,270	$ 1,253,679
Watch	9,857	69,123	0	36,114	115,094
OAEM	934	10,973	0	881	12,788
Substandard	5,647	27,901	0	5,772	39,320
Doubtful	4,190	5,878	0	2,011	12,079
Total	$ 121,942	$ 948,626	$ 10,344	$ 352,048	$ 1,432,960

The following table presents the credit risk profile of the CTBI's residential real estate and consumer loan portfolios based on performing or nonperforming status, segregated by class, as of September 30, 2015 and December 31, 2014:

(in thousands)	Real Estate Construction	Real Estate Mortgage	Home Equity	Consumer Direct	Consumer Indirect	Total
September 30, 2015						
Performing	$ 61,495	$ 693,968	$ 87,822	$ 125,644	$ 377,184	$ 1,346,113
Nonperforming (1)	731	12,219	802	203	419	14,374
Total	$ 62,226	$ 706,187	$ 88,624	$ 125,847	$ 377,603	$ 1,360,487
December 31, 2014						
Performing	$ 61,427	$ 698,210	$ 87,544	$ 121,995	$ 315,131	$ 1,284,307
Nonperforming (1)	985	14,255	791	141	385	16,557
Total	$ 62,412	$ 712,465	$ 88,335	$ 122,136	$ 315,516	$ 1,300,864

(1) A loan is considered nonperforming if it is 90 days or more past due and/or on nonaccrual.

The total of consumer mortgage loans secured by real estate properties for which formal foreclosure proceedings are in process totaled $5.3 million at September 30, 2015 compared to $5.9 million at December 31, 2014.

A loan is considered impaired, in accordance with the impairment accounting guidance, when based on current information and events, it is probable CTBI will be unable to collect all amounts due from the borrower in accordance with the contractual terms of the loan. Impaired loans include nonperforming commercial loans but also include loans modified in troubled debt restructurings where concessions have been granted to borrowers experiencing financial difficulties. These concessions could include a reduction in the interest rate on the loan, payment extensions, forgiveness of principal, forbearance, or other actions intended to maximize collection.

The following tables present impaired loans, the average investment in impaired loans, and interest income recognized on impaired loans for the periods ended September 30, 2015, December 31, 2014, and September 30, 2014:

	September 30, 2015		
(in thousands)	Recorded Balance	Unpaid Contractual Principal Balance	Specific Allowance
Loans without a specific valuation allowance:			

Commercial construction	$4,669	$ 4,669	$ 0
Commercial secured by real estate	30,318	31,551	0
Commercial other	7,163	8,804	0
Real estate mortgage	1,189	1,189	0
Loans with a specific valuation allowance:			
Commercial construction	3,411	3,412	719
Commercial secured by real estate	835	1,075	317
Commercial other	754	935	312
Totals:			
Commercial construction	8,080	8,081	719
Commercial secured by real estate	31,153	32,626	317
Commercial other	7,917	9,739	312
Real estate mortgage	1,189	1,189	0
Total	$48,339	$ 51,635	$ 1,348

	Three Months Ended September 30, 2015		Nine Months Ended September 30, 2015	
(in thousands)	Average Investment in Impaired Loans	*Interest Income Recognized	Average Investment in Impaired Loans	*Interest Income Recognized
Loans without a specific valuation allowance:				
Commercial construction	$4,864	$ 41	$5,142	$ 160
Commercial secured by real estate	30,713	316	30,357	985
Commercial other	7,312	73	9,182	201
Real estate mortgage	1,183	13	1,090	37
Loans with a specific valuation allowance:				
Commercial construction	3,445	0	3,712	0
Commercial secured by real estate	841	6	2,244	7
Commercial other	776	1	788	1
Totals:				
Commercial construction	8,309	41	8,854	160
Commercial secured by real estate	31,554	322	32,601	992
Commercial other	8,088	74	9,970	202
Real estate mortgage	1,183	13	1,090	37
Total	$49,134	$ 450	$52,515	$ 1,391

	December 31, 2014				
(in thousands)	Recorded Balance	Unpaid Contractual Principal Balance	Specific Allowance	Average Investment in Impaired Loans	*Interest Income Recognized
Loans without a specific valuation allowance:					
Commercial construction	$5,653	$ 5,654	$ 0	$ 5,415	$ 205
Commercial secured by real estate	31,639	33,268	0	34,650	1,180
Commercial other	13,069	14,597	0	15,663	783

Real estate mortgage	1,277	1,277	0	1,507	53
Loans with a specific valuation allowance:					
Commercial construction	3,974	3,974	734	4,216	0
Commercial secured by real estate	2,718	2,876	827	4,376	11
Commercial other	738	862	181	531	1
Totals:					
Commercial construction	9,627	9,628	734	9,631	205
Commercial secured by real estate	34,357	36,144	827	39,026	1,191
Commercial other	13,807	15,459	181	16,194	784
Real estate mortgage	1,277	1,277	0	1,507	53
Total	$59,068	$ 62,508	$ 1,742	$ 66,358	$ 2,233

