TRUSTMARK CORP
Form 10-Q
May 09, 2012

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

Form 10-Q

þ QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended March 31, 2012

or

o 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 000-03683

Trustmark Corporation
(Exact name of registrant as specified in its charter)

Mississippi (State or other jurisdiction of incorporation or organization)	64-0471500 (I.R.S. Employer Identification No.)
248 East Capitol Street, Jackson, Mississippi (Address of principal executive offices)	39201 (Zip Code)

(601) 208-5111
(Registrant's telephone number, including area code)

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 þ No o

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). Yes þ No o

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 the definitions of “large accelerated filer,” “accelerated filer” and “smaller reporting company” in Rule 12b of the Exchange Act.

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

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

As of April 30, 2012, there were 64,765,581 shares outstanding of the registrant’s common stock (no par value).

PART I. FINANCIAL INFORMATION
ITEM 1. FINANCIAL STATEMENTS

Trustmark Corporation and Subsidiaries
Consolidated Balance Sheets
($ in thousands)

	(Unaudited) March 31, 2012	December 31, 2011
Assets		
Cash and due from banks (noninterest-bearing)	$ 213,500	$ 202,625
Federal funds sold and securities purchased under reverse repurchase agreements	6,301	9,258
Securities available for sale (at fair value)	2,595,664	2,468,993
Securities held to maturity (fair value: $56,713-2012; $62,515-2011)	52,010	57,705
Loans held for sale (LHFS)	227,449	216,553
Loans held for investment (LHFI)	5,774,753	5,857,484
Less allowance for loan losses, LHFI	90,879	89,518
Net LHFI	5,683,874	5,767,966
Acquired loans:		
Noncovered loans	100,669	-
Covered loans	74,419	76,804
Less allowance for loan losses, acquired loans	773	502
Net acquired loans	174,315	76,302
Net LHFI and acquired loans	5,858,189	5,844,268
Premises and equipment, net	156,158	142,582
Mortgage servicing rights	45,893	43,274
Goodwill	291,104	291,104
Identifiable intangible assets	18,821	14,076
Other real estate, excluding covered other real estate	75,742	79,053
Covered other real estate	5,824	6,331
FDIC indemnification asset	28,260	28,348
Other assets	356,678	322,837
Total Assets	$ 9,931,593	$ 9,727,007
Liabilities		
Deposits:		
Noninterest-bearing	$ 2,024,290	$ 2,033,442
Interest-bearing	6,066,456	5,532,921
Total deposits	8,090,746	7,566,363
Federal funds purchased and securities sold under repurchase agreements	254,878	604,500
Short-term borrowings	82,023	87,628
Subordinated notes	49,847	49,839
Junior subordinated debt securities	61,856	61,856
Other liabilities	150,723	141,784
Total Liabilities	8,690,073	8,511,970
Shareholders' Equity		
Common stock, no par value:		

Authorized: 250,000,000 shares		
Issued and outstanding: 64,765,581 shares - 2012; 64,142,498 shares - 2011	13,494	13,364
Capital surplus	282,388	266,026
Retained earnings	944,101	932,526
Accumulated other comprehensive income, net of tax	1,537	3,121
Total Shareholders' Equity	1,241,520	1,215,037
Total Liabilities and Shareholders' Equity	$ 9,931,593	$ 9,727,007

See notes to consolidated financial statements.

Trustmark Corporation and Subsidiaries
Consolidated Statements of Income
($ in thousands except per share data)
(Unaudited)

	Three Months Ended March 31, 2012	2011
Interest Income		
Interest and fees on loans	$75,796	$76,270
Interest on securities:		
Taxable	18,384	19,992
Tax exempt	1,366	1,383
Interest on federal funds sold and securities purchased under reverse repurchase agreements	6	8
Other interest income	330	332
Total Interest Income	95,882	97,985
Interest Expense		
Interest on deposits	7,353	9,719
Interest on federal funds purchased and securities sold under repurchase agreements	171	338
Other interest expense	1,414	1,553
Total Interest Expense	8,938	11,610
Net Interest Income	86,944	86,375
Provision for loan losses, LHFI	3,293	7,537
Provision for loan losses, acquired loans	(194)	-
Net Interest Income After Provision for Loan Losses	83,845	78,838
Noninterest Income		
Service charges on deposit accounts	12,211	11,907
Bank card and other fees	7,364	6,475
Mortgage banking, net	7,295	4,722
Insurance commissions	6,606	6,512
Wealth management	5,501	5,986
Other, net	3,758	762
Securities gains, net	1,050	7
Total Noninterest Income	43,785	36,371
Noninterest Expense		
Salaries and employee benefits	46,432	44,036
Services and fees	10,747	10,270
Net occupancy - premises	4,938	5,073
Equipment expense	4,912	5,144
ORE/Foreclosure expense	3,902	3,213
FDIC assessment expense	1,775	2,750
Other expense	13,068	9,532
Total Noninterest Expense	85,774	80,018
Income Before Income Taxes	41,856	35,191
Income taxes	11,536	11,178

Net Income	$30,320	$24,013
Earnings Per Common Share		
Basic	$0.47	$0.38
Diluted	$0.47	$0.37
Dividends Per Common Share	$0.23	$0.23

See notes to consolidated financial statements.

Trustmark Corporation and Subsidiaries
Consolidated Statements of Comprehensive Income
($ in thousands)
(Unaudited)

	Three Months Ended March 31, 2012	Three Months Ended March 31, 2011
Net income per consolidated statements of income	$30,320	$24,013
Other comprehensive loss, net of tax:		
Unrealized gains on available for sale securities:		
Unrealized holding losses arising during the period	(1,916)	(946)
Less: adjustment for net gains realized in net income	(648)	(4)
Pension and other postretirement benefit plans:		
Change in the net actuarial loss during the period	980	753
Other comprehensive loss	(1,584)	(197)
Comprehensive income	$28,736	$23,816

See notes to consolidated financial statements.

Trustmark Corporation and Subsidiaries
Consolidated Statements of Changes in Shareholders' Equity
($ in thousands)
(Unaudited)

	2012	2011
Balance, January 1,	$1,215,037	$1,149,484
Net income per consolidated statements of income	30,320	24,013
Other comprehensive income	(1,584)	(197)
Common stock dividends paid	(14,900)	(14,866)
Common stock issued-net, long-term incentive plans:		
Stock options	33	401
Restricted stock	(1,187)	(620)
Excess tax benefit from stock-based compensation arrangements	674	976
Compensation expense, long-term incentive plans	1,127	1,038
Common stock issued, business combinations	12,000	-
Balance, March 31,	$1,241,520	$1,160,229

See notes to consolidated financial statements.

Trustmark Corporation and Subsidiaries
Consolidated Statements of Cash Flows
($ in thousands)
(Unaudited)

	Three Months Ended March 31, 2012	2011
Operating Activities		
Net income	$ 30,320	$ 24,013
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for loan losses	3,099	7,537
Depreciation and amortization	6,589	5,853
Net amortization of securities	1,618	1,559
Securities gains, net	(1,050)	(7)
Gains on sales of loans, net	(6,460)	(3,101)
Decrease in FDIC indemnification asset	60	-
Bargain purchase gain on acquisition	(2,754)	-
Deferred income tax provision (benefit)	1,880	(355)
Proceeds from sales of loans held for sale	378,255	242,755
Purchases and originations of loans held for sale	(388,370)	(195,964)
Originations and sales of mortgage servicing rights, net	(4,478)	(3,480)
Net decrease in other assets	3,940	29,455
Net increase (decrease) in other liabilities	10,674	(9,728)
Other operating activities, net	2,993	1,480
Net cash provided by operating activities	36,316	100,017
Investing Activities		
Proceeds from calls and maturities of securities held to maturity	5,699	30,806
Proceeds from calls and maturities of securities available for sale	234,155	147,958
Purchases of securities available for sale	(374,785)	(283,517)
Net decrease in federal funds sold and securities purchased under reverse repurchase agreements	2,957	10,047
Net decrease in loans	74,593	68,952
Purchases of premises and equipment	(6,909)	(2,487)
Proceeds from sales of premises and equipment	-	374
Proceeds from sales of other real estate	10,039	15,399
Net cash received in business combination	78,151	-
Net cash provided by (used in) investing activities	23,900	(12,468)
Financing Activities		
Net increase in deposits	315,587	381,707
Net decrease in federal funds purchased and securities sold under repurchase agreements	(349,622)	(149,219)
Net increase (decrease) in short-term borrowings	74	(274,385)
Common stock dividends	(14,900)	(14,866)
Common stock issued-net, long-term incentive plans	(1,154)	(219)
Excess tax benefit from stock-based compensation arrangements	674	976
Net cash used in financing activities	(49,341)	(56,006)

Increase in cash and cash equivalents	10,875	31,543
Cash and cash equivalents at beginning of period	202,625	161,544
Cash and cash equivalents at end of period	$ 213,500	$ 193,087

See notes to consolidated financial statements.