(in thousands)	September 30, 2014 Recorded Balance	Unpaid Contractual Principal Balance	Specific Allowance
Loans without a specific valuation allowance:			
Commercial construction	$5,250	$ 5,251	$ 0
Commercial secured by real estate	33,010	34,086	0
Commercial other	15,972	18,247	0
Real estate mortgage	1,874	1,875	0
Loans with a specific valuation allowance:			
Commercial construction	4,149	4,149	734
Commercial secured by real estate	6,070	6,219	1,273
Commercial other	586	710	211
Totals:			
Commercial construction	9,399	9,400	734
Commercial secured by real estate	39,080	40,305	1,273
Commercial other	16,558	18,957	211
Real estate mortgage	1,874	1,875	0
Total	$66,911	$ 70,537	$ 2,218

	Three Months Ended September 30, 2014		Nine Months Ended September 30, 2014	
(in thousands)	Average Investment in Impaired Loans	*Interest Income Recognized	Average Investment in Impaired Loans	*Interest Income Recognized
Loans without a specific valuation allowance:				
Commercial construction	$5,259	$ 44	$5,330	$ 172
Commercial secured by real estate	33,290	261	34,464	858
Commercial other	17,577	248	16,421	619
Real estate mortgage	1,860	12	1,583	44
Loans with a specific valuation allowance:				

Commercial construction	4,213	0	4,270	0
Commercial secured by real estate	6,076	5	4,912	9
Commercial other	587	0	460	0
Totals:				
Commercial construction	9,472	44	9,600	172
Commercial secured by real estate	39,366	266	39,376	867
Commercial other	18,164	248	16,881	619
Real estate mortgage	1,860	12	1,583	44
Total	$68,862	$ 570	$67,440	$ 1,702

*Cash basis interest is substantially the same as interest income recognized.

Included in certain loan categories of impaired loans are certain loans and leases that have been modified in a troubled debt restructuring, where economic concessions have been granted to borrowers who have experienced financial difficulties. These concessions typically result from our loss mitigation activities and could include reductions in the interest rate, payment extensions, forgiveness of principal, forbearance or other actions. Modifications of terms for our loans and their inclusion as troubled debt restructurings are based on individual facts and circumstances. Loan modifications that are included as troubled debt restructurings may involve either an increase or reduction of the interest rate, extension of the term of the loan, or deferral of principal and/or interest payments, regardless of the period of the modification. All of the loans identified as troubled debt restructuring were modified due to financial stress of the borrower. In order to determine if a borrower is experiencing financial difficulty, an evaluation is performed to determine the probability that the borrower will be in payment default on any of its debt in the foreseeable future without the modification. This evaluation is performed under CTBI's internal underwriting policy.

When we modify loans and leases in a troubled debt restructuring, we evaluate any possible impairment similar to other impaired loans based on the present value of expected future cash flows, discounted at the contractual interest rate of the original loan or lease agreement, or use the current fair value of the collateral, less selling costs for collateral dependent loans. If we determined that the value of the modified loan is less than the recorded investment in the loan (net of previous charge-offs, deferred loan fees or costs and unamortized premium or discount), impairment is recognized through an allowance estimate or a charge-off to the allowance. In periods subsequent to modification, we evaluate all troubled debt restructuring, including those that have payment defaults, for possible impairment and recognize impairment through the allowance.

During 2015, certain loans were modified in troubled debt restructurings, where economic concessions were granted to borrowers consisting of reductions in the interest rates, payment extensions, forgiveness of principal, and forbearances. Presented below, segregated by class of loans, are troubled debt restructurings that occurred during the three and nine months ended September 30, 2015 and 2014 and the year ended December 31, 2014:

	Three Months Ended September 30, 2015				
(in thousands)	Number of Loans	Term Modification	Rate Modification	Combination	Post-Modification Outstanding Balance
Commercial:					
Commercial secured by real estate	5	$ 346	$ 0	$ 165	$ 511
Commercial other	1	1,139	0	0	1,139
Total troubled debt restructurings	6	$ 1,485	$ 0	$ 165	$ 1,650

Nine Months Ended
September 30, 2015

(in thousands)	Number of Loans	Term Modification	Rate Modification	Combination	Post-Modification Outstanding Balance
Commercial:					
Commercial secured by real estate	13	$ 953	$ 0	$ 165	$ 1,118
Commercial other	4	1,193	0	0	1,193
Residential:					
Real estate mortgage	1	0	0	290	290
Total troubled debt restructurings	18	$ 2,146	$ 0	$ 455	$ 2,601

	Three Months Ended September 30, 2014				
(in thousands)	Number of Loans	Term Modification	Rate Modification	Combination	Post-Modification Outstanding Balance
Commercial:					
Commercial construction	1	$ 7	$ 0	$ 0	$ 7
Commercial secured by real estate	4	2,416	0	67	2,483
Commercial other	4	451	0	0	451
Total troubled debt restructurings	9	$ 2,874	$ 0	$ 67	$ 2,941

	Nine Months Ended September 30, 2014				
(in thousands)	Number of Loans	Term Modification	Rate Modification	Combination	Post-Modification Outstanding Balance
Commercial:					
Commercial construction	1	$ 7	$ 0	$ 0	$ 7
Commercial secured by real estate	7	2,647	0	67	2,714
Commercial other	7	512	0	0	512
Residential:					