Trustmark Corporation and Subsidiaries
Notes to Consolidated Financial Statements
(Unaudited)

Note 1 – Business, Basis of Financial Statement Presentation and Principles of Consolidation

Trustmark Corporation (Trustmark) is a multi-bank holding company headquartered in Jackson, Mississippi. Through its subsidiaries, Trustmark operates as a financial services organization providing banking and financial solutions to corporate institutions and individual customers through approximately 170 offices in Florida, Mississippi, Tennessee and Texas.

The consolidated financial statements in this quarterly report on Form 10-Q include the accounts of Trustmark and all other entities in which Trustmark has a controlling financial interest. All significant intercompany accounts and transactions have been eliminated in consolidation.

The accompanying unaudited condensed consolidated financial statements have been prepared in conformity with U.S. generally accepted accounting principles (GAAP) for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by U.S. GAAP for complete financial statements and should be read in conjunction with the consolidated financial statements, and notes thereto, included in Trustmark's 2011 annual report on Form 10-K.

Operating results for the interim periods disclosed herein are not necessarily indicative of the results that may be expected for a full year or any future period. Certain reclassifications have been made to prior period amounts to conform to the current period presentation. In the opinion of Management, all adjustments (consisting of normal recurring accruals) considered necessary for the fair presentation of these consolidated financial statements have been included. The preparation of financial statements in conformity with these accounting principles requires Management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and income and expense during the reporting period and the related disclosures. Although Management's estimates contemplate current conditions and how they are expected to change in the future, it is reasonably possible that in 2012 actual conditions could vary from those anticipated, which could affect our results of operations and financial condition. The allowance for loan losses, the valuation of other real estate, the fair value of mortgage servicing rights, the valuation of goodwill and other identifiable intangibles, the status of contingencies and the fair values of financial instruments are particularly subject to change. Actual results could differ from those estimates.

Note 2 – Business Combinations

Bay Bank & Trust Company

On March 16, 2012, Trustmark National Bank (TNB) completed its merger with Bay Bank & Trust Co. (Bay Bank), a 76-year old financial institution headquartered in Panama City, Florida. Trustmark acquired all outstanding common stock of Bay Bank for approximately $22 million in cash and stock, comprised of $10 million in cash and the issuance of approximately 510 thousand shares of Trustmark common stock valued at $12 million. This acquisition was accounted for under the acquisition method in accordance with FASB ASC Topic 805, "Business Combinations." Accordingly, the assets and liabilities, both tangible and intangible, are recorded at their estimated fair values as of the acquisition date. The purchase price allocation is deemed preliminary as of March 31, 2012 and is expected to be finalized in the second quarter of 2012.

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The statement of assets purchased and liabilities assumed in the Bay Bank acquisition is presented below at their estimated fair values as of the acquisition date of March 16, 2012 ($ in thousands):

Assets		
Cash and due from banks	$	88,154
Securities available for sale		26,369
LHFI, excluding covered loans		98,053
Premises and equipment, net		9,466
Identifiable intangible assets		5,454
Other real estate		2,569
Other assets		4,014
Total Assets		234,079
Liabilities		
Deposits		208,796
Other liabilities		526
Total Liabilities		209,322
Net assets acquired at fair value		24,757
Consideration paid to Bay Bank		22,003
Bargain purchase gain		2,754
Income taxes		-
Bargain purchase gain, net of taxes	$	2,754

The preliminary bargain purchase gain represents the excess of the net of the estimated fair value of the assets acquired and liabilities assumed over the consideration paid to Bay Bank. The gain of $2.8 million recognized by Trustmark is considered a gain from a bargain purchase under FASB ASC Topic 805. The gain was recognized as other noninterest income in Trustmark's consolidated statements of income for the three months ended March 31, 2012. Included in noninterest expense are non-routine Bay Bank transaction expenses totaling approximately $2.6 million (change in control and severance expense of $672 thousand included in salaries and benefits; contract termination and other expenses of $1.9 million included in other expense).

The identifiable intangible assets represent the core deposit intangible at fair value at the acquisition date. The core deposit intangible is being amortized on an accelerated basis over the estimated useful life, currently expected to be approximately 10 years.

Loans acquired from Bay Bank were evaluated under a fair value process involving various degrees of deterioration in credit quality since origination, and also for those loans for which it was probable at acquisition that TNB would not be able to collect all contractually required payments. These loans, with the exception of revolving credit agreements, are referred to as acquired impaired loans and are accounted for in accordance with FASB ASC Topic 310-30, "Loans and Debt Securities Acquired with Deteriorated Credit Quality." Refer to Note 5 – Acquired Loans for further information on acquired loans.

The operations of Bay Bank are included in TNB's operating results from March 16, 2012 and did not have a material impact on TNB's results of operations. Therefore, pro forma information is not presented.

Heritage Banking Group

On April 15, 2011, the Mississippi Department of Banking and Consumer Finance closed the Heritage Banking Group (Heritage), a 90-year old financial institution headquartered in Carthage, Mississippi, and appointed the Federal Deposit Insurance Corporation (FDIC) as receiver. On the same date, TNB entered into a purchase and assumption agreement with the FDIC in which TNB agreed to assume all of the deposits and purchased essentially all of the assets of Heritage. The FDIC and TNB entered into a loss-share transaction on approximately $151.9 million of Heritage assets, which covers substantially all loans and all other real estate. Under the loss-share agreement, the FDIC will cover 80% of covered loan and other real estate losses incurred. Because of the loss protection provided by the FDIC, the risk characteristics of the Heritage loans and other real estate covered by the loss-share agreement are significantly different from those assets not covered by this agreement. As a result, Trustmark will refer to loans and other real estate subject to the loss-share agreement as “covered” while loans and other real estate that are not subject to the loss-share agreement will be referred to as “noncovered” or “excluding covered.” The loss-share agreement applicable to single family residential mortgage loans and related foreclosed real estate provides for FDIC loss sharing and TNB’s reimbursement to the FDIC for recoveries of covered losses for ten years from the date on which the loss-share agreement was entered. The loss-share agreement applicable to commercial loans and related foreclosed real estate provides for FDIC loss sharing for five years from the date on which the loss-share agreement was entered and TNB’s reimbursement to the FDIC for recoveries of covered losses for an additional three years thereafter.

Pursuant to the provisions of the Heritage loss-share agreement, TNB may be required to make a true-up payment to the FDIC at the termination of the loss-share agreement should actual losses be less than certain thresholds established in the agreement. To the extent that actual losses on covered loans and covered other real estate are less than estimated losses, the applicable true-up payable to the FDIC upon termination of the loss-share agreement will increase. To the extent that actual losses on covered loans and covered other real estate are more than estimated losses, the applicable true-up payable to the FDIC upon termination of the loss-share agreement will decrease. TNB calculates the projected true-up payable to the FDIC quarterly and records a FDIC true-up provision for the present value of the projected true-up payable to the FDIC at the termination of the loss-share agreement. The FDIC indemnification asset is presented net of the FDIC true-up provision. Changes in the FDIC true-up provision are recorded to noninterest income.

The assets purchased and liabilities assumed for the Heritage acquisition have been accounted for under the acquisition method of accounting (formerly the purchase method). The assets and liabilities, both tangible and intangible, are recorded at their estimated fair values as of the acquisition date. The fair value amounts are subject to change for up to one year after the closing date as additional information relating to closing date fair values becomes available.

The statement of assets purchased and liabilities assumed in the Heritage acquisition are presented below at their estimated fair values as of the acquisition date of April 15, 2011 ($ in thousands):

Assets		
Cash and due from banks	$	50,447
Federal funds sold		1,000
Securities available for sale		6,389
LHFI, excluding covered loans		9,644
Covered loans		97,770
Premises and equipment, net		55
Identifiable intangible assets		902
Covered other real estate		7,485
FDIC indemnification asset		33,333
Other assets		218
Total Assets		207,243
Liabilities		
Deposits		204,349
Short-term borrowings		23,157
Other liabilities		730
Total Liabilities		228,236
Net assets acquired at fair value		(20,993)
Cash received on acquisition		28,449
Bargain purchase gain		7,456
Income taxes		2,852
Bargain purchase gain, net of taxes	$	4,604

The bargain purchase gain represents the net of the estimated fair value of the assets acquired and liabilities assumed and is influenced significantly by the FDIC-assisted transaction process. Under the FDIC-assisted transaction process, only certain assets and liabilities are transferred to the acquirer and, depending on the nature and amount of the acquirer's bid, the FDIC may be required to make a cash payment to the acquirer. The pretax gain of $7.5 million recognized by Trustmark is considered a bargain purchase transaction under FASB ASC Topic 805. The gain was recognized as other noninterest income in Trustmark's consolidated statements of income for the year ended December 31, 2011. For the three months ended March 31, 2012, the operations of Heritage added revenue of $3.1 million and net income available to common shareholders of $1.7 million.

Fair Value of Acquired Financial Instruments

For financial instruments measured at fair value, TNB utilized Level 2 inputs to determine the fair value of securities available for sale, time deposits (included in deposits above) and FHLB advances (shown as short-term borrowings above). Level 3 inputs were used to determine the fair value of both LHFI and covered loans, identifiable intangible assets, covered other real estate and the FDIC indemnification asset. The methodology and significant assumptions used in estimating the fair values of these financial assets and liabilities are as follows:

Securities Available for Sale

Estimated fair values for securities available for sale are based on quoted market prices where available. If quoted market prices are not available, estimated fair values are based on quoted market prices of comparable instruments.

Acquired Loans

Fair value of acquired loans is determined using a discounted cash flow model based on assumptions regarding the amount and timing of principal and interest payments, estimated prepayments, estimated default rates, estimated loss severity in the event of defaults and current market rates.

Identifiable Intangible Assets

The fair value assigned to the identifiable intangible assets, in this case core deposit intangibles, represent the future economic benefit of the potential cost savings from acquiring core deposits in the acquisition compared to the cost of obtaining alternative funding from market sources.

Other Real Estate, Including Covered Other Real Estate

Other real estate, including covered other real estate, was initially recorded at its estimated fair value on the acquisition date based on similar market comparable valuations less estimated selling costs.

FDIC Indemnification Asset

The FDIC indemnification asset was initially recorded at fair value, based on the discounted value of expected future cash flows under the loss-share agreement.

Time Deposits

Time deposits were valued by projecting expected cash flows into the future based on each account’s contracted rate and then determining the present value of those expected cash flows using current rates for deposits with similar maturities.

FHLB Advances

FHLB advances were valued by projecting expected cash flows into the future based on each account’s contracted rate and then determining the present value of those expected cash flows using current rates for advances with similar maturities.

Please refer to Note 16 – Fair Value for more information on Trustmark’s classification of financial instruments based on valuation inputs within the fair value hierarchy.

Note 3 – Securities Available for Sale and Held to Maturity

The following table is a summary of the amortized cost and estimated fair value of securities available for sale and held to maturity ($ in thousands):

	Securities Available for Sale				Securities Held to Maturity			
March 31, 2012	Amortized Cost	Gross Unrealized Gains	Gross Unrealized (Losses)	Estimated Fair Value	Amortized Cost	Gross Unrealized Gains	Gross Unrealized (Losses)	Estimated Fair Value
U.S. Government agency obligations								
Issued by U.S. Government agencies	$31	$ -	$ -	$31	$-	$ -	$ -	$-
Issued by U.S. Government sponsored agencies	102,489	140	(688)	101,941	-	-	-	-
Obligations of states and political subdivisions	197,312	11,079	(157)	208,234	40,393	4,133	(2)	44,524
Mortgage-backed securities								
Residential mortgage pass-through securities								
Guaranteed by GNMA	19,108	956	-	20,064	4,089	295	-	4,384
Issued by FNMA and FHLMC	279,597	6,595	(23)	286,169	586	29	-	615
Other residential mortgage-backed securities								
Issued or guaranteed by FNMA, FHLMC or GNMA	1,576,899	43,021	-	1,619,920	4,743	83	-	4,826
Commercial mortgage-backed securities								
Issued or guaranteed by FNMA, FHLMC or GNMA	321,687	10,013	(1,382)	330,318	2,199	165	-	2,364
Asset-backed securities / structured financial products	23,670	23	-	23,693	-	-	-	-
Corporate debt securities	5,292	30	(28)	5,294	-	-	-	-
Total	$2,526,085	$ 71,857	$ (2,278)	$2,595,664	$52,010	$ 4,705	$ (2)	$ 56,713

December 31, 2011

U.S. Government agency obligations										
Issued by U.S. Government agencies	$3	$-	$-		$3	$-	$-	$-		$-
Issued by U.S. Government sponsored agencies	64,573	229	-		64,802	-	-	-		-
Obligations of states and political subdivisions	190,868	11,971	(12	)	202,827	42,619	4,131	(2	)	46,748
Mortgage-backed securities										
Residential mortgage pass-through securities										
Guaranteed by GNMA	11,500	945	-		12,445	4,538	336	-		4,874
Issued by FNMA and FHLMC	340,839	7,093	-		347,932	588	28	-		616
Other residential mortgage-backed securities										
Issued or guaranteed by FNMA, FHLMC or GNMA	1,570,782	44,183	-		1,614,965	7,749	133	(1	)	7,881
Commercial mortgage-backed securities										
Issued or guaranteed by FNMA, FHLMC or GNMA	216,698	9,497	(176	)	226,019	2,211	185	-		2,396
Total	$2,395,263	$73,918	$(188	)	$2,468,993	$57,705	$4,813	$(3	)	